Social Security

International Update:

Recent Developments in Foreign Public and Private Pensions

September 2012

Europe

Slovak Republic

On September 1, a new law went into effect that reduces contributions to second-pillar mandatory individual accounts and reallocates them to the first-pillar public, pay-as-you-go (PAYG) program. As a result, contributions to the second pillar fell from 9 percent of earnings to 4 percent, while contributions to the PAYG program increased from 9 percent of earnings to 14 percent. (Contributions to second-pillar individual accounts are drawn from the total employer contribution of 14 percent; employees continue to contribute 4 percent to the PAYG program only.) The government's position is that the new measure is necessary to reduce the country's public deficit to under 3 percent of gross domestic product (GDP) as required under the European Union's Stability and Growth Pact; according to data from Eurostat—the European Union's statistical office—the country ended 2011 with a deficit of 4.8 percent of GDP.

The new law also allows existing members to opt out of the second pillar from September 2012 through January 2013, with their second-pillar account balances transferred to the first-pillar PAYG program. Once the funds have been moved to the state-run pension provider, Socialna Poistovna, the worker will be credited with an equivalent number of years of contributions to the public system. The government expects that around 60,000 workers (from the 1.45 million current second-pillar account holders) will choose to opt out during that period. This marks the third time that the government has allowed workers to opt out of the second pillar: the previous two opt-out periods, which took place in 2008 and 2009, led to 106,000 and 66,000 participants, respectively, leaving the second pillar.

In January 2005, the Slovak Republic introduced its two-pillar pension system, consisting of a reformed PAYG pillar and individual accounts that are mandatory for new entrants to the workforce. A law that passed in March 2009 made participation voluntary for new entrants to the workforce; however, that law was subsequently reversed in September 2011.

Sources: "Slovak Republic," *International Update*, US Social Security Administration, December 2008 and November 2011; "Pension Scheme to Be Changed, Again," *The Slovak Spectator*, July 9, 2012; "Slovak Parliament Curbs Payments to Private Pension Funds," *Agence France Presse*, August 10, 2012; "Pensions Reform Bill Passes Slovakian Parliament," *IPE.com*, August 16, 2012; Eurostat statistics database, European Commission, http://epp.eurostat.ec.europa.eu/portal/page/portal/statistics/themes.

Asia and the Pacific

Malaysia

In September, Malaysia implemented the voluntary Private Retirement Scheme (PRS), a new defined contribution retirement savings program open to all Malaysian residents aged 18 or older. The PRS supplements the government-run mandatory retirement system and is designed to increase the level of retirement savings for all segments of the population.

Under the PRS, approved providers, or asset management companies, must offer a range of investment funds with varying degrees of risk: three default funds (growth, moderate, and conservative) and four other fund types. (To date, 8 providers and 24 investment products have been approved.) Participants have the option of contributing to more than one fund managed by a single provider, or of contributing to multiple funds offered by several providers; they also have the option of switching funds within a provider at any time, or of changing providers once a year. Individuals who choose a PRS provider but do not make a fund selection are assigned to one of the three default funds based on their age group.

There are no specific requirements for contribution amounts or at what intervals they are made; employees and employers (on behalf of their employees) are permitted to contribute to the PRS. Measures to encourage participation in the PRS include—

- personal tax incentives of up to 3,000 ringgits (US$961) for contributions by individuals;
- employer tax deductions of up to 19 percent of employer income for PRS contributions (the same as under the Employee Provident Fund (EPF)); and

- tax exemptions for investment earnings of individual accounts.

The administrative organization for the PRS consists of the following:

- The Securities Commission regulates and supervises all fees and intermediaries to ensure proper functioning of the PRS industry and protection of participant financial interests.
- A newly created Private Pension Administrator is responsible for recordkeeping.

Malaysia's public pension system includes the mandatory EPF for private-sector employees and certain public-sector employees and a social insurance program for casual workers and employees up to age 55 earning 3,000 ringgits or less a month. Since January 2010, the EPF has also managed the voluntary EPF1 Malaysia Retirement Savings Scheme for self-employed individuals and others without a fixed monthly income (unemployed spouses, farmers, fishermen, and so forth); participants receive a prorated annual government subsidy in addition to the EPF annual dividend (currently 2.5 percent of assets under management).

Sources: "Malaysia," *International Update*, US Social Security Administration, November 2010; *Private Retirement Scheme (PRS),* Securities Commission Malaysia, 2012, http://www.sc.com.my/eng/html/ppa/PRS_booklet_web.pdf; Securities Commission Malaysia, press release, July 18, 2012; "Scheme a Great Investment Alternative," *New Straits Times*, July 20, 2012; "Details of Private Retirement Scheme (PRS)," Granduan2U, July 23, 2012, http://www.graduan2u.com.

Reports

Social Security Administration

The Social Security Administration has released *Social Security Programs Throughout the World: Europe, 2012*—part of a four-volume series that provides a cross-national comparison of the social security systems in 45 countries in Europe. It summarizes the five main social insurance programs in those countries: (1) old-age, disability, and survivors; (2) sickness and maternity; (3) work injury; (4) unemployment; and (5) family allowances. The other regional volumes in the series focus on the social security systems of countries in Africa, Asia and the Pacific, and the Americas.

World Bank

The World Bank recently released *International Patterns of Pension Provision II: A Worldwide Overview of Facts and Figures*, a cross-country and regional comparison of data on mandatory pension systems around the world. The report updates and significantly expands the scope of the first report published in 2000. The new report is divided into three sections: background statistics, pension design, and performance.

The first section presents demographic and labor market statistics. According to the report, the percentage of the population aged 65 or older in developed countries is projected to increase by more than two-thirds (to 26.1 percent) by 2050 and nearly triple (to 14.7 percent) in less developed countries. Similarly, the population aged 80 or older in the developed world is projected to increase from 3.7 percent (in 2005) to 9.4 percent (by 2050) and from 0.8 percent to 3.6 percent in less developed regions.

The table below shows the current and projected old-age dependency ratio (the population aged 65 or older divided by the population aged 15 to 64) for 2010 and 2050, respectively, by region. Sub-Saharan Africa has the lowest ratio and a relatively low projected increase, while the ratios in East Asia and the Pacific and the Middle East and North Africa are expected to triple.

Current and projected old-age dependency ratios, by region, 2010 and 2050

Region	2010	2050
East Asia and the Pacific	10.7	32.8
Europe and Central Asia	15.2	28.2
Latin America and the Caribbean	10.2	26.7
Middle East and North Africa	13.4	40.2
South Asia	7.8	19.1
Sub-Saharan Africa	5.6	8.7
High-income OECD	22.5	40.2

SOURCE: *International Patterns of Pension Provision II,* World Bank, June 2012.

The second section of the report deals with broad pension system design and "operational parameters" (such as qualifying conditions, benefit formulas, and indexation). Among the findings related to system design are the following:

- About 65 percent of all mandatory national pension systems are defined benefit and mostly publicly managed, pay-as-you-go systems. Some 30 percent of mandatory systems are defined contribution.
- More than 30 countries have second-pillar, mandatory privately managed individual accounts.
- Most high-income Organisation for Economic Co-operation and Development (OECD) countries (and about 80 countries worldwide) have some type of noncontributory flat-rate benefit (either universal or means tested).
- About half the countries surveyed in the report have separate systems for civil servants and other groups. The trend has been to integrate those separate systems with the national system.

The findings relating to the operational parameters include the following:

- Retirement ages are rising around the world and there is a trend toward equalizing the statutory or legal retirement age for men and women.
- The average minimum length of service/contribution requirement is 16 years. Among the various regions, the average ranges from 8 years in South Asia to 28 years in Eastern Europe and Central Asia.
- Of the 115 countries examined, about 20 percent use lifetime average earnings in their benefit formulas, and about 45 percent use the highest or final earnings.
- Most high-income OECD countries regularly index benefits, but many middle- and low-income countries make ad hoc increases. Indexation methods include prices, wages, and/or longevity.

The last section of the report presents basic system performance measures, such as coverage and public pension spending. Among the highlights related to performance are the following:

- The majority of the economically vulnerable are not covered by a pension system. Less than 30 percent of the global labor force is actively contributing to a pension system, and less than 20 percent of the older population receives benefits.
- The majority of contributors are in the formal sector. In countries where the majority of the labor force is in the informal sector or where the self-employed and agricultural workers are a significant part of the economy, contributory pension coverage is low.
- Over the past few decades, public pension spending has increased in most countries. Pension expenditures in high-income OECD countries as a percentage of gross domestic product are the highest in the world. This group of countries also has the highest rate of coverage.

Source*: International Patterns of Pension Provision II: A Worldwide Overview of Facts and Figures*, World Bank, June 2012.

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