PENSION SYSTEMS IN CEE COUNTRIES

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Content

Preface

In the past decades, all Europeans countries have been profoundly affected by population aging mainly because of declining fertility and increasing life expectancy. This scenario, however, has created enormous financial pressure on the PAYG pension systems, while the changing labor market has aggravated this challenge. Facing the similar but not equally sizable challenge, nearly all European countries had reformed their pension systems since the mid-1990s, in order to institutionally maintain its financial sustainability.

Compared to western European countries that has produced a large number of literatures on pension system reforms, so far we still know little about what has happened in the Central and Eastern European countries. And this is the main purpose that we decided to publish this book. In this book, there are totally 16 research reports written by the experts in the field, aiming to provide an overview of the pension systems in the CEE countries. The content covers the key challenges, main reforms and consequences, public expectations and major obstacles to overcome. The reports have indicated that, the CEE countries share much in common not only within the CEE block, but also with western European countries: First, they have encountered the very similar challenges, including drastic population aging and a growing number of informal jobs; Second, they have adopted almost the same reform approaches: namely, lifting the retirement age, cutting the benefits, increasing pension eligibility and putting more restrictions on early retirement and mostly importantly introducing a multi-pillar pension system. Certainly, the above reforms in the EEC countries has also been characterized by its demographic change: the decreasing proportion of its economically active population, especially the younger workers who incline to migrate to the western European countries. It is not surprising that this population emigration will make the financial situations of pension reforms more complicated. Moreover, the reports also illustrate that some EEC countries need to do more to safeguard the sustainability of pension systems, and others will face daunting challenges in ensuring an equitable pension scheme and guaranteeing an acceptable living standard for all retirees.

The reports are originally published as the summer issue of the Weekly Briefings in June, 2021, which is a key product of the China-CEE Institute. Nevertheless, the views in the book are solely represented by the individual authors instead of the China-CEE Institute.

The China-CEE Institute, registered as a non-profit limited company in Budapest, Hungary, was set up by the Chinese Academy of Social Sciences (CASS) in April, 2017. The China-CEE Institute builds ties and strengthens its partnerships with academic institutions and think tanks in Hungary, other Central and Eastern European countries, as well as other parts of Europe. The China-CEE Institute aims to facilitate scholars and researchers to carry out joint research projects and conduct field studies, to organize seminars and lecture series, to provide training programs for younger researchers and students, and finally to publish academic books, research reports and journal articles.

We wish this book will be beneficial to enrich people’s understandings on the challenges and coping strategies of pension reforms in the CEE countries. In fact, population aging and its potential impact on pension systems is a universal phenomenon. It has been widely recognized that great efforts need to be made all over the world in order to address this big issue, including maintaining the sustainability, increasing the feasibility and extending the coverage of pension schemes to protect all aged persons in need in the context of rapid demographic changes and uncertain economic growth. There is a popular Chinese saying: a jade can be polished by stones from other mountains. We believe that we can learn a lot from the trajectories and strategies of pension reforms in the CEE countries. Certainly, it is also an invaluable ingredient of publishing this book.

Prof. Dr. PENG Shuyi

Institute of European Studies, CASS

Pensions system in Albania: an overview

Marsela Musabelliu

Pensioners in Albania today are perhaps the generation that has been impacted the most by the socio-economic changes that the country endured in the past 30 years. Born during the Second World War or into a socialist regime, this generation found themselves in 1991 thrown into a harsh reality of turbo-capitalism. Years of work in state owned enterprises, cooperatives or government jobs, were not taken into account. Most were left jobless, their children fled the country and they were told to abide to the new, draconian rules and regulations. As they witnessed life as they knew it fade away, so did their pensions.

Introduction

Currently there around 665,900 retirees in Albania, composed by urban retirees 550,000 persons and rural retirees 115,000 persons. Their average pension is 85$ in rural areas and 140$ in urban areas. There is needed a minimum insurance period for an old age pension from 15 to 20 years, with a maximum of 35 years for a full pension, for both women and men. The average age of retirement is 62 for women and 65 for men.

The most common account among retirees in Albania is that they rely heavily on financial support of their offspring. This is also witnesses by the main description of remittances from abroad: the recipient usually is the parent.

Reform process and pensions in Albania since 1991

Prior to 1991 the initial social security system was gradually consolidated into two schemes: one for public sector employees and another for members of agricultural cooperatives.

This system was very generous and provided complete social protection. It was based on the solidarity of generations and there was present a very egalitarian practice, the maximum pension was set at no more than twice the minimum pension.

Profound transformation of the political and socio-economic situation in the 1990s, made it necessary to undertake a radical reform on social insurance system.[1] The Albanian Government, with the assistance of the World Bank after 1990, designing the reforms intended to secure the financial sustainability of the social security system for pensioners' and to support social sustainability/adequacy of benefits.

On May 11th, 1993, the Parliament approved the Law No. 7703 "*On Social Insurance in Republic of Albania*". The document claims that reformation of the old scheme of social insurance is reached by establishing a new system, whose foundations should carry the principles of social justice. [2]

The system built in 1993, provided integration into the new system of pensions of individuals who worked in the former agricultural cooperatives by establishing a new formula for pensions' calculation.

After 1993 the General System of Social Insurance is based on the contributory principle. The overall system of social insurance consists of: Compulsory Social Insurance, Voluntary Social Insurance, Supplementary Social Insurance and Special State Pensions. The system management is carried out by the Social Insurance Institute (SII), as a public independent state institution.

The second wave of pension reform (2002) increased retirement ages, adding five years for both men (60–65 years old) and women (55–60 years old) during a transitional period (2002–2024), while the minimum insurance period for old age pensions was reduced from 20 to 15 years. The termination of employment as an eligibility criterion for old age pension was abolished, so retirees may have a pension and continue working and paying social insurance contributions.

The last wave of pension reform in 2015 aimed to gradually increase and equalize retirement ages for men and women to 67 years by 2056, and extend the insurance period to 40 years by 2032. During the period 1993–

[1] ISSH (2020). Statistika kryesore të sigurimeve shoqërore. Retreived from: http://www.issh.gov.al/wp-content/uploads /2021/04/Perb_12_20-web_07_04_2021.pdf

[2] Ministry of Finance of the Republic of Albania, Social Insurance Institute. Retrieved from: http://www.issh.gov.al/

2016, the average real retirement age has increased from 53.2 to 63.2 years old.

The *status quo* and reform orientation of pension system

A basic non-contributory pension was introduced for Albanians above age 70 without any source of income As a result, the main indicators of the social insurance system changed during the period of reforms 1990–2016. Although the years of working life was extended from 53 years in 1993 to 63 years in 2016, the share of pensioners to total population continued to increase.

Parametric reforms of social insurance will Improvement of the contributions' collection and facilitation of business procedures through delegating the contribution collection from the social insurance structures to tax offices is also in plan. [1]

[1] Xhumari M.V. (2020) Albania. In: Ní Léime Á. et al. (eds) Extended Working Life Policies. Springer, Cham. https://doi.org/10.1007/978-3-030-40985-2_6

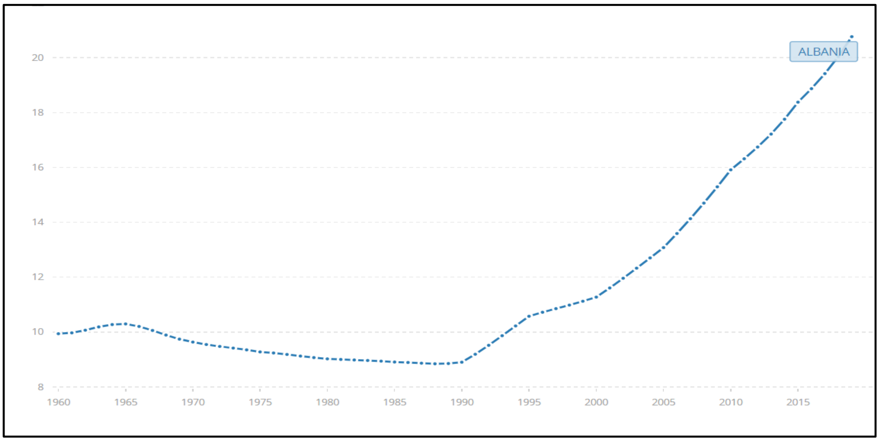
Some indicators of the pension system in Albania, 1990–2016

Main indicators/Year	1990	1993[a]	2016
Share of pensioners/total population	9.8%	13.4%	19%
Formal age of retirement	45–65 years old	50–65 years old	55–65 years old, still in the process of increasing
The average real age of retirement	57.1	53.2	63.2
Maximum insurance period for a full old age pension	15–25	20–35 years	35 years, still in the process of increasing
Replacement rate (average old age pension/average wage)	74.2%	56.4%	41.7%
Dependency ratio (number of pensioners/number of contributors)	4.5:1	1.6:1	1.1:1
Percentage of social insurance contributions/wage	19%	42.5% out of which 31.7% for pensions	27.9% out of which 21.6% for pensions
Subsidy from state budget to social insurance budget as % of GDP	–	1.80	1.89

Source: Xhumari, M.V. (2020, Springer)

The trend of pensions for Albania can be better analyzed by the age dependency ratio (specifically the ratio of older dependents--people older than 64--to the working-age population per 100 working-age population). Data from the World Banka are displayed in the table below:

Age dependency ratio, old (% of working-age population) - Albania



Source: World Bank

Due to changes in demographic patterns of fertility, life expectancy and migration, the old age dependency ratio nearly doubled (from 8.6% in 1989 to 16.7% in 2011) and is expected to grow to 32.9% by 2030.

Challenges and development trend of pension system

The financial instability of the scheme. A very large share of social protection schemes is funded by the state budget and increasing the number of beneficiaries will make financing impossible. The relatively high number of retirees compared to the young age of the population makes the scheme unsustainable in the long run. If the support ratio continues to deteriorate, the system's sustainability and ability to pay relevant pensions in the long run will be compromised. This is also a result of low age of retirees due to the early retirement in the 1990s.

And still, pension expenditure in Albania is at the lower end of the spectrum compared with the European Union (EU) and other Western Balkan countries.[1]

Unemployment and informality. The high level of unemployment, undeclared work and non-participation in the scheme of the self-employed

[1] World Bank's Advisory Services and Analytics (ASA). Albania: Pension Policy Challenges in 2020. Retrieved from: https://documents1.worldbank.org/curated/en/110911593570542693/pdf/Albania-Pension-Policy-Challenges-in-2020.pdf

in agriculture will be a huge social burden for the society in the coming years, as this uninsured category will not be entitled to benefits.

By law, employers and the self-employed pay contributions based on the minimum wage defined each year by the government, but often employees in the private sector declare just the minimum wage for payment of contributions, as it has the highest return for benefits. As a result, about 90% of old age pensions are at the minimum level of benefits necessary to survive.

High emigration rate of labor force. On one side the emigration abroad is financially supporting retirees in Albania, on the other this is a percentage of the population that does not pay taxes and social security in the country. Thus migration is deterioration the pensions' situation because the ones that leave Albania are in their prime working years.

Poor link between contributions paid and pensions received. The system dependency rate (NVS), which expresses the ratio between contributors and beneficiaries, will increase from about 86 retirees per 100 contributors in the base year to about 120 retirees per 100 contributors in 2032. After it will remain above this level until at the end of the forecasted period, marking a slight decline in 2080 where this ratio will be 118 retirees per 100 contributors. [1]

The aging of the population will lead to an increase in the coefficient of dependence of the elderly, which from 23% in 2012 increases to 41% in 2030. Then the growth rate is gradual, going to 56.8% in 2055 and reaches the highest value, 68.9%, in 2080. Such an increase in the dependency ratio of the elderly makes the current pension system financially and demographically unaffordable. If it continues to provide benefits in a ratio similar to average salary as today and in case it will give benefits to all seniors.[2]

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[1] Telo, I. (2017). Popullsia e Shqipërisë dhe probleme të saj. Mirgeeralb. Retrieved from: http://www.revistademografia.al/ilia_telo_artikulli_demografise_nr1_2017.html

[2] Xhumari M.V. (2020) Albania. In: Ní Léime Á. et al. (eds) Extended Working Life Policies. Springer, Cham. https://doi.org/10.1007/978-3-030-40985-2_6

Gender gap. Gender gap in pensions is currently 16,384 Albanian Lek (ALL) for men and 13,072 ALL for women, in average women receive a 20% less income than men in their retirement years. Unfortunately, for most women the transition into retirement equates to a transition into poverty. Introduction of the social pension, as a means-tested social assistance for those above age 70, is especially directed towards women, who have higher unemployment rates, lower contribution periods and greater life expectancy compared to men.

Conclusion

The current pension scheme, if it continues as it is, in the future will provide much lower benefits than today compared to the average wage and the state will continue to have fiscal deficits. Most importantly, a part of the population will not receive pensions at all due to the non-participation of today's working age population in the pension system.

The current conditions are already gloomy enough, however, if we are to take into consideration the trend and serious projections, the situation will deteriorate further.

Depopulation, informality, poor application of labor laws, lack of serious unions, and absence of adequate policies are making Albanian elderly the most vulnerable group of the society.

Pension system in Bosnia and Herzegovina

Zvonimir Stopić

Summary

Two entities in Bosnia and Herzegovina have been operating separate public pension systems. Pension reforms in the Federation of Bosnia and Herzegovina have been only minimal, although broader reforms have been considered necessary. Republika Srpska led the reform process by launching a pension reform in 2011 to restore its fiscal balance and reduce pension contribution arrears. Reforms in Federation of Bosnia and Herzegovina have been implemented only since March 2018, resulting in a system with similar parameters to those of RS.

Introduction

The Pension and Disability Insurance System in Bosnia and Herzegovina is a classic Bismarckian type labour-based system of social insurance with a progressive 'single pillar'. Accrual of pension rights is based on payment of contributions, and the level of the final pension benefit is determined by the level of salary/wage during the active insurance period, adjusted for annual accrual rates. Contributions are paid into an autonomous extra budgetary fund and are mandatory for all employed persons. The existing pension system is based on traditional principles of social insurance: principle of legality; rights from pension insurance, conditions for acquiring those rights and quantification of those rights as defined by law; principle of intergenerational solidarity: reciprocity and solidarity.

Reform process of pension system

Two entities in Bosnia and Herzegovina have been operating separate public pension systems. Republika Srpska (RS) led the reform process by launching a pension reform in 2011 to restore its fiscal balance and reduce pension contribution arrears. Reforms in Federation of Bosnia and

Herzegovina (FBiH) have been implemented only since March 2018, resulting in a system with similar parameters to those of RS. The outlook of both pension systems is stable for the next decade, during which both entities would need to consider further pension reforms. These reforms would need to improve pension adequacy and ensure fiscal and social sustainability of the pension system, such as raising the retirement age and tightening early retirement options, as well as implementing policies to improve labor participation. With pension system parameters temporarily sustainable, the focus of reforms in both entities has increasingly been on improving administrative capacity and user-friendliness of pension administration; addressing specific pension system issues such as early retirement in hazardous occupations, privileged pensions, and the disability assessment process; and reducing the stock of unpaid pension contributions. Unpaid pension contributions in both entities have been mounting over the past three decades, creating eligibility obstacles for insured individuals and financial problems for the fiscal authorities. In both entities, great legal and organizational efforts have been put into developing and encouraging voluntary pension savings through tax stimulus and automatic enrollment in a voluntary opt-out model.

Pension reforms in the FBiH have been only minimal, although broader reforms have been considered necessary. New legislation on Pension Insurance in the FBiH was enacted in March 2018. Even though this legislation addresses the long-term fiscal sustainability problems in the pension system, the PAYG system still prevails. The defined benefit system of the past is being replaced by the introduction of a defined contributions system. Requirements for receiving an early old-age pension will be significantly stricter than before. The requirement for early retirement in 2018 for men was 35.5 years of paid pension insurance and 60.5 years of age, while for women it was 30.5 years of pension insurance and 55.5 years of age. This limit will increase for both men and women every year by half a year of age and half a year of paid pension insurance before reaching the 40-year limit of paid pension insurance. A more rigorous set of benefit reductions has been introduced, which act as a disincentive to early retirement: 4% annual reduction compared to prior 0.5% reduction for each year below age 65, according to the Law on Pension and Disability Insurance from 2019. In the first months after the adoption of the new law, 39% of the elderly population (65 years of age and older) may not be collecting any increase in state pension. Legislation created an increase that applied to 54,785 pensioners whose pensions increased by 10%, and another 53,454 who received an increase of 5%. Another outcome of the reform was that the deficit of the pension insurance fund was reduced.

In the RS, the right to a retirement pension can be reached at 65 years of age, if she or he has been paying insurance contributions for at least 15 years. An insured person who has not reached the age of 65 but who has 40 years of work experience and insurance contributions can retire at the age of 60. Women may retire earlier than men; at age 58 if they have paid 35 years' pension insurance. A widow is entitled to a family pension if, when her husband dies, she is over the age of 50 or over 45 and incapable of working.

The status quo and reform orientation of pension system

The pension system in Bosnia and Herzegovina has two components: a public pension system (age pension and disability pension) and voluntary, private pension insurance which is an open voluntary pension funds with no limitations on membership and closed voluntary funds where membership is limited to specific groups (e.g. employees of specified employers). The risks covered by pension and disability insurance are: old age, disability, death and physical disability. Rights arising from these risks are: the right to an old-age pension, disability and family pension, as well as the right to an allowance for physical disability. Over 80% of older persons are pensioners; of these, about 10% receive wartime disability allowances and about 5% receive social welfare. As a condition for receiving an old-age pension, an insured person is entitled to an old-age pension when he or she attains 65 years of age and at least 15 years of insurance, or at least 20 years of pensionable service, or when he/she attains

40 years of insurance service regardless of his/her age, according to Article 40 of the Law on Pension and Disability Insurance from 2018. Pension insurance is mandatory for: a person employed on a labour contract, a self-employed person, clerics and farmers. A person who does not pay compulsory insurance may pay voluntary insurance under certain conditions, as provided for by the law. An insured person has the right to financial compensation in the case of physical damage caused by injury at work or occupational diseases or if they need care. A person not involved in the compulsory insurance system can pay voluntary insurance, as there is no legal obligation to do so, under certain conditions. Voluntary pension funds fall into Pillar III of pension insurance, a voluntary component of the pension system.

The high spending on pensions is partly the result of many people receiving disability pensions at pre-retirement age. According to the data of Agency for Statistics of Bosnia and Herzegovina, many working-age people receive pensions, but around 39% of older people may not be collecting any state pension.

Challenges and development trend of pension system

The situation in pension funds is very similar in both entities of Bosnia and Herzegovina. For example, approximately 58% of all funds available in the FBiH are for old-age pensions, 16% for disability and 25% for family pensions. The share of old-age pensions has been increasing in both entities. The average size of pension benefits in both entities is very low. Average pensions in the FBiH and RS amounted to approximately € 189 and € 175 per month, respectively. From 2010, the average values of pensions have been mostly stagnant while the number of pension beneficiaries has been increasing. The amount of average pension is almost the same between the FBiH and RS. In relative terms, the average pension is 31% of the average gross wage. However, in view of the pension formula and the fact that the average total number of insurance contributions is 33 years, the replacement rates documented above suggest that there are certain pensioners who have had short periods of contributions but who have managed to be eligible for pensions.

Conclusion

Reforms in Federation of Bosnia and Herzegovina have been implemented only since March 2018, resulting in a system with similar parameters to those of Republika Srpska. The outlook of both pension systems is stable for the next decade, during which both entities would need to consider further pension reforms. These reforms would need to improve pension adequacy and ensure fiscal and social sustainability of the pension system, such as raising the retirement age and tightening early retirement options, as well as implementing policies to improve labor participation.

Pension System In Bulgaria

Evgeniy Kandilarov

Summary: The pension insurance system in Bulgaria is based on the development of the so-called three pillars:
- first pillar - mandatory state pension insurance as an element of the State social insurance;
- second pillar - additional mandatory pension insurance in pension funds managed by licensed pension insurance companies;
- third pillar - additional voluntary pension insurance in pension funds managed by licensed pension insurance companies.

The current Bulgarian pension system came into force with the Mandatory Social Insurance Code on 1 January 2000 (renamed the Social Insurance Code [SIC] in 2003). The main goal of the three-pillar pension model is to combine the advantages of the pay-as-you go and capital-based systems to ensure pension income that would substitute a significant part of the income before retirement.

The pension system in Bulgaria has undergone substantial structural reforms since the late 1990s when the Bulgarian government launched a process of preparation of a strategy for pension reform. The process of developing the strategy was coordinated by the World Bank. Its main strategic goals fit into the logic of consolidation the budget and stabilization of macroeconomic framework and policies required by the country international donors (WB and IMF). This brings the concept of pension reform known as 'Chilean' or 'multi-pillar pension model', which is developed by the World Bank in the early 1980s.

Finally in Bulgaria the traditional pay-as-you-go system was transformed into a three-pillar system through the introduction of compulsory and voluntary fully funded pillars.

For the first time voluntary private pensions were introduced in 1995. Other aspects of the pension reform include the separation of the State social insurance budget from the State budget, the establishment of specialized funds, and the introduction of the tripartite management of the State social insurance system. The current Bulgarian pension system came into force with the Mandatory Social Insurance Code on 1 January 2000 (renamed the Social Insurance Code [SIC] in 2003).
The main objectives of the reform were to stabilize the existing public insurance system (first pillar), and to allow the Bulgarian population to receive higher incomes after retirement through participation in second and third pillars of the pension system. From 2000 onwards, parametric reforms in the first pillar were implemented. The same year, a mandatory second pillar system for workers in hazardous occupations was implemented. It was followed in 2002 by a mandatory second pillar for all employees.

The first pillar is a pay-as-you-go public pension insurance system. Promoting the principle of mandatory participation and universality, the first pillar covers all economically active persons. It is financed through contributions from employers and employees, as well as through transfers from the State budget for covering all non-contributory pension benefits and some non-contributory periods, which are regarded as insurance periods. In the period 2009-2015 the State was participating as a "third insurer" and was paying contributions equal to 12 percent of the total insurance income of all insured persons. As of 2016 the State contribution was abolished. In addition, the State has the obligation to cover any remaining financial gaps and deficits of the public pension system.
The first pillar is administrated by the National Social Security Institute (NSSI), which is responsible for the entitlement and payment of pensions and other social insurance benefits in the event of one's temporary incapacity to work, maternity and unemployment. The pension policy is formulated and implemented by the Ministry of Labour and Social Policy.

The second pillar is a supplementary mandatory pension insurance system. It is based on individual retirement savings accounts managed by private pension insurance companies. The second pillar is comprised of two types of pension funds: Universal Pension Funds and Professional Pension Funds. The Universal Pension Funds (UPF) of Supplementary Mandatory pension insurance (second pillar) cover all persons insured through the public pension insurance born after 31 December 1959 and provide supplementary life-long old-age pensions as well as payments in case of death. They are still in accumulation phase and the first pensions are expected to be paid this year.

The Professional Pension Funds (PPF) of Supplementary Mandatory pension insurance (second pillar) are mandatory funds for early retirement intended to cover all persons working at hazardous environment (labour 'at risk').

The third pillar is a supplementary voluntary pension insurance system. It is a pension savings scheme based on voluntary contributions deposited in private pension funds that are maintained by licensed pension insurance companies. Currently, two types exist: the Voluntary Pension Funds and the Occupational Pension Funds. The latter are provided under occupational schemes and are based on collective agreements. Contributions to the third pillar are paid by the members themselves or by their employers and they are tax-exempt up to a certain limit. Benefits can be paid in the form of life annuities, fixed-term annuities, lump sums or programmed withdrawals for survivors' benefits.

The pre-reform system in Bulgaria was a pure Pay As You Go system, the design of which suffered from various problems. The retirement age of 55 for women and 60 for men was quite low. Employees in various occupations could retire even earlier, and early retirement was used as a means of cutting the workforce during the transition period. Evading social security contributions was a widespread practice, and the dramatic rise in unemployment led to a fall in the number of contributors. The link between contributions and benefits was weak, as pension benefits were based on the three best-earning years. To remedy the situation, the government developed a reform strategy that was implemented after 2000. Key measures included lowering the overall contribution rate and gradually increasing employee contributions.

The pensions system has undergone a number of reforms over the years. The changes are aimed at raising the retirement age and trying to ensure better pension provisions. On 28 July 2015, the National Assembly adopted important changes to the Social Security Code.

The first change was a 2 percentage point increase in social security contributions - 1 point from the beginning of 2017 and 1 point from the beginning of 2018. Such a mild increase was recommended in a 2013 report by the World Bank. There is no new increase of the social insurance contribution for pensions since the beginning of 2019.

The second change in the amended Social Security Code consists of raising the retirement age. In 2015, the retirement age for men in Bulgaria was 63 years and 10 months; for women it was 60 years and 10 months. In 2017, it was raised gradually for both men and women to finally reach the target of 65 years by 2029 for men and by 2037 for women. For men, the retirement age began to increase by 2 months in 2017 and by 1 month in every subsequent year. For women, the retirement age began to increase at a faster pace – by 2 months each year from 2017 until 2029 and by 3 months each year from 2030 to 2037. The required length of service / contribution period (which was in 2015 38 years and 2 months for men and 35 years and 2 months for women) began also to increase gradually for both genders, by 2 months each year staring from 2017 until it reaches 37 years for women and 40 years for men.

At the same time, there are many employees, who can retire earlier, even with shorter periods of service, on the base of the quality of their working conditions (for example, miners, part of workers in metallurgy, employees in the civil aviation etc.). This early retirement applies also to employees in military services, police, security services, supervisors in prisons and others.

Finally, a third important change and the most controversial one consists of the possibility for people who have insurance contributions, based both on the first and the second pillar of the pension system, to make multiple shifts between their savings. Those who have paid insurance contributions for the second pillar in a private pension fund can choose to transfer their pension savings from that fund to the national pension fund (which is state-owned) and continue to pay the amount of the two contributions into the national pension fund. It is also possible to shift funds back.

In conclusion we have to say that the pay-as-you go system is based on the principles of solidarity between generations. This means that the working generation of today, through their social security contributions, provides the payment of pensions to the pensioners. At the same time the deterioration of the demographic structure means that the number of working persons is decreasing and that poses major challenges to the state social security system in paying adequate pensions in the future.

Currently, the Bulgarian pension system is facing serious demographic challenges. In 2021, pension expenditures are expected to reach 9.9% of GDP. Between 2025 and 2034, the share of pension expenditures in GDP is expected to remain at a relatively constant level of around 10.0%. According to the Ministry of Finance, in the period from 2035 to 2060, as a result of the aging process and the expected higher life expectancy, the fiscal pressure on the state pension system will increase and the cost of pensions as a share of GDP will start to grow, reaching its highest value of 12.5% in 2060.

Reform Process of Pension System in Croatia

Valentino Petrović

Summary

The goal of this paper is to present and explain the main factors that shaped Croatia's pension system from the early 1990s onwards. As previously explained in many studies dealing with this issue, Croatia's pension system had followed the structure and reforms of other Central and Eastern Europe (CEE) countries, but the country suffered from the economic and social consequences of the Homeland War; therefore, many people had an opportunity to use the benefits of early old-age pension or invalidity pension. In the late 1990s and early 2000s, major reforms were initiated which changed the structure from the intergenerational solidarity principle to the three-pillars pension system.

Introduction

This paper deals with the structure of the pension system in Croatia and will present the factors that shaped the system as it was during the 1990s, as well as the subsequent reform in the early 2000s. The pension system in Croatia was always heavily debated among political actors and almost every political option had its respective opinion on how should it be structured and (re)formed. Compared to other Central and Eastern Europe (CEE) countries, Croatia underwent almost similar reforms[1]; however, the country had an additional factor that was reflected in the pension system to a large extent, that is, the Homeland War.

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[1] Pension Funds Online. Pension System in Croatia. *Wilmington Publishing & Information* https://www.pensionfundsonline.co.uk/content/country-profiles/croatia.

Reform Process Since the 1990s

When talking about the pension system in Croatia it is unavoidable to mention demographic trends that provoked major changes in the structure of the country's workforce. This problem has remained present since the early 1990s and many papers have been written about this particular subject and how it affected the current state of the art. However, before we tackle the specificities of challenges that the country needs to face, we shall briefly present how was the pension system reform process introduced. As it was mention in the introduction, "Croatia and its pension system not only had to cope with the deep structural transformation that came with the transition from communism to capitalism in the early and mid-1990s, but also with the disastrous consequences of the war in the former Yugoslavia. Apart from human and material losses, the war also led to a dramatic increase in the number of pensioners and a drop in the size of the active workforce"[1]. As evidenced in the paper written by Predrag Bejaković, a scientist from the Institute of Public Finance, the ratio between the number of people with pension insurance and the number of pensioners has been on a decline ever since the 1980s. For example, in 1980, the ratio was 4,04. Ten years later, in 1990, the ratio was 3,00, meaning that the number of pensioners has risen significantly. Again, ten years later, in 2000, during the time when the demographic trends and consequences of the Homeland War were evident the most, the ratio was 1,36[2]. This indicates that the number of people with pension insurance is dropping, while the number of pensioners, that is, the people with a possibility to retire, has been rising, especially in the mid-1990s. Moreover, "the PAYG system in place until 1998 was not able to deal with these shocks due to low retirement age, a weak link between contributions and benefits, and generous benefits. This

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[1] Pension Funds Online. Pension System in Croatia. *Wilmington Publishing & Information* https://www.pensionfundsonline.co.uk/content/country-profiles/croatia.

[2] Bejaković, Predrag. Mirovinski sustav. 101-110. *Institut za javne financije* http://www.ijf.hr/rosen/rosenic/mirovinski.pdf.

is why major pension reforms were initiated in a gradual, step-by-step manner. The Croatian government implemented parametric reforms of the PAYG system in 1999 and introduced mandatory and voluntary pension funds in 2002"[1].

Demographic Trends That Affect the Pension System

There is a number of demographic trends that seriously affect the structure of the Croatian pension system and subsequently have a considerable impact on the country's economy in general. Ever since Croatia joined the European Union in 2013, the country has witnessed a rising number of people who decided to move to other European countries in search of a better life and better job opportunities. Croatia has already lost a large number of highly educated people, but also the people who were working in other sectors, all of whom were paying contributions for the pension system. The economic effects of the COVID-19 also contributed to a declining level of employed people. Just as the number of employed people started to rise again and the country's economy was stabilized, the novel coronavirus caused many people to face losing their jobs, regardless of economic measures that the Government had introduced in order to prevent an economic downturn. Furthermore, the country's population is aging and there are indications that the number of people above 65 is going to rise in the upcoming years. Also, many people opt to choose early retirement before they meet all the conditions required to be eligible for full retirement, that is, the old-age pension. Finally, the definition of disability has become a subject of different interpretations, while the conditions for invalidity pension were not clear enough which caused many people to opt for it well. There were also various groups who enjoyed a privileged status such as "World War II veterans, former political prisoners, academics, police and military personnel (…) Retirement age was low at 60 for men and 55 for

[1] Pension Funds Online. Pension System in Croatia. *Wilmington Publishing & Information* https://www.pensionfundsonline.co.uk/content/country-profiles/croatia.

women. Early retirement was fairly easy and there were various supplements for years without contribution"[1]. All of this caused a crisis in the country's pension system and the previous governments had to respond by implementing different measures and reforms in order to stabilize the pension system as a whole.

The Three-Pillars Structure

The first reform that was introduced consisted of minor but important changes. For example, the retirement age for both men and women was risen to 65 and 60 years, respectively. Additionally, the number of disability or invalidity pensions was reduced due to a change of invalidity definition. Lastly, the formula to calculate the pensions was also changed[2]. However, a major reform was implemented when a three-pillar system was introduced in 2002 and changed the current pension system structure which was based on the intergenerational solidarity principle. Nowadays, "the first two pillars are mandatory for every employed citizen (…) while the third one refers to voluntary pension savings with state incentives. Contributions of all employees in the Republic of Croatia for mandatory pension insurance (first and second pillar) amount to 20% of their gross salary, while each individual may decide on the amount of contributions made to the third voluntary pension pillar"[3]. The people in the first fund or the first pillar are those who were 50 years old in 2002 when the second fund was founded or between 40 and 50 years old in 2002 but did not

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[1] Pension Funds Online. Pension System in Croatia. *Wilmington Publishing & Information* https://www.pensionfundsonline.co.uk/content/country-profiles/croatia.

[2] Bejaković, Predrag. Mirovinski sustav. 101-110. *Institut za javne financije* http://www.ijf.hr/rosen/rosenic/mirovinski.pdf.

[3] Hrvatsko mirovinsko osiguravajuće društvo. Croatian pension system. https://hrmod.hr/en/croatian-pension-system/.

“become voluntary users of the second fund at the time”[1]. Those people who are insured through the first pillar are paying 20% of their gross salary as a contribution, while those who are part of both the first and second pillar are paying 20% of contributions as well, however, they pay 15% from the first pillar and 5% from the second pillar. The second pillar is governed by privately-owned companies which are under the supervision of HANFA (Croatian Financial Services Supervisory Agency – *Hrvatska agencija za nadzor financijskih usluga*, Croatian translation). The third pillar refers to “individual capitalized savings based on payments to a voluntary pension fund. Membership in a voluntary pension fund is intended for any person who, by making payment to the fund, becomes eligible for state incentives and the yield generated by investing these funds”[2].

Conclusion

The reform of the pension system in Croatia is a topic that is being discussed every once in a while, but it appears that it will remain highly unpopular at least in terms of possible changes in the length of service and retirement age. A major concern remains: the negative demographic trends evidenced in a rising number of the older population (those above 65 years of age) while, at the same time, many young people who should be a backbone of the country in the near future are going abroad in search for better job opportunities.

[1] Everything you need to know about Croatia’s pension system (in 2021). *expatincroatia.com* https://www.expatincroatia.com/croatia-pension-system/.

[2] Hrvatsko mirovinsko osiguravajuće društvo. Croatian pension system. https://hrmod.hr/en/croatian-pension-system/.

Pension System in the Czech Republic

Ladislav Zemánek

Summary

The Czech Republic´s pension system belongs to those with continuously financing. The model was inherited from the socialist state before 1989. The existing pattern was legally established in 1995 and since that time no substantial change has been carried out except for the introduction of voluntary savings in private funds. Despite several attempts to reform the system, strengthening the capital component, made by right-wing cabinets in the past decades, the model is very paternalist. The reform draft which is under preparation does not lead to liberalisation and substantial strengthening of individual responsibility.

Introduction

The present pension system was introduced in 1995 and is compound of two parts: (1) a continuously financed model paying out pensions while being funded predominantly by social insurance revenues; (2) complementary and voluntary individual savings through private pension funds with state support. Participation in the continuously financed system is obligatory just as the levies are. Pensions consist of fixed and variable components and the basic condition for getting a state pension is that the pensioner contributed at least 35 years to the social insurance system and reached the retirement age. The Czech Republic´s pension model and its efficiency are heavily dependent on population development. The voluntary component is related to the situation in the financial market.[1]

The status quo

[1] I analyse some aspects of the Czech pension system in another briefing. See Zemánek, L. *Relying on the State Pension No More: The Pension System Unsustainable* (2021, May 26), china-cee.eu. Retrieved June 18, 2021, from https://china-cee.eu/2021/05/26/czech-republic-social-briefing-relying-on-the-state-pension-no-more-the-pension-system-unsustainable/.

In terms of the total expenditures on pensions, these account for approximately 8.4% of the GDP (the average figure in the EU is 12.6%). From the European perspective, the Czech pension is very below-average, even though the incumbent Government has increased pensions significantly at the cost of undue expenses and indebtedness. Generally, the living standard of the Czech citizens slumps by more than 50% after retirement, which is similarly below-average in the EU comparison. Pension equals roughly 41% of the average gross salary.[1] Nowadays, around 3.6 million pensions are being paid off by the state, 99% of them are financed by the Czech Social Security Administration, subordinated to the Ministry of Labour and Social Affairs, and the rest is secured by the Ministry of Justice and Ministry of the Interior.[2]

The Ministry of Labour and Social Affairs under the leadership of Jana Maláčová, a young representative of the Czech Social Democratic Party, has started preparing a reform of the pension system. It established the Commission for Just Pensions in January 2019 which was to elaborate proposals, taking into consideration analyses and recommendations presented by the OECD Report, requested by the Ministry of Labour and Social Affairs and the Ministry of Finance, in the course of 2020. The body is composed of representatives of all Parliamentary political parties, non-partisan experts and interested NGOs. It has focused especially on the following issues: (1) differences between men and women in terms of their old-age pensions; (2) possibilities of earlier retirement in the case of chosen professions; (3) revision of the widow´s and widower´s pensions; (4) revision of the so-called third pension pillar which is a voluntary instrument for individual pension savings with state contributions; (5) overall restructuring of the pension system and securing sources of finance.

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[1] Marek, D., Franče, V. *Jaké budou důchody?* (2019, September), Deloitte.com. Retrieved June 12, 2021, from https://www2.deloitte.com/content/dam/Deloitte/cz/Documents/deloitte-analytics/Jake_budou_duchody.pdf.

[2] Strnadová, D., Vacková, E. Penzijní závazky rostou. *Statistika & my*, 04, 2021, s. 40. Retrieved June 12, 2021, from https://www.statistikaamy.cz/wp-content/uploads/2021/04/18042104.pdf.

The Ministry initiated the standard interdepartmental proceedings at the end of the last year, putting forward the reform draft to the Government Legislative Council, an advisory body for the cabinet´s legislative work, this May. Subsequently, the document shall be turned over to the Government and the Parliament. However, there is a real risk that the Chamber of Deputies will not manage to debate the reform in time, since the election will be held in October. Once the term ends up, all matters, laws and amendments expire and the process has to start all over again. The destiny of the recent pension reform is therefore uncertain.

Contours of the reform

The reform draft addresses three major problems of the current system: (1) non-transparency; (2) inequity; (3) unsustainability, thus emphasising the need for principles of transparency and comprehensibility, equity and long-term sustainability.[1] Regarding the first point, the problem is that any citizen cannot calculate the pension he/she will be receiving after retirement. It complicates substantially financial planning and management. The most responsible way how to cope with the lack of information and extreme uncertainty is to build the sources of income independently on the state pension which applies more to entrepreneurs and self-employed persons. It is thus crucial to create a transparent system enabling anybody to calculate their pension at any moment without relying on data-free prognoses and expectations. As for the second point, the Ministry together with the Commission opines that the existing system is unjust because it puts women at a disadvantage. The gender discrepancy emerges primarily from the period of parental leave, during which women receive lower income. It consequently has an impact on the amount of the old-age pension. In addition, people working in especially strenuous professions (e.g. miners, welders or nurses) are not allowed to retire prematurely without negative effects on their pension. In consequence of the legal condition demanding participation in the social insurance system for at least 35 years, some people are not eligible for getting state pension at all irrespective of the fact

[1] *Spravedlivá důchodová reforma* (2021, June 07), mpsv.cz. Retrieved June 13, 2021, from https://www.mpsv.cz/spravedliva-duchodova-reforma.

that they worked for decades. As far as the third point is concerned, the very problem arises from the logic of the system itself and its financing. Virtually all expenditures on the pensions are covered by the insurance premium revenues of actual labour forces. These state expenditures reach up to 31.4% of expenses from the state budget. It follows that the system is utterly dependent on premium incomes. And these are dependent on economic performance as well as the number of working people. Given the long-term social trajectories (first and foremost, ageing) and absence of diversified sources of finance, the pension system is vulnerable and potentially very unstable.

Basing on these observations, the Ministry formulated several reform steps. The present first pillar shall be divided into two: zeroth pillar is to provide the same pension to all pensioners irrespective of their incomes (preliminarily 10.000 CZK/400 EUR) while the updated first one should derive the amount depending on the previous incomes, the period of social insurance as well as on the parental leave, education period, military service and so forth. According to the draft, the period of participation in the social insurance system shall be shortened to 25 years. In addition, the retirement age for those working in strenuous professions is to be decreased, the income tax for working pensioners should be reduced and every citizen will be given an opportunity to calculate their future pension. Regarding the sources of finance of the system, the zeroth pillar is to be financed from state tax revenues.[1] These measures are scheduled to be carried out no later than 2025.

Challenges and prospects

If the current system remains unchanged, the real pension will be decreasing in relation to the average salary. The present figure of 40% would drop. The legal obligation requiring an adjustment in line with inflation and development of salaries would inevitably lead to shortfalls,

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[1] *Architektura nového důchodového systému* (2020, January), duchodovakomise.cz. Retrieved June 14, 2021, from http://duchodovakomise.cz/wp-content/uploads/2020/01/Architektura-noveho-systemu.pdf.

unsustainable for a long period. The system can be further preserved in the case of an increase in social insurance and gradual postponement of the retirement age. But especially the first solution is hardly feasible given the high labour taxation in the Czech Republic.[1]

Even though the abovementioned reform would bring a positive move in some regards, it rather underestimates the third pillar, i.e. individual capital pension savings. As a whole, restructuring is not substantial, remaining just a soft reform. The financial sustainability of the updated system is fully dependent on tax reform and strengthening of efficiency of the tax system. This pension reform will not diversify the financial sources essentially, since these limit themselves to the tax and insurance premium revenues. It follows that the draft does not cope with the principal challenge of the future, which is the ageing of the population. It is beyond any doubts that such a reform would prolong the sustainability of the system, mitigating the most serious problems of the present state of affairs, however, it will deepen the citizens´ dependence on the state and state paternalism at the same time. This orientation will be undermining any efforts to make people more responsible for their retirement.

Conclusion

The existing pension system is economically unsustainable without a massive increase in the state budget revenues through the tax burden or significant postponement of the retirement age. Recently, pension reform is under preparation with the participation of all Parliamentary parties, which makes the project legitimate. This fact will also help to put it into practice, notwithstanding the risk that the current Chamber of Deputies might not manage to pass it until the end of their mandate in autumn. Although the reform would bring a positive move in some regards, it does not entail a substantial change in the model in defiance of this is desirable. Citizens should be engaged in creating reserves in capital funds. Naturally,

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[1] Marek, D., Franče, V. *Jaké budou důchody?* (2019, September), Deloitte.com. Retrieved June 12, 2021, from https://www2.deloitte.com/content/dam/Deloitte/cz/Documents/deloitte-analytics/Jake_budou_duchody.pdf.

it is not only a question of pension reform but also the development of the Czech capital market, financial education and strengthening of the market mechanisms.

The Estonian Pension System: Caring and Sharing

E-MAP Foundation MTÜ

Many primary and secondary schools around the world have a practice of issuing different certificates and awards that are not directly related to a student's academic performance. One of those is a certificate for 'sharing and caring', which, quite often, is rated among both students and parents as high as anything granted for an academic merit. In a metaphoric way, a country's pension system is something that the society has in place for 'sharing with' and 'taking care of' a very special and the most experienced societal segment, an older generation. Some years before, these people were the driving force of a given economy, producing goods and services, rising their children, trying to make their country a better place, adding plenty of value to their respective industries of involvement, and, more specifically, paying taxes. Since they get closer to their retirement, the state needs to 'climb' on a higher level of responsibility in the context of being ready to look after the advanced in years.

As declared, the aim of the Estonian pension system is to help people in the process of maintaining their current standard of living and monthly income when they retire.[1] The country's private pension system has a feature that is common for an OECD member – it is "based on individual savings accounts, and composed of two components, a mandatory and a voluntary one", while there are "no occupational pension schemes" existing in the

[1] 'Estonian pension system overview' in *Pensionikeskus*. Available from [https://www.pensionikeskus.ee/en/pension-system/estonian-pension-system-overview/].

country[1]. However, from 1991 and well before the OECD times (the country joined the organisation only in May 2010[2]), Estonia had to go through a range of dramatic as well as successful economic reforms, namely *1)* liberalising prices, industry and trade, *2)* reintroducing its own currency, and *3)* privatising the vast majority of state-owned companies at a very early stage after regaining independence[3].

Together and separately, these were considered a major necessity for the country to show its genuine politico-economic intentions as a liberal democracy. The first cabinet of Mart Laar (October 1992 – November 1994) made a dramatic difference, so the world would recognise Estonia's prospective impact on regional and global economies. The next step would logically be getting involved into structural institutional reforms, including taxes, healthcare, and, certainly, pensions. Commonly to all former titular republics of the USSR, the Soviet legacy left Estonia with a version of the so-called Pay-As-You-Go (PAYG) system, which was linked "to former wage and with high replacement rates reaching 80%", while having "[t]he statutory retirement age was 55 for women and 60 for men"[4]. In January 1991, less than a year before Estonia would regain its independence from the collapsing Soviet Union, it introduced a payroll ('social') tax to start collecting additional funds for "health services, old-age benefits and child

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[1] 'Estonia: Review of the private pensions systems' in *OECD*, October 2011, p. 7. Available from [https://www.oecd.org/daf/fin/private-pensions/49498084.pdf].

[2] 'Estonia and the OECD' in *OECD*. Available from [https://www.oecd.org/estonia/estoniaandtheoecd.htm].

[3] Ringa Raudla and Karsten Staehr, 'Pension Reforms and Taxation in Estonia' in *Baltic Journal of Economics*, 2003, 4:1, p. 64.

[4] Raudla and Staehr, p. 69.

benefits", interlinking a majority of social benefits with the minimum wage[1].

It was only the beginning of the process, because a completely new normative base (to be discussed at length) was needed to be adopted. For example, from 1993, the Act on State Living Allowances became in legal force to regulate the pensions system when Estonia was still an economy-in-transition. Being disrupted by the 1940 occupation but having got back on track in the process of re-establishing an independent republic and market economy, Estonia decided to completely overhaul the institute of pensions "by the introduction of a 3-pillar system, implemented in stages from 1998 and completed by mid-2002"[2]. Operationally, the funded pension framework started embracing "a comprehensive regulatory system", because, by 2001, the Government managed to merge a number of different topic-associated organisations into the issue-focused authority, the Estonian Financial Supervision Authority (FSA), which was tasked to license "all types of financial institutions" involved into the process[3].

It was a big call for Estonia to become one of the first countries in Central-Eastern Europe to get a 3-pillar pension system underway. As described in a classy 2003 academic research, the idea of the scheme was featured "by partially voluntary participation, diversion of tax revenues from the public pension system to private fund and relatively 'high-powered' incentives"[4]. In structural details, the integral elements of the system, which has not (in

[1] Anu Toots, 'Effect of Estonian Social Security Reform on Old-Age Poverty: achievements and problems', 2000 as cited in Raudla and Staehr, p. 69.
[2] Raudla and Staehr, p. 64.
[3] 'Estonia: Review of the private pensions systems', pp. 9-10.
[4] Raudla and Staehr, p. 65.

principle) substantially changed to date, were as follows. The **first pillar** was represented by a 'state pension' that would be financed in the usual way – via PAYG way of 'feeding' the segment with the funds. As noted, the first pillar-associated payout would be linked with the person's "work and earnings history"[1]. The idea was/is simple – the "state pension should guarantee an income that covers minimum living expenses", and it was/is "based on redistribution – current workers cover the pensions of future pensioners with their social tax payments"[2]. Objectively, as argued by *Swedbank*, since the population of Estonia is aging, "the number of pensioners is increasing, therefore the pensioners' own contribution to their future savings is becoming increasingly important"[3], and the prospective pensioners' involvement into the subsequent pillars is appearing to be crucial for the ultimate success of reaching a financially secured retirement.

The **second pillar** is "a fully funded defined-contribution pension", where "[c]ontributions based on the individual's earnings are assigned to his or her pension account, administered by private funds" and "[p]articipation is compulsory for persons born in 1983 or later, but voluntary for older persons"[4]. In principle, the second pillar is depended on a person's income. *SEB* specifies that, "[u]pon joining the second pillar, 2% of […] gross wages are transferred to [the] personal pension account each month" with the state adding another 4% to this being worked out of the social tax paid on [the person's] wages"[5]. Evidently, the higher earnings the prospective

[1] Raudla and Staehr, p. 64.
[2] 'Estonian pension system' in *SEB*. Available from [https://www.seb.ee/eng/pension/estonian-pension-system].
[3] 'My pension assets' in *Swedbank.* Available from [https://www.swedbank.ee/private/pensions/my/pensionAssets?language=ENG].
[4] Raudla and Staehr, pp. 64-65.
[5] 'Estonian pension system'.

pensioner has, the bigger the actual pension will be prepared for him when the time comes. Swedbank gives an estimate that the first and second pillars combined will "account for 40% of [the person's] pre-retirement income"[1]. *OECD* makes a call that a personality who has 40 years of service should expect the net benefit-salary ratio to be estimated of about 15-20%
from the second pillar[2].

Finally, the **third pillar** would consist of "additional voluntary retirement savings encouraged by preferential tax treatment"[3]. It allows everybody to make any supplementary contributions towards their retirement fund. The idea, as underlined by *SEB*, "the pension should make up approximately 65% of the pre-pension income, so that the accustomed standard of living could be preserved"[4]. Interestingly enough, as *Swedbank* states, the third pillar "is the only option for long-term saving that the state supports with a tax rebate", meaning that "[i]ncome tax will be refunded from third pillar pension contributions that are up to 15% of your gross income but not more than EUR 6,000 per calendar year"[5].

Everything was relatively stable until 2019, when the second cabinet of Jüri Ratas was formed, and its coalitional agreement had a call on reforming the country's second pillar pension system. The story of making this happen was outlined in a few briefings for 2019 and 2020. Experiencing an extraordinary twist, the bill on the second pillar's 'refurbishing' ended up

[1] 'My pension assets'.
[2] 'Estonia: Review of the private pensions systems', p. 18.
[3] Raudla and Staehr, p. 65.
[4] 'Estonian pension system' in SEB. Available from [https://www.seb.ee/eng/pension/estonian-pension-system].
[5] 'Why contribute to the 3rd pillar?' in *Swedbank*. Available from [https://www.swedbank.ee/private/pensions/pillar3/description].

‘visiting’ even the Supreme Court, when President Kersti Kaljulaid “twice refused to give her assent, on the grounds the changes were unconstitutional”[1]. However, the country’s highest-level judicial body did not find any legal discrepancies in the document, constitutional norms wise, and the bill became an integral part of Estonia’s legislation. What is that all about?

The 2021 Estonia pension reform makes the process of fundraising in the second pillar to be entirely voluntary. As reported, the law provided for an opportunity that an individual can withdraw her/his accumulated savings from the second pillar before retirement age; in a significant addition, there is an option for the same person to re-join the scheme after 10 years[2]. Those who are happy with the current status quo in terms of their contributions to the second pillar do not need to be bothered – for them, ‘business and usual’ will be the main slogan. It is also provided that “[n]ext to pension funds, there will come a pension investment account, where [a person] can invest second-pillar money [herself/himself] [3]. Naturally, a withdrawal before retirement is subjected to 20% income tax[4], and, since the implemented reform dramatically liberalised the social ‘treatment’ of the second pillar, Pensionikeskus notes that a “[g]reater freedom also means greater responsibility for securing an adequate income for retirement in the future”[5]. There was a report issued that, in the period from January until March 2021,

[1] Gail Moss, ‘Controversial Estonian pension reforms cross the finishing line’ in *IPE*, 29 October 2020. Available from [https://www.ipe.com/news/controversial-estonian-pension-reforms-cross-the-finishing-line/10048673.article].
[2] Moss.
[3] ‘Pension Reform 2021’ in *Pensionikeskus*. Available from [https://www.pensionikeskus.ee/en/pension-reform-2021/].
[4] Moss.
[5] ‘Pension Reform 2021’.

152,179 valid applications were submitted for the second pillar's withdrawals, forecasting that about EUR 1.29 billion will be taken out by the population (or nearly 25% of the second pillar-associated fund as it was standing "on the eve of the law change allowing withdrawal")[1].

Starting from 1 January 2017, the pensionable age has been gradually increasing to reach 65 years of age by 2026, and the system has an old-age pension age correlated with the year of birth[2]. The latest 'shake-up' in Estonia's pensions system made a range of necessary adjustments to the following range of laws, which frame the process up in the most comprehensive and legally solid way: Funded Pensions Act, Estonian Central Register of Securities Act, Guarantee Fund Act, Investment Funds Act, Law of Succession Act, Income Tax Act, Social Tax Act, and Old-Age Pensions under Favourable Conditions Act[3]. In general, the 'sharing and caring' for Estonia is going in a relatively smooth way. The impact of the 2021 pensions reform will be seen closer to the end of 2022. The market will need to see where the money from the second pillar will be placed. Time will show.

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[1] 'Second pillar withdrawals slow greatly, third pillar applications rocket' in *ERR*, 13 May 2021. Available from [https://news.err.ee/1608211231/second-pillar-withdrawals-slow-greatly-third-pillar-applications-rocket].

[2] 'Pension, types of pensions and benefits' in *Social Insurance Board*. Available from [https://sotsiaalkindlustusamet.ee/en/pension-benefits/pension-types-pensions-and-benefits#Old-Age%20Pension].

[3] 'Legal acts' in *Pensionikeskus*. Available from [https://www.pensionikeskus.ee/en/pension-system/estonian-pension-system-overview/legal-acts/].

The Pension System in Hungary

Csaba Moldicz

Better health, longer-living societies are the achievements of modernization and of the technological progress that has taken place over the last five decades, but the success itself created the question of how to sustain the pension systems that were created to deal with the health care and retirement issues of much younger societies. In those societies, the ratio of working to non-working people did not place such a financial burden on the younger classes, while we must admit that older people can generally work longer in many cases because of their better health. The question of how to create a system that is geared to the long term arises, therefore it is more difficult to adapt to a new environment can respond to the challenges ahead.

Reform in the Hungarian pension system since 1990 – an introduction

The history of the Hungarian pension system covers three periods. The first lasted from 1990 to 1997, when reforms aimed at adapting the pension system to the new political system and market economy conditions. During this period, the Hungarian economy was marked by mass unemployment and 1.2 million jobs were lost. The financial basis of the pension system was undermined in this way, as the pension payments of these 1.2 million people were missing from the system. In addition, mass unemployment was partially managed through early retirement and disability pensions. As a result of these policies, pension system expenditures increased significantly and accounted for more than 10 percent of the declining GDP.

The next period was from 1998 to 2010, when private pension funds were created and added to the already existing system. The reform was originally initiated by the State Reform Commission in 1994, but the original proposal was significantly reformulated when the Ministry of Finance implemented the reform in 1997. The introduction of the private pension funds was based on ideas from the IMF and the World Bank. They argued that the participation of foreign banks and insurance companies in countries with capital shortages would have a positive impact on investments, boost the economy and indirectly create jobs. The social liberal government in Hungary opted for the Argentine model, which meant partial privatization of the pension system. Membership in the newly established private pension funds was mandatory for new workers, while those already in the system were free to choose whether they would take up membership. Social contributions were partially diverted to the private pension funds with about 31 percent of all social contributions going to the privatized pension system. This also means that the public pension system dominated the system despite privatization. When the proposal was implemented, the reform was heavily criticized by the opposition, and Fidesz argued that if the new pension system were to be implemented, international capital would gain a foothold in Hungary.

The third period of the Hungarian pension system began in 2011, when private pension funds were nationalized, and the possibility of early retirement and disability pensions was reduced or eliminated. As a result of the reform, the pension system again consists of two parts: the public pension fund and the voluntary private pension funds.

The present state of the Hungarian pension system

The drastic steps leading to a major overhaul and redesign of pension system can be explained by macroeconomic factors. We must not forget that the Hungarian economy had to be bailed out by the IMF and European Commission after the collapse of Lehman Brothers in 2008. The decline in GDP and the subsequent financial crisis led to the collapse of budget revenues, which directly caused a crisis in the pension system. The diversion of private pension funds to public pension funds was initially considered temporary, but after fourteen months, the government allowed people to voluntarily pay back into the public private funds, and about 97 percent of people took advantage of this option. The diverted assets accounted for 10 percent of Hungary's GDP.

Table 1. The Hungarian Pension System after 2011		
Pillar	Responsible authorities	Financing
0. Minimum pension and allowance for elderly people	Pension insurance fund and local authorities	Mandatory social contributions and taxes
1. Mandatory pension	Pension insurance fund	Mandatory employees' and employers' social contributions
2. Voluntary pension	Private insurance funds	Private savings
Source: Szikra (2017): A magyar nyugdíjrendszer 2011 óta		

Basically, there are three main institutions that administer and maintain the Hungarian pension system:

— the Pension Insurance Fund is the fund through which the financial processes of the pension system take place.

— the General Directorate of Pension Insurance acts as the central budgetary authority, which is part of the Ministry Human Capacities.

Pension Insurance Control Commission controls the efficient use of pension funds.

Challenges

The Hungarian society is an aging society as many other European countries are. In 2020, the old-age dependency ratio was 30.3. The indicator shows the ratio of elderly people (over 65 years old) compared to the population between 15 and 64 years old. In 2015, this indicator was 22.7. The difference between the two years shows the need for a reaction and a reform of the pension system. The sustainable change would be to increase the number of newborn children, which is a very clear goal of the Fidesz-KDNP government. Changing demographics are difficult to achieve and even if they are successful, it will take many years before this policy can lead to a significant improvement in the financing of the pension system. The Hungarian ratio is below the EU average and is the second lowest among the Visegrad countries.

The aging process can be easily represented by the aging index, which shows the ratio of elderly people (over 65 years old) compared to the population under 15 years old. This indicator is less useful for the analysis of the pension system, but it shows the aging process of the Hungarian society. The indicator was 139.6 in 2020, while the index was much lower in 2005 (99.9). When it comes to the aging index, it shows significant differences between regions, while the old-age dependency ratio mentioned above does not. In Budapest, the aging index was 156.8, while the same index in Pest County was 103.9.

Table 2. Dependency ratio and aging index in Hungary between 2005 and 2020

	2005	2010	2015	2020
Old-age dependency ratio	22.7	24.2	26.5	30.3
Aging index	99.9	112.6	123.6	136.6

Source: Hungarian Central Statistical Office database

As a result of these processes, we can claim that the next reform of the Hungarian pension system seems to be inevitable. After the summary of the prevailing tendencies, the following steps can be done in theory:

— The significant increase of pension contributions. The level of contributions is not low, and we should add that the low taxation of Hungarian companies is one of the main competitive advantages of the Hungarian economy, so this step is highly unlikely. It would stifle Hungarian companies and have a negative impact on foreign investments.

- The retirement age can be increased. Although this step would be highly unpopular amongst Hungarian citizens, we cannot rule out this possibility due to European and global trends.
- A reduction in pension payments would also be negatively received by the public and would have a negative impact on the life quality of pensioners.

Table 2. Old-age dependency ratio (2019, %)	
EU-27	31.4
Belgium	29.5
Bulgaria	33.2
Czechia	30.4
Denmark	30.6
Germany	33.2
Estonia	31.0
Ireland	21.6
Greece	34.6
Spain	29.5
France	32.5
Croatia	31.6
Italy	35.7
Cyprus	23.8

Latvia	31.7
Lithuania	30.4
Luxembourg	20.7
Hungary	*29.3*
Malta	27.6
Netherlands	29.5
Austria	28.2
Poland	26.4
Portugal	33.9
Romania	28.1
Slovenia	30.5
Slovakia	23.5
Finland	35.1
Sweden	31.9
Source: Eurostat	

Strengthening voluntary savings and supporting demographic trends seem to be the steps preferred by the Hungarian government and these steps fit better into the development strategy of the Hungarian economy, which basically puts a strong emphasis on increasing self-sufficiency in every economic sector. This also explains the strong anti-migration stance of the Hungarian government, which does not want to solve Hungary's demographic problems by increasing the influx of workers into the country, which would alleviate the problems in the short term, but would completely change the demographic trends of the country in the long term.

Summary

As we have seen in the analysis, the Hungarian pension system underwent two significant changes in the last three decades, the 1997 and 2010 reforms, which took the pension system in two different directions. The first was a neoliberal attempt to partially privatize a public task, namely the care of the elderly. As mentioned above, the reform was inspired by the plans and proposals of the IMF and the World Bank. Partial privatization might have served the wealthy and the state of the public budget better, but it would have left the less fortunate strata of Hungarian society in the lurch. It is clear that the return to a fully public pension system solved most of these problems and led the Hungarian government to look for other alternatives.

Pension System in Latvia

Nina Linde

Summary: The recovery of Latvian independence in 1991 raised a big question regarding the sustainable pension system in the country. Until 1995 attempts to build the system were not successful but later with the help of the World Bank Latvia has built the pension system, which still functions. It took six years to implement the concept in reality. Today Latvia has a three-level pension system, where the first one is the state compulsory scheme of non-refined pensions, the second one is the state scheme of funded pensions and the third one is the private voluntary pension scheme. The biggest challenge for the system is ageing Latvian society and there is no assurance that this system will be able to survive under these circumstances.

Introduction

Latvia is one of the first countries in the post-Soviet area, which, following the collapse of the Soviet Union, was supported by the World Bank to make the reform of the pension system. Since 2001, the three-level pension system is functioning in Latvia and shows considerably good results so that citizens have a clear understanding that their pension can provide them with a quality life in their retirement. However, there is one big concern that currently cannot be solved and it is the ageing society. So, it is very difficult to forecast if this system can provide future generations with what they earned.

Reform process of pension system since 1990

In 1991, after the recovery of the Latvian independence and since that time had to think about the new pension system. One of the main tasks was to establish a financially sustainable system, as far as possible preventing the population's rapid ageing risks, as well as creating favourable incentives for social insurance subject to social contributions. The transformation of the pension system was started in 1991 as it was clear that the Soviet pension system was unable to exist in the market economy. It was designed for many incentives for different groups, though it lacked financial coverage. In 1991, the Parliament adopted the Law on "State Pensions", but the principles of pension costs incorporated were too generous and financially it was impossible to implement them. The 1993 Law "On State Pensions Calculation Procedures" turned out to be unsuccessful, as the main source of pension costs was the state budget (which has been severely limited in Latvia) without the involvement of workers. Given the rapid fall in the birth rate, as well as the fact that demographic trends were generally negative, it became clear that the state budget alone, in the long run, will not be able to provide pensions. Therefore, a system reform was needed. The pension system that functions in Latvia today was introduced in 2001 and consists of three different levels. One of the most important points to consider was the ageing population in the country and further explained how the updated pension system solves this issue.

Since July 2001, there are 3-level pension systems in Latvia:

- 1st pension level (state compulsory scheme of non-refined pensions);
- 2nd pension level (state scheme of funded pensions);
- 3rd pension level (private voluntary pension scheme).[1]

In the 1st level of the pension system, everyone who commits social insurance contributions participate. Payments are carried out by current pensioners of the contributions made, as well as on the personal account of everyone who makes contributions, registers pension information. Before

[1] Manapensija.lv. (2021). Pensiju sistēma. Available at: https://www.manapensija.lv/lv/pensiju-sistema/pensiju-sistema/.

making an accrual of pension, retirement capital is recalculated - the amount of pension is recalculated in accordance with regulatory acts.

A part of social contributions is sent to the 2nd pension level - or on the cumulative pension scheme. Then the funds are sent to the investment plan chosen by the person, where the managing pension plan specialist invests them in financial markets. Investments in financial markets allow not only to preserve the accumulated pension capital, but also increase its value.

Additionally, it is possible to make contributions to the 3rd pension level - a private voluntary pension scheme. A future pensioner can make contributions to one of the private pension funds. As in the 2nd pension level, the managing specialist makes the investment of these funds in the financial markets. Every person can receive this pension starting from 55 years old - until the retirement age is reached.

The status quo and reform orientation of the pension system

The pension reform, which leads to the current pension system, started in 1995 in cooperation with the World Bank. The main principle of the pension system: the larger the present social contributions; the larger the pension later. The simultaneous existence of all three pension levels ensures the stability of the pension system, since it allows to align possible demographic or financial risks at each level.

The main objectives during the creation of the new pension system were:

- To create three levels of the pension system, which would allow the country and each individual to have a respectable level of welfare after retiring;
- To create a secure state pension system where the amount of the pension depends on the volume of social security contributions;
- To establish an efficiently administered financing system;

- To increase the retirement age, thus ensuring the reduction in the numerical ratio of workers and pensioners, and reducing the load of the social insurance system;
- To stimulate the economic development of the country by providing opportunities to invest in the national economy, thus developing the financial and capital market.[1]

In 2014, a gradual increase in the retirement age from 62 to 65 years of age for both men and women was initiated, i.e., for 3 months each year, by 2025 the age of 65 will be reached. The decision to increase retirement age was based on the ageing population tendency as well as on the overall growth of life expectancy.

Challenges and development trend of pension system

In 2018 and 2019 there have been reforms that can have a positive impact on the profitability of pension funds.[2] Regarding the funded pension investments since 2018, limits were raised, allowing active funds to invest up to 75% of the assets of the Fund (against 50% previously), which can potentially provide a higher return on investment in the long term. In previous years, the reform was carried out concerning the funded pension fund charges, which together with active competition from the administration of the cheapest index funds, contributed to a significant reduction in commissions, which in turn has a positive impact on the net profitability.

The OECD data shows that in relation to GDP, at the end of 2019, Latvian pension savings in all pension products (16.7%) exceeded Lithuanian ones

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[1] Likumi.lv. (1997). Par valsts sociālo apdrošināšanu. Available at: https://likumi.lv/doc.php?id=45466

[2] Likumi.lv. (2021). Par Finanšu sektora attīstības plānu 2021.-2023. gadam. Available at: https://likumi.lv/ta/id/321834-par-finansu-sektora-attistibas-planu-2021-2023-gadam

(8.3%), but slightly lagging behind Estonia (18.5%).[1] At the same time, OECD national total pension fund assets amounting to 92% of the GDP. It should be noted that the growth rate of assets in all the Baltic States is faster than the average OECD growth. Most of the pension funds in Latvia constitute state-funded pension plans at the end of December 2020 already reached EUR 5.08 billion. In contrast, according to the Financial and Capital Market Commission, private pension funds reached EUR 566 million in the third quarter of 2020. OECD statistics show that the average pension funds (both the second and third levels) real operating efficiency during the longest year was low and in 15-year-incision even negative, and is among the lower-level countries of the OECD. However, the efficiency of long-term funds is important for the next 20, 30 or 40 years, since this will be a defining factor in the future regarding the number and amount of pensions.

According to most demographic projections, the number of Latvian people in the coming decades will continue to decline. That is the main challenge for the current Latvian pension system. The pension system, where the contributions made by workers receive existing retirees are suitable for countries where the number of citizens increases or is relatively stable. However, Latvia has clearly observed signs of an ageing population. Since the number of workers decreases and the number of people achieved retirement age increases, the proportion of workers who need to be facilitated by pension costs are decreasing. As a result, social contributions will either be raised or pensions reduced.

Conclusion

The evolution of the pension system in Latvia has led to a three-level system that allows people to have a wealthy retirement. Every Latvian resident can see what are his or her pension savings at any point in the life. Overall, this approach looks sustainable and motivate making bigger social

[1] OECD. (2021). Global pension statistics. Available at: http://www.oecd.org/daf/fin/private-pensions/globalpensionstatistics.htm

contributions to have better conditions in old age. However, this model would perfectly work if there is no ageing society tendency, which definitely exists in Latvia. So, the question regarding the viability of this system is still open and need to be addressed by the government.

Lithuania's pension system amidst challenges and opportunities

Linas Eriksonas

The increasing inflationary pressures on the economy mounting due to the COVID-induced public expenditures and the low-interest rates have put the most vulnerable members of society, especially the pensioners, in dire straits. The need to raise the pensions have become a must for the government as it approaches the end of the first year in office. In July, facing the repeated calls by the pensioners' associations and heeding to the recommendations of the EC and OECD experts, the government announced a new pension reform that it expects would allow increasing the level of the basic pensions as the economy grows.

Below is a brief overview of the current situation that the country faces as it tries to address relative poverty among the senior citizens of society in a rapidly ageing society - navigating between demographic challenges and the opportunities for a more market-driven approach to ensure a more satisfactory livelihood for pensioners. It considers the means and policy measures that aim to create more value out of social security.

Lithuania's society has undergone a tremendous demographic change during the last two decades. Since the access to the European Union, which opened the labour market to the Lithuanian nationals, almost a third of the working population left the country. During the last two decades, the population has plummeted from 3,5 million inhabitants to the old-time low of 2,8 million, and the numbers are further on the decrease. During the period 1990 – 2020, the labour market lost one million inhabitants who emigrated for work or because of other socio-economic reasons, while only 372 thousand immigrants came to the country to replace them.

One can argue that at the time, mass emigration has decreased the level of long-term unemployment and even brought some indirect benefits as experienced, for example, through a burgeoning remittance economy. In 2010, at the height of emigration, the personal remittances reached their peak and amounted to 4,52 per cent of GDP. However, the medium and long-term impact of out-migration on the economy was negative. The economic migrants and their families have constituted the most productive parts of Lithuanian society, people in their 20s and 30s. Their loss to communities added additional pressure on the demographic balance and, in turn, on the pension system. The country lacks enough workforce to earn adequate pensions required for the retirees, who constitute about 35 per cent of the population.

Hence, the retirement age increase for a long time became the only viable, if not a very sustainable, solution. In the early 1990s, Lithuania inherited a Soviet-style pension system characterised by generous early retirement provisions, privileges for certain occupational groups, and a weak link between contributions and benefits. When the reform process began in 1995, the retirement age was gradually increased to 62.5 years for men and 60 years for women (reached in 2006).

In 2011 the parliament agreed to prolong the pension age from 60 years for women and 62 years for both men and women to 65 years in 2026 to be raised by four months annually for women and by two months – for men. Accordingly, the pension age in 2021 for women was set at 63 years and four months and for men – 64 years and two months. The main argument for extending the pension age was the need to decrease the number of pensioners amidst the rapidly dwindling working force due to out-migration and mortality due to the worsening public health. The politicians further argued that Lithuania has to increase the pension age to be compatible with the advanced EU Member States, where the pension age on average was about 65 years.

However, after soon it became apparent that prolonging the retirement wage alone would not suffice to ensure decent livelihoods for senior citizens. The savings for pensions have started to be seen as investment vehicles that could create additional economic value, catering to the needs of the financial sector and the citizens concerned with their future pensions in the uncertain times. A three-pillar pension system created in 2004 has slowly taken off during the time of the booming economy before the financial crisis of 2008-2009. The system has survived the crisis and, following an additional reform in 2019, created additional possibilities for pension funds to participate in the financial markets.

The first pillar consists of state social insurance, where the employers and the employees pay contributions to Sodra (The State Social Insurance Fund Board under the Ministry of Social Security and Labour) from paid wages. A person becomes entitled to an old-age pension when one has accumulated the required number of working years. The minimum period of pensionable service in Lithuania is 15 years, and the minimum is 32 years (in 2021), but it will reach 35 years in 2027. To accumulate years of pensionable service, one must contribute at least 12 minimum monthly salaries per year.

In 2021 the basic salary in Lithuania has amounted to 440 EUR but to qualify for this minimum pension, one needs to meet the minimum number of years spent in employment. Yet, the number of working years required for obtaining a basic pension has constantly been increasing. To put into perspective, in 1994 the minimum number of years was only 25, in 2021 – 32 and, as society rapidly ages on, in 2027, the minimum number of working years is due to reach 35.

The second pillar is called pension accumulation, where part of the contributions to pension funds are paid from the state budget but the employee also contributes to the accumulation. Since 2019, the second pillar of pensions in Lithuania has been reformed as follows. An employee contributes 3 per cent of the so-called salary "on paper" (a gross salary), with a state incentive of 1.5 per cent of the country's average wage in the previous year. Contrary to most other CEE countries, Lithuania's second pillar is not mandatory. It is made up of individual accounts, but employees are free to choose whether to join or not. Acceptance of second pillar pensions has been strong and participation has increased rapidly. The second pillar funds have grown to 5 billion euros with the main size of the funds (1,2 billions) invested in the funds of the age group 40-46 years.

During the last few years Lithuania's pension funds have performed remarkably well. In 2020 the annual yield of Lithuania's pension funds (4,9 per cent) was listed among the top 10 performing OECD countries, according to the pension funds. During the first-half of this year the Lithuanian pension funds have doubled on their performance with an average yield of 11,4 per cent for January-June, while within the funds for the age group 33-39 reached a record-high yield of 14,13 per cent. The second quarter witnessed the yield of 4,7 per cent.

The third pillar of pension saving is entirely private, where the working person pays the amount and frequency of contributions one wants to make after concluding a contract with the pension company. The third pillar is still underdeveloped and consists of voluntary pension funds or life insurance products. Only 200 million euros have been invested in these funds. The average return on investment for the first half of the year in 2021 was 8,2 per cent.

However, the pension funds cater to the future generation of the pensioners, while the current one faces the difficulty of meeting the ends due to rising inflation that affects the price level of products and services. Thus, the government decided to increase the basic pension level by abandoning the principle, according to which the basic pension depended on the number of years spent in employment. Instead, a new principle is being adopted. According to the planned provisions, the pensions would depend on the contributions paid while in employment. On 26 August, Minister of Social Security and Labour Monika Navickienė announced by the end of 2022, a new way of defining the amount of the basic pension could reduce poverty by 25 per cent.

The increase of pensions and the pension model that the government plans to present to the Parliament during the autumn session are not the only measures the government is taking to improve the quality of life for the elderly. There is already a single person's allowance, which will reach its first recipients in November. From January, this benefit will increase and will reach almost half a million people. The aim is to achieve by 2024 that the pension (including the basic pension and the one in the second-pillar pension funds) could amount to about 50 per cent of the average salary in the country. To compare, the EU average is 60 per cent.

However, achieving this goal can become an increasingly fleeting target as society continues to age due to the negative demographic trends that have little prospect to revert unless the migration policy opens the borders to the organized immigration of skilled workforce. At the beginning of the year, the European Commission published the Green Paper on Aging, which outlines the principles for the respective directive to be adopted in few years. The document specifically mentioned that "to keep the national old-age dependency ratio constant in 2040 relative to 2020", projections suggest that a number of the EU Member States would have to extend working life. The EC has singled out Lithuania (along with Luxembourg), where working life would have to be extended to the envisioned maximum, that is 72 years, while, for example, Malta, Hungary and Sweden would have to extend working life to 68 years. However, their working life until 72 years might not be feasible as the existing average age for men in Lithuania is shorter than the envisioned working age by half a year. Hence, the pension system planners need to consider whether there will be time for pensioners to enjoy their pensions, and start creating the pre-conditions for the longer lives for citizens.

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Pension System in Montenegro

Vojin Golubovic

The existing pension system in Montenegro was exposed to numerous challenges since 1990s, i.e. since the beginning of the transition period. Among them, funding challenges were dominant due to the huge rate of unemployment and undeclared work, falling fertility rates, an ageing population, as well as the slow overall growth of the economy. Negative demographic trends and decreased employment are just some of many reasons that have spurred the implementation of pension reform. However, some challenges still persist, which impose the need for further reforms.

Introduction

The pension system in Montenegro is so-called PAYG (pay-as-you-go), or system of intergenerational solidarity, i.e. the system of current financing. This system was inherited from the SFRY[1] which faced serious crisis at the end of 1980s. Apart from challenges that PAYG systems all over the world started to face, during the 1990s, Montenegro has been faced with some additional challenges, including economic sanctions, recession, privatization and economic restructuring. All had a negative impact on the then pension system and pointed to the need to reform it.

Reform process of pension system since 1990

The reform of the pension system in Montenegro was initiated due to a number of problems that called into question its sustainability and hindered

[1] Socialist Federal Republic of Yugoslavia.

its functioning. Having in mind that PAYG system assumes that the contributions made by current workers are used to pay for current pensions, the most important reasons for reform were demographic developments in the country. The demographic reasons are related to the ageing of the population, which has resulted in an increased burden on the guaranteed pension funds of the state. The demographic picture of Montenegro has significantly changed due to the war, which caused further increases in the number of pensioners (or pension system beneficiaries) in relation to the number of employees paying pension contributions (or pension system contributors). During 1990s and at the beginning of 2000s, the dependency ratio (or number of the employed persons paying contributions in relation to the number of pensioners) has constantly fallen.

The result was an increased gap between the inflow and outflow of money in the state pension fund. The reasons for reforming the PAYG system are obvious. There were no guarantees that in the future there would be sufficient funds to sustain pension payments, or even to raise the standard of living of the pensioners. Like other PAYG systems in the region, during that period the Montenegrin system featured low ages for retirement (60 for men and 55 for women), a full oldage pension entitlement based on 35 and 30 years of service for men and women respectively, and various supplements for years of service, irrespective of contributions actually paid[1]. Also, contribution rates were high during previous years, and this is one of reasons for the reform of the system. Contribution rates amounted to 12.3% of the gross wage in 1980, and this rate had an increasing trend and achieved 24% of the gross wage in 1994. This rate was valid until first reform measures in 2003.

In addition, early retirement and less strict rules for disability pensions have been used as tools for solving redundancy problems in the economy. On the other hand, the Government has tolerated undeclared work as a coping mechanism in Montenegrin households. All this has led to an increased

[1] This include additional payments for injury, hard work conditions, special privileged occupations, doubling the service period for veterans, etc.

number of pensioners and a decreased number of contributors, since the largest part of job creation has been in the informal economy.

The initial intention was to implement pension reform in Montenegro through three pillars of pension insurance. The first step in implementation was reform of the current PAYGO pension system (first pillar). To date, a reform of the pension system included tweaks in the mandatory pension insurance. Specifically, this involved a reform of the PAYG system in 2003 by a drafting of the new Law on Pension and Disability Insurance[1]. The law began to be implemented on January 1st, 2004. It does not change the current status of pensioners, but it postulates a better and more secure material position for all pensioners and aims for better performances of the labour market, as well as a better link between salaries that employees receive and pensions that they will receive in the future. Reform measures of Law were related to gradual increase of age limit for pension to 65 years for men and 60 years for women; gradual increase in the number of years that are included in pension calculations; change of pension formula by the appliance of a system of personal points;pension adjustment with a rate of 50% of growth rate of wages and 50% of CPI inflation; Contribution rate was decreased gradually in the following years to 20.5%[2].

These initial reform measures resulted in some positive developments in short term. However, further reform measures were needed but the period until 2020 was characterized by some minor changes in the legislation and a proposed gradual increase of pensionable age[3]. Also, the previous adjustment of pensions according to the so-called Swiss formula is changed. Instead of the previous formula, according to which pensions were indexed to 50% of the consumer price change and 50% of the wage change, pensions have started to be adjusted according to a new formula which implies a growth of pensions which is the sum of 75% of the growth rate of CPI and 25% of the growth rate of wages.

[1] "Official Gazette of the Republic of Montenegro", No. 54/03
[2] Currently, the employee pays 15%, while employer pays 5.5%.
[3] The pensionable age was set to be 67 by 2040.

The status quo and reform orientation of pension system

The current situation is such that reforms of the PAYG system address, or to some extent mitigate, the negative effects of demographic and economic factors. However, despite the reform measures described above, the current situation is unsustainable in the long run. The current reform orientation does not take into account any changes other than changes under the first pillar of pension insurance (changes of PAYG system).

In mid 2020, after two year debate and negotioation between social partners, the new law amending the 2003 Law on Pension and Disability Insurance was drafted and adopted. The changes proposed by government were initiated with the aim to discourage early retirement. The main change was related to the change of age limit for pension which is currently 66 for men and 61 and 9 months for women. According to the proposed change, new pensionable age should be 66 for men, and 64 for women which will be reached in 2028. Also, significant change is related to the pension's level adjustment and the pension formula, because "rotating formula" is introduced: pensions are indexed to 75% of the parameter with the highest rate of change and 25% of the parameter with the lowest rate of change (wage change and CPI). However, if the application of this rotating formula shows that the level of pensions should be reduced (due to negative growth rates of any of the parameters), it will not be applied in that accounting period. Also, the pensions are not calculated on the basis of the entire contribution period (this was the case prior the 2020 reform), because one quarter of the working period when worker registered the lowest wage is excluded from the calculation.

According to the statistics of Pension and Disability Insurance Fund (PIO Fund[1]), the average pension in Montenegro in April 2021 amounted 293,25

[1] According to the Law on Pension and Disability Insurance, the funds raised for pension insurance are managed by the Pension and Disability Insurance Fund (PIO Fund).

EUR, while the minimum pension amounts 145 EUR and is received by 16 thousands out of 129 thousands pensioners, which is 12,4%. The minimum pension is three times lower than average wage in the country. The share of old-age pension beneficiaries in the total number of pensioners in Montenegro is almost 58% percent, disability pension beneficiaries 17% percent, and family pension beneficiaries 25%. However, the participation of old-age pensioners is increasing from year to year, while the number of disability pensions is decreasing which is the consequence of previous reform measures.

Challenges and development trend of pension system

Although a legislative framework was introduced for the third pillar (voluntary private pension savings) in 2006[1], this voluntary savings system has not taken root, and current reform directions do not place particular emphasis on any significant changes in this regard. Thus, although the original plan was a three-pillar pension system, the status quo allows for social peace with significant transfers from the state budget for the missing funds of the state pension fund.

However, challenges imposed by negative demographic trends still persist and imply further need for pension system reform. These challenges are related to the fact that despite the numerous measures the ratio between pensioners and workers is still unfavourable in Montenegro. This ratio used to be 1 pensioner to 7 workers in 1980s, but today that ratio is almost equalized. Also, certain population projections made by the national statistical office MONSTAT indicate that there will be a further increase in the share of the population older than 65 in the total population.[2]

[1] The Law on Voluntary Pension Funds was adopted ("Official Gazette of the Republic of Montenegro", No. 078/06)

[2] According to the low fertility scenario, the size of the population over the age of 65 will increase from less than 15% in 2011 to 28.4% of the total Montenegrin population in 2060.

Hence, if the pension system in Montenegro is not going to be further reformed, the burden on the state budget will increase, which may affect the need for further borrowing of the country, or reforms in tax policies that may result in tax increases. On the other side, second pillar (mandatory private pension saving) was never introduced due to high transitional costs that accompany introduction of such system.

Additionally, according to the replacement rate projection conducted by Institute for Strategic Studies and Prognoses, pension amounts will decrease over time relative to wages received by workers before retirement, which ultimately means that potential wage growth will not be accompanied by an increase in pension benefits. In addition to the ratio of the number of insured persons and pensioners, an important indicator of the financial sustainability of the pension system is the share of PIO Fund expenditures in total GDP. The growth of this share again indicates the need to find alternative ways of financing the pension system.

The Macedonian pension system: trends and challenges to sustainability

Gjorgjioska M. Adela

In spite of several reforms undertaken in the past years, the Macedonian pension system has been described as unsustainable and in need of urgent reform. Until 2008 some improvements have been noted, however there has been a continuous deterioration in the years since. The main reasons for this assessment have been the growing share of pension expenditures within the broader economy and the increase in the amount of transfers for pensions from the central budget which has contributed to the growth of the public debt. In the absence of major positive shifts in the economy, the pension system will continue draining the public finances in light of anticipated demographic challenges and the continuously rising deficit of the Pension and Disability Insurance Fund.

Reform of the pension system since 1991

In 1991 the Republic of Macedonia began establishing an independent pension and disability insurance system by setting up the Pension and Disability Insurance Fund of Macedonia (PIOM). Since 1994, the pension system in the country has been regulated by the Law on Pensions and Disability Insurance, which has undergone significant modifications and amendments in the years that followed. [1] Following the reforms implemented in 2000, in addition to PIOM (which is state-owned and managed), private pension funds have also been integrated in the pension system. As a result, the current system consists of three pillars:

[1] Pension and Disability Insurance Fund of N.Macedonia, available at, http://www.piom.com.mk/en/about-us/ accessed on 30.06.2021

Pillar 1 is known as the Statutory Pension Scheme. It consists of mandatory insurance, which is paid out to PIOM, and it is generated through the principle of generational solidarity - pay as you go (PAYG), providing earnings-related benefits based on the length of working service. Wages contributions of insurers are used to pay out the pensions of current and future pensioners. The first pillar provides part of the old-age pension, disability and survivors' pension benefits, and the minimum pension benefit. It is mandatory for all economically active people, including all employees, self-employed persons and farmers.

Pillar 2 is also known as the Statutory Funded Pension Scheme. It is also mandatory and a fully funded pension insurance scheme, which is run by (one of the two) private pension companies supervised by the state, providing benefits linked to accrued pension capital. The second pillar pays out part of the old-age pension. Since january 2003, all insurers pay part of their contributions (7%) to the private pension funds. All the others can choose whether or not they will join the Statutory Funded Pension Scheme. In 2019, the second pension pillar consisted of three pension fund management companies: Sava Pension Company, KB First Pension Company and Triglav Pension Company. As of November 30, 2019, the total number of members in the private pension companies was 507,439. Thereby, the value of the net assets in the mandatory pension funds (second pillar) amounted to Denar 74,889 billion (about EUR 1.22 billion).[1]

Pillar 3, which is also known as the Supplementary Pension Scheme, was introduced in 2007.[2] It is a voluntary and a fully funded pension insurance which includes both personal schemes (for people between 15 and 70 years

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[1] In 2019 the net assets of the private pension funds represented 10.8% of the total assets of the financial institutions in Macedonia.

[2] Radio Mof (2019). Analysis- Hundreds of millions of euros in the private pension funds - how are the insurers' money protected, published on 06.02.2019, available at https://www.radiomof.mk/analiza-stotici-milioni-evra-vo-privatnite-penziski-fondovi-kako-se-chuvaat-parite-na-osigurenicite/ accessed on 30.06.2021

of age) and occupational-based schemes. The benefits paid from the supplementary pension scheme are similar to those from the second pillar, with the only difference that voluntary pension scheme members can decide to withdraw accumulated assets from third-pillar individual accounts as a lump sum, which is not allowed in the mandatory system.[1] In 2019 there were two voluntary pension funds in the country: Sava pension plus and KB First Open Voluntary Pension Fund – Skopje. As of November 30, 2019, a total of 24,998 persons were members of the third pillar (voluntary pension funds) whose net assets amounted to Denar 1.91 billion (EUR 31.07 million).

The main rationale behind the establishment of the second and third pillar and the introduction of private funds within the pension system was the need to increase the pension funds by allowing private pension funds to invest the money of the insurers in various instruments such as stocks, mutual funds and securities.

The status quo of the pension system

There are three pension types available: old-age pension; disability pension and survivor pension. The main requirement of old-age pension is age (62 for women and 64 for men) and years of service (minimum of 15 years). The survivor pension is available to members of the family of a deceased contributor. The disability pension is available to people who have experienced an injury at work or occupational disease/disability.[2] In 2009,

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[1] Gerovska, M., M., *ESPN Thematic Report: Assessment of Pension Adequacy in the former Yugoslav Republic of Macedonia*, 2017, document prepared for the European Commission

[2] Petreski, B, Gacov, P. (2018). Sustainability of the pension system in Macedonia Comprehensive analysis and reform proposal with MK-PENS – Dynamic Microsimulation Model, Finance Think, available at https://www.financethink.mk/wp-content/uploads/2018/06/Pension-analysis-EN.pdf accessed on 30.06.2021

there were a total of 278,463 pension beneficiaries in Macedonia, and in July 2020 that number increased to 324,893. Most of the pensioners (215,450 or 66.3%) were beneficiaries of old-age pensions and the average pension was 15 412 denars.[1] Between 2010-2018, the pension contribution from gross wages was 18% (reduced from 21,2% until 2008). Announcements that contribution will drop to 17,6% failed to materialise due to the deficits in the PIOM. In 2018, the contribution rate for pension and disability insurance increased from 18% to 18.4%, and in 2019 to 18.8%.

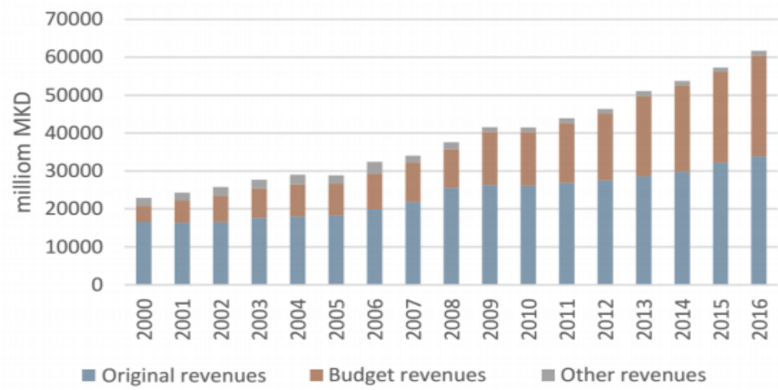
Challenges and reform orientation of the pension system

The dominant share of the revenue in the PIOM comes from wages contributions. However, a large share also comes from the budget transfers from the central fiscal budget of the country, which puts an additional strain on the budget deficit and has a negative implication on the financing of other fiscal expenditures. In 2016, 56,4% of revenues of the PIOM came from wages contributions. 43,6% came as a transfer from the central government budget. Transfers from the central budget to the Fund have grown steadily over time: in 1994, they amounted to 2% of GDP, in 2004 they reached 3% of GDP and are likely to increase to 5% by 2040.[2]

[1] Economy and Business (2020). Вториот пензиски столб чува над една милијарда евра пензиски заштеди“, Економија и бизнис, година 21, број 257/257, јануари 2020, стр. 59.

[2] Stojkov, A. (2017). „Пензионерски главоболки“, Економија и бизнис, година 19, број 233, ноември 2017, стр. 24-27.

Graph 2: PDIF's revenue structure, 2000 - 2016



Source: PDIF

There are several reasons that have been responsible for the rise. The period of neoliberal transformation (in the 1990s and 2000s) was characterised by a severe socio-economic crisis, which resulted in the constant rise in the number of retirees-pension beneficiaries. This was one of the mechanisms used to deal with the surplus labour force in the country. At the same time, the number of unemployed people in the country was on a constant rise, reducing the wages contributions to PIOM. Furthermore, the overall reduction in the trust in the institutions decreased insurers' confidence in the security of pensions and stimulated the spread of evasion of pension contributions or the declaration of lower wages in order to pay lower pension contributions. Additionally, the multiple ad-hoc pension increases in Macedonia have been noted as one of the factors undermining its fiscal consolidation (European Commission, 2016).[123] Finally, another challenge comes from the demographic changes which by 2030 will lead to people over 60 representing 41% of the population, which will practically block the pay-as-you-go system.

According to the World Bank "the reforms enacted since 2018 will stabilize the system over the near term."[4] In the list of positive steps taken they include the Law on Pension and Disability Insurance, which plans to address pension system fiscal sustainability, adequacy of multi-pillar pensions, and overpaid and underpaid contributions to the funded pillar.[5]

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[1] Similarly, the International Monetary Fund, in its annual report for 2017, argues that the increased budget deficit in recent years is also partly due to the great increase in pensions, creating the need for pension reform aimed at fiscal and pension consolidation (IMF, 2017)

[2] Petreski, B, Gacov, P. (2018). Sustainability of the pension system in Macedonia Comprehensive analysis and reform proposal with MK-PENS – Dynamic Microsimulation Model, Finance Think, available at https://www.financethink.mk/wp-content/uploads/2018/06/Pension-analysis-EN.pdf accessed on 30.06.2021

[3] The pressure for higher pensions is mainly driven by the power of retirees to impact policies, due to their increasing numbers and their importance as an electorate (Kruse, 2010)

[4] World Bank (2019). FYR Macedonia Special Focus Note: Pension Reform, available at https://documents1.worldbank.org/curated/en/895551549468307274/pdf/134426-WorldBankSpecialFocusNotePensionsNovemberFINAL.pdf accessed on 30.06.2021

[5] Moreover, they mention the pension policy measures aimed to secure fiscal sustainability and strengthen equity, which includes: (i) the price (CPI) indexation of pensions with a supplementary 25-percent wage indexation in case a real GDP grows above 4 percent per year; (ii) harmonization of accrual rates by lowering the PAYG-only accruals for post-2018 service and raising all service year accruals for the second-pillar participants; and (iii) a contribution rate increase by 0.4 percentage points in 2019 as well as 2020, World Bank (2019). FYR Macedonia Special Focus Note: Pension Reform, available at https://documents1.worldbank.org/curated/en/895551549468307274/pdf/134426-WorldBankSpecialFocusNotePensionsNovemberFINAL.pdf accessed on 30.06.2021

Conclusion

The key factors that affect the sustainability of the Macedonian pension system include: demographic changes, labour market movements as part of the broader economy, and pension adjustment to the potential of the economy. Imbalance between the amount of pensions and the potential of the economy to finance those pensions is the major factor for the unsustainability of the pension system. The deficit in the pension system in Macedonia - the difference between the original revenues and total expenditure of the Pension and Disability Insurance Fund - has a tendency to grow over time. In spite of a small slowdown in 2019 and 2020, the trend remains. This has fiscal implications in view of the large contributions to the Fund which come from the national budget. In the absence of systemic changes in the economy, any future pension reform will result in the increase of costs and the reduction of benefits for the insurers, such as the increase in the contribution rate from 18% to 22% or an increase of the retirement age-limit for old-age pension by 2 years from 62 years for women and 64 years for men to 65 and 67 years, respectively). In such a context, the long term sustainability of the pension system will depend on developments in the broader economy. Namely, the larger the labour force the larger will be the wage contributions to the pension funds. Therefore, the long-term sustainability of the pension system in the country will be largely dependent on the overall condition of the economy, which includes the condition of the workforce, the rate of employment and the emigration trends.

Rapid population ageing a challenge for the pension system

Konrad Rajca

Poland faces major challenges in reforming its pension system in the context of a very rapid population aging. People of retirement age accounted for more than 22 percent of the population in 2019[1]. According to the forecasts of the Social Insurance Institution, people over 65 years of age will constitute 1/3 of the entire population in 2050[2]. In the coming decades, Poland can be a leader in the European Union in terms of the rate of population aging. The Polish pension system consists of the third pillars - the Social Insurance Fund managed by the Social Insurance Institution (ZUS), the funded element - the Open Pension Funds (OFE) and voluntary supplementary pension insurance. The first two pillars are mandatory. The government plans to liquidate the Open Pension Funds (OFE), from where funds would be transferred to ZUS and to individual retirement accounts. The retirement age in Poland is 65 for men and 60 for women.

Introduction

In the Polish pension system, a pension is paid from the Social Insurance Fund, managed by the Social Insurance Institution (ZUS). Upon reaching the general retirement age (60 for women and 65 for men as of 2017), it is up to each individual to decide whether he or she wishes to exercise this right immediately or later due to the individual's desire to continue working. What is important is that the later you retire, the higher your pension will be. The amount of the pension depends on the sum of paid and indexed pension insurance contributions, the amount of indexed initial capital, the

[1] The Central Statistical Office https://stat.gov.pl/infografiki-widzety/infografiki/infografika-dzien-babci-i-dziadka-21-22-stycznia,23,6.htm

[2] Social Insurance Institution https://www.zus.pl/documents/10182/167561/ZUS+w+liczbach/72262321-87a3-4df1-b535-93d686bc21bc

amount of funds accumulated on the subaccount and the average life expectancy[1].

Diversity of the pension system

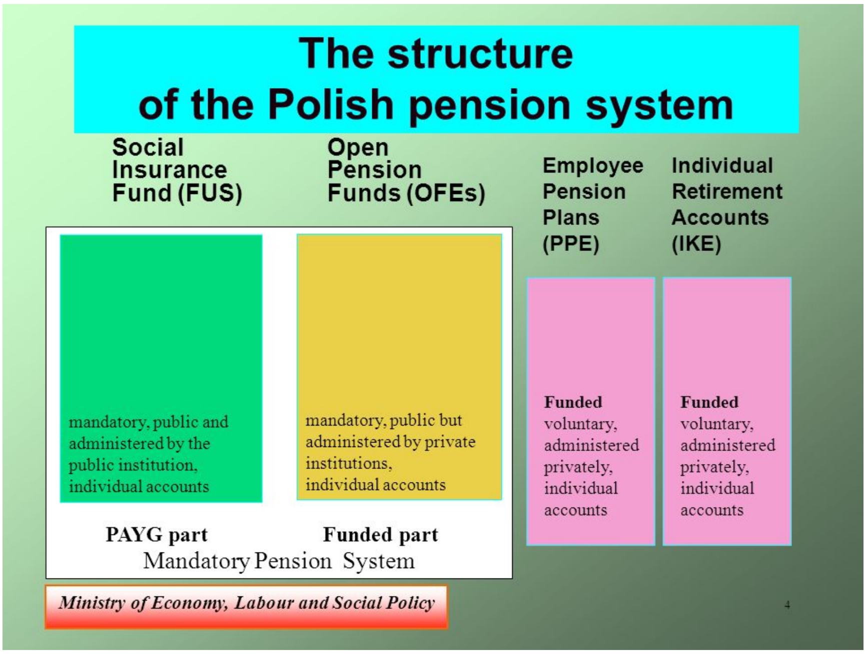
Poland has a number of separate parallel pension systems operating under different rules. Most people are covered by the system operated by the Social Insurance Institution (ZUS), but according to different rules. Persons born before 1949 and not eligible to receive mining pensions or other retirement benefits from outside the general system receive pensions according to the rules set forth in the 1999 reform of the social insurance system. According to this reform, the main criteria for receiving a pension are reaching retirement age and having a sufficiently long insurance period (seniority) consisting of contribution and non-contribution periods. The amount of the pension only indirectly depends on the amount of contributions paid in the past. The key factor in this case is to properly document the insurance seniority, which mainly consists of the length of service[2].

Pension contributions are recorded in two systems - under the pay-as-you-go system: on an individual account and sub-account kept by the Social Insurance Institution (ZUS) - obligatory, and under the funded system: on an account in the Open Pension Fund (OFE) kept by the General Pension Society (Towarzystwo Emerytalne). The value of funds in OFEs fluctuates depending on the value of the financial instruments (treasury bonds, shares) in which the funds from the contributions have been invested. There are also additional voluntary forms of pension insurance in Poland - the so-called third pillar. The programs in operation are: PPE - employee pension

[1] The Act on Pensions from the Social Insurance Fund https://isap.sejm.gov.pl/isap.nsf/DocDetails.xsp?id=WDU20210000291

[2] Social Insurance Institution's retirement calculator https://www.zus.pl/swiadczenia/emerytury/kalkulatory-emerytalne/emerytura-na-nowych-zasadach/kalkulator-emerytalny-prognozowana-emerytura

schemes, IKE - individual retirement account, IKZE - individual pension security accoun, PPK - employee capital plans.



Presentation on theme: "New Pension System in Poland - How to Classify in Accordance with SNA 93 and ESA 95”, Krzysztof Pater, Undersecretary of State Ministry of Economy, Labour. https://slideplayer.com/slide/9495657/

Occupational pension schemes

The rules described above do not apply to certain occupational groups which are covered by occupational pension schemes, such as: uniformed services, miners, teachers, railwaymen, prosecutors, judges, as well as farmers and other groups who are accounted for through the National Agricultural Social Insurance Fund (KRUS). These groups have completely different rules for calculating pensions, a lower retirement age and more favourable conversion factors for years of service, which in practice means that their employers pay lower contributions and the insured receive higher pensions or, paying very low contributions, receive lower pensions. KRUS revenues cover only a small part of the benefits it pays out, the rest being subsidized from State Treasury funds. According to many experts, the agricultural system of KRUS contributes to the growth of hidden unemployment and the shadow economy, and pension privileges for particular groups are a burden on the pension system. The situation is similar in the case of the mining industry, where pensions subsidized by the State Treasury are justified by hard working conditions and occupational risk.

Reform of the system in the 1990s

During the economic transformation after 1990, discussions about the future of the pension system raised the issue of long-term financing of retirement benefits, especially in view of the new demographic phenomenon of declining birth rates. The result of these debates was the 1998 pension reform, which introduced three pillars into the pension system (the existing Social Insurance Institution - Pillar I, Open Pension Funds - Pillar II and Pillar III - voluntary, additional forms of pension insurance).

The reform consisted in replacing the previous pay-as-you-go mechanism with a new pay-as-you-go system. General pension companies and open pension funds managed by them were created, creating the second pillar of the social security system for people in the post-working age, in which participation of most working citizens was obligatory. The possibility of voluntary additional saving for years after the end of working life was also created within the third pillar of the social security system. For this purpose, firstly, occupational pension schemes were created, and later, after several years, also the possibility of saving for future retirement within the system of individual pension[1] accounts was created.

[1] Paweł Kulpaka, Warsaw School of Economics (https://www.ue.katowice.pl/fileadmin/_migrated/content_uploads/17_P.Kulpaka_Funkcjonowanie_systemu....pdf

The Open Pension Funds (OFE), which appeared as a result of the pension reform of 1999, were supposed to increase the expected size of pensions by investing a portion of contributions in the capital market. Apart from the "traditional" pension from ZUS, Poles were to receive an "extra" pension from OFEs. In time, this was to become the main pension for Poles. However, optimistic assumptions did not withstand the clash with reality. The construction of the open pension fund, whose goal - according to its creators - was not only to finance pensions, but also to supply the financial markets, i.e. mainly the stock market and listed companies, is still controversial. According to many experts, the system contributes to an increase in the state budget deficit.

Limitation of Open Pension Funds

In 2011, the process of slow extinction of the Open Pension Funds (OFE) began. The contribution transferred to OFEs was then drastically reduced. The Social Insurance Institution (ZUS) created a new subaccount for the part of the contribution that was no longer transferred to OFEs. With this operation, the government of Prime Minister Donald Tusk wanted to reduce the deficit of the public finance sector[1]. In 2013, in view of the growing public deficit and the imminent necessity to launch OFE payments, the debate on the construction of the second pillar flared up again and the role of OFEs was significantly reduced. On April 15, 2019, Prime Minister Mateusz Morawiecki's government unveiled a plan to transfer savings from the Open Pension Funds (OFEs) to individual retirement accounts or to the Social Insurance Institution (ZUS), which is still pending. The implementation of the plan means in practice the liquidation of OFEs. Earlier, on January 1, 2019, the government adopted a law on Employee Capital Plans (PPK), which provides for the creation of a private, voluntary system of accumulating retirement savings. The program involves the state,

[1] Businessinsider.pl portal https://businessinsider.com.pl/twoje-pieniadze/reformy-emerytalne-historia-ofe-i-ppk/5z3bvjn

employers and employees. An employee - participant of PPK - may contribute to PPK from 2 to 4 percent of his salary. The employer, on the other hand, will contribute from 1.5 to 4 percent of salary.

Perspectives for the system

The decline in the female fertility rate, which began in the late 1980s and deepened dramatically in the 1990s after the onset of Poland's political and economic transformation, has drastically reduced the number of births, leading to a rapid population ageing process. The lack of simple replacement of generations will result in a decrease in the number of living Poles in the near future and a gradual shrinkage of the population. The growing demographic challenges in Poland, inevitably accompanied by significant economic processes, are forcing a reform of the pension system.[1]

In November 2020, the number of pensioners to whom ZUS pays benefits exceeded the psychological barrier of 6 million people. - This means that in 5 years the number of pensioners in the Social Insurance Institution (ZUS) has increased by 20 percent, or by 1 million people compared to the data from 2015 - says Dr. Antoni Kolek, the President of the Pension Institute. According to him, this means that the aging of society is already taking place in the Polish system, and exceeding this psychological barrier shows that there are increasingly difficult times ahead for the Polish economy. - It should be borne in mind that the increase in the state's recurrent expenditures resulting from social transfers requires obtaining more funds necessary to cover these expenditures and reduces investment opportunities or transferring funds for other public tasks, e.g., education or health care system - emphasizes Dr. Kolek. According to forecasts of the Pension

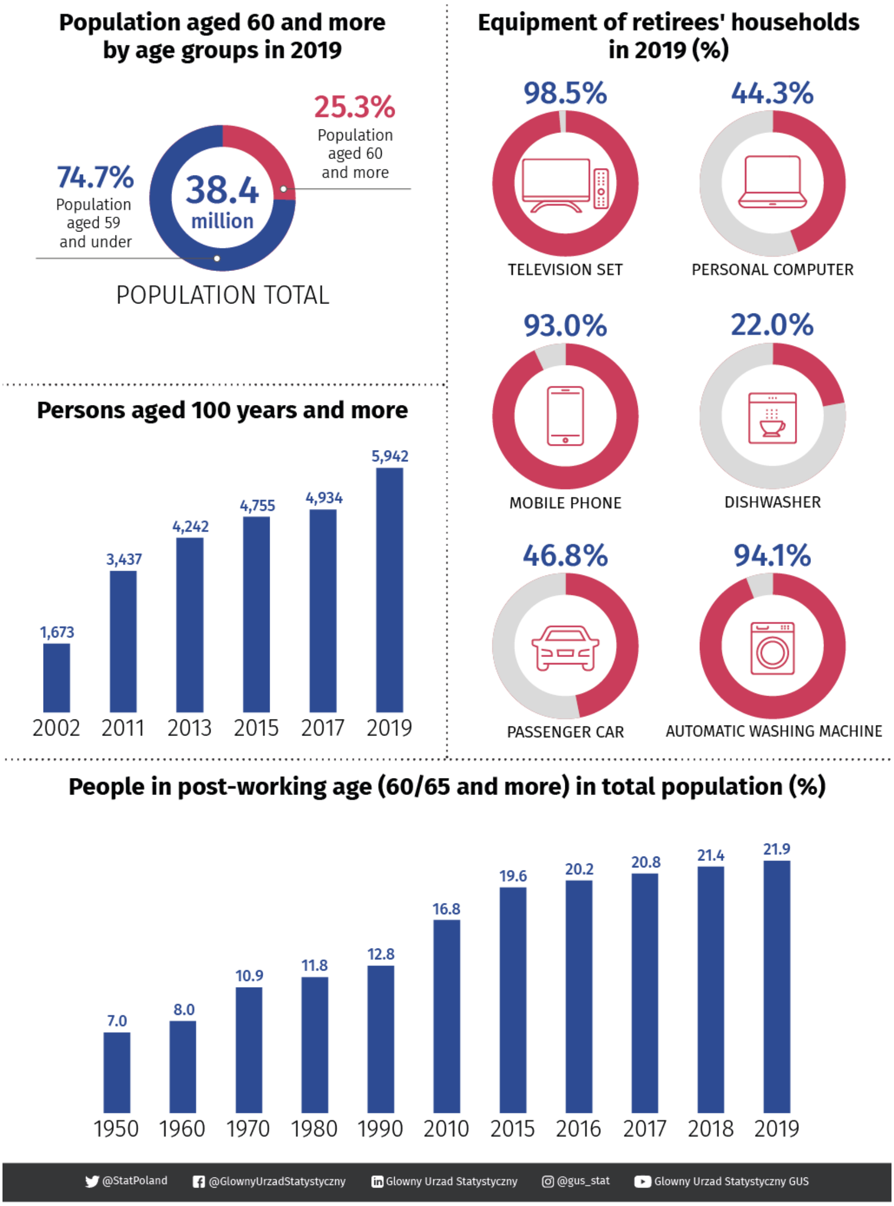
[1] Paweł Kulpaka, Warsaw School of Economics (https://www.ue.katowice.pl/fileadmin/_migrated/content_uploads/17_P.Kulpaka_Funkcjonowanie_systemu....pdf

Institute, another additional million of benefit recipients should be expected within the next 5 years [1].

In the coming decades, Poland will be a leader in the European Union in terms of the rate of population aging. "Today, our country's population is relatively young - the median age is about 40. Among EU countries, there are only four where it is lower. By 2040, however, the median age in Poland will increase by more than 10 years. In no other EU country will this increase be so large. In 2040, Poland will be among a small group of 11 countries in the world, where the median age will be higher than 50" - analysts from the Institute of Structural Research, based on forecasts of the United Nations and the European Commission.[2]

[1] Prawo.pl portal https://www.prawo.pl/kadry/ilu-osob-otrzymuje-emerytury-z-zus-dane-zakladu-ubezpieczen,505607.html

[2] Debate of the " Parkiet" daily https://www.parkiet.com/Ubezpieczenia/302089987-System-emerytalny-nie-potrzebuje-rewolucji.html



The Central Statistical Office https://stat.gov.pl/en/infographics-and-widgets/infographics/infographics-grandmothers-and-grandfathers-day-21-22-january,44,7.html

Proposed changes

Most economists believe that the way to solve the upcoming pension system crisis should be raising the retirement age. One of the proposals, which would ease these problems, are the so-called "citizens' pensions", which have been advocated for years by, among others, Jarosław Gowin, Deputy Prime Minister and Minister of Development, Labor and Technology. In the past, Prime Minister Mateusz Morawiecki has also spoken favorably about this concept, which assumes that all pensioners will receive the same benefit from the state budget. However, most economists are against the concept, arguing that it is an expensive system, discouraging from working, and also giving rise to political temptations. Supporters, however, point to the simplicity of the idea. Experts also point to the necessity of changing the rules of granting pensions so that they take more account of the amount of contributions paid in, as well as the introduction of a system of incentives to work as long as possible.

Conclusion:

The aging of the Polish society and the increase in the number of people of retirement age require a comprehensive reform of the pension system, which should be adapted to the demographic changes. Current changes go in the direction of abolishing OFEs - the capital element in the pension system - and strengthening the employee capital plans. These changes, however, are considered by many experts to be insufficient and driven by ad hoc economic needs, similar to the actions of previous governments.

Pension System in Romania

Oana Popovici

Romania's pensions system since 1990 is based on the solidarity between generations, meaning that pensions are paid based on the contributions of current employees. Starting with 2008, two other pension Pillars where added to this system, under which funds are privately managed and invested. Still, the system continues to be largely dependent on the state pension, which is no longer sustainable due to decreases in the birth rate, emigration and other specific problems of the labour market. A new reform of the pensions system is envisaged under the National Recovery and Resilience Plan, with the aim of being presented to the Parliament until the end of 2022. However, the measures are delicate and bitter for the political party assuming them.

Similar to other socialist countries, after the 1990s, Romania's pension system was based on the principle "pay as you go", in which retirees were paid from the contributions of current employees, while the amount of pensions was related to the level of income, based on periods of minimum contribution. In such pension system, the dependency ratio between the number of retirees and the number of employees, which are the contributors to the pension system, is highly important. From a good dependency ratio of 3.42 in 1990 in Romania, the situation has constantly deteriorated. The demographic change has created problems for the pension system, as the population has declined due to the negative rate of growth and emigration. Another reason for the change in the dependency rate was early retirement. During the years, the labour law was frequently changed, allowing at some point the retirement at age 50 for women and at age 55 for men, and the introduction of a number of professions into a higher risk category, which enabled early retirement with full rights.

The first major overhaul of the pensions system was made in 2000. Back then, the envisaged measures intended the creation of a second pillar of pensions, besides the pension provided by the state, with mandatory contributions privately managed. A third pillar of pensions was also introduced, formed by optional contributions. The introduction of the second and third pillars faced the opposition of employee unions, who wanted to be better involved in the design of the system. Therefore, the law was adopted in the last period of the mandate of the Government back then and immediately cancelled in the first meeting of the new Government. However, the problems have continued. There was a drastically decrease in the number of employees, an increase in the number of the retirees having special pensions based on their belonging to some professional categories, the reduction of the revenues to the state budget as well as the large number of early retirements. As a consequence, the principle of "solidarity between the generations" has become dysfunctional not only in Romania, but on a European scale, and it was replaced by the principle of benefiting of lifelong savings at the retirement age. In 2008, at the recommendation of the World Bank, the law which is currently available has entered into force, regulating the pensions system in Romania on three pillars, quite similar to the ones proposed in 2000.

Therefore, the pension system in Romania is currently structured on three Pension Pillars, as follows: Pillar I – the public pension system; Pillar II – compulsory pensions privately managed; Pillar III – voluntary pensions. The first pillar continues to function under the format of a redistributive system, based on intergenerational solidarity according to which the contributions of current employees are forming the budget of social insurance funds, from where pensions to the retirees in the system are granted. The pensions are calculated based on a "pension point" which is established by the policy makers.

Under Pillar II, a part of the contribution to social insurance funds are redirected towards private companies that will further invest the money. In 2008, the amount of the contribution was established at 2% of the gross salary, intended to increase to 6% within 10 years. At present, the share of social security contributions is 25% of the gross salary. A percentage of 21.25% is directed to Pillar I (public pension), and, due to successive amendments to the legislation, the amount transferred to Pillar II remained capped at 3.75% instead increasing to 6%. Pillar II has been designed to be mandatory, in order to ensure savings for each citizen. Therefore, the amounts to the second Pillar are collected from each employee's individual contribution to social insurance funds. Pillar III has a similar functioning mechanism, only that there is a distinct contribution that will be collected from the gross monthly salary income, on a voluntary basis. Both Pillars II and III are funds entirely independent of the state budget and under the management of financial institutions, free of political intervention. The effective private pension at the retirement age under Pillars II and III will depend on the money collected in the individual accounts, so on the contributions made during the active life, but also on the return obtained from the investments made by the fund administrator. However, the total amount due may not be less than the value of the contributions paid. The privately managed funds had good return on investments so far. The total return achieved by the Pillar II pension funds, starting with 2008 until the end of 2019, corresponds to an average annual return of 8.35%. In 2019, Pillar II recorded the best yield in the last 9 years. There are seven mandatory private pension funds which achieved an average yield of 11.8% in 2019. The evolution was good even during the pandemic.

Despite the reform of the pensions in 2008, the pensions system did not improve its sustainability, as it is still largely dependent on the first Pillar (the state pension). Here, the problems are structural, given that there are too few contributors and too many retirees, which generates a problem of financial sustainability that will worsen in the coming years. In Romania, there are currently 5.2 million pensions and 5.6 million active employees (without including civil servants and staff in the public order and defence system), according to the National Institute of Statistics. In addition, the effective retirement age is much lower than the European average, certain professional categories having the privilege to retire at 45 years. Under the continuous decrease of the birth rate and increased emigration, forecasts indicated that it risks collapse in 2030, when a large number of actual employees will reach the retirement age.

Policymakers are considering a new reform of the pensions, at present under the auspices of the National Recovery and Resilience Plan (NRRP), although the topic was systematically on the agenda of Romanian Governments. The European Commission calls on the Government to make the pension system sustainable, meaning to keep spending at its current level. The NRRP provisions, drawn by the Romania policymakers, provides some important points for balancing the pension system. The general objective of the pension system reform is to achieve a new legislative framework to correct inequities, to respond to the Country Specific Recommendations of the European Commission, to ensure the sustainability and predictability of the system and to respect the principle of contributory beneficiaries of pension rights. However, these provisions caused tensions not only in the public space, but even within the governing Coalition. Among them, there are the elimination of the possibility of early retirement; raising the standard retirement age (from 65 years for men and 63 for women at present) in order to be correlated with life expectancy; freezing pensions at the current level, but with targeted increases for minimum pensions; maintaining a full contribution period of 35 years both for women and men and revisiting the exceptions for various professional categories; changing the way the pension is calculated, based on a stable formula and an automatic indexation, instead of ad-hoc increases, which would ensure the medium- and long-term predictability of pension expenditure, thus eliminating all possibilities of intervention due to political interests.

However, the reform of the pension system is a very delicate and unpopular topic. In addition, it is very difficult to be managed, as the laws on special pensions was defended by various decisions of the Constitutional Court so far. It is clear that the losses in terms of popularity and public appreciation for the party trying to enhance such a reform are very high. However, the measures, delayed in the last years, have to be taken. Romania has a large budget deficit, where the contribution of the pensions system is significant. Such a deficit is difficult to be financed if the interest rates at international level will increase, therefore measures for its reduction are becoming urgent. In addition, according to specialists, the budget cannot be financed only through economic growth, since the nature of the problems is structural.

For the moment, even the provisions of the NRRP are contradicted by policymakers, in an attempt of calming the situation, therefore no clear path is established yet. However, the measures cannot be postponed for too long. The Minister of Labour stated that a new reform law for the pension system will be presented in Parliament by the end of 2022, in order to fulfil the schedule submitted under the NRRP.

Serbia: The road to (un)sustainable pension system

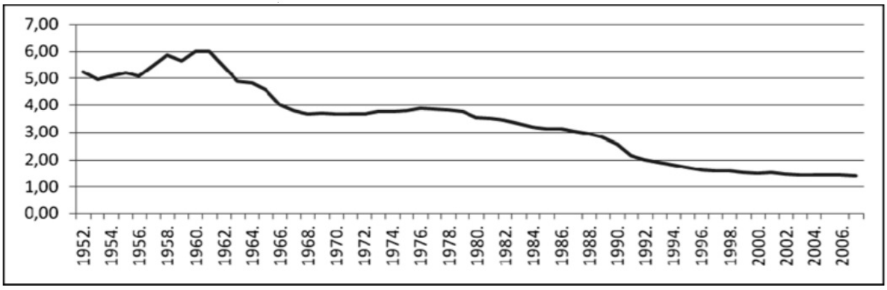
Ivona Ladjevac

This article illustrates the basic characteristics of Serbia's pension system. It analyzes its weaknesses and lists the already implemented reforms. In the last segment, reforms are proposed in order to avoid the collapse of the pension system, along with the list of objective obstacles to their implementation.

Background

The pension system in Serbia is based, as in many countries, on the principle of intergenerational solidarity. It is a "pay as you go" model of the pension system in which funds for the payment of current pensions are provided with income generated on the basis of current payments to the pension fund. This system was set up by German Chancellor Bismarck about 120 years ago. It is actually a collectivist scheme, where the collective in the form of the state manages the money of pensioners who "invested" it in their youth in order to have an economically secure old age. It has been shown that the system can function if the population is relatively young and if the GDP grows in the long run, then, current pensions can be financed from contributions paid by generations of employees. The problem arises when the ratio of employees to retirees deteriorates in the sense that fewer and fewer employees finance an increasing number of retirees.

In order for the existing pension system in Serbia to function, the ratio of employees who pay contributions to the pension fund to the number of pensioners should be 3:1. Now that ratio is 1: 1,01. Hence, the funds of the pension fund in Serbia cover only about 50% of the total expenditures for pensions, and the remaining part is provided from the budget. The deteriorating condition of the Serbian pension system has been evident for many years as can be seen in the scheme below:



Source: Serbian Pension Fund (PIO)

The scheme shows that the pension system has sunk below its optimal point in the year 1987 related to the ratio between employees and retirees. Unfortunately, demographic trends in Serbia are such that they do not promise an improvement in the foreseeable future. According to the Serbian statistics bureau, the current population amounts to 6.871.547 people. Web-site World meter sets present-day Serbian medium age at 41,6 and fertility rate at 1,46. Forecast for 2050 sets medium age at 48.8, while fertility rate remains unchanged. Therefore, reforms are needed in order to have a sustainable pension system.

Minor reforms: delaying the inevitable

During the war years, the disintegration of communist Yugoslavia and the embargo that followed, the pension system of Serbia several times has been bankrupted. At the time, both pensions and salaries of public servants were miserably low. During the period of consolidation, the reform of the pension system began. The first step was to tighten the conditions for retirement for beneficiary social groups: the army, the police, and the security services. As for standard pensions, the final amount of each individual pension is being calculated by using three components: 1) pension point formula, 2) indexation of the pension point in correlation to the average salary and 3) pension age limit. All of the reform measures have been implemented in a way to tighten the conditions for retirement and to relieve the financial pressure on the pension fund.

The pension point formula has been changed so that instead of the ten best years of service (ten years with the highest salary), the income during the entire service is included in the calculation of the pension. In this way, of course, the monthly sum of pension that is paid to the beneficiaries is being reduced. Nowadays, the maximum monthly coefficient is limited to five times the average salary, and the maximum total coefficient is limited to 3,8.[1] Empirically, this means that roughly speaking, it is "not profitable" to earn over 2,000 EUR per month, more precisely earnings exceeding that amount will not affect the pension income you'll receive after you retire. This formula is designed to protect the pension system, and, in fact, it discriminates against people with high incomes, which in Serbia, to be fair, are not many.

There is always a certain delay between adjusting the level of average salary and pension income. However, the gap between the pensions and the salaries in Serbia took drastic measures: as in 2002, the average pension was 73% of the average salary; in 2010 − 63,8%, and in 2020 −46.18%.[2] It is notably that the gap is getting bigger and bigger. As of 2020 the newest version of the indexation, the so-called Swiss formula has been implemented. It defines that the pensions will grow in the amount that equals 50% of annual GDP growth + 50% of the annual inflation rate. After the initial 4% growth in January 2021, the joy of the elderly citizens was short-lived because the implementation of this formula will actually lead to a permanent increase in the gap between salaries and pensions. After all, the pensions will always grow at a two times slower pace.

The third component – the pension age limit has constantly being increased. Today it is 65 years of age, and at least 15 years of service for men, and 63

[1] coefficient 1 = average monthly salary in Serbia cca 500 EUR.
[2] Statistics Bureau of Serbia (combination of reports known to author) – Republički zavod za statistiku.

years of age, and at least 15 years of service for women. The plan is to equalize retirement conditions for men and women by 2032 to 65 years of age.

However, as people live longer and receive pensions longer, it seems that extending the retirement age after age 65 is inevitable. If the whole system is calibrated in such a way that contributions to the pension fund are paid for an average of 40 years, and people receive a pension for an average of 15 years, that balance is disturbed with the extension of life expectancy. Of course, it is possible to increase contribution rates, but this is not practical, both because of competitiveness and because of labor costs. In other words, this measure would be unpopular both with workers whose net wages would be reduced and with employers who would pay a higher contribution to the pension fund. Another unfavorable circumstance is that today, young people are employed later because they study longer, career breaks are more frequent and working period is reduced.

Also, there are two very harmful tendencies in the Serbian labor market that should be addressed too. First of all, the most of the employers are tending to officially register workers on a minimum wage, while the rest of their wages are paid illegally in cash. Such tendency directly leads to the reducing the amount of the payment to the pension fund and thus contributing to its collapse. Second, young people are aware of all the unfavorable circumstances related to their future retirement age and do not pay much attention to the contributions that are deducted from their salaries and paid in the pension fund. Their disinterest is based on the belief that they won't even receive a pension. More precisely, they believe that the pension fund will go bankrupt before they reach the retirement age. Therefore, they prefer to be paid a larger amount of cash rather than contributing to the pension fund.

The only viable solution

As an alternative to the "pay as you go" system, private pension insurance is increasingly in focus. It is a system of capital accumulation based on the idea that the funds from the collected contributions should be available to its owner. The key advantage of the accumulation system is that the economic function of pensions is utilized in this system because the contributions paid by employees represent their savings for their old age. Therefore, there is a direct link between the amount paid into the pension fund and the pension sum. By placing pension insurance contributions on the capital market, they increase by the amount of return on investment, and in addition, the total savings in the country increase as well, which, through a larger volume of investments, affects the increase in economic growth. With the introduction of this system, the state has no obligation to finance possible deficits of pension funds, its role in this model is to provide an institutional environment for the operation of private pension funds and capital markets.

Weaknesses of this pension system model mainly relate to the possibility of unsuccessful investment of pension funds, in that case, then the pension fund may go bankrupt, and people who have invested their contributions may be left without their money and promised security in old age. There are numerous examples of such scenarios and the most famous are those in Iceland and the UK. Another risk is the high inflation rate.

Unfortunately, the citizens of Serbia have very bad experiences both with failed investment banks, which were in fact Ponzi's schemes, and with a high inflation rate. For this reason, the share of private pension insurance in Serbia is very small and it is progressing slowly (only 9% of the population)[1].

Conclusion

[1] Source: Central Bank of Serbia – Narodna Banka Srbije (2019).

Finally, pension system reform in Serbia is absolutely necessary. It requires gradual abandonment of the current financing system and a gradual transition to private pension insurance. But, the biggest problem is a lack of trust. Even mere announcement of abandonment of the current pension system would create panic among the retirees and the older working force. This would create very negative political pressure because pensioners are traditionally the most reliable electorate and, as a rule, support the ruling party (whatever it may be). Therefore, it is difficult to expect that any government would make radical decisions on this issue. The promotion of private pension funds is the only realistically feasible solution.

Slovak Pension System in a Nutshell

Michaela Čiefová

The topic of the present text is a description of the pension system in the Slovak Republic, including its recent development as well as the current state and challenges. The baseline of our analysis will be a glance at demographic developments in the country, mostly characterised by the phenomenon of ageing population, that is one of the features of contemporary Slovak population. At the moment, an amendment to the law on retirement pensions is being discussed, as it should remove the upper age line for the entry to one's retirement and bring some more changes to the pension system.

Introduction

Pension system in the Slovak Republic has been subject to several amendments, as the demography and other social affairs are to be reflected in it. A large reform was implemented in 2003, creating three pillars of pension insurance and saving.[1] Social insurance and pensions fall under the competencies and responsibilities of the Ministry of Labour, Social Affairs and Family of the Slovak Republic. As stated on the Ministry's official webpage, it is its task to ensure a peaceful future for everybody. Moreover, the goal is to facilitate fair redistribution of pensions.[2]

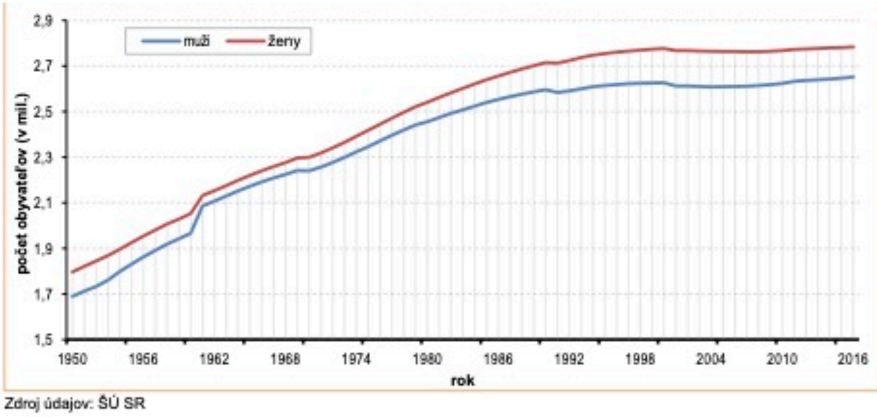
[1] Ministry of Labour, Social Affairs and Family of the Slovak Republic (2021): Dôchodkový systém.
[2] Ministry of Labour, Social Affairs and Family of the Slovak Republic (2021): Sociálne poistenie a dôchodkový systém.

The objective of this briefing is to illuminate the development, current state and future challenges of the Slovak pension system, taking into consideration the contemporary demographic trends.

Demographic development in Slovakia

The lifestyle of Slovaks seems to have undergone changes throughout the recent years. The younger generation is aware of the existing career and personal development opportunities, borders are no longer closed, the world has opened to the people to explore it. Financial independence, promotion possibilities and inner motivation to work have postponed the age at which people usually start their own family. What used to be normal in the past, namely becoming mother at the age of 18 or 20, is now rather an exception than a rule. It is not unusual to encounter a 35-years old woman who is just about to give birth to her first-born child. Apart from the shift in the age, what has changed as well is the number of children per woman. Families have become smaller; many couples prefer having one child only. All of this has contributed to significant changes in demographic structures in the Slovak Republic, with population aging being one of the most serious issues. In spite of that, the country's population is still slightly growing, as we can see in Graph 1 below, demonstrating the development of Slovak population since 1950. The red curve indicates women; the blue one the number of men. The numbers are in millions.

Graph 1 – Population development in the Slovak Republic (1950-2016)



Source: Podmanická, Z. (ed.) (2017): Hlavné trendy populačného vývoja v SR v roku 2016. Bratislava: Statistical Office of the Slovak Republic, p. 7.

Without doubts, demographic developments are always to be paid attention to, due to their being closely linked to economic, social policy as well as political situation, and also to pension systems. The issue of population developments should be debated not only on the level of national economies, but globally as well.[1]

Taking population structure and demographic tendencies into account is crucial for creation of relevant pension policies. Ageing population and lower natality result in an increase of age when the citizens are allowed to retire. In accordance with the legal regulations concerning social insurance, the retirement age in Slovakia is calculated with regards to three factors, namely the year of birth, gender, and the number of children that have been raised. Let us include several examples for illustration. A woman born in 1944 with no children entered retirement at the age of 57. Another woman born in the same year with three or four children had a right to retire earlier, more specifically at the age of 54. In case of 5 children, the retirement age of a 1944-born woman was 53. A woman born in 1965 is supposed to work

[1] Čiefová, M. – Raneta, L. (2017): Demografické trendy na Slovensku a v Rakúsku, p. 77, 84.

until she is 63 years and 10 months old, provided she has no children, while a woman of the same age with more than two children will work until she reaches 62 years and 10 months (or 62 years and 4 months, respectively).[1] Indeed, we can see the retirement age has been extended significantly, counting in years.

As population ageing or decreasing natality have been a problem of many developed countries, it is possible Slovakia will "copy" their demographic tendencies. For instance, research aimed at comparison of the demographic situation in Slovakia and Austria revealed that the current Slovak population pyramid resembles Austrian population pyramid from 30 years ago. Indeed, Slovak population of the present day can be characterised by an increase in total numbers of inhabitants, while the percentual representation of children has decreased throughout the last decades. On the other hand, what needs to be remembered is the immigration to Austria. In fact, Austria has accepted far more migrants than Slovakia for the past years, which contributed to its population growth. Even though more people have immigrated to Slovakia as those who have left the country, the numbers are in comparison with countries such as Austria only marginal. Of course, this hypothesis is based on the fact that cultural and historic circumstances in the two countries show certain similarities.[2] Still, we do not expect that migration would significantly contribute to population growth in Slovakia in the future, hence compensating for the lower natality. Furthermore, based on predictions, the population of Slovakia is expected to start declining around the year 2030, probably in 2025.[3]

Types of pensions in the Slovak Republic

[1] Ministry of Labour, Social Affairs and Family of the Slovak Republic (2021): Dôchodkový vek.
[2] Čiefová, M. – Raneta, L. (2017): Demografické trendy na Slovensku a v Rakúsku, p. 83-84.
[3] Podmanická, Z. (ed.) (2017): Hlavné trendy populačného vývoja v SR v roku 2016, p. 8.

In Slovakia, several groups of people are entitled to a financial contribution from the state. The pension scheme includes following categories:

- retirement pension,
- early retirement pension,
- pension for physically challenged people,
- pension for widows and widowers,
- pension for orphans.[1]

Obviously, it is defined in detail who can be entitled to which type of pension, and there are also responsibilities of the individuals towards the social insurance company. As for the contribution to the elderly – to those who have retired – this contribution is paid out from the retirement insurance, with the purpose to ensure people some income for the future. In order to have a right for this kind of contribution, the pensioner needs to fulfil two conditions, which are as follows (specific cases and exceptions are not analysed within this text):

- have at least 15 years of old age insurance, and
- reach the respective retirement age.[2]

In the previous text, we provided some examples of retirement age based on the number of raised children. At the moment, the upper age to enter retirement is 64 years, relating to women without children and men, and is guaranteed by the law.[3] Several weeks ago, the media reported on the government's intention to further prolong the working years of Slovaks, thus removing the line of 64 years. The retirement age should be calculated with regards to life expectancy. In the praxis it would mean that the age of

[1] Sociálna poisťovňa (2021): Dôchodca a žiadateľ o dôchodok.
[2] Sociálna poisťovňa (2021): Starobný dôchodok.
[3] Pravda (2020): Dôchodkový strop 64 rokov a penzijný vek nie je to isté.

retiring would be prolonged based on increasing life expectancy. The objective of this step is to retain financial sustainability of the first pension pillar. The media cited the Ministry of Labour, Social Affairs and Family of the Slovak Republic, saying that in case this becomes reality, the pensioners would spend approximately the same number of years in their retirement. According to the Ministry of Labour submitting the proposal, such thing would improve solidarity among generations. Another point of the proposal is aimed to allow people to allocate a certain percentage of their taxes to their parents' retirement contribution. Besides, further suggestions are included, for instance an increase of orphans' contribution. To remind, this is just an amendment proposal to the social insurance law, the content of which is planned to be discussed shortly.[1] Should it eventually become law or not, the Slovak pension system is likely to be subject to other changes in the future, reflecting the demographic tendencies.

Conclusion

Similarly as many countries all around the globe, Slovakia is facing the problem of population ageing. Unsatisfactory demographic developments represent a burden for social and pension systems of the countries that simply cannot be ignored and will be one of the challenges to deal with also in the future. The pension system in the country has already been reformed several times. Indeed, population development is a dynamic phenomenon which requires constant monitoring and subsequent adaptation of the relevant policies. Therefore, further changes of the pension system may be foreseen.

[1] SME (2021): Dôchodkový vek sa má opäť predlžovať podľa strednej dĺžky života

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Pension System in Slovenia

Helena Motoh

In the three decades after the establishment of Slovenia as a country, the pension system which was inherited from the former Yugoslavia, was reformed and amended several times to respond to the challenges posed by the economic and social trends of different periods. The ongoing challenge of the rapidly changing population makes a more radical renewal of the pension system imminent.

Reform process of pension system 1990–1999

Pension system that was in place at the beginning of the 1990s dated back to the period after the Second World War, when the universal social security laws were passed on the basis of the pre-war legislation of the Kingdom of Yugoslavia. In 1983 the first Pension and Disability Insurance Act was adopted in the Socialist Federative Republic of Slovenia, which set the principle of pensions matching the average salaries and not the living costs. For the first time this law included self-employed persons and farmers. Pensions were to be financed from the subventions paid by the working population and were thus based on the solidarity principle. Minimum pension and minimum basis of assessment, where the best series of 10-year salaries was taken into account. Retirement age was 55 for women and 60 for men with the minimum length of employment at 20 years and full length of employment of 40 years for men and 35 years for women.

In the time of political and economic transition in the late 1980s and early 1990s when many employers went bankrupt, the pension system was under pressure due to the increasing trends of early retirement of the unemployed. In the early 1990s the pension system thus suffered both from the increase of pension expenditures and the falling numbers of paying employers. To address these trends, the first Pension and Disability Insurance Act was adopted in the Republic of Slovenia in 1992. In this Act, the length of employment was not sufficient for retirement, but the criterion of age also had to be met: 55,5 years for men and 50,5 years for women. The basic pension was set at the 85% of the salaries received by the retired person in his/her active employment period. The change did not have a significant impact on the number of newly retired. The age of retirement has not risen much, especially because the cost of purchasing the additional years of calculated employment period (such as the education years) was very low. To stimulate economic growth, in 1996 the obligatory payments into the pension funds by the employers were lowered, which – at the same number of beneficiaries – caused a serious deficit in the national pension fund, which had to be compensated by state funds.

Reform process of pension system 2000–2013

The pension system was amended again with the 2000 reform. The need for the reform was obvious: a growing number and ratio of the retired population as high as 1 retired person per 1,5 working active person, longer education, lower natality and higher life expectancy. New Pension and Disability Insurance Act (ZPIZ-1) was adopted, making the retirement conditions more demanding. The retirement age was raised to 58 with the employment length now higher for both men (38 years) and women (40). The basic pension was set at 72.5% of the average salary in which the calculated best consecutive years were now 18 instead of the previous 10. The 2000 reform also established a three-pillar system of pension funds, supplementing the obligatory pension payments with collective and individual voluntary pension insurance payments.

The two goals the next reform period in 2010-2013 were to achieve the financial sustainability of the pension system and decent pensions, while also aiming at the higher ration of active working population and the raised amounts of voluntary second- and third- pillar payments. The new Pension and Disability Insurance Act (ZPIZ-2) was adopted in 2013, putting in place a reform of all three pillars of pension system. The reform was based on the principle of improving the ration between beneficiaries and employed population primarily by changing the prerequisites for retirement. Regardless of the length of employment, the minimum age was now set as a condition for full pension. Both men and women had to be of at least 60 years of age if they fulfilled the 40 years of employment, but they receive a lowered pension until they fulfil the age requirement as well. The age requirement for full pension is 65 for both genders.

The status quo and reform orientation of pension system

Although another reform of the pension system was prepared and announced several times by the following governments, no substantial change was made. Several successive amendments of the Pension and Disability Insurance Act were adopted, the last one, ZPIZ-2I adopted in March this year. The changes, however, are small and mostly aim in two directions: establishing a system of equal requirements for men and women and motivating the employees to work longer. As of the ZPIZ-2G amendment of January 2020, the scale of vesting percentages for men are set to be gradually harmonized with the scale of vesting percentages for women over a six-year period. The goal date when the scales are harmonized is set for January 1st 2025. The late employment was already stimulated by the ZPIZ-2. If pension beneficiaries work after being retired and are thus included in the obligatory pension insurance system for full time employment, receive 40% of the age pension they would be entitled to receive if not working, for the next three years, while after that period the pension received in addition to their employment income goes down to 20%. In ZPIZ-2G amendment, a similar stimulation was adopted also for those retired employees who do not work full time, but work at least half-time, entitling them o a proportionate part of the 40% pension for the three years period and a proportionate part of the 20% pension after that.

Going against the grain of this general orientation of the evolving pension system, a recent change in the regulations caused lots of public debate and criticism. As part of the Covid-19 crisis legislation packages, Articles 21 and 22 of the Seventh package (PKP7) allow for a deregulation of layoffs of older employees. According to PKP7 they could be laid off if they fulfil the requirements for retirement, without listing any reasons for the layoff. The criticism for this regulation was twofold. First, the critics pointed at the unconstitutionality of the regulation, which deprived a part of the workforce of their employment rights based solely on their age. For this reason, the trade unions appealed to the Constitutional Court to review the proposed regulation. On the other side, many critics also pointed at the consequences for the pension system, for which the sudden numerous layoffs could mean an influx of newly retired, a situation which the already stretched pension system could not endure. As of now, the Constitutional Court procedure is still underway.

Challenges and development trend of pension system

The greatest challenge for the pension system in Slovenia is posed by the dramatic aging of the population. The demographic prognosis for Slovenia show that – based on the prediction of stable migration influx –, in 2060 only less than half of the population will be active working population, while the ratio in favour of the retired population will be growing. The analysis made recently also pointed at the fact that the financial dependency patterns are worrying especially for the older population. While young population before employment relies greatly on private transfers, the retired population remains substantially dependent on the public transfers, i. e. pensions, which makes this segment of population even more vulnerable in case of pension system reforms or limited pension fund sustainability. Slovenia also ranks very low in regard of the employment of elderly population. Only less than half of people (47.3%) over 55 years of age still work, which is considerably lower than the OECD average (61.5%) and far below countries like Sweden (78.4%) or Germany (71.5%). Most of Slovenian working population (75%) retire as soon as they fulfil retirement requirements, on average at 60,5 years for women and 62,33 years for men.

Conclusions

The demographic trends and the retirement trends in Slovenia call for another imminent pension reform, after no substantial changes have been made since the last reorganisation of the system with the three-pillar structure two decades ago. Although the many consecutive smaller amendments of the last Pension and Disability Insurance Act that were made in the last decade together amount to several substantial changes, especially in the aspect of prerequisites for retirement, the effects are not sufficient and without serious long-term strategic revision in form of a systematic reform of the pension system the current status of the retirement system might not be fit to face the demographic changes predicted for the next decades.

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