Social Security

International Update:

Recent Developments in Foreign Public and Private Pensions

December 2006

Europe

France

In October and November 2006, France launched the National Employment Plan (NEP) to increase the employment rate of older workers. The NEP, a product of extensive consultation among the Social Affairs Ministry, business groups, and unions, aims to raise the labor force participation rates of French workers aged 55–64 from the current 38 percent to 50 percent by 2010, the recommended European Union target. As such, the NEP will provide employment incentives for individuals to work beyond the normal retirement age of 65 and encourage employers to keep workers older than age 50 in the workforce. According to the French government, higher employment rates among older workers are essential to address the expected impact from population aging on the unfunded public pension system.

NEP's measures related to work and retirement will:

- Remove (progressively) by 2010 the *Delalande contribution* tax that since 1987 has required firms to pay 3 months' gross salary to any discharged employee older than age 50. Organisation for Economic Co-operation and Development (OECD) studies indicate that while the *Delalande contribution* may discourage some firms from firing older workers (the original intent), its principal impact has been to reduce the hiring of older workers.
- Create a new temporary 18-month, one-time renewable labor contract for unemployed persons aged 57 or older. The government developed the temporary labor contract in response to evidence that the existing penalties for firing older workers may discourage employers from hiring them (see *Delalande contribution* above). The objective of the new labor contract is to help older unemployed persons reenter the labor force before they reach the minimum retirement age of 60. To qualify, workers over the age of 56 must have been either searching for a job for at least 3 months or be registered with an unemployment program that provides retraining. The temporary labor measure becomes effective in 2007.
- Increase the public pension bonus for workers who remain in the workforce beyond the early retirement age of 60. The current bonus of 3 percent would be maintained for the first year of work after age 60. It would rise to 4 percent for each year worked from ages 61–64, and then increase to 5 percent for each year a worker remains in the labor force past the normal retirement age of 65.
- Allow employees to work part time beyond age 60 *and* receive a portion of their public pension. The program will be available until 2008 for workers who have contributed to the public pension system for 150 quarters.
- Create a series of dedicated training programs and job placement services for older, long-term unemployed workers. These programs would seek to improve the chances of unemployed persons over age 50 finding a job from the current 33 percent to 45 percent by 2010.

The government has earmarked €10 million (US$13.1 million) to finance the NEP program. Separately, it has already spent €3 million (US$3.9 million) on an NEP media campaign that included televised ads, radio programs, and a Web site. Additional information related to the NEP is accessible through the French Government Portal at http://www.premier-ministre.gouv.fr/en/information.

Like many countries, France is facing rapid population aging due to fertility rates below population replacement (1.87 children per woman in 2005) and longer life expectancy at birth (approximately age 77 for men and age 84 for women in 2005). The result is an increase in the dependency ratio—the population aged 65 or older relative to those of working age (ages 20–64)—from the current 25 percent to a projected 50 percent in 2050. By 2050, the government projects public pension system expenditures to rise from the current 10.6 percent of gross domestic product (GDP) to nearly 13.0 percent of GDP.

Sources: *OECD Observer*, August 2003; *Synthesis Report on Adequate and Sustainable Pensions: Annex (Country Summaries)*, European Commission, 2006; *Employers Law*, July 7, 2006; Watson Wyatt, October 2006; and *Pension & Benefits Daily*, October 31, 2006.

United Kingdom

On November 8, Parliament passed the Companies Law that allows occupational pension fund directors to receive liability insurance from plan sponsors. The law reforms the current regulations that determine how British firms are created, operated, and dissolved. The law also contains a provision allowing a company hired as a pension fund trustee, its parent company, or a subsidiary to insure an occupational pension fund director against liability for certain pension fund-related losses. The new law will become effective October 2007.

In 2004, Parliament repealed the law that allowed plan sponsors and pension-related companies to provide indemnity to pension fund directors. Since then, many pension fund directors voluntarily acquire director's liability insurance with their own funds; however, this insurance is often costly and difficult to obtain. According to a July 2006 ruling by the Law Commission (an independent body established by the legislature to review and recommend reforms), a lack of indemnity acts as a deterrent for potential pension fund trustees, many of whom are not necessarily pension experts. Indemnity insurance offers pension fund directors protection against personal liability from occupational pension fund losses unless the loss is a result of fraud.

Sources: Norton Rose, August 2006; *Practical Pensions Law*, November 2006; Reuters, November 8, 2006; and *Global Pensions*, November 10, 2006.

The Americas

Canada

On November 9, 2006, the Premier of Ontario created the Ontario Expert Commission on Pensions to analyze employer-sponsored defined benefit pension plans in the province. The commission is part of the government's overall effort to modernize provincial law, boost economic competitiveness, and address changes that may affect private defined benefit pensions. The commission will address the impact of historically low long-term interest rates, increasing life expectancy, and recent pension-related regulatory and legal decisions on employer-sponsored defined benefit plans. The commission expects to send a report to Ontario's Minister of Finance in the summer of 2008.

The five-member commission will review potential changes to both the Ontario Pension Benefits Act (OPBA), which has not been substantially amended since 1986, and the Pension Benefits Guarantee Fund, an insurance fund for defined benefit plans in the province. The commission will also review pension legislation proposed by the federal government and the provincial governments of Quebec, Alberta, Manitoba, and New Brunswick. (See also the June and August 2006 issues of *International Update*.) The commission has requested input from the private pension community and the public.

The commission will focus specifically on:

- Preserving, encouraging, and safeguarding defined benefit pension plans and keeping them affordable for members and plan sponsors;
- Balancing the rights and obligations of employers, plan members, and pensioners; and
- Ensuring the solvency of pensions in light of changes in demographics and the workforce.

Since 1997, the share of Ontario workers participating in employer-sponsored pension plans has remained constant at about 40 percent. Today Ontario has more than 2 million members registered in over 7,500 employer-sponsored pension plans, of which 51 percent are defined benefit pension plans with over 1.7 million participants. However, nationally from 1992 to 2004, the number of Canadian employer-sponsored defined benefit pension plans decreased from 29 percent to 21 percent amid growing solvency concerns.

Sources: *Back from the Brink: Securing the Future of Defined Benefit Pension Plans*, Association of Canadian Pension Management, August 2005; *Improving Ontario's Pension System: Ontario Expert Commission on Pensions' Terms of Reference*, Ministry of Finance, November 2006; *Toronto Star*, November 10, 2006; Canada NewsWire, November 13, 2006; plansponsor.com, November 13, 2006; fscogov.on.ca, November 30, 2006; statcan.ca, November 30, 2006.

Peru

On November 9, Peru's Central Reserve Bank (BCRP) increased the limit on how much pension fund management companies (AFPs) can invest abroad. According to BCRP President Julio Velarde, the bank raised the limit from 10.2 percent to 12 percent of assets under management and may authorize future incremental increases at the rate of either 0.05 percent or 1 percent every month or 2 until the limit reaches the legal maximum of 20 percent. The Association of AFPs recommended raising the limit to 15 percent by the end of 2006.

There is broad industry agreement that the increase in allowable foreign investments will help diversify the AFPs' portfolios and reduce investment risk, particularly since the pension fund assets are growing at a faster pace than the domestic markets can absorb.

Of the 44.5 billion nuevos soles (US$14.5 billion) in assets managed by all five AFPs, 43 percent are in domestic stocks, 20 percent in government bonds, and the rest in a variety of investments such as certificates of deposit and other types of bonds. The AFP pension system's average real rate of return over the past 10 years has been 8.4 percent. (See also the August 2006 issue of *International Update*.)

From the inception of the individual accounts system in 1993 until December 2005, AFPs provided their members with one fund. Now, AFPs may offer up to three funds of varying degrees of risk: a mixed or balanced fund (the original fund when only one was permitted); a growth fund; and a preservation of capital fund. (See also the January 2006 issue of *International Update*.)

Sources: *Boletín Estadístico AIOS*, Número 15, junio de 2006; AFP Integra, *Novedades—Normas Legales*, noviembre de 2006; *Business News Americas*, November 3, 2006; Reuters—Noticias Latinoamericanas, 3 de noviembre de 2006; *Boletín Semanal del Sistema Privado de Pensiones: Año 2006 - Nº 45; Global Pensions*, November 6, 2006.

Trinidad and Tobago

On October 13, 2006, Trinidad and Tobago's Parliament passed a law that expanded pension coverage and increased the government-funded means-tested pension maximum benefits by 17 percent to keep up with inflation, the consumer price index, and rising wages since 2004. When the legislation takes effect on January 1, 2007, the maximum monthly means-tested benefit will increase by TT$200 (US$32) to TT$1,350 (US$215) per month. The means-tested benefit income threshold will also rise next month, from TT$1,000 (US$159) to TT$2,150 (US$342) per month. Trinidad and Tobago's per capita gross national income is TT$5,464 (US$870) per month.

Benefits paid under the expanded system will be reduced incrementally for incomes above TT$1,000 (US$159) per month. The new legislation also changes the name of the means-tested benefit from Old-Age Pension to Senior Citizens' Grant.

The means-tested old-age pension is available to citizens aged 65 or older with at least 20 years of residence. The government estimates that about 10,000 additional individuals will qualify for this benefit at an added cost of TT$136 million (US$21.7 million) annually.

Trinidad and Tobago also has a contributory pay-as-you-go pension system. Since the new law raises the means-tested pension income ceiling, more contributory pay-as-you-go public pension system beneficiaries are expected to qualify for the Senior Citizens' Grant. The contributory program covers employees aged 16–64. Employees contribute 2.8 percent and employers contribute 5.6 percent of weekly earnings between TT$130 (US$21) and TT$1,010 (US$161). Benefits are paid to workers beginning at age 60 with at least 750 weeks of contributions.

Sources: *Social Security Programs Throughout the World: The Americas*, 2005; *Budget Statement of the Prime Minister and Finance Minister*, October 4, 2006; *Caribbean Net News* (Port of Spain), Trinidad, October 7, 2006; *The Trinidad Guardian* (Port of Spain), October 14, 2006; *Budget 2007 Speech & Analysis 2006*, Republic Bank, October 2006; *Country Profile: Trinidad and Tobago 2006*; BBC News, October 24, 2006.

Asia and the Pacific

Australia

On November 13, 2006, Australia's Treasury Department officially announced the establishment of a reserve fund, called the Future Fund, to address rising public employee pension plan liabilities. Currently, public employee pension plan liabilities amount to A$98 billion (US$76 billion). According to the government, if left unchecked these pension plan liabilities are projected to reach A$140 billion (US$109 billion) by 2020.

The Future Fund Act 2006, which received Royal Assent on March 23, 2006, allowed the government to establish the Future Fund with an initial deposit of A$18 billion (US$13.8 billion) on May 5, 2006. The government plans to contribute another A$14 billion (US$10.7 billion) in early 2007. Proceeds from the recent sale of the government's 51.8 percent stake in the telecommunications company Telco will inject an additional A$15.5 billion (US$11.9 billion) into the fund.

Australia's public employees are covered under one of three pension plans: the Commonwealth Superannuation Scheme (CSS), the Public Sector Superannuation Scheme (PSS), and the Public Sector Superannuation Accumulation Plan (PSSAP). The CSS, which closed to new members on July 1, 1990, is a defined benefit plan. The PSS, which closed to new members on July 1, 2005, is also a defined benefit plan. The PSSAP, which began accepting newly hired public employees on July 1, 2005, is a defined contribution plan. Retired government workers receive more than A$4.5 billion (US$3.49 billion) in defined benefit superannuation benefits annually. By 2020, annual public employee pension expenditures are expected to increase to A$7.5 billion (US$5.8 billion) as the public sector workforce ages.

Under the PSSAP, the public employees' defined contribution retirement plan, the government as employer contributes at least 15.4 percent of an employee's biweekly salary. Public employees have the option of making additional unlimited contributions and choosing from a variety of investment funds.

The Australian Reward Investment Alliance (ARIA) manages the PSSAP Fund, the CSS Fund, and the PSS Fund. ARIA comprises economic experts appointed by the government to maximize investment returns solely in the interest of public employees.

Both private- and public-sector employees are also eligible for participation in Australia's means-tested Old Age Pension (OAP). The OAP retirement age is 65 for men and 62.5 for women, which is gradually rising to 65 by 2013. OAP beneficiaries must be Australian residents for 10 consecutive years (5 consecutive years if the total time in the country exceeds 10 years). Eligible OAP beneficiaries still working at least 960 hours in their eligibility year may defer the OAP benefit for 12 months to 60 months. Biweekly benefits are currently A$512.10 (US$400.77) for singles with biweekly income less than A$1,422.75 (US$1,113.44) and A$855.40 (US$669.44) for couples with income less than A$2,381 (US$1,863.37).

Sources: *Social Security Programs Throughout the World: Asia and the Pacific, 2004*; *Global Pensions*, November 11, 2006; *Australian Government Future Fund*, Australia Treasury Department; *InfoWorld*, November 21, 2006; *Commonwealth Superannuation Scheme*, *Public Sector Superannuation Accumulation Plan*, *Public Sector Superannuation Scheme*, Australia Department of Finance and Administration, November 2006; *Centrelink*, Australia Department of Human Services, November 2006.

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