Social Security

International Update:

Recent Developments in Foreign Public and Private Pensions

May 2015

Europe

Slovenia: Organization for Economic Cooperation and Development Releases Survey

On May 4, the Organization for Economic Cooperation and Development (OECD) released its *Economic Survey for Slovenia 2015*, which highlights positive change over the past two years and areas that need improvement. In 2011, Slovenia spent 11.4 percent of gross domestic product on old-age and survivor pensions, compared with an average of 7.9 percent in OECD countries. Even though the pension reform implemented in 2013 put the system on a more sustainable path in the medium term, these measures did not go far enough. The country's older population (aged 65 or older) is growing at a faster pace than in many other OECD countries. By 2060, Slovenia's older population is expected to represent 29 percent of the total population (17% in 2013); the population aged 80 or older could increase at an even faster pace and reach 11 percent (nearly triple) by 2050. At the same time, the dependency ratio (working population aged 14 to 64 compared to the older population) is projected to decline from 4 to 1 to 1.8 to 1. As a result, with no additional changes, the report projects a 6 percentage point increase in age-related expenditures by 2060.

The report also finds that most pensioners rely mainly on the public pension system. Private pensions do not provide a significant portion of retirement income mainly because the government does not offer sufficient incentives for private pensions.

In addition, according to the report, the labor force participation rate of workers aged 55 to 64 is low. While the high cost of dismissing a worker may benefit older workers, the high cost of hiring is a disadvantage. Workplace age discrimination is another cause for the low participation rate; widespread in part due to "negative attitudes towards older workers and misconceptions about their ability."

The report also draws attention to a number of important changes made by the 2013 pension reform:

- Raising the retirement age gradually to 65 (from 63 (men) and 61 (women)).
- Increasing the number of years used in the benefit formula (from the 18 best to the 24 best years).
- Raising the minimum age for a full benefit from 58 to 60 (with 40 years of contributions).
- Improving the maximum increase in benefits for deferred retirement (from 7.2 percent to 12 percent).
- Changing the indexation of benefits from the increase in average gross salary to a combination of 60 percent of the increase in the average gross salary and 40 percent in the cost of living.

The report makes a number of recommendations regarding pensions and encouraging older workers to remain in the labor force including:

- Linking the minimum and full retirement ages to life expectancy.
- Changing the benefit formula to cover lifetime earnings.
- Modifying the formula for indexing benefits to give inflation a greater weight.
- Establishing ways to encourage private pensions.
- Increasing incentives for older workers to remain in the labor force.
- Adapting the workplace for older workers, such as providing training programs designed for older workers and shifting workers to less strenuous jobs.

Sources: *Social Security Programs Throughout the World: Europe 2012* and *2014*, U.S. Social Security Administration, August 2012 and September 2014; "Economic Survey of Slovenia," Organization for Economic Cooperation and Development, May 2015.

United Kingdom: Implements Pension Law Changes

The Pension Schemes Act 2015, part of the government's reform of private pensions, received Royal Assent on March 3. Provisions of the law, which took effect on April 6, include more flexibility for the individual, expanded options for shared risk in pension plans, and new requirements for advising individuals. The law also contains changes first introduced by the Taxation of Pensions Act 2014, which gave defined contribution (DC) plan members more flexibility in accessing their benefits. (Defined benefit (DB) plans must transfer to a DC plan to be eligible for this option.)

Provisions of the 2015 Act include:

- Changing the rules on transferring funds and creating three new categories of benefits: 1) money purchase (essentially DC), 2) shared risk, also called "Defined Ambition" by the government (flexible benefits other than money purchase benefits), and 3) final salary and career average benefits that are not flexible. A member with different categories of benefits in the same plan may transfer his or her funds in one category to another plan and leave the funds in any other category in the original plan.
- Creating new definitions of private pension according to the "pension promise." A DB plan provides a specific replacement rate at a specific age. A shared risk plan has a pension promise that applies to a portion of the benefit (retirement pension or a lump sum benefit). A DC plan has no pension promise.
- Establishing the framework for "collective benefits." Once the regulations are set, occupational and personal pension plans will allow members (and other parties, including employers) to pool different types of risk.
- Requiring a DB plan member to seek "appropriate independent advice" before he or she transfers funds to a DC plan. This requirement will apply to transfers of at least £30,000 (US$46,298). Plan trustees must verify that members have received appropriate independent advice.
- Setting up a new free service called Pension Wise that provides impartial advice on the different retirement options. The service is run by the Pensions Advisory Service and Citizens Advice Bureau.

Sources: "Pension Schemes Act," 2015; "Freedom and Choice in Pensions: It's Just around the Corner," Bond Dickinson *Pensions Newsletter*, March 2015; "Our Guide to the Pension Schemes Act 2015," Lane, Clark & Peacock LLP, March 2015; "Pension Schemes Act 2015," Hymans Robertson, March 2015; "UK: Pensions Scheme Act 2015," Mondaq, April 7, 2015.

The Americas

Dominican Republic: Changes to the Disability Pension Rules

On April 26, the National Social Security Board (CNSS) approved a resolution that modifies the rules regarding the disability pension. As part of the mandatory individual account program, private insurance companies (under contract with the pension fund management companies) provide long-term disability benefits to workers assessed with at least a 50 percent loss of earning capacity up to age 60. The new rules extend that limit to age 65 and increase the number of years a worker has to apply for benefits, from two to seven, after the disability began. More than 50,000 individuals could be affected by these new rules.

The insurance company pays the accountholder's contribution to the individual account while he/she is receiving a disability pension. When the disability pension is terminated, the insured person may access the individual account balance to purchase a price-indexed annuity or make programmed withdrawals.

The resolution also instructs the Directorate of Information and Defense of the Social Security Beneficiaries (DIDA) to disseminate the information about the new changes. DIDA, created as part of the social security law that set up the system of individual accounts, is subordinate to the CNSS. DIDA's main functions are promoting social security, informing accountholders of their rights and duties, and conducting studies that evaluate the services provided by various social security institutions.

The individual accounts are administered by five pension fund management companies with total assets under management of US$5.4 billion and 2.9 million accountholders as of December 2014. Less than 50 percent of accountholders regularly make contributions. Employees contribute 2.87 percent of covered earnings and employers contribute 7.1 percent of covered payroll. A retirement benefit is paid at age 60 with at least 30 years of contributions.

Sources: "DIDA," Instituciones y Detalles, no date; *Social Security Programs Throughout the World: The Americas, 2013,* U.S. Social Security Administration, March 2014; "Afiliados por Sistema," AIOS Estadísticas, 2015; "Aportantes por Sistema," AIOS Estadísticas, 2015; "Fondos Administrados Al 31.12.2014 y 30.9.2014," FIAP Estadísticas, 2015; "CNSS Extiene Plazos para Optar por Pensión de Discapacidad y Sobrevivencia," Noticia, el 27 de abril de 2015.

Ecuador: A New Law Changes the Labor Code

On April 15, the legislature approved the Labor Justice Law, which modifies the country's labor code. Three provisions of the law apply to pensions: 1) extending pension coverage to unpaid housewives; 2) modifying the government's mandatory contribution to old-age, survivors, and disability insurance (OASDI); and 3) changing the method of indexing benefits.

Under the new law some 1.5 million unpaid housewives could be eligible for the mandatory public pay-as-you-go pension system. The government's goal for this year is enrolling 400,000 women. (The government values the housewives' work at some 1 percent of gross domestic product (GDP).) Once implemented, insured women will pay contributions based on family income, as a percentage of the basic unified salary (salario básico unificado or SBU, currently $354 a month). The rates range from 25 percent of the SBU for family income of less than 50 percent of the SBU to a rate of 100 percent or more of the SBU for family income that is equal to or greater than 150 percent of the SBU. The government will determine its contribution annually according to the General Budget. (A projected cost for the initial 400,000 women is $43 million for 2015.) A retirement benefit will be paid at age 65 with at least 240 monthly contributions. The qualifying conditions for disability (assessed as totally and permanently disabled) and survivor pensions will vary according to age, from 6 monthly contributions between ages 15 and 25 to 60 contributions at age 46 or older. Benefits for women in low-income families will be higher than those for high-income families. Work injury benefits will also be available.

In addition, the new law eliminates the 40 percent that the government has been required to contribute to the cost of OASDI pensions since the 1940's. (Sixty percent of the cost is paid by employee, employer, and the self-employed person's contributions). Instead, the government must contribute only when the Ecuadorean Social Security Institute (IESS) does not have the economic resources to meet its obligations for paying social security benefits. In 2015, 40 percent of the cost of pensions amounts to about $1 billion a year. According to the Economist Intelligence Unit, the government needs those funds because the decrease in the price of oil has hurt the country's finances. It forecasts Ecuador's fiscal deficit for 2015 to reach 6.1 percent of GDP. Proposals to fill the gap in funding include raising the retirement age, increasing contributions, and lowering benefit levels.

The third social security-related provision of the new law changes the way benefits are indexed. Since 2010, annual adjustments range from 4.31% to 16.16%; lower benefits are adjusted at a higher rate than higher benefits. Under the new rules, benefits are adjusted according to increases in the average rate of inflation in the previous year.

IESS regulates and administers the OASDI program (as well as sickness and maternity, work injury, and unemployment programs), which covers all employed persons. The OASDI contribution rates for the private sector are 8.64 percent of earnings (employee) and 1.10 percent of payroll (employers). The retirement age depends on the number of contributions: at any age with at least 480 months of contributions; age 60 with at least 360 months of contributions; age 65 with at least 180 months of contributions; or age 70 with at least 120 months of contributions.

Sources: *Social Security Programs Throughout the World: The Americas, 2013,* U.S. Social Security Administration, March 2014; "Reforma No Plantea Cómo Sustituir Subsidio del 40%," *El Comercio*, el 7 de abril de 2015; "Aprobada la Ley de Justicia Laboral, que Reforma la Seguridad Social," *El Universo*, el 14 de abril de 2015; "Ley Orgánica Para La Justicia Laboral y Reconocimiento del Trabajo en el Hogar," el 15 de abril de 2015; "Ecuador Politics: Government Ends Pension Contribution in Labour Reform," Economic Intelligence Unit, April 21, 2015; "El Manejo del Seguro de Pensión Jubilar del Ama de Casa, en Debate," *El Comercio,* el 4 de mayo de 2015.

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