Social Security
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International Update:

Recent Developments in Foreign Public and Private Pensions

May 2010

Europe

Estonia

On April 7, the Estonian parliament passed a law that will gradually increase the retirement age for men and women beginning in 2017 until it reaches age 65 in 2026. Currently, men can retire at age 63 with at least 15 years of employment and women at age 60 and 6 months with at least 15 years of employment. (The retirement age for women is gradually increasing by 6 months each year until it is equalized with that of men at age 63 in 2016). The law also requires the government to conduct a study in 2019 to determine whether additional measures, such as a further increase in the retirement age, may be needed to ensure the long-term sustainability of the pension system.

The Estonian pension system consists of a first-pillar, public pay-as-you-go (PAYG) program; second-pillar individual accounts that are mandatory for new entrants to the labor force and workers born after December 31, 1982; and third-pillar voluntary individual accounts. Until recently, workers contributed 2 percent of earnings to the second-pillar individual accounts, and employers contributed 20 percent of gross payroll, of which 16 percent was diverted to the PAYG program and the remaining 4 percent to the second-pillar individual accounts. However, in an effort to stem rising budget deficits during the global economic crisis, the government passed a law in June 2009 that temporarily reallocated the entire 20 percent employer contribution to the first pillar through 2010. (The employer contribution rate will gradually revert to the original allocation by 2012). In addition, the June 2009 law allows workers to temporarily reduce their second-pillar contributions through 2012.

Sources: *Social Security Programs Throughout the World: Europe, 2008*; "Baltic States," *International Update*, August 2009, U.S. Social Security Administration; "Estonia May Raise of Retirement Age," *RIA Oreanda News Agency*, March 22, 2010; "International Headlines," *Mercer*, April 7, 2010; "Estonian Government Backs Increased Retirement Age," *HIS Global Insight Daily Analysis*, April 9, 2010.

Switzerland

In a March 7 referendum, Swiss voters rejected a parliamentary-approved law, which would have further lowered the conversion rate used to calculate individual annuities for mandatory occupational pension plans. Actuarial experts had advised the government to lower the conversion rate in anticipation of declining investment returns and increasing life expectancy of the Swiss population. The referendum outcome (73 percent against the change in the conversion rate) was interpreted as reflecting widespread uneasiness among voters about the future level of retirement incomes. Following the referendum, the government announced that parliamentary negotiations would be needed to build a new consensus regarding future levels of retirement earnings.

When the mandatory second-pillar pension law was introduced in 1985, the conversion rate was fixed at 7.2 percent, and this remained in place through 2004. In the first revision of the law, the conversion rate was to be reduced, depending on age and sex, to between 6.8 percent and 7.15 percent over a 10-year period starting in January 2005. The new law, which was rejected on March 10, would have further lowered the conversion rate to 6.4 percent by 2016. The conversion rate is considered the legal minimum, and pension funds are free to use higher rates.

The mandatory occupational pension plans supplement the Swiss compulsory public pension program, financed on a pay-as-you-go basis. The net replacement rate after taxes for the first two pillars (public pension and occupational pension) amounts to 70–80 percent of preretirement income, on average. A third pillar is composed of various voluntary tax-exempt savings vehicles operated by the country's banking and insurance institutions.

Sources: "Switzerland," *International Update*, October 2004, U.S. Social Security Administration; "Should You Take A Lump-Sum or Annuitize? Results from Swiss Pension Funds," CESIFO Working Paper No. 1610, November 2005; "Swiss Pension Plans for SMI Companies," Towers Watson, 2009; "Referendum Result: No Reduction in the Minimum Conversion Rate," Credit Suisse Pension Fund, March 2010; "Swiss Voters Reject Government-Backed Occupational Pension Scheme," HIS Global Insight Daily

Analysis, March 8, 2010; "Seven in Ten Voted Against Swiss Conversion Rate Cut," IPE.com, March 8, 2010.

United Kingdom

The Pensions Regulator (TPR) recently released *The Corporate plan: 2010-2013*, the latest 3-year agenda of the regulator of work-based pension plans in the United Kingdom. Among the themes listed are strategies to improve pension plan governance and administration, reduce risks to defined benefit (DB) and defined contribution (DC) plan members, prepare for the impact from mandatory automatic enrollment of employees into work-based pension plans in 2012, and improve regulatory practices.

According to the agenda, from 2010–2013, the regulator will—

- Continue to emphasize to trustees the importance of setting prudent funding targets and encourage them to work with employers to resolve plan deficits quickly;
- Support employers in carrying out their duties related to automatic enrollment (beginning in 2012), while designing and building an effective compliance regime;
- Monitor DC plan trustees and providers to ensure that plans are effectively administered and suited to members' needs;
- Improve standards of DB plan administration (such as better recordkeeping);
- Continue to monitor transfers of pension risk away from employers to ensure that, where such practices occur, plan members' benefits are protected;
- Continue to direct agency resources to areas posing the greatest risk to pension plan members, educate and guide the pension industry on best practices, and reduce the risk from claims on the Pension Protect Fund (which provides compensation to members of eligible DB plans where sponsoring employers become insolvent and plan assets insufficient).

The document also discusses the recent update of TPR's Web site design, including the use of simple guides for those new to pensions as well as regulatory guidance and codes of practice for the more traditional audience of trustees and pension professionals. Separately, TPR recently announced the forthcoming release of a leaflet to inform employers of their new duties under the upcoming workplace pension reform. TPR will soon be consulting with employers regarding their duties and the agency's enforcement strategy for the automatic enrollment of employees in pension plans beginning in 2012.

The full report is available at http://www.thepensionsregulator.gov.uk/docs/corporate-plan-2010-2013.pdf.

Sources: "UK Pensions Regulator Announces Three-Year Agenda," Plansponsor.com, March 30, 2010; The Pensions Regulator press release, March 30, 2010.

Asia and the Pacific

Australia

On April 22, the government-appointed Super System Review panel, formed in May 2009 to examine the country's nearly 20-year-old superannuation system, issued a preliminary report on the superannuation industry regulatory structure entitled *MySuper: Optimising Australian Superannuation*. This report is the third in the series; the first one, released in December 2009, dealt with governance of superannuation funds, and the second report, released in March 2010, focused on the operational aspects of the superfund industry. The final report, covering all three topics, is expected to be released on June 30, 2010.

The latest report focuses on the issue of choice, outlined in the panel's December 2009 report on governance. The panel found that the current regulatory infrastructure of the superannuation industry is too complex and costly for most workers; most workers do not actively choose a fund, and the fees associated with the funds disproportionately affect smaller accounts. Current research indicates that more than 80 percent of Australian workers are in a default superannuation fund, and the average account balance for all workers is less than A$25,000 (US$23,170).

The panel recommends creating a type of simple low-cost, diversified fund called MySuper, which would replace the default funds throughout the industry. Both fees on contributions and "trailing commissions" (an annual fee paid to a sales agent for as long as the client's money remains in an account) would be prohibited. A separate report commissioned by the panel found that if MySuper was implemented, the cost of this new type of fund for some members could be at least half of their current costs.

MySuper would also require automatic enrollment in survivors insurance with an opt-out provision; providers would be allowed to offer disability insurance as well. In addition, the panel envisions some type of "postretirement product," such as annuities associated with MySuper. These products would have to be developed together with the superannuation industry. The government wants to change the current widespread practice of taking a lump-sum benefit at retirement in favor of annuities and other forms of periodic payments.

The full report is available at http://www.supersystemreview.gov.au/content/downloads/mysuper_paper/mysuper_second_phase_one_20100420.pdf.

Sources: "Australia," *International Update*, January and April 2010, U.S. Social Security Administration; *MySuper: Optimising Australian Superannuation*, Australian Government, April 20, 2010; Australian Government press release, April 20, 2010.

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