Focus on France

The 2010 Reform of the French Old-Age Pension Program

On November 10, a major reform of France’s public pay-as-you-go (PAYG) system for private-sector workers became law. The law includes a series of measures aimed at delaying the transition from work to retirement, including an increase in the legal retirement age (for both men and women) from age 60 to 62 and from age 65 to 67, at which point a full retirement benefit can be received without reduction (provided all other contribution requirements are met). The reform law also introduces a series of other changes to address issues such as easing the transition to retirement of workers in arduous and dangerous occupations, improving the employment prospects of older workers, and reducing the retirement income differential between men and women.

Background

In contrast to other industrialized countries with mature social security systems, France has a long history of frequent pension reforms, dating from the inception of the current system in the immediate aftermath of World War II. Successive governments have attempted to stabilize the financing of the French old-age pension system, most recently in 1993, 1999, 2002, and 2007. The current government had originally scheduled a major pension reform to occur in 2012, but the sharply deteriorating financial situation of the basic old-age pension system (regime général d’assurance vieillesse des travailleurs salariés, or CNAV) prompted them to embark on the reform in 2010. While the current economic slowdown in France contributed to the financial disequilibrium, the principal cause is the rapid aging of the French working population. From 1960 to 2010, the number of active contributors for each pensioner fell from 4:1 to 1.8, respectively, with a further decline to 1:2 contributors projected by 2050. Despite the fact that France has one of the higher birth rates among European countries, the French pension system has been negatively impacted by the aging of the baby boom generation, as well as by marked French preference for early retirement, with the average worker currently retiring at age 59.4 compared to the European average of 61.2.

The annual deficit of the basic old-age pension program was estimated at 32 billion euros (US$42 billion) in 2010, and it is projected to rise to 70 billion euros (US$92 billion) in 2030 and to 102 billion euros (US$135 billion) in 2050. In April 2010, the government of President Nicolas Sarkozy released a preliminary document outlining its plans for the reform of the basic PAYG pension program, which covers the majority of workers in the private sector. In proposing the reform, the government moved to gain popular support by eliminating from the outset certain approaches for tackling the financial crisis of the pension system, including any move to a funded individual account approach for financing, a reduction of benefits for current pensioners, or a lowering of the replacement rate for future pensioners. The government’s draft law was submitted to Parliament in June 2010, setting off widespread protest strikes led by French labor unions, as well as an intense political debate.

Key Elements of the Reform Package

- **Raising the legal retirement age.** This provision has undoubtedly attracted the most attention (and opposition) from the French stakeholders. From the financing standpoint, it is the most significant change, estimated to save the system some 20 billion euros (US$26 billion) by 2018. The law gradually increases the legal retirement age from the current age of 60 for insured persons born after 1951, reaching age 62 by 2018.

- **Increasing the retirement age for full benefits.** The 2010 law also introduces an important change with respect to the age at which the pension can be received without penalty of reduction, gradually raising it for insured persons born after 1951 from
Special Early Retirement Provisions

The provision that raised the retirement age to 67 to receive full benefits drew considerable criticism from labor unions and advocates for disabled persons, who were quick to point out that the new requirements could fall heavily on workers who are, for one reason or another, unable to complete a full career for pension purposes. The final reform legislation, therefore, contains a number of provisions to address this criticism and to open the door to earlier retirement options for certain subgroups of the population.

The new legislation introduces an early retirement option for workers who have been exposed to arduous and dangerous workplaces. Beneficiaries of this new early retirement benefit may exit the labor force as early as age 60, provided they are able to prove a disability evaluated at 20 percent of total incapacity (10 percent in certain exceptional cases) that is directly related to dangerous and arduous conditions experienced at the workplace. Moreover, the amount of the benefit will not be subject to an actuarial reduction regardless of the number of years of contributions to the old-age insurance program. An estimated 30,000 persons out of an annual total of 700,000 new beneficiaries are expected to benefit from this new early retirement option.

In an effort to limit the number of workers who qualify for this new provision, the 2010 reform legislation includes new requirements for employers to protect workers from undue exposure to dangerous and arduous working conditions. Effective 2012, employers must maintain records of employees who are exposed on a continuing basis to physically demanding tasks as well as repetitive and high-pressured work. These records, which will also be available to workers, will include information on the type and length of exposure, as well as the preventive measures taken by the employer. Employers with 50 or more workers will be required to submit to the government a copy of the collective bargaining agreement or an action plan to address the exposure of workers to dangerous and arduous conditions. Workers may be eligible for compensatory benefits (part-time arrangements, supplementary paid holidays, bonuses, and so forth) if they have been consistently exposed to arduous working conditions, but are not yet eligible for an early retirement benefit. In creating this new early retirement benefit, the French government steered away from an approach that would have designated certain professions as being dangerous or arduous, but rather based the new right on an individual’s documented exposure over the working life to unhealthy working conditions.

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Other subgroups of the population also are singled out in the new law as being eligible for early retirement options, including the following.

- Workers who began their careers from ages 14 through 17 will continue to benefit from early retirement as early as age 58.
- Mothers born before 1956 with three children, who have interrupted their working careers to raise at least one of the children, will continue to be eligible for retirement at age 65 without a reduction in benefits.
- Disabled workers will be able to benefit from early retirement at age 55.

Women and the 2010 Reform

During the course of the energetic public debate leading up to the adoption of the 2010 reform, the issue arose as to whether women would be winners or losers in the outcome of the reform. The government response was to emphasize that the principal reason that women have generally received less pension income (on average about one-third less) than men is that they generally have shorter work histories and work for less pay. This gap is however gradually narrowing. A possible explanation provided by the government is that special measures promulgated over the years to protect women who bear children are finally paying off. Among those measures, a mother receives 2 years of pension contribution credits for each child, regardless of whether or not she ceases to be employed to care for a child (one year of credit may be shared with the father if both parents agree).
Additional credits are paid on behalf of mothers who choose to remain at home for limited periods to care for a child; approximately 2 million women currently receive these additional credits each year.

The 2010 reform takes a step further to help women earn higher pensions by fully taking into account cash maternity benefits as earnings when calculating entitlement to retirement benefits. These measures as well as other labor regulations appear to be having a gradual impact on lengthening the number of contribution years women are acquiring for pension purposes. It is estimated that women aged 45 or older may arrive at retirement with an equal or even higher number of contribution years than men.

The new pension law, moreover, reinforces existing measures that make it illegal to pay unequal compensation to men and women. Along with similar measures on behalf of older workers, the reform law requires that employers develop an action plan to reduce any existing earnings gaps between men and women. If a plan is not submitted nor approved by the government, the employer will be liable for fines equal to 1 percent or more of the combined payroll of all the employees of the enterprise.


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**Europe**

**Norway**

In an effort to address rising pension expenditures because of the rapid aging of Norway’s population, extensive reforms to the existing pay-as-you-go National Insurance Scheme will be implemented on January 1, 2011. The reforms, which are likely to produce lower benefits (especially for high earners), include a flexible retirement age and modified indexation rules that aim to encourage longer working lives and link benefits to longevity trends. The reforms will be phased in based on year of birth. Norwegians born in 1963 or later will have their pension based entirely on the reformed system, while benefits for those born from 1943 through 1953 will accrue benefits entirely according to the old rules. Under transition rules for those born from 1954 through 1962, benefits will accrue proportionally under both regimes. Without reform, the government forecasts that old-age pension benefits as a percentage of gross domestic product would increase from approximately 6 percent in 2001 to approximately 15 percent in 2050. Over roughly the same time, the ratio of workers to pensioners is expected to decline from 4.6:1 in 2006 to 2.7:1 in 2050.

Key elements of the reformed pension system include the following.

- **A flexible retirement age ranging from ages 62 to 75 that will be phased in beginning in 2011.** Individuals will be able to draw a pension and continue to work; the benefit amount will be adjusted by a longevity factor based on the age of the individual at the time of retirement. Under the current rules, the normal retirement age is 67, and individuals can defer their pension past that age—up to age 70—and accumulate credit toward a higher benefit.

- **A change in the calculation of old-age benefits to be based on the worker’s average lifetime contributions (from ages 13 to 75) plus credits for missing periods that are due to unemployment or caregiving.** In addition, pension benefits will be adjusted annually by wage growth minus 0.75 percentage points (benefits will not be adjusted downward in the event of declining wages). Currently, a pension is calculated on the highest 20 years of earnings (for a full benefit after working a maximum of 40 years), and benefits are indexed to national wage changes.

- **An income-tested pension that will replace the current flat-rate contributory public pension.** The new income-tested pension is guaranteed to be at least as high as the minimum pension payable under current law.

Public old-age benefits in Norway currently consist of a flat-rate contributory pension, a special supplement (paid to individuals with low income), and an earnings-related pension. Together, the flat-rate contributory pension (granted to residents who have lived in Norway for 3 or more years from ages 17 through 66) and the supplement form the minimum pension. Mandatory occupational pensions supplement the public benefit.

The Americas

**Bolivia**

On December 10, a new pension reform law entered into force that lowers the retirement age and nationalizes the system of individual accounts. Provisions of the new law will be implemented in 2011 and include—

- **Lowering the retirement age from 65 to 58 for both men and women and to even younger ages for mothers and miners.** Mothers will be able to retire 1 year earlier for each child up to a maximum of 3 children. Miners will be permitted to retire at age 56 or younger, with a reduction of 1 year for every 2 years worked in the interior of a mine, up to a maximum reduction of 5 years.

- **Transferring management of the system’s two pension funds to a new government agency, the Long-Term Social Security Manager.** Workers will continue to pay a monthly administrative fee of 0.5 percent of earnings. Currently, two foreign companies manage some 34 billion bolivianos (US$5 billion) for about 1.3 million workers.

- **Setting up a solidarity benefit for those workers who do not qualify for a guaranteed minimum benefit (180 months of contributions), but have at least 10 years of contributions.** A solidarity fund will subsidize these benefits and will be financed by contributions from workers (0.5 percent of earnings), employers (3 percent of payroll), and an additional contribution from workers earning more than 13,000 bolivianos (US$1,900) per month (the amount of the additional contribution is not yet specified).

The current system of individual accounts replaced the public pay-as-you-go system in 1997. All salaried workers including armed forces personnel are covered by the system; participation for the self-employed is voluntary. Account holders are required to contribute 10 percent of earnings per month to an individual account; employers may make voluntary contributions on behalf of employees.


**Chile**

The Central Bank of Chile raised the pension funds’ limit on foreign investment to allow them to further diversify their portfolios. The overall percentage of assets permitted in foreign instruments rose from 60 percent to 65 percent on December 1, 2010, and will continue to increase by 5 percent every 3 months until it reaches 80 percent on September 1, 2011. These figures represent the overall limit for each pension fund management company (AFPs). AFPs offer five different types of pension funds with varying risk and return options; their allowable investments (both domestic and foreign) range from a maximum of 80 percent in variable-rate instruments (such as equities) for Fund A to 5 percent for Fund E. In addition to the increase in the overall ceiling, the Central Bank has set new limits on foreign investment for each fund type, shown in Table 1.

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SOURCE: Banco Central de Chile, Comunicado de Prensa, el 4 de noviembre de 2010.

At the end of October 2010, total assets under management for all six AFPs were 68 trillion pesos (US$140 billion), and 47.5 percent of these assets were invested abroad (ranging from 71.4 percent for Fund A to 4.8 percent for Fund E).

According to the rules for the Chilean “multifunds,” workers (up to age 55 for men and 50 for women) may choose any of the five funds throughout their working lives; older workers are not permitted to select Fund A, the riskiest. Those who do not make a choice are automatically assigned according to their age (for example, for Fund B, up to age 35 for both men and women). As of May 2010, about 60 percent of account holders had been assigned to a fund.

Sources: “¿Cómo Se Diferencian los Distintos Tipos de Fondos?” Superintendencia de Pensiones, 2010; “Multifondos: Resultados y Tendencias,” Número 69, junio 2010; Banco Central de Chile, Comunicado de Prensa, el 4 de noviembre de 2010; “Chile: El Banco Central Sube Límite de Inversión...”
Kenya

The Minister of Finance recently announced a change in the early withdrawal rules for Kenya’s voluntary occupational pension plans. Under the new rules, workers who leave their jobs before reaching the normal retirement age of 60 (for both men and women) may withdraw their own contributions with accumulated interest, as well as 50 percent of employer contributions, provided they contributed to the occupational pension plan for at least 3 years. Any remaining funds must stay in the account until the worker reaches the normal retirement age. The new rules reverse a law passed in June 2005 that restricted early withdrawals to only a worker’s own contributions.

The change in the early withdrawal rules comes amid concern that many workers would not live long enough to receive their retirement funds. According to estimates by the World Health Organization, life expectancies at birth are 53 years for men and 55 years for women, and are thus significantly lower than the normal retirement age of 60.

As of 2007, there are approximately 1,357 occupational pension plans in Kenya, with total assets under management currently estimated at 200 million shillings (US$2.5 million). The voluntary occupational pension plans supplement a provident fund program administered by the National Social Security Fund.