Social Security

International Update:

Recent Developments in Foreign Public and Private Pensions

October 2013

Europe

Belarus

On September 3, the president of Belarus signed a decree that increases the minimum contribution period to qualify for an old-age pension, from 5 years of paid contributions to 10 years, effective January 1, 2014. According to the government, the change is necessary to improve the long-term sustainability of the country's pay-as-you-go (PAYG) public pension program in the face of rapid population aging. Recent data from the United Nations project an increase in the old-age dependency ratio—the population aged 65 or older as a percentage of the population aged 15 to 64—from around 20 percent in 2010 to 36 percent in 2050 (under a medium fertility scenario). At the same time, the total population of the country is expected to have one of the steepest declines in the world, from the current 9.4 million to 7.4 million in 2050 (a decrease of 21.3 percent).

Belarus's PAYG public pension program covers all employed people residing permanently in the country and is financed by an employee contribution of 1 percent of earnings and an employer contribution that varies according to industry and business. (Most employers contribute 28 percent of gross payroll.) The retirement age is 60 for men and 55 for women. The full pension is paid with 25 years (men) or 20 years (women) of coverage, and a partial pension is paid to those with fewer years of coverage. Nonworking citizens who are not eligible for a social insurance benefit but are at least age 60 (men) or age 55 (women) may receive a social assistance benefit that is financed by the government.

Sources: *Social Security Programs Throughout the World: Europe, 2012*, US Social Security Administration, 2012; *World Population Prospects: The 2012 Revision*, United Nations, 2012; Ministry of Taxes and Duties press release, September 4, 2013; "Pensions: Lower Guarantees for the Sake of Stability," *Belarus in Focus*, September 10, 2013; "The Minimum Contribution Period for a Belarus State Pension is Doubled to 10 Years," *Mercer*, September 12, 2013.

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The Americas

Inter-American Development Bank Report

On October 16, the Inter-American Development Bank released *Mejores Pensiones Mejores Trabajos (Better Pensions Better Jobs),* which examines ways to improve low pension coverage in Latin America and the Caribbean. According to the report, despite major pension reforms in the region, currently only about 40 percent of adults aged 65 or older receive a contributory pension and about 20 percent receive a noncontributory pension. However, most of the contributory and noncontributory pensions are not high enough to eliminate old-age poverty or to maintain an adequate standard of living. In addition, because of rapid population aging, the ratio of workers to adults aged 65 or older is projected to fall from the current 9.6:1 to 3.2:1 by 2050; with no changes, the cost of noncontributory pensions across the region could almost triple from the current 1 percent of gross domestic product.

The report emphasizes the relationship between low coverage and the size of the informal labor force. A large informal labor force most often means that a high proportion of the labor force is not covered by social security. Only about 45 percent of workers in the region contribute to a pension system because the majority of workers are in the informal sector; those workers include low-income earners and workers in small companies, many of whom constitute the emerging middle class. Even among workers who contribute to a pension system, many may not qualify for a benefit because they often switch between formal and informal employment. The report finds that 21 percent of workers in the formal labor market (both salaried and nonsalaried workers) will not be there within the year.

The report presents a number of reasons for the large informal labor force, including the following:

- Many systems exclude the self-employed (also called nonsalaried workers).
- The costs to the formal sector set by the state can be as high as 50 percent of payroll, which include pensions, health, and other costs such as unemployment insurance.
- The process of monitoring and enforcing the rules is often weak.

The report argues that it is possible to move toward universal coverage and create more jobs in the formal sector. The recommendations include—

- Introducing an antipoverty noncontributory pension for all citizens with strict eligibility criteria, a stable long-term financing source, a strong institutional structure, and protection from the political cycle;
- Gradually incorporating nonsalaried workers who traditionally have been excluded from social security;
- Setting up special administrative mechanisms to facilitate contributions;
- Subsidizing retirement savings in the labor market;
- Monitoring and enforcing the rules; and
- Providing information and financial education.

Source: *Mejores Pensiones Mejores Trabajos: Hacia La Cobertura Universal en América Latina y el Caribe,* Banco Interamericano de Desarrollo, junio 2013.

Asia and the Pacific

India

On September 18, the Pension Fund Regulatory and Development Authority (PFRDA) Act 2013 received presidential assent, formalizing PFRDA's status as pension regulator of the National Pension System (NPS) after nearly 10 years of operation under a provisional mandate. In the absence of statutory authority, PFRDA did not have the power to take action against asset managers, annuity providers, and other market participants without going to court; it now has that authority. The regulator's new status is expected to increase private-sector pension participation and open up the pension sector to foreign investment. Only around 12 percent of the estimated 460 million workers in India's labor force are covered by a formal pension plan or provident fund.

Pension experts expect the law to attract more NPS subscribers with a number of measures that include—

- Introducing an option for minimum assured returns on specific investment products; and
- Allowing domestic pension fund managers to forge joint ventures with foreign funds (up to 26 percent ownership) in an effort to obtain greater expertise in managing long-term savings, foster competition, and ensure higher returns for investors.

Depending on an individual subscriber's choice of risk-return portfolio, the NPS continues to offer market-linked products through a variety of investment choices: equities (in which subscribers have the option to place up to half of their account) and government and corporate bonds (managed professionally by private fund managers from which subscribers can choose). If no pension manager is selected, contributions are invested in a life-cycle portfolio based on a subscriber's age.

PFRDA was established by executive order on an interim basis in August 2003 after India's Parliament failed to pass the necessary legislation. (Subsequent unsuccessful legislative attempts to formalize its status also occurred in 2005 and 2011.) Since January 1, 2004, the NPS has been mandatory for new public employees of the central government and of state governments that adopted the program. The system was open on a voluntary basis to the private sector on May 1, 2009. PFRDA currently oversees eight pension fund managers for private-sector employees and three fund managers for central and state government employees. In August 2013, the total number of NPS subscribers, including government employees, was roughly 52.8 million, or 1.1 percent of India's workforce, with total assets under management of 350 billion rupees (US$5.7 billion).

Sources: "With BJP Support, Pension Bill Gets Nod After 8 Years," ENS Economic Bureau, September 5, 2013; "An Empowered Pension Regulator at Last," livemint.com, September 10, 2013; "Does the Changed NPS Work Any Better?" *Hindustan Times*, September 14, 2013; "India: New Pension Law Enhances Framework for National Pension System," Towers Watson, September 26, 2013; "Rebooting Pensions," *The Financial Express*, September 30, 2013.

New Zealand

On October 17, the government announced that KiwiSaver default providers will maintain the same conservative investment strategy with 15 to 25 percent invested in growth funds, rather than moving to a life-cycle approach based on a member's age, as proposed by fund managers. The government indicated that the conservative approach offers stable returns that can build confidence in KiwiSaver, and that default funds should be considered temporary until members find the best fund for themselves. KiwiSaver, introduced in 2007, is a type of subsidized retirement savings plan that supplements the country's flat-rate universal pension, known as New Zealand Superannuation (funded by general revenues). New entrants to the labor force and new employees who do not have a KiwiSaver account are automatically enrolled in a KiwiSaver plan, but may opt out. Those workers who do not choose a provider are assigned to one of the default providers.

The decision to continue the same investment strategy followed the government's review of the default providers. As a result, the government also kept the same selection criteria for default providers in the next tender (to be held later this year); those criteria include investment capability, governance, experienced senior management, sound risk-management policies, appropriate default and nondefault products, and the ability to offer competitive fees. In addition, a new requirement will be added: Default providers will have to offer financial education and impartial financial advice to account holders (by actively contacting them).

Because the 7-year term for the current five default providers ends in June 2014, the government expects to choose up to 10 providers in the next tender. If a current default provider is not chosen in the next tender, the existing members will have the option to remain with the same provider. If they do not make a choice, they will be redistributed evenly among the approved default providers. At the end of March, about 22 percent of the 2.1 million members were in a default fund. Total KiwiSaver assets under management are NZ$16.6 billion (US$13.8 billion), of which 20.5 percent are held by default providers.

Sources: "Future KiwiSaver Default Provider Arrangements," Offices of the Ministers of Finance and Commerce, 2013; "Default KiwiSaver Funds Stay Conservative," 3 News, October 17, 2013; "KiwiSaver Default Provider Review Completed," beehive.govt.nz, October 17, 2013; *KiwiSaver Report for the Year Ended June 2013*, Financial Markets Authority, October 21, 2013; "New Zealand Publishes KiwiSaver Default Provider Decisions," *Mercer International Highlights,"* October 21, 2013.

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