Europe

Finland Implements Reform to Earnings-Related Pension Program

On January 1, Finland implemented a multipart reform to its earnings-related pension program that increases the retirement age for most workers, alters the periods and rates of benefit accrual, and amends the early and partial retirement options. The government approved the reform in January 2016 after it reached an agreement with Finland’s social partners on changes to the national pension system in September 2014. The government contends that the reform is necessary because the average length of working careers has not kept pace with recent life expectancy gains. (Finnish life expectancy at age 60 increased from 21.5 years in 2000 to 24.1 years in 2015.) The Finnish Centre for Pensions, which oversees the earnings-related pension program, projects that the average effective retirement age in Finland will rise from 60 years and 8 months in 2015 to 62 years and 5 months by 2025, as a result of the reform.

The key provisions of the reform (effective January 1, 2017, unless otherwise noted) include:

- Raising the minimum retirement age gradually (by three months a year) from 63 to 65 for persons born after 1954, and automatically linking future increases (of up to two months a year) to changes in life expectancy.

- Raising the maximum retirement age (the age at which mandatory coverage ceases) from 68 to 69 for persons born from 1958 through 1961 and to age 70 for those born after 1961; it remains age 68 for persons born before 1958.

- Establishing a target retirement age above the minimum retirement age for each age group. Benefits claimed at or after the target retirement age are not subject to reductions for life expectancy. (The benefit formula includes a life expectancy coefficient that adjusts accrued benefits according to changes in life expectancy.)

- Lowering the earliest age for benefit accrual from 18 to 17 for employed persons; it remains age 18 for self-employed persons.

- Standardizing the benefit accrual rate at 1.5 percent of annual earnings across all age groups, up to the maximum retirement age. This change will be fully effective in 2026; from 2017 to 2025, the accrual rates for covered workers are 1.5 percent for those younger than age 53, 1.7 percent for those aged 53 to 62 (down from 1.9 percent), and 1.5 percent for those aged 63 or older (down from 4.5 percent).

- Applying the monthly bonus for deferred benefits at the minimum retirement age rather than the maximum retirement age. For each month the claiming of benefits is deferred past the minimum retirement age, the final pension increases by 0.4 percent (4.8 percent on an annual basis). The bonus is paid on top of the basic benefit accrual rate of 1.5 percent of annual earnings if the insured person works.

- Using total earnings in benefit calculations. (Previously, an insured person’s pension contributions were deducted from the covered earnings used in the calculations.)

- Introducing a years-of-service pension for workers who have had long careers in arduous occupations. Starting in January 2018, workers with at least 38 years of coverage will be eligible to retire at age 63 with no penalty if they can demonstrate that their capacity to work has diminished due to long periods of physically demanding labor.

- Replacing the part-time old-age pension with a partial old-age pension. Starting in February 2017, insured persons can choose to receive either 25 percent or 50 percent of their accrued pensions as early as age 61 (rising to age 62 in 2025, after which it will be linked to life expectancy). However, claiming a partial pension before the minimum retirement age permanently reduces the benefit amount by 0.4 percent for every month of early partial retirement. If a partial pension is claimed after the minimum retirement age, then the monthly bonus of 0.4 percent for deferred benefits
is added to the benefit amount. Unlike the part-time pension it replaces, the partial pension has no work requirements.


Poland Approves Law Lowering Retirement Ages

On December 19, the Polish president signed into law a pension reform bill that reduces the retirement ages under Poland’s multipillar pension system to age 60 for women and age 65 for men. The law, which will go into effect on October 1, 2017, reverses a previously mandated increase in retirement ages passed by the former government in June 2012 and implemented in January 2013. Under that law, the retirement ages were set to gradually increase—by one month in January, May, and September each year—from age 60 to 67 for women (by 2040) and from age 65 to 67 for men (by 2020). (Currently, the retirement ages are 61 and 1 month for women and 66 and 1 month for men.) The reversal, which was a pre-election commitment of the new government, is expected to cost upwards of 10 billion zloty (US$2.4 billion) a year starting in 2018.

Poland’s pension system consists of a public, first-pillar notional defined contribution (NDC) program, a voluntary second pillar of privately managed individual accounts, and a voluntary third pillar of retirement savings accounts. Workers participating in the second pillar contribute 6.84 percent of covered earnings to the NDC program and 2.92 percent of covered earnings (plus up to 1.75 percent of contributions for annual administrative fees) to individual accounts; employers contribute an additional 9.76 percent to the NDC program only. (Employees who opt out of the second pillar contribute the full 9.76 percent to the NDC program.) New entrants to the labor force must choose whether to participate in the second pillar within their first four months of employment.


Asia and the Pacific

Japan’s Legislature Approves Public Pension Reform Provisions

On December 14, Japan’s Diet approved a reform package that includes a reduction in pension benefits—by changing how current benefit payments are adjusted and restricting future pension increases relative to wages and inflation—under the National Pension System (NPS) and Employee Pension Insurance (EPI) system and other minor reforms (mostly affecting the EPI system). The law will be phased in over the next several years. The legislation is designed to ensure the long-term financial sustainability of the public pension system given the aging population, rising costs for old-age benefits, and the economic and wage stagnation observed in recent decades. In the current fiscal year, total pension expenditures exceed 10 percent of Japan’s gross domestic product and are expected to rise significantly as the projected old-age dependency ratio (population aged 65 or older to the working-age population aged 20 to 64) nearly doubles over the next several decades. While the reform will reduce pension benefits, the government aims to ensure that future pension levels of younger workers do not fall too far below those of current retirees and those expected to retire soon.

In 2004, Japan implemented a comprehensive reform to strengthen the public pension system. The reform introduced an automatic adjustment mechanism for pensions (the so-called “macroeconomic slide”), which ensures that benefit increases are less than the rate of inflation or wage increases. This mechanism was intended to address the effects of Japan’s shrinking labor force and increasing life expectancy by gradually reducing benefit levels. However, it does not apply during periods of deflation; hence, benefit levels have only been reduced once (in fiscal year 2015) due to a long period of deflation in the country. Under the new law, starting in fiscal year 2018 (April 1, 2018 through March 31, 2019), the macroeconomic slide mechanism will be modified to include periods of deflation. Any unrealized benefit reduction prevented by a deflationary environment
will be delayed to the next fiscal year or later, until the unused reduction can be applied when consumer prices rise.

In addition, the new law introduces a new method—beginning in fiscal year 2021 (April 1, 2021 through March 31, 2022)—that changes the relationship of pension amounts to the movements in wages and prices. Under the current system, only if both average earnings and inflation decrease are pensions adjusted downward, and then by the decline in inflation. The new method will reduce pensions if only average earnings fall without reference to inflation.

Additional minor changes introduced by the new law include:

- In April 2017, mandatory coverage of part-time employees will be extended under the EPI system to companies with fewer than 500 employees. In October 2016, coverage for part-time employees was initially required for large companies (500 or more employees) by reducing the monthly salary threshold for EPI registration from 108,333 yen (US$925) to 88,333 yen (US$755) and by lowering the required weekly number of hours worked from 30 to 20. To qualify under the latest rules, part-time employees in all firms (both large and small) must still work at least 20 hours a week, but they only need to earn 88,000 yen (US$752) or more per month.

- In October 2017, certain governance changes will be made to the Government Pension Investment Fund, the reserve fund for the public pension system.

- In April 2019, new mothers will begin receiving a four-month exemption from EPI premium payments.

Japan has a pay-as-you-go public pension system that includes two major programs: the earnings-related EPI and the flat-rate NPS. Historically, the NPS has covered all residents, including lower-wage and part-time employees, while the EPI has covered full-time employees. Individuals who do not satisfy the EPI salary threshold are required to join the NPS. NPS members make all contributions themselves, while employers and employees share EPI contributions.


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**Uruguay and the United States Sign Totalization Agreement**

On January 10, the United States and Uruguay signed a totalization agreement to exempt U.S. and Uruguayan employers and workers from dual social security tax liability. Before the agreement can enter into force, each country has to complete a review process: The Uruguayan General Assembly must ratify the agreement; in the United States, the president must transmit the agreement to Congress for a required 60-day review period.

The agreement will exempt U.S. citizens sent by U.S.-owned companies to work in Uruguay for five years or less from paying social security taxes to Uruguay. Uruguayan citizens sent to work temporarily in the United States by Uruguayan-owned companies will receive similar tax treatment. As a result, employers will pay social security taxes only to their workers’ home countries.

Individuals who have worked in both countries but do not meet the minimum benefit eligibility requirements for either system may qualify for a benefit based on combined coverage credits from both countries. Combined coverage periods may be used to calculate retirement, disability, and survivor benefits.

At present, the United States has totalization agreements with 26 countries. In addition, recently signed agreements with Brazil and Iceland are currently in the review process.

**Sources:** E-mail communication with the Office of International Programs, U.S. Social Security Administration, January 2017; U.S. International Social Security Agreements, U.S. Social Security Administration, https://www.socialsecurity.gov/international/agreements_overview.html.