International Update

Recent Developments in Foreign Public and Private Pensions

August 2018

Europe

Lithuania Modifies Social Security Contribution Rates and Introduces a Covered Earnings Ceiling

On June 28, the Lithuanian Parliament approved a law that modifies employer and employee social security contribution rates and introduces a covered earnings ceiling for contributions, effective January 2019. Under the new law, the employer contribution rate will fall from 31.18 percent of monthly payroll to 1.47 percent, and the employee contribution rate will rise from 9 percent of monthly earnings to 19.5 percent. (Employee contributions finance old-age, disability, and survivor pensions; and medical benefits. Employer contributions finance old-age, disability, and survivor pensions; cash sickness and maternity benefits; medical benefits; work injury benefits; and unemployment benefits.) Contributions will be paid on earnings up to a new annual covered earnings ceiling set at 120 times the average monthly wage in the previous year for 2019, 84 times the average monthly wage in the previous year for 2020, and 60 times the average monthly wage in the previous year for 2021 and onwards. (The ceiling does not apply to contributions to medical benefits.) The new law is part of a series of laws passed in late June that include an increase in personal income taxes (by shifting from a flat-rate tax of 15 percent to a progressive tax of 20 or 27 percent, depending on earnings) and a statutory wage increase to compensate for the higher income tax and social security contribution rates. According to the government, the reforms aim to reduce the cost of labor to businesses and make the social security contribution system more transparent.

Lithuania's pension system consists of a social insurance program, a voluntary individual account program, and a social assistance program. The social insurance program covers public- and private-sector employees, self-employed persons, and certain other persons. To receive an old-age pension, a worker must have reached the normal retirement age of 63 and 8 months (men, gradually rising by 2 months a year until reaching age 65 in 2026) or 62 and 4 months (women, gradually rising by 4 months a year until reaching age 65 in 2026) and have at least 15 years of contributions. The full pension is paid with at least 30 years and 6 months (gradually rising to 35 years in 2027) of contributions. The individual account program was introduced in 2004 and covers all employed persons younger than the normal retirement age; while participation is voluntary, once enrolled, the decision may not be reversed. Upon reaching the normal retirement age, workers must generally use their accumulated assets to purchase an annuity. The social assistance old-age pension is paid at the normal retirement age to workers who have less than 15 years of contributions.

Sources: Seimas of the Republic of Lithuania press releases, June 28, 2018; "Seimas Galutinai Palaimino Mokesciu Reforma," Verslo Zinios, June 28, 2018; "Lithuanian Reforms Lower Tax Burden for 1.3 Million," Atlas Network, July 13, 2018; "Lithuania – Individual Tax Reform Sees Burden Shifted to Employees," KPMG, July 17, 2018; *Social Security Programs Throughout the World: Europe, 2018*, U.S. Social Security Administration, September 2018 (forthcoming).

Asia and the Pacific

Australia Implements New Superannuation Rules for Home Purchases and Sales

On July 1, the Australian government implemented new rules under the country's superannuation program that allow participants to use a portion of their account balances for first-time home purchases and to make special contributions after selling their homes at age 65 or later. Under the rules of the First Home Super Saver (FHSS) measure, participants can withdraw up to A$30,000 (US$22,200) of their voluntary contributions plus any earnings on those contributions to help cover the down payment on a first home. By contrast, under the rules of the Downsizer Contribution measure, participants aged 65 or older can contribute up to A$300,000 (US$222,000) of the proceeds from selling a home. (For a couple, each qualifying member can contribute up to A$300,000.)

The two measures are intended to help younger Australians become homeowners by giving them access to more financial resources and encouraging older Australians to move into more age-appropriate housing. According to data from the Organisation for Economic Co-operation and Development (OECD), housing prices across Australia have risen by around 42 percent since 2010, and by nearly double that percentage in certain urban areas.

To take advantage of the FHSS measure, a superannuation participant must be aged 18 or older and have never owned property in Australia (though exceptions may be made in cases of financial hardship). The participant can allocate up to A$15,000 (US$11,100) of his or her voluntary concessional (before-tax) and/or nonconcessional (after-tax) contributions toward a first-time home purchase (up to a total of A$30,000). The participant must currently reside or intend to reside in the purchased property.

To qualify for the Downsizer Contribution measure, a participant must have lived in the sold home for at least 10 years. The sale proceeds contribution is not a nonconcessional contribution and does not count toward contribution or account balance limits. However, the contribution does count toward the A$1.60 million (US$1.18 million) lifetime transfer balance cap. (This cap limits the amount of superannuation savings that a participant can transfer into retirement plans providing tax-free income.)

Australia's superannuation program is a mandatory occupational pension program covering employees with gross monthly earnings of at least A$450 (US$334). Under the program, employers must contribute 9.5 percent of payroll (gradually rising by 0.5 percentage points a year from 2021 until reaching 12 percent in 2025) to privately managed superannuation funds. Although employees are not required to contribute, the government offers tax incentives and matching funds to encourage voluntary contributions. To receive old-age benefits, an individual must be aged 57 or older (gradually rising to age 60 by July 2024) and permanently retired (or in an approved transition-to-retirement arrangement). Retirees with fewer financial resources may also be eligible for the means-tested noncontributory Age Pension and various supplemental benefits financed and administered by the Australian government.

Sources: First Home Super Saver Tax Act 2017; Treasury Laws Amendment (Reducing Pressure on Housing Affordability Measures No. 1) Act 2017; *Social Security Programs Throughout the World: Asia and the Pacific, 2016*, U.S. Social Security Administration, March 2017; "Federal Budget 2017: Prospective Buyers Welcome First Home Super Saver Scheme," Australian Broadcasting Corporation, May 9, 2017; Federal Budget 2017: Super and Downsizing Plans Welcomed for Older Australians," *Sydney Morning Herald*, May 9, 2017; "First Home Super Saver Scheme," Australian Taxation Office, June 28, 2018; "Downsizing contributions into superannuation," Australian Taxation Office June 29, 2018; "Residential Property Price Indices," OECD Statistics, August 8, 2018.

International

Organisation for Economic Co-operation and Development Releases Report on the Effects of New Financial Technology

On April 9, the Organisation for Economic Co-operation and Development (OECD) released *Financial Markets, Insurance and Pensions: Digitalisation and Finance*, a report examining the financial market, insurance, and pension effects of rapid advances in financial services digital technology (or Fintech). (Fintech includes several new and emerging technologies—including big data, cloud-based computing, artificial intelligence, and biometric technology—that affect how consumers engage with financial service providers.) The report provides an analytical framework for understanding recent developments in financial markets driven by advances in Fintech, and examines how these developments have affected the management and delivery of insurance and pensions. It concludes by providing specific examples of Fintech, including robo-advisors that help individuals manage their pension savings.

In the chapter on pensions, the report finds that Fintech has had positive effects on pension design and delivery. In particular, the report's key findings include:

- *Better accessibility*: Fintech has increased the accessibility of pensions by improving communications between pension providers and savers, giving savers more control over their investments and greater participation in financial decisions. These developments are particularly important for millennials (persons born from 1980 to 2000), who expect to use technology to access financial services.
- *Increased transparency*: Fintech has increased trust in pension plans by making them more transparent and comprehensible for savers.
- *Increased efficiency:* Fintech has simplified the management of pension plans by allowing savers to

manage more of their own data. By making pension management more efficient, Fintech can lower the cost of private pension products.

- *Greater government involvement:* Governments in OECD-member countries have supported the development of new Fintech by establishing special regulatory mechanisms and helping pension providers better understand existing regulatory requirements. In addition, several countries have implemented online pension dashboards that enable pension savers and beneficiaries to keep track of multiple pension accounts using one application.

The report offers robo-advisors as an example of a Fintech that can improve the design and delivery of pensions. Robo-advisors provide automated financial planning services to pension savers, often at a lower cost than traditional human advisors. These automated advisors can be particularly useful for individuals who manage their own investments—such as personal savers and defined contribution pension plan members—because they typically face numerous financial choices and have fewer accumulated savings to manage. Other advantages offered by robo-advisors include automatic portfolio rebalancing to maintain a desired level of risk, automatic reinvestment of dividends, financial education, and various self-directed tools to aid financial planning. To protect pension savers, however, the report urges governments to extend their financial protection laws—including those dealing with conflict of interest, transparency, and disclosure—to robo-advisors.

While the report highlights the benefits of Fintech, it also notes that the rapid pace of change in digital technologies and financial services can have negative consequences for pension savers. For example, Fintech can exclude individuals who do not use digital communications, while Fintech users might place too much trust in technological solutions. In addition, data privacy and security risks increase as pension providers use larger quantities of data to deliver improved services that may fall outside the scope of existing financial regulations.

Source: *Financial Markets, Insurance and Pensions: Digitalisation and Finance*, Organisation for Economic Co-operation and Development, April 9, 2018.

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