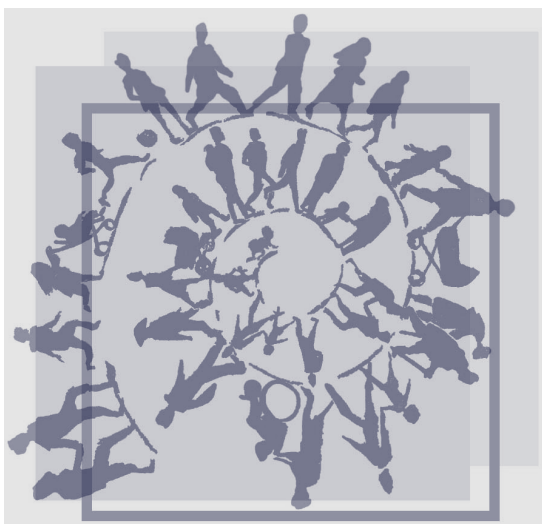




*Adequate pensions at a lower cost
to public budgets: is it possible?*

Between rules, discretion and good
policy making: balancing pensions'
adequacy and sustainability



THE POLISH PRESIDENCY SEMINAR ON
SUSTAINABLE PENSIONS
29-30 SEPTEMBER, CRACOW

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Defining pension adequacy

- Adequacy and sustainability as joint and interlinked objectives of social policy
- Adequacy is defined nationally as part of the broader implicit or explicit social contract which sets the design of the pension system
- There are also accepted internationally benchmarks and standards
- EU OMC: Adequate old-age pension systems should prevent poverty in the old age but also provide income replacement after retirement preventing sharp decline in living standards



Benefit adequacy in international standards

- Nearly all EU member countries ratified:
 - either ILO Convention no 102 (C.102) on minimum standards in social security or
 - European Code of Social Security (ECSS) of the Council of Europe,
 - and some ratified in addition also ILO Convention no 128 on Invalidity, Old-age and Survivors benefits (C.128).



Benefit adequacy in international standards (2)

- All three instruments stipulate that, if basic income security is to be provided mainly by the earnings-related pensions, the minimum replacement rate should be guaranteed at least for those with earnings lower than average earnings levels
- C.102 and ECSS requires the minimum replacement rate to be at least 40% (C.128: 45%) of previous earnings already after 30 years of contributions
- Reduced pensions should be provided for those with shorter contributions periods.



Benefit adequacy in international standards (3)

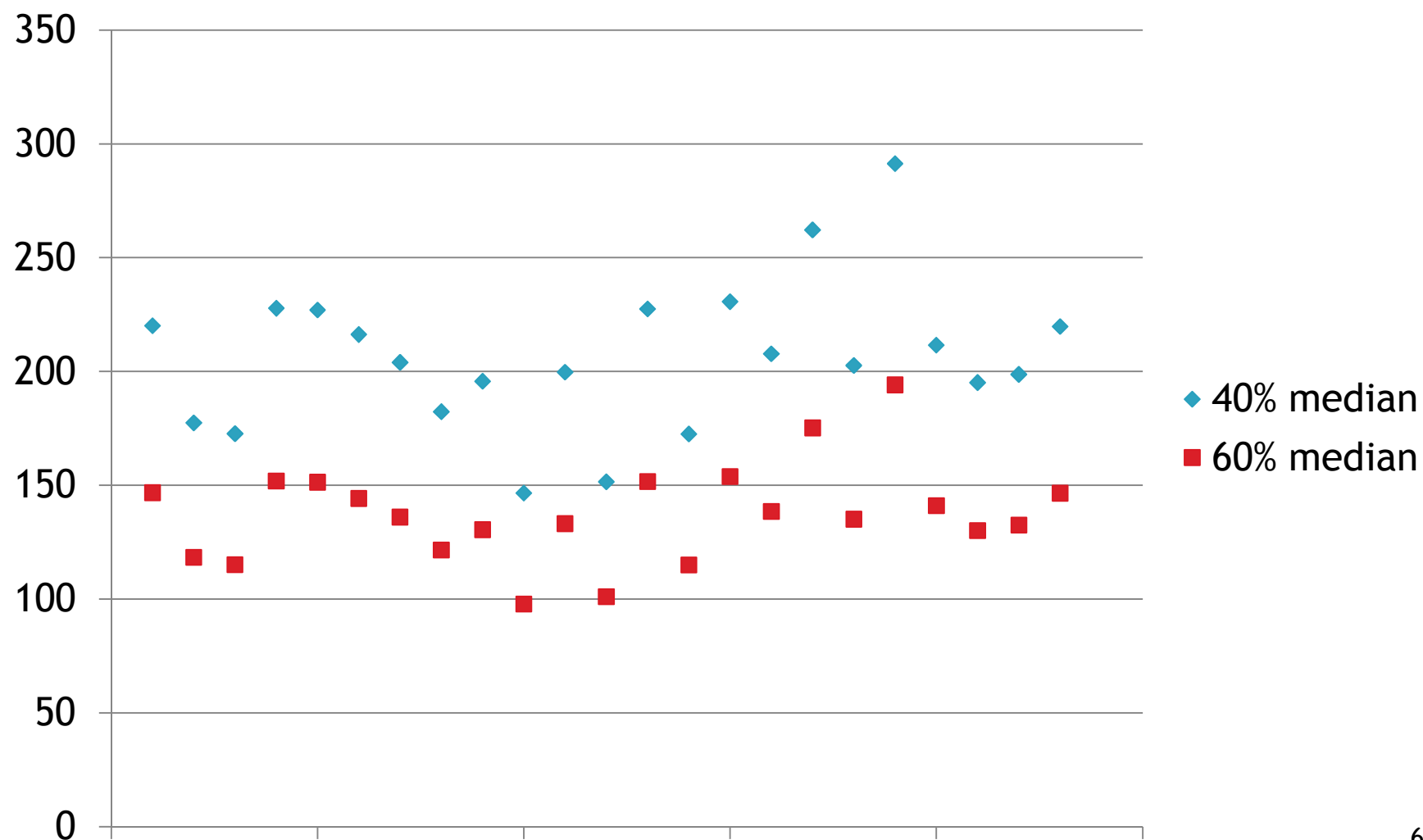
- If pensions are paid at a flat rate, its amount should not be lower than 40 per cent (C.128: 45 per cent) of prevailing levels of earnings of unskilled manual workers
- This applies as well to pensions provided as means-tested benefits but the level of such pensions should also meet another criterion:
 - they “shall be sufficient to maintain the family of the beneficiary in health and decency”



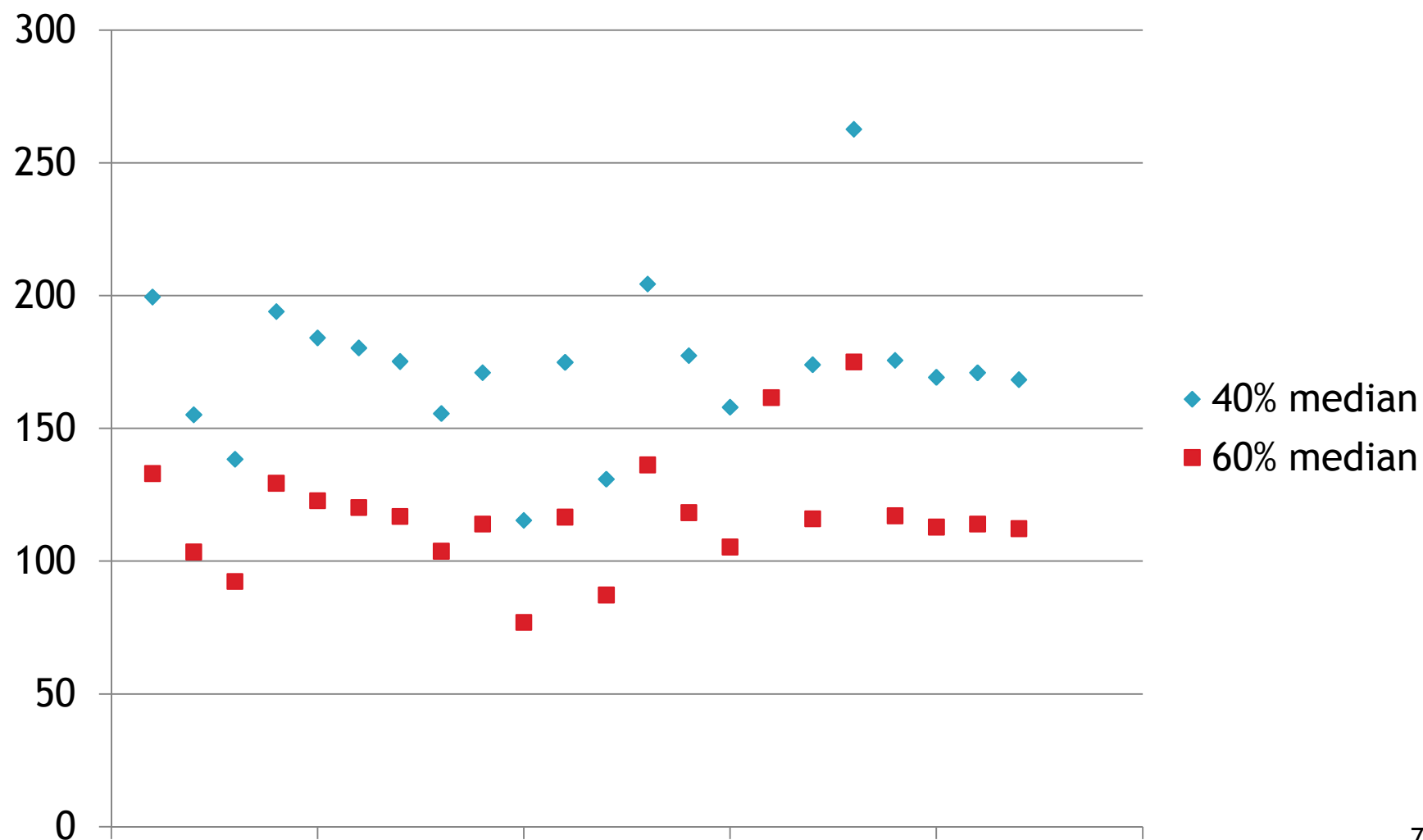
Benefit adequacy in international standards (4)

- Threshold replacement rates stipulated by the international standards were set up based on reviews of actual policies in member countries and national preferences with respect to minimum benefit setting in the middle of the previous century
- However, relevance of these standards is being recurrently reconfirmed by constituents of ILO and Council of Europe, most recently by the 100th Session of the International Labour Conference held in June 2011

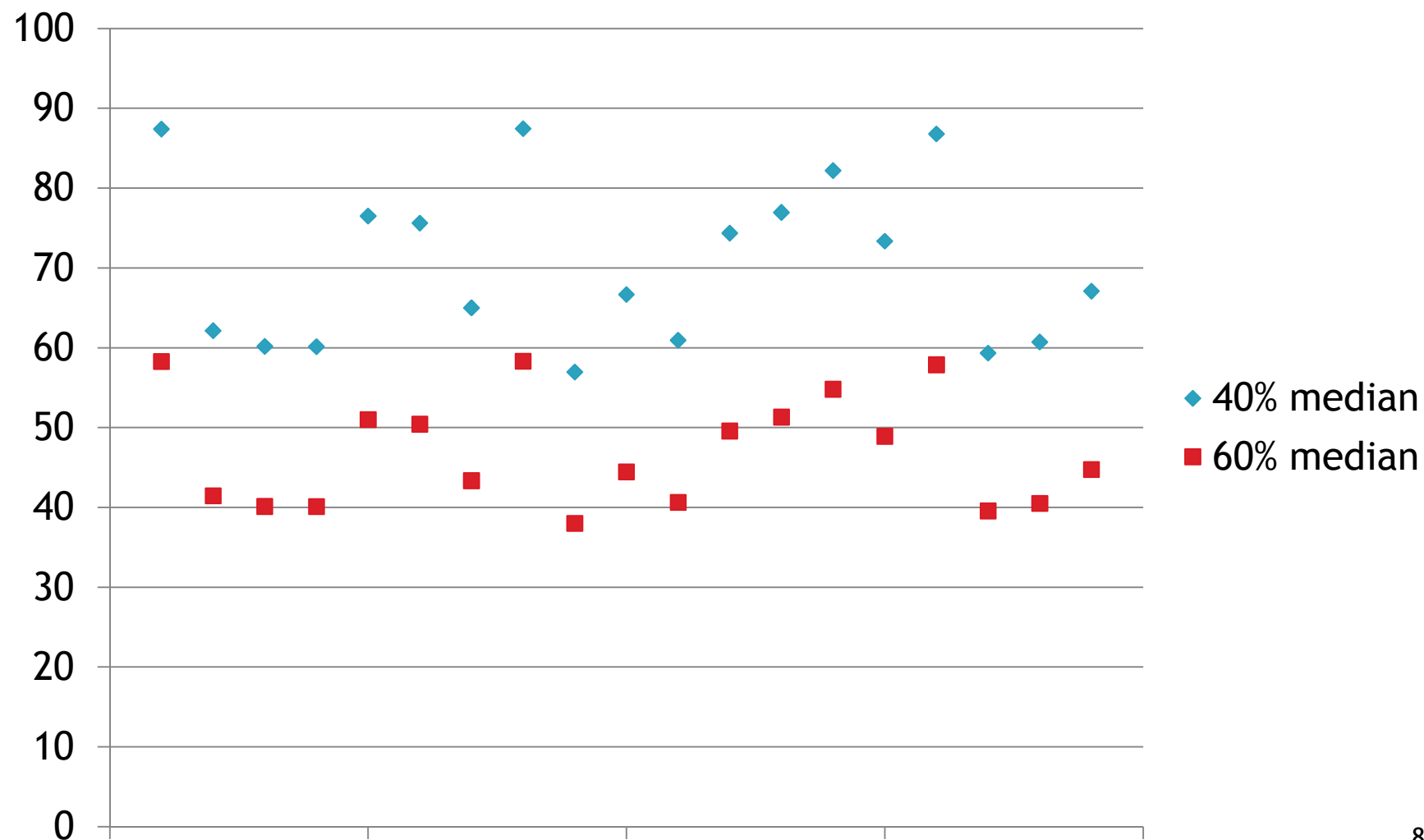
40% of gross average earnings as percentage of poverty line (EU member countries, 2008)



40% of female gross average earnings as percentage of poverty line (EU member countries, 2008)



40% of minimum wage as percentage of poverty line (EU member countries, 2008)





Future replacement rates from contributory pensions will be significantly reduced

- Reforms implemented or being implemented across Europe are significantly reducing replacement rates provided through the contributory, earnings related parts of the national pension systems
- Replacement rates after 30 years in many countries will be lower than 40 per cent required by international standards
- Many of those with shorter or broken careers and low incomes will not be eligible to pensions from contributory parts of the pension system high enough to prevent them from falling into poverty in the old-age



Protection of those with broken careers and lower life-time incomes weakened

- Many new reformed pension schemes are not just translating differentiation of earnings at the labour market into differentiation of pensions: these differences are actually amplified
- Reforms often removed from benefit formulas redistributive components aimed to protect against poverty those with lower earnings and shorter careers
- For a time being this changes has not yet been everywhere adequately compensated by increased role of various non-contributory provisions like basic minimum pensions or subsidies to contributions of those caring for children or sick and elderly, unemployed, persons with disabilities etc.

How to prevent from poverty those with lower incomes and those having no possibility to have long unbroken careers?



- Either one should preserve or restore in one way or another the redistributive defined benefit formulas or
- Secure that in the overall pension system there are much stronger than before non-contributory income guarantees (like basic state pension, universal or means-tested) as well as contribution subsidies compensating adequately some non-contributory periods



Relevance of social protection floor concept

- The International Labour Conference of 2011 gave support to the concept of social protection floor defined as a set of basic social security guarantees that ensure that over the life cycle all in need can afford and have access to essential health care and have income security at least at a nationally defined minimum level
- International Labour Conference in 2012 will consider adoption of the ILO Recommendation on social protection floor
- The questionnaire inquiring to the possible contents of such recommendation was send to all member states on 1 August 2011 and responses are expected by 1 November.



Relevance of social protection floor concept (2)

- The social protection floor concept was developed having in mind mainly to fill coverage gaps - mainly with non-contributory benefits - in developing countries where large portions of the population have no social security coverage at all
- However, this concept is relevant anywhere where people for various reasons cannot be adequately covered by existing contributory provisions



Automatic mechanisms versus good policy making

- Many reforms introduce various automatic mechanisms to ensure long-run financial sustainability of pensions
- There is no similar mechanisms to guarantee adequacy other than good policy making based on agreed adequacy targets through well informed social dialogue
- Pension reforms should not aim at keeping policy makers away (that's not only unrealistic also undesirable: one needs pension policy as part of the overall social policy)
- We need political and social mechanism to make sure that decisions taken by politicians are the right ones, balancing shorter and longer term needs as well as balancing benefit adequacy with financial sustainability