

## CONSIDERATIONS ON PENSIONS REFORM

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### 1. Pensions Reform in the World

The last decades have shown a magnification in the problems associated with having national pensions systems in more and more countries around the world. In this context, the PAY-AS-YOU-GO (PAYG) pension systems, exclusively based on solidarity between generations, is facing more and more difficult problems which are in need of solution.

Their origin is found in the evolution and demographic tendencies concerning concomitant population ageing with reduced birth rate, the longer average life duration, inflation, the bigger and bigger costs needed by the post-active period in early retirement, in growing the quality of life and, very importantly, in reducing the rate of dependence (respectively reducing the number of tax payers and growing the number of pensioners). Most of the countries of the world are confronting this kind of situations. If we refer to the European Union only, the demographic changes will remodel the entire economy and society. The tendencies resulted from the reduced birth rate, the growth of the average life time and the life chance at birth, but also the ageing of the "baby-boom" generation, contributes to the aging phenomenon of the population. In the same group of countries it is estimated that, between the years 2005-2050, there will be fundamental changes in the population structure on age groups. Those of age over 65 years will represent in the year 2050 over 30% of the total population, unlike 17% at the present, while the weight of the population of 24 years old will be reduced

at the same time, from 30% to 23%. This process will be alike in many countries, Japan and South Korea will be the first in this classification. These entire phenomenon generate huge pressure over the budgets of social assurance, which cannot cope with the expenses levels which the pension payments implicate. We are talking about their level, but also about the longer period in which the pensions must be paid to those in right. This is why in many countries these are already alarming financial consequences of the demographic tendencies and it is tried finding some equitable solutions for all the existent generations at a given moment into the society, but also the following generations.

The sources of finance for the pensions are substantially different from one country to another, because of the national legislations but also by the economical and social situation of every one. In most of the countries the main source is represented by the employed people which is constituted in a central fund from which are paid almost immediately the pensions to the rightful pensioners. So, we are talking about an income redistribution, principle on which is based the PAYG system. Being given the big problems concerning the fund insufficiency this way collected for paying the pensions, many countries have took into consideration the reform of the national systems of pension by which the responsibility for the incomes from the post-active period does not go only to the state, but also to the employer and the employee. Along these measures, in parallel is put at the growth of the

retirement aging, the lowering of benefits offered by the state and passing to the private administration but strictly supervised. Other solutions that are already meet, especially in the developed countries, concerned the retirement on stages, meaning the passing from the active period with a normal program to the period of gradual retirement, by a flexible or a program reduced on a certain period of time, this for having a more working population. This helps for at least two reasons: the people concern don't become from producers of incomes – consumers of social assurances budgets, but on the contrary, they continue to produce, giving this way a contribution to the social assurances budget even if, obviously, with a smaller cote. Encouraging the growth of birth rate, bigger efforts for professional formation, growing the flexibility of the workforce and reducing the unemployment represent some other measures that are took into consideration. The birth rate growth creates supplementary necessities at the family level, which must be covered by a proper social politics, like: support for taking care of the child, the total or partial payment of the state or day nursery, part time schedule for both parents until a certain age of the child, the employers accepting in parallel the influences over the parents career. Along with all these encouraging immigration creates the possibility of some future contributions, but bring also among with it other complex problems that which the receiving countries must cope with, among with integrating in the new society is one of the most important.

The main purpose of the pension system is that of helping the population to realize a balanced allocation of the financial resources along the life of the citizens. This thing is realized by transferring a part of the resources from the active period to the post active/period. The passing to the reform is firstly a political decision, but which has at its basis long time objectives (and sometimes too much on a short term) but

also elements of social and economic character.

The reforms represent a hard to realize and hard to implement process, because the main problem represented by the finance of the deficit and creates by passing from the PAYG system – based on the income redistribution, towards the new project (based on economy and investments).

The World Bank, which has developed constant preoccupations for defining a more efficient system, sustains a model reform based on three pillars, in which it is combined the facts of the three people mentioned.

- Pillar 1 – consists of the redistributive type of public pension system, legislated by the law nr. 19/2000 which has become available on the 1<sup>st</sup> of April 2001. This system is obligatory for all the people whose income are over a limit, their professional status does not matter (employed or professional free). The system is formed by contributions at social assurances and the ones assured by this system will obtain a pension which will be calculated on the basis of a point system which takes into consideration the whole active life of that person. The main objective of this component is to redistribute the incomes obtained as pensions, as well as constituting an assurance network for the aged people;

- Pillar 2 – consists of universal funds of pensions, administrated privately. This component will become obligatory, after a period of transition defined by an optimal condition, for all the people whose income are over a stabilized limit and which have a certain number of years until pensioning. The universal pension funds will be financed by the transfer of a part of the social assurance contribution, stabilized by the yearly law of the social state assurance budget, for the people that will be obligated (or will choose) to have contribution to both obligational components of the pension system.

These funds are based on the capitalization principle, meaning to

accumulate and invest the sums of savings in a period of time. They will be privately administrated, with the purpose of an optimal allocation of the existent resources, to maximize the profit from investments and to encourage the developing of the financial markets;

- Pillar 3 – consists in the existence of some facultative schemes of pension. These schemes will be generally addressed to the people with upper incomes or to those who wish higher pensions than those that will be supplied by the two obligatory components. The objective of these facultative schemes is to permit their participants to develop plans of economy by addressing to flexible pension schemes, which can be adjusted concerning the individual preferences and necessities. There will be different forms of this kind of schemes, like: individual plans of pension, schemes of sector pension or of enterprise organized by the employers or the unions.

In the three components of the new pension system purposed there is a tight interdependence. The first two are based on collecting and distributing the social assurance contributions by the National House of Pensions and Other Rights of Social Assurances, and the components based on capitalization and private administration (the second and third) will be supervised and regulated by a single institution – the Commission of Regulation and Supervising of the Pension Societies. In the Government's opinion, to introduce a new pension system with more components will lead to higher pensions than those obtained by the redistributive system with a single component, will assure the financial sustainability on long term, also the equal treatment of all its beneficiaries, in parallel with a significant injection of funds on the intern market of capital, with positive effects over the economic growth, and the population standard. The old structures concerning the pensions could not have functioned any longer. They have been created in a time while there were a bigger part young

population and a smaller part aged people, which were generally poor and ill and who spent a short time as pensioners.

In reality, every country creates and/or adjusts its own system of pension, concerning the specific situation, viewed under multiple aspects: evolution and demographic perspectives, the financial and economical situation, the fiscal system and so on. For reaching success, it is necessary a systematic approach, unitary for the whole reform process.

Some countries have elaborated the legislation and have passed to implementing a different PAYG system, for example Chile, Poland, Czech, Hungary, Bulgaria, etc. Others consider the necessity of pension system reform using the purposed model or appealing to other models, like South Korea, Thailand, New Zealand, Turkey, Slovakia, and Romania. From the experiences of the countries that have already passed to this system there can be dispatched some coordinates:

- the state pension level can be kept at a minimum level;

- it is necessary a legislative frame initially, usually it is modified subsequently; for example, in Poland, the law which regulates the pensions for the Second Pillar has suffered 230 modifications compared to the initial form;

- reforms can be made gradually, so that the shock of finance necessity to be reduced at minimum, so that there are found alternative methods of finance (sums obtained from privatization, intern or foreign borrowings);

- passing from the "defined benefit" (DB) system in which there are promised sums well defined, clear to be paid in the pensioning time, to the "defined contribution" (DC) in which is stabilized the contribution level, but the sums that will be paid under the forms of rents are not guaranteed; the actual Holland model represents an example of success for applying DB, and the Poland model, for applying DC;

- creating new encouraging conditions for simulating savings by the fiscal legislation (for the obligatory one and for the optional one);

- the necessity of a legislation to assure the transparency, supervision, control, security, efficiency: clear regulations for costumer protection, responsibilities for the fund administrators, sellers, coherent and consistent approaching at a product level but also as a channel of distribution level;

As remarkable successes concerning the pension systems we can mention Holland and the Scandinavian countries, which have had as a base common element in their strategy a variety of politics based on reducing unemployment as much as possible, an equilibration of income distribution and substantial economic performance along the growth of the minimum payments. The consequences of an equal pension system will be found at a macroeconomic and microeconomic level. Here are a few of them:

- eliminating the pressure over the budget of social assurances;

- stimulating the economic growth by investing the sums accumulated in economy, creating new workplaces, reducing the unemployment;

- the population economies help at the growth of the capital markets, the mobilized actives grow and help to develop some big and of long term projects of reform on the work market.

Regardless to the model of reform adopted, the existence of a proper fiscal treatment to permit sustainability is very important, it will create an equilibrium for the sold on a short term – therefore the most difficult aspect – fiscal viability on long term and stimulants paid to the tax payers. The experts in the domain consider the most right mode the system in which the taxation is made in the time of payment of the pensions, while the contributions are deductible. Obviously, the approach is different for the Pillar number two obligatory and The third pillar optionally. In the last mentioned case, there may be

stipulations for the global income limited to a certain annual level for not making in favor those with very high income. In parallel it is useful also encouraging the private economies by extending the fiscal facilities over the life assurances and certain forms of economy.

Preoccupations appear also at the level of other international organizations, like The International Monetary Fund, which has emphasized that in the last year, when the euro zone has recorded a slower economic growth (2%), compared to the global average growth rate of 5%, this has determined the deepness of the problems the pension systems confront with. The works will aggravate as long as the ageing of the population will grow, especially after 2010, in many countries; that is why it is recommended approaching these real problems by increasing the retirement age and encouraging the population to save for their pension time.

Many countries that confront with this situation adopt gradually proper measures. For example, it is stipulated that, increasingly, retirement in Germany will take place at the age of 67 years, in parallel with a reduction of the benefits accorded by the state; in Great Britain, a growth of the pension age to over 65 years, identical for man and woman. Actually, in the conditions of (numeric) reduction of population, as it is shown in the ONU studies, the only way to sustain economic growth is by growing the participation of all the categories that usually have a lower rate of participation, like woman (in many countries still the percentage of active woman is low), the people with disabilities, the unqualified people, the people who officially have a retirement age.

It is important to mention that there is no universal network of the pension systems and reforms to have success in any country, this being determined by the concrete situation and especially by the political option of each state. The reforms that have been done until the present show us the fact that

success is tightly bound to more ample economic reforms, based on reducing the retirement / unemployment in parallel with adopting some politics made to change the states attitude, the companies management, the management of the syndicates, the role of the young compared to the of the young ones, the women and those that have past their first age, in society and economy.

The efficient functioning of the work market is essential for the availability of the social protection systems, contributing to social cohesion, an essential objective for the social politics of the real democratic states.

## 2. Pensions Reform in Romania

In Romania also, in the contemporary period, there are two phenomenon that lead to demographic unbalances with direct effects over the state pension systems:

- **population ageing**, because growing the life standard has lead to enlarging the hope of living;

- **birth rate decrease**, with a direct effect over the number of tax payers at the public pension systems;

- **the working force migration** from Romania, also, with an effect, over the number of tax payers of the public pension systems;

The pensions from the public system are insufficient for a decent life and represent an average of 35% of the net salary. The social state assurance contributions at the public pension system are a system of ineffective investment because the money that employers pay at the social assurance are paid to the pensioners without any time to invest them.

On the work force market it is recorded a personal crisis, and, implicit,

the small numbers of employees. On the other hand, the state pension system is vulnerable at unemployment.

In order to readjust the public pensions system, a new system based on multiple levels has been implemented (see table no. 1)

By implementing the multi-pillar system there will be assured to offer me more than 15%, approximate 80% of the brute salary.

In the case of the obligatory private pensions, they have the role as participants, all the people that contribute to the state social assurance system under the age of 35 years, in an obligatory way, and for the people with an age of 35 until 45 years, optionally. Someone who is assured, in the case of the obligatory private pensions, will have a single account at a single society of private administrated pension funds.

The 9,5% contribution for the social, supported by the assured one, will be redirected to the obligatory private pension system, as it follows:

- 2% in the last year

- progressively, in every year it will grow but it is said that it will keep up until 2016, when it will reach the value of 6%.

The employer will not be overtaken to do and overwhelming accidental trip, and the employer is not welcomed to participate to the constitution of the fund of private obligatory pensions. The money accumulated from investing the contributions supported by the assured is the property of the assured, and the minimum level of the sum accumulated is guaranteed by the state (minimum the monthly contributions paid until pensioning).

Table no.1. System based on multiple levels

PILLAR 1	PILLAR 2	PILLAR 3
<ul style="list-style-type: none"> <li>▪ the actual public pension payment system named Pay-As-You-Go</li> <li>▪ it is based on the principle of social solidarity: the employee pays for another person (a pensioner)</li> <li>▪ the collective contribution system;</li> <li>▪ assures a low but sure level of pension;</li> <li>▪ The employee will become more implicated 3,5% of the brute salary from the brut salary, which is now, 9,5%</li> <li>▪ the contribution of the employer will maintain to the actual level concerning the work conditions;</li> <li>▪ the state pension will maintain its role of social protection, but at a more reduced level</li> </ul>	<ul style="list-style-type: none"> <li>▪ the obligatory system of private pensions, applicable from 09.17.2007;</li> <li>▪ predefined contribution system;</li> <li>▪ the progressive redirection of the states contribution for the for the private pension system until the level of 6%;</li> <li>▪ it is based on the principle of individual gesturing;</li> <li>▪ every employee will invest for its own pension;</li> <li>▪ the employer has the only role to conciliate in this system.</li> </ul>	<ul style="list-style-type: none"> <li>▪ the facultative system of private pensions – available since may 2007;</li> <li>▪ system of predefined individual contributions;</li> <li>▪ supplementary to the contributions concerning the states social assurance;</li> <li>▪ we can supplementary contribute towards up to one glass; at this level the maximum is 15% of the brute income;</li> <li>▪ the employer can implicate himself actively by according this benefit for the employees in the limit of 15% of the brute income.</li> </ul>
<b>30%</b>	<b>20%</b>	<b>30%</b>

The proper age when the private obligatory pension may be received is the legal age of pensioning. The payment of the obligatory private pension is made monthly as long as the person lives. The one assured has the possibility to choose for the transfer from a fund of obligatory private pensions if he can transfer from one fund of obligatory pension to another, in certain conditions. In the case of private facultative pensions, all the people that have incomes regardless of age can participate. A person who is a participant to the facultative private system pensions.

In the system of the private facultative pensions the employee and the employer can also contribute in a limit of 15% from the brute income, implicating a financial supplementary effort because it is more to pay compared to the contributions to the obligatory pension

systems. The money accumulated from investing the contributions paid to the employees and to the employers is the employees' property. The proper age to be able to receive the obligatory facultative pension is 60 years old. The private monthly paid facultative pension can be paid monthly like the pension all life long, and in certain conditions, it can be paid as a monthly pension for a determined time (5 years) or as an integral sum when reaching the legal age. From a fiscal regime point of view, the contributions paid are deductible for an employee at the level of 200 euro/year from the income tax, and for the employer at the level of 200 euro/year engaged from the profit tax. Also, there is the possibility to transfer from a fund of pensions to another, growing/diminishing the contribution, suspending or even

stopping the contribution, at the option of the insurer.

The pension system is guaranteed by many mechanisms, like:

- **by the state** – in a direct way by:

a) authority subordinated directly to the Parliament which has the regulation and supervising role of the pension system;

b) similar to the fund constituted by the banking system.

- **legislative:**

a) the law stipulates that a private pension fond cannot be declared in a failure state;

b) strict regulations concerning the politics of investments;

c) permanent monitoring –

d) the client receives monthly the sum deposited by him monthly from which commissions are out.

-**control** assured by the depositor (the bank).

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