



International Update

Recent Developments in Foreign
Public and Private Pensions

January 2022

Europe

Spain Implements Pension Reform Law

On January 1, Spain's government implemented a new law that makes numerous reforms to the country's old-age pension system, which include increasing early retirement penalties, expanding pension deferral bonus options, eliminating social security contributions for certain older workers, establishing a new sustainability mechanism, adopting a new benefit adjustment method, and creating a new social security agency. The law codifies many of the changes agreed to by the government, labor unions, and employer associations in the 2020 Toledo Pact. The law's main aims are to improve the financial sustainability of Spain's pension system while bolstering the retirement security of current and future retirees. In addition, the European Commission is requiring Spain and other European Union members to enact significant economic reforms, including pension changes, as a condition for receiving assistance from the bloc's €724 billion (US\$820 billion) pandemic recovery fund established in February 2021. (Spain is slated to receive around €140 billion [US\$159 billion] from the fund, which would make it one of the largest recipients.) According to the government, Spain spent 12 percent of its gross domestic product (GDP) on public pensions in 2021, which was up from 9.6 percent a decade earlier.

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

- *Increasing early retirement penalties:* The contributory pension program continues to allow insured individuals to claim their old-age pensions up to 24 months early if they have at least 35 years of contributions (for voluntary retirement) or up to 48 months early if they have at least 33 years of contributions (for involuntary retirement, which occurs when older individuals become unemployed for reasons beyond their control, such as a business closure). However, under the new law, the penalties for voluntary and involuntary retirement are now applied to the pension amount (rather than the regulatory earnings base used to calculate the pension) and on a monthly (rather than quarterly) basis. In addition, the penalty rates for voluntary retirement have been redesigned so that they not only vary depending on the length of a pensioner's contribution record, but also the duration of early retirement (with the penalty rates progressively increasing for each month of early retirement up to the maximum 24 months). Starting on January 1, 2024, the new penalty rates will also be gradually phased in over a 10-year period for individuals who are currently subject to special early retirement penalty rules because they have higher lifetime earnings. Although the maximum penalties for involuntary early retirement have not changed, those retiring under this option can now choose to use the penalty rates for voluntary early retirement in the calculation of their pensions if they are more favorable.
- *Expanding pension deferral bonus options:* Individuals who defer claiming their contributory old-age pensions until after the normal retirement age can now choose to receive a 4 percent pension increase for each year of deferral, a lump-sum payment of up to €12,000 (US\$13,591.20)—depending on their base pension amounts—for each year of deferral, or a combination of these two bonuses. Previously, the only bonus option was a pension increase of 2 percent to 4 percent (depending on the length of a retiree's contribution record) for each year of deferral.
- *Eliminating social security contributions for certain older workers:* Workers and their employers are now exempt from paying most social security contributions if the workers have reached the normal retirement age and continue to be employed.
- *Establishing a new sustainability mechanism:* The law has established an Intergenerational Equity Mechanism (MEI) to replace the Sustainability Factor for keeping the pension system in financial balance. (The Sustainability Factor was created in 2013 but later suspended.) Under the MEI, a social security reserve fund will be used to augment the pension system's revenues (up to 0.2 percent of GDP a year) starting in 2033 if the system's projected expenditures to 2050 exceed those submitted to the

European Commission in 2024. If the reserve fund proves unnecessary, its assets will be used to boost pensions or reduce contribution rates. To finance the reserve fund, employers and employees will pay additional contributions from 2023 to 2032; employers will contribute 0.5 percent of covered payroll and employees will contribute 0.1 percent of covered earnings. If the reserve fund is insufficient to cover projected shortfalls, the government, unions, and employers will negotiate additional measures to raise revenues or reduce expenditures.

- *Adopting a new benefit adjustment method:* Contributory old-age pensions will now be adjusted each January based on the annual change in Spain’s consumer price index (CPI) registered in November of the previous year. However, if the previous year’s CPI change was negative, no benefit adjustment will be made. This method replaces one based on a revaluation index, which linked benefit adjustments to several factors, including the pension system’s revenues and expenditures. As a result of the new method, the government increased contributory pensions by 2.5 percent at the beginning of 2022.
- *Creating a new social security agency:* By July 1, 2022, the government must approve additional legislation creating a State Agency for Social Security Administration that will centralize and modernize social security administration in Spain. Currently, the country’s social security system is administered by several public entities, including the National Institute of Social Security (contributory pensions) and the Institute of Elderly and Social Services (non-contributory pensions and in-kind complementary benefits).

Spain’s old-age pension system consists of contributory and noncontributory programs. To qualify for a contributory old-age pension, an individual must have reached age 66 and 2 months (gradually rising to age 67 by 2027) and have at least 15 years of contributions, including 2 years within the last 15 years before retirement. (The normal retirement age is reduced to age 65 for individuals with at least 37 years and 6 months of contributions.). The noncontributory old-age pension is paid to individuals who have reached age 65, have resided in Spain for at least 10 years since age 16 (including the last 2 years before retirement), and have household income below certain limits.

Sources: *Social Security Programs Throughout the World: Europe, 2018*, U.S. Social Security Administration, September 2018; “Informe de evaluación y reforma del Pacto de

Toledo,” *Boletín Oficial de las Cortes Generales*, November 10, 2020; “El Pleno del Congreso ratifica el informe del Pacto de Toledo,” *Seguridad Social*, November 19, 2020; *Ley 21/2021, 2021*; “EU Opens Path for Spain to Receive \$11 Billion in Recovery Funds,” *Bloomberg*, December 3, 2021; “Así serán los cambios en las jubilaciones anticipadas en 2022 con la reforma Escrivá,” *El Economista*, December 13, 2021; “Las Cortes Generales aprueban la ley que garantiza el poder adquisitivo de las pensiones,” *Ministry of Inclusion, Social Security, and Migration*, December 22, 2021; “Los nuevos coeficientes reductores de las jubilaciones anticipadas empiezan a aplicarse el sábado,” *Cinco Días*, December 30, 2021.

Africa

Uganda Allows Early Provident Fund Withdrawals

On January 4, the Ugandan president approved a law that allows participants of the country’s provident fund program (the National Social Security Fund, or NSSF) who are aged 45 or older and have at least 10 years of contributions to withdraw up to 20 percent (50 percent if disabled) of their account balances before the normal retirement age of 55. Previously, early withdrawals were only allowed if the participant: (1) was aged 50 to 54 and ceased employment at least a year before the withdrawal request; (2) switched to an approved private pension plan, or (3) permanently emigrated from Uganda. The new early withdrawal option is meant to provide financial relief to workers who have been adversely affected by the COVID-19 pandemic. According to the World Bank, the pandemic has led to widespread business closures, permanent layoffs, a rapid slowdown of economic activity (particularly in the informal sector), and a shift in labor from services to agriculture. As a result, household incomes have fallen and the country’s gross domestic product grew by only 2.95 percent in 2020, compared with 6.44 percent growth in 2019.

The NSSF covers private-sector workers in firms with at least five workers; voluntary coverage is possible for workers who previously had mandatory coverage and for employees of firms with fewer than five workers. Employees contribute 5 percent of gross monthly earnings (at least 7.5 percent for the voluntarily insured) and employers contribute 10 percent of gross monthly payroll. As of June 30, 2021, the NSSF held around 15.5 trillion shillings (US\$4.4 billion) in assets under management.

Sources: *Social Security Programs Throughout the World: Africa, 2019*, U.S. Social Security Administration,

September 2019; “NSSF Earns UGX 1.8T in Income, Assets Hit UGX 15.5T,” National Social Security Fund, September 23, 2021; “Uganda At-A-Glance,” World Bank, November 4, 2021; “Ugandan Leader Signs Law Allowing Workers Early Access to Pensions,” Reuters, January 1, 2022; “President Museveni Signs 20% Midterm Access NSSF Bill,” *The Independent*, January 5, 2022.

International

Organisation for Economic Co-operation and Development Releases Pensions at a Glance 2021: OECD and G20 Indicators

On December 8, the Organisation for Economic Co-operation and Development (OECD) released *Pensions at a Glance 2021: OECD and G20 Indicators*, its biennial report examining public and private pension systems in the 38 OECD-member countries and the G20 countries. The 2021 edition covers pension reforms implemented from September 2019 to September 2021, the COVID-19 pandemic’s effects on current and future pensioners, and the important role of automatic adjustment mechanisms (AAMs) in supporting pension sustainability. (AAMs are predefined rules that automatically change pension program parameters, such as retirement ages and benefit amounts, in response to changes in demographic, economic, or financial conditions.) The report also has chapters addressing important developments in pension design, generosity, and financing; the well-being of older persons; and demographic and economic trends.

According to the report, the main long-term challenge facing pension systems in OECD and G20 countries continues to be providing financially sustainable pensions in the context of widespread population aging. Although the COVID-19 pandemic has caused at least 2.5 million deaths in OECD countries, its economic effects on old-age pensioners and pension systems have been limited. During the past 2 years, for example, pensioners received targeted income support in 15 OECD countries. In addition, most OECD countries implemented temporary measures to protect workers and their future pensions, including expanding job retention programs, subsidizing pension contributions, expanding unemployment insurance, and extending social protections to self-employed persons. However, these interventions have done little to alleviate the long-term financial pressures facing many pension systems.

Other notable findings from the report’s general analysis of recent pension reforms and trends include:

- Despite a slowdown in life expectancy gains in many OECD countries since 2010, population aging will continue to accelerate over the next 2 decades. By 2060, the size of the working-age population (ages 20 to 64) is expected to decline by more than one-quarter in most Southern, Central, and Eastern European countries as well as in Japan and South Korea. At the same time, the ratio of persons aged 65 or older to those of working age is expected to nearly double by 2060, and the median age across all OECD countries is projected to increase from around 41 in 2020 to around 47 by 2050.
- Under current law, the average normal retirement age in OECD countries will increase about 2 years by the mid-2060s. Future normal retirement ages will range from 62 (Colombia, Luxembourg, and Slovenia) to 69 or more (Denmark, Estonia, Italy, and the Netherlands). In addition, there will continue to be lower normal retirement ages for women (compared to men) in Colombia, Hungary, Israel, Poland, and Switzerland.
- There have been limited legislated changes to retirement ages in OECD countries since 2019, with one increase (Sweden), two postponed increases (Ireland and the Netherlands), and several expansions of early retirement (Denmark, Ireland, Italy, and Lithuania). Among non-OECD countries, Brazil introduced minimum retirement ages (along with contribution rate increases and benefit formula adjustments) to improve pension sustainability.
- Economic modeling suggests that full-career, average-wage workers in OECD countries can, on average, expect to receive after-tax retirement income from mandatory pension programs equal to 62 percent of their pre-retirement earnings. This figure ranges from less than 40 percent (Chile, Estonia, Ireland, Japan, Lithuania, Poland, and South Korea) to 90 percent or more (Hungary, Portugal, and Turkey).
- OECD countries have implemented a variety of reforms to their earnings-related pension programs, including raising contribution rates to boost future pensions (Mexico), increasing benefit amounts (Hungary, Poland, and Slovenia), ending mandatory participation in supplemental private pensions (Estonia), and replacing mandatory notional defined contribution auxiliary pensions with funded defined contribution pensions (Greece).

- A few OECD countries (Australia and Chile) have allowed early withdrawals of retirement savings to compensate for economic difficulties, which will likely result in lower future retirement benefits.

In its examination of AAMs, the report finds that about two-thirds of OECD countries use some form of automatic adjustment in their pension systems, including notional defined contribution pension designs (6 countries), qualifying conditions linked to life expectancy changes (7 countries), benefit adjustments based on demographic indicators or other factors (6 countries), and balancing mechanisms (7 countries). The report argues that, compared with discretionary parametric reforms, AAMs permit more transparent and equitable pension adjustments and help avoid lengthy political negotiations. However, the report acknowledges that AAMs can only provide financial sustainability if they are politically sustainable, which requires broad political agreement when they are introduced.

Source: *Pensions at a Glance 2021: OECD and G20 Indicators*, Organisation for Economic Co-operation and Development, December 8, 2021.

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