

TAKING STOCK OF THE SPANISH PENSION REFORMS

EU-China Social Protection Reform Project
Training in France on Multi-tiered Design of
Pension System

Lyon, July 2015



GOBIERNO
DE ESPAÑA

MINISTERIO
DE EMPLEO
Y SEGURIDAD SOCIAL

Antonio BLAZQUEZ MURILLO
Advisory Member for Planning and Financial
Economic Analysis of Social Security
General Directorate for the Regulation of the
Social Security

EU approach: Social protection against poverty

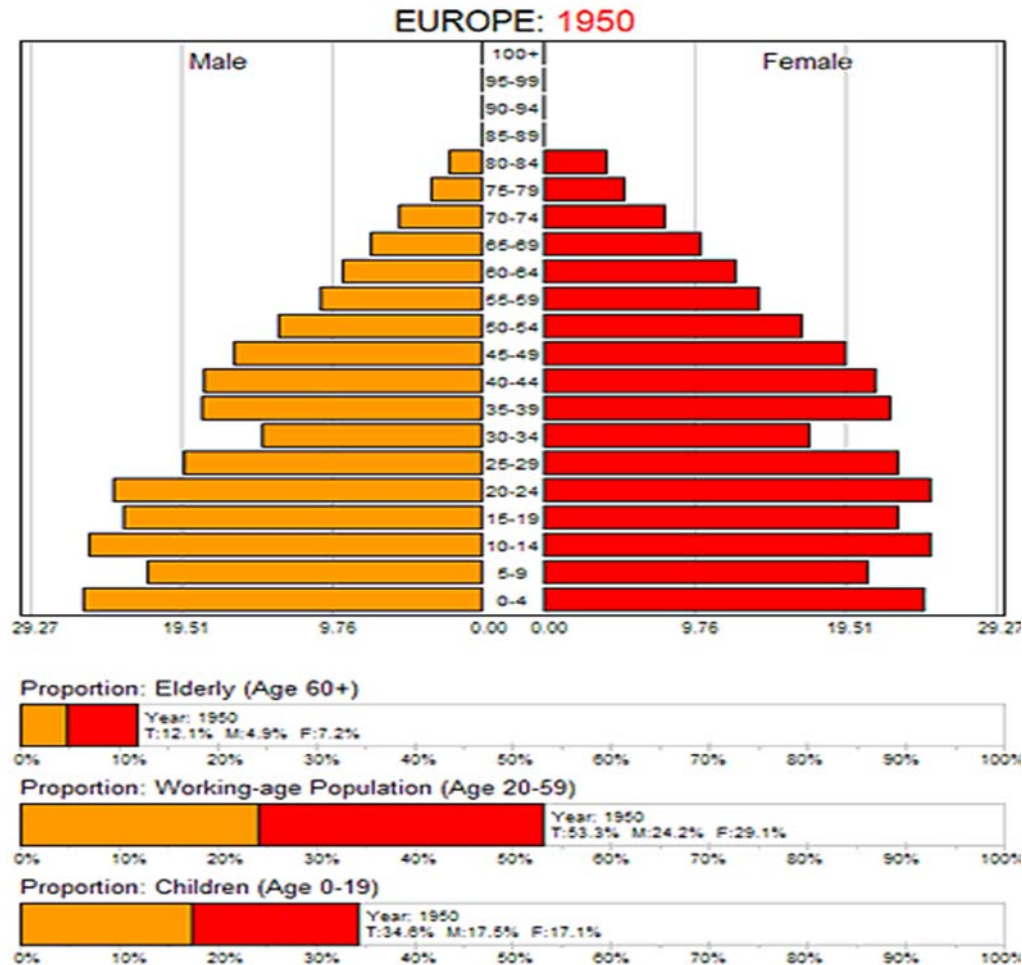
- **The poverty for people 65+ in the EU is comparable to those in working age.**
 - At risk of poverty rate 2013 for Total Population: 16.6%
 - At risk of poverty rate 2013 for 65 years or over: 13.8%
- **Women in the EU are at higher risk of poverty than men (gender gap also in pensions)**
- **Young generations in the EU face increasing poverty rates**

EU approach: Major challenges to EU social protection systems

- **Short-term challenge: The economic crisis and its aftermaths**
 - Financial, economic and public budget crises aggravate the situation for social protection schemes (fiscal constraints and employment impacts)
- **Medium and Long-term challenge: Demographic ageing**
 - Ageing of the 'baby-boomers' generation
 - Increasing longevity amid persistently low birth rates
 - Shrinking EU working age population
 - Future generations: strengthening intergenerational solidarity

EU approach: Population by Age and Sex (1950 – 2050)

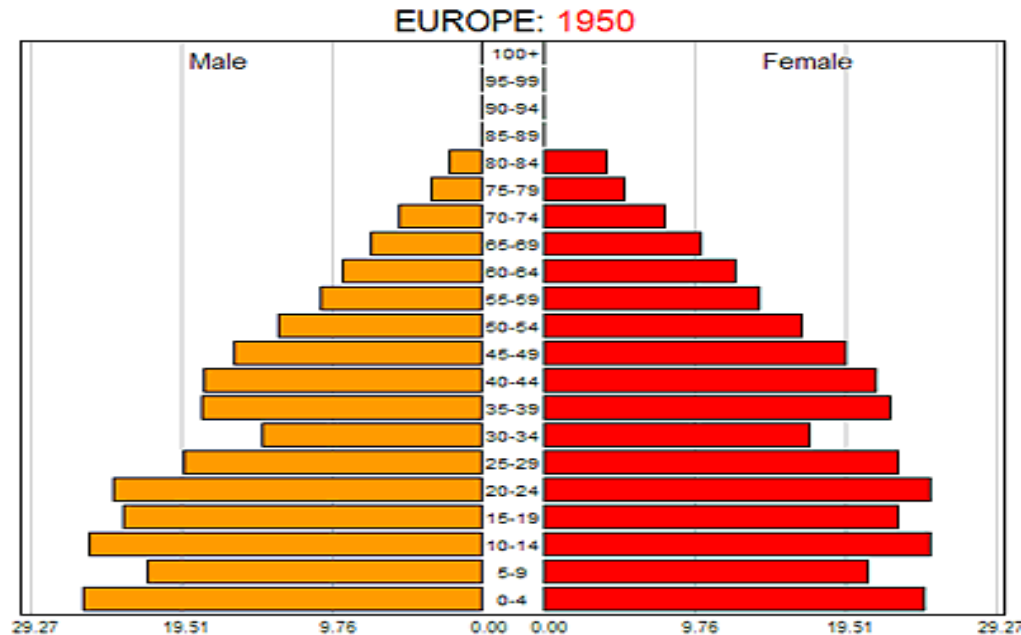
Population by Age and Sex (1950 – 2050)



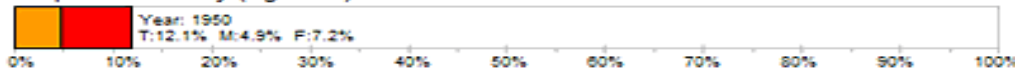
Source: United Nations Population Division

EU approach: Population by Age and Sex (1950 – 2050)

Population by Age and Sex (1950 – 2050)



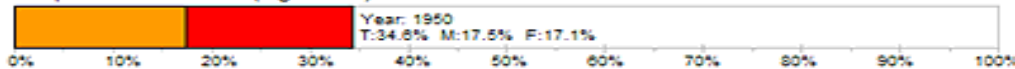
Proportion: Elderly (Age 60+)



Proportion: Working-age Population (Age 20-59)

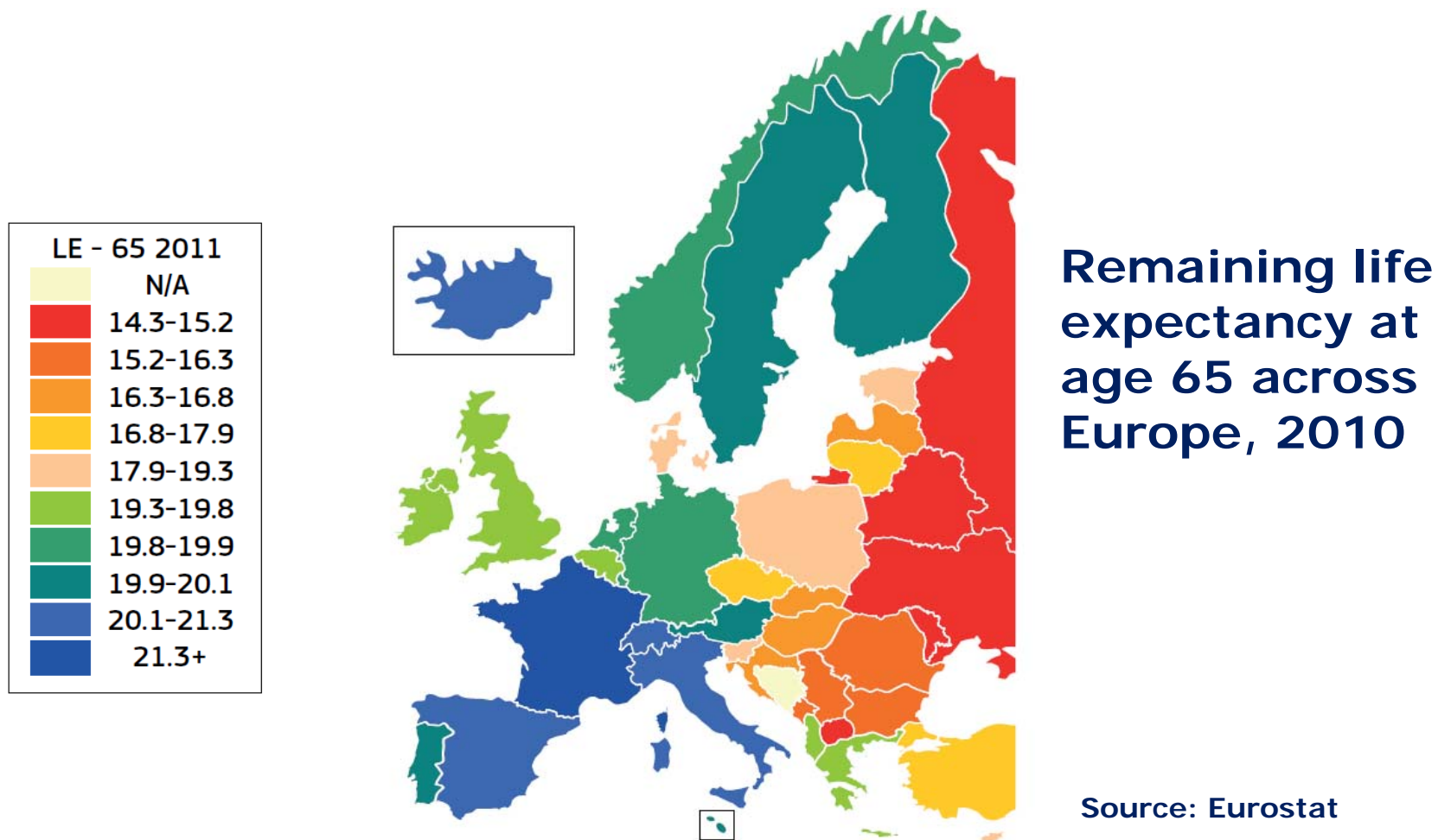


Proportion: Children (Age 0-19)



Source: United Nations Population Division

EU approach: Remaining life expectancy varies across EU



EU approach: How to address these challenges? The answer is **active ageing**

□ A Social Investment Approach

- Empowering and supporting people in crucial stages of their lives, starting in childhood
- Focusing on prevention (keeps larger economic and social costs from arising in the future)
- Developing human capital (gives people the skills and capabilities to participate in society)

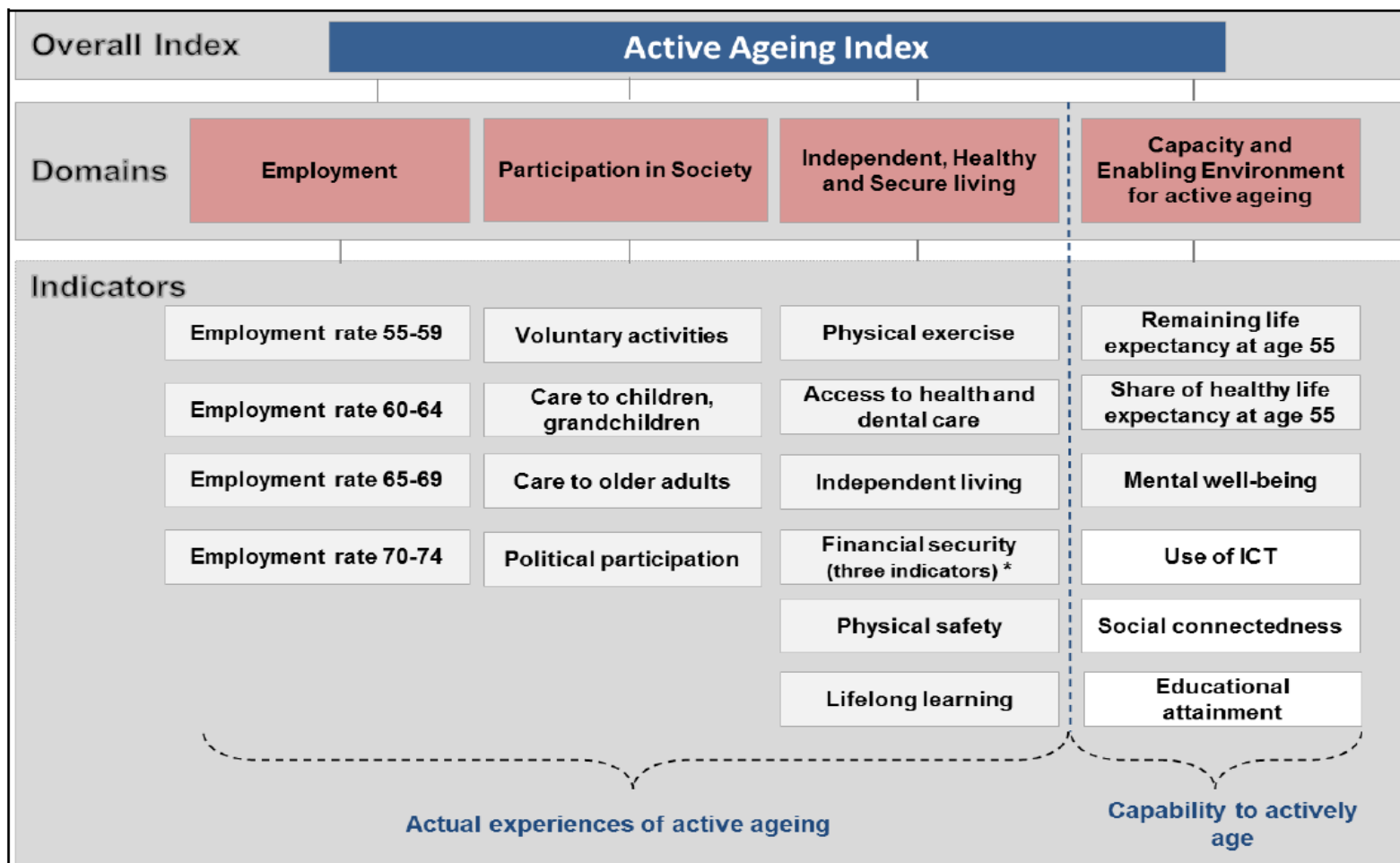
EU approach: How to address these challenges? The answer is **active ageing**

□ Long term care, Health care and Pensions

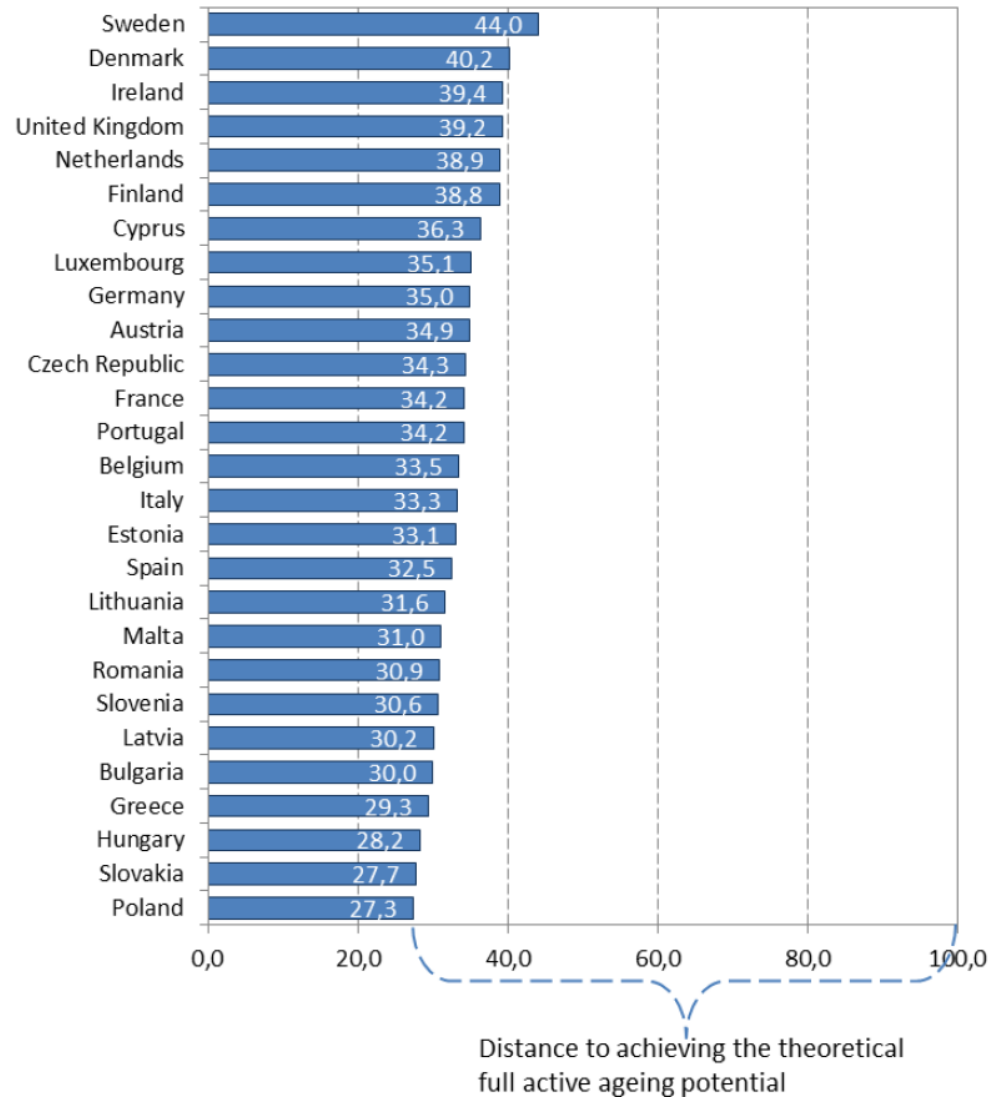
- Policies reducing care demand (improving prevention, rehabilitation and the capacity for independent living)
- Policies boosting care services quality (support informal carers; raise quality care provision; use of ICT in drives for higher productivity)
- Ensuring accessible, high-quality and sustainable health care
- Policies improving the sustainability and adequacy of public pension schemes

EU approach: Active Ageing Index

The Active Ageing Index (AAI) is a new analytical tool that aims to help policy makers in developing policies for active and healthy ageing

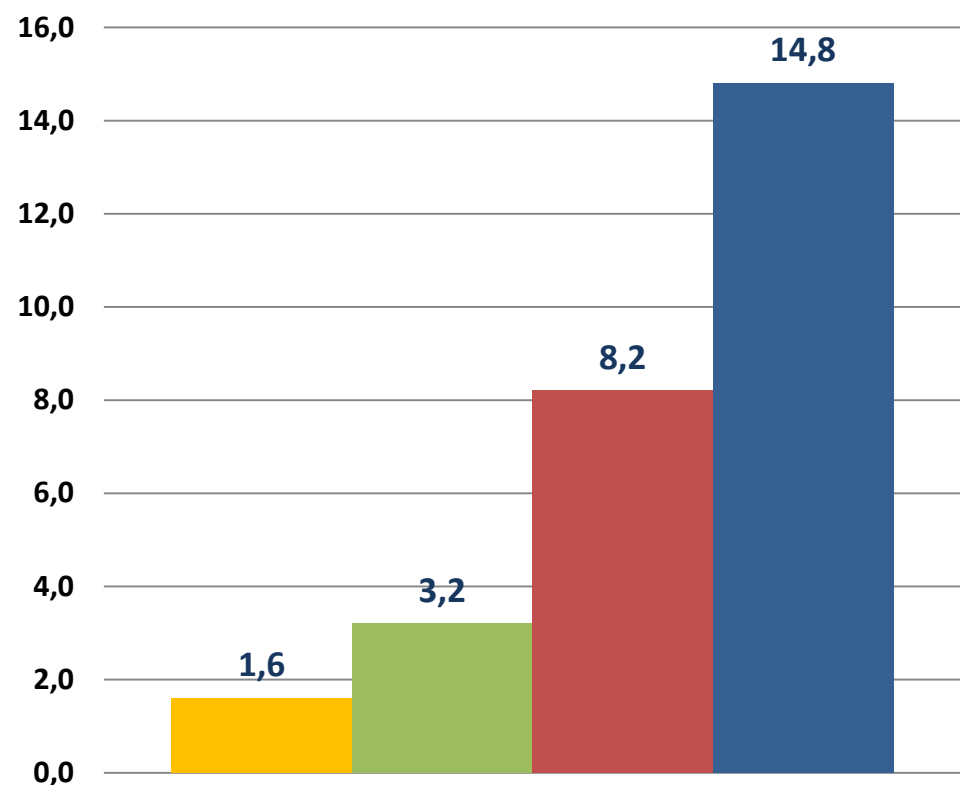


EU approach: Active Ageing Index



EU approach: Expenses in the EU dedicated for social protection benefits

Social protection benefits in % of the GDP (EU-27, 2011)



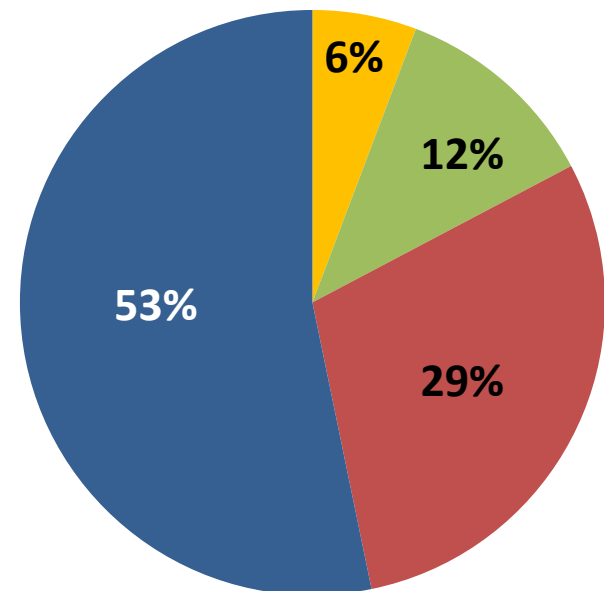
■ Unemployment

■ Family/Housing/Social exclusion

■ Sickness/Health care

■ Pensions

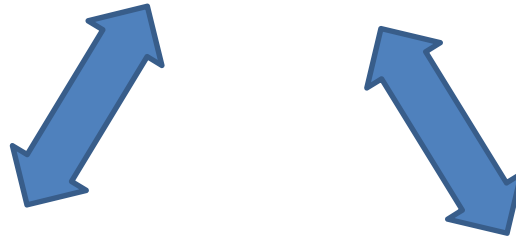
Social protection benefits as % of total social expenditure (EU-27, 2011)



Public Spanish Social Security System

How does it work?

solidarity



pay-as-you-go
Contributory
Pension system

Social and
political
agreement

Public Spanish Social Security System

9,7 Million Pensions

9,2 Million contributory pensions

500.000 non contributory pensions and family benefits

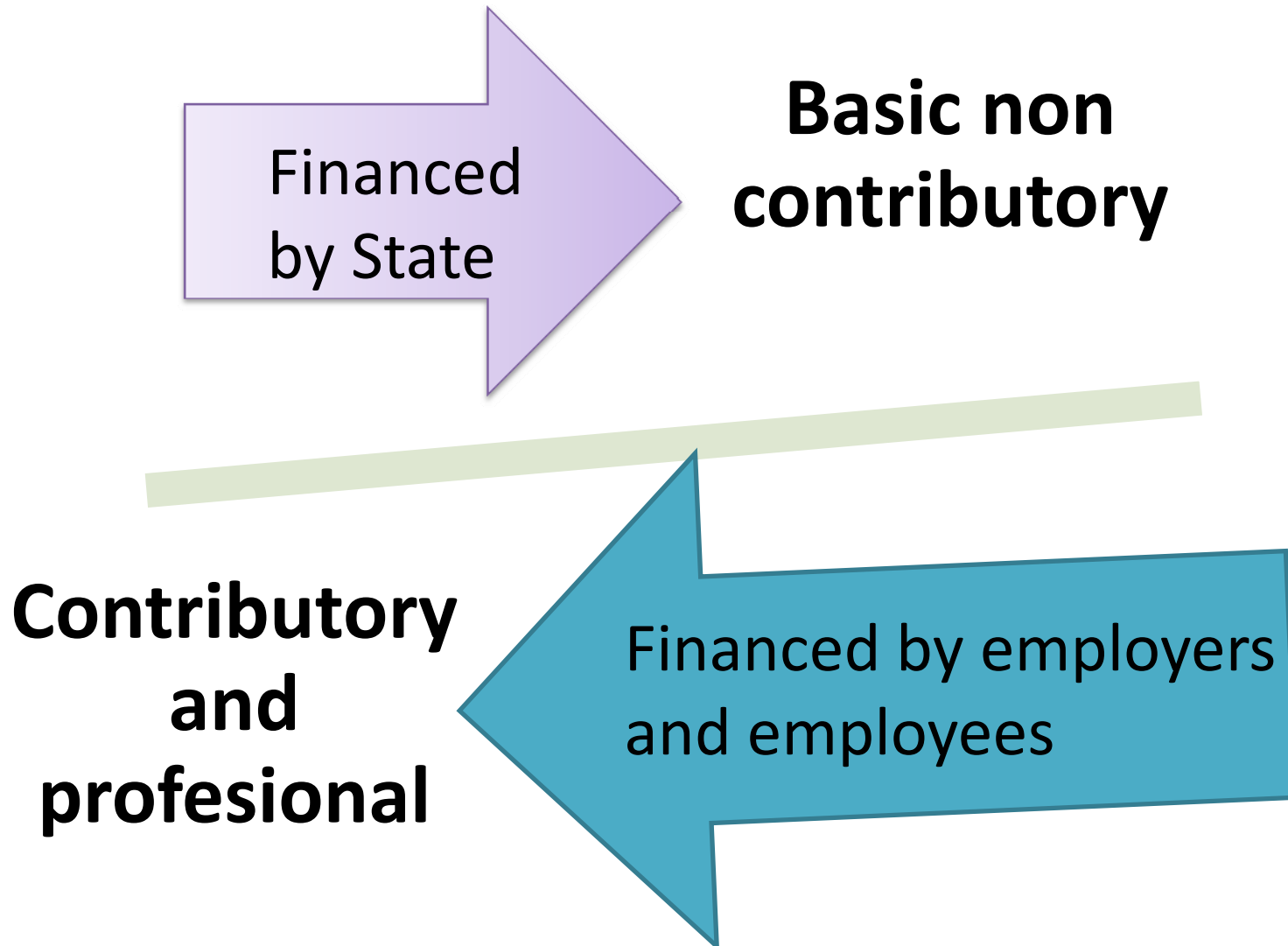


Along for 115 years

Public Spanish Social Security System

MODALITIES	BENEFITS	APPLICATION FIELD	FINANCING
a) BASIC NON CONTRIBUTORY	<p>Non contributory pensions</p> <p>Health care</p> <p>Family benefits</p> <p>Social services</p> <p>Employment promotion</p>	All residents who haven't enough resources	Tax financed by State allocations to the Social Security budget
b) CONTRIBUTORY AND PROFESSIONAL	<p>Pensions (income replacement, proportional to wages) with guaranteed minimum amounts</p> <p>Other economic benefits (Temporary incapacity, Maternity, Risk during pregnancy, Unemployment, etc.)</p> <p>Accidents at work and occupational diseases</p>	Mandatory for all employees or self-employed, with minimum and maximum amounts for benefits and contributions	<p>With contributions of employers and employees, with tax financed for minimum pension supplements</p> <p>With social contributions and some State allocations to some of the unemployment benefits</p>

Public Spanish Social Security System /Modalities



... Separation of income sources

- Since 2013 Non Contributory benefits are totally financed by general taxes.
- In 2015, the State has allocated €13.073 million:

€7,563.02

million for
minimum top-
ups of
contributory
pensions.

€2,402.87

million for non
contributory
pensions

€ 3,107.11

million for
other non
contributory
benefits such as
family
protection.

CHALLENGES



Guarantee a public pension system that anticipates to the economic and demographic challenges

The prevention of the risk of poverty

The social security pension is the main source of income after retirement

OBJECTIVE

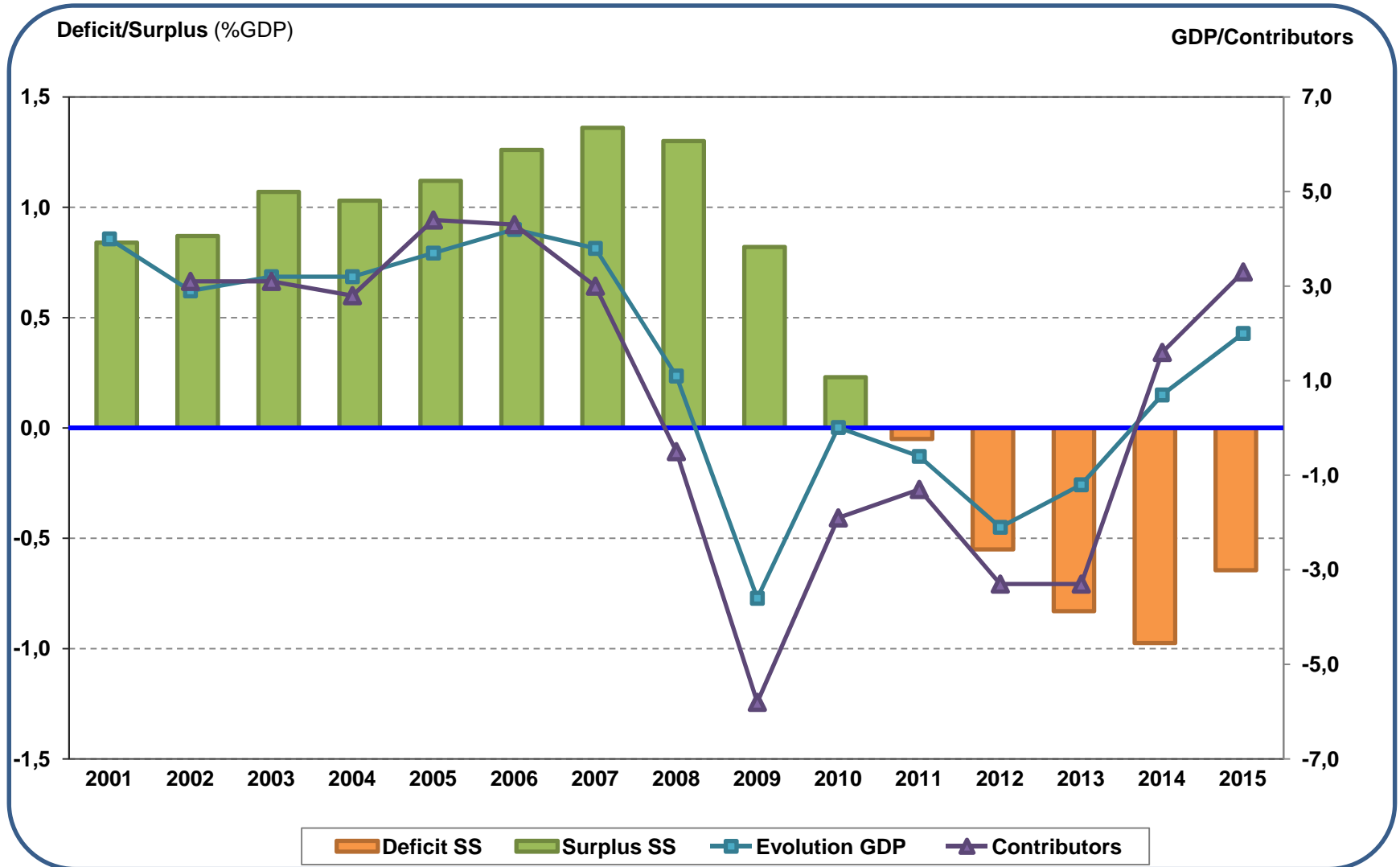
- Maintain a mandatory “*pay as you go*” public pension system for all workers

The system must achieve:

- 1 – Sustainability
- 2 - Adequacy of pensions

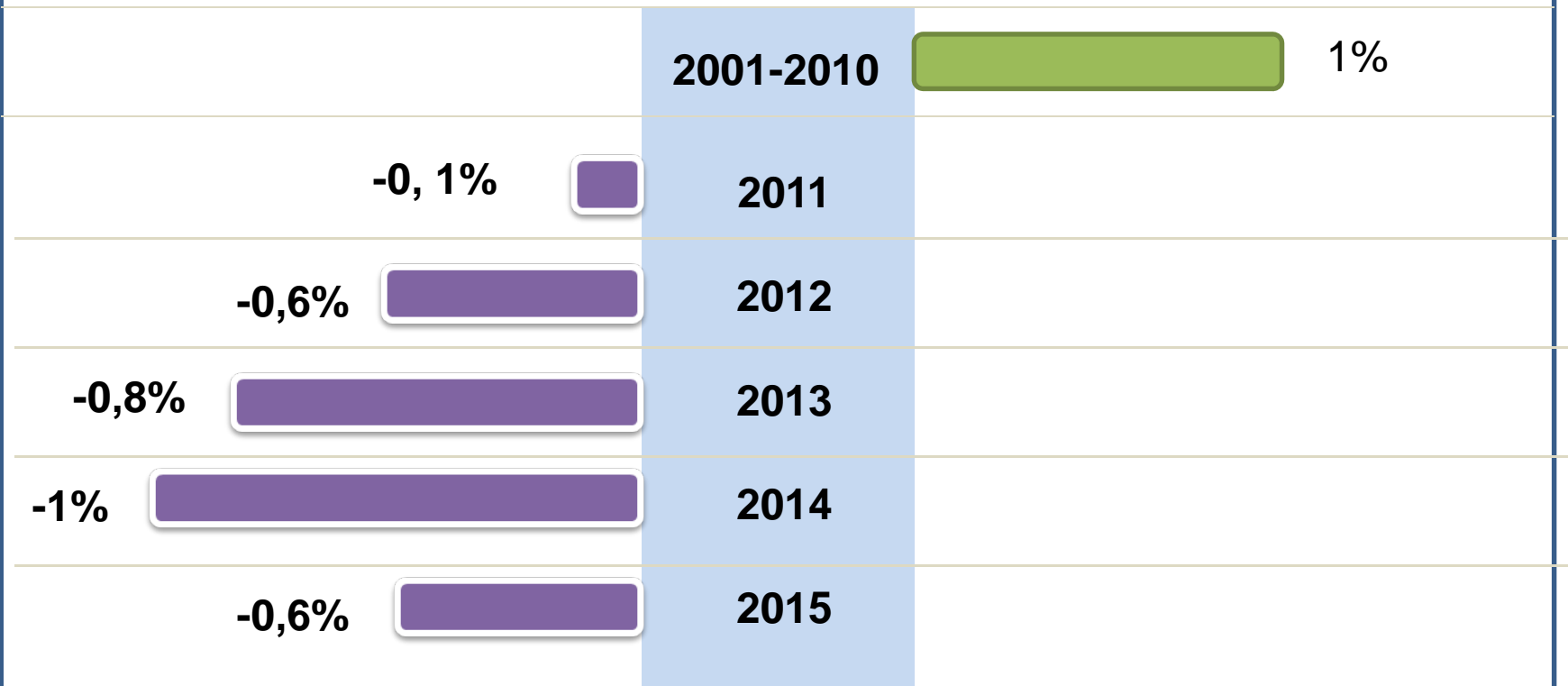
The funding requirements and the adequacy of benefits are assessed by using **revenue's and expenditure's projections in the medium and long term**. These forecasts drive the reforms in the Social Security System.

Spanish Social Security is nowadays deeply hit by the crisis and in the future by the aging population.

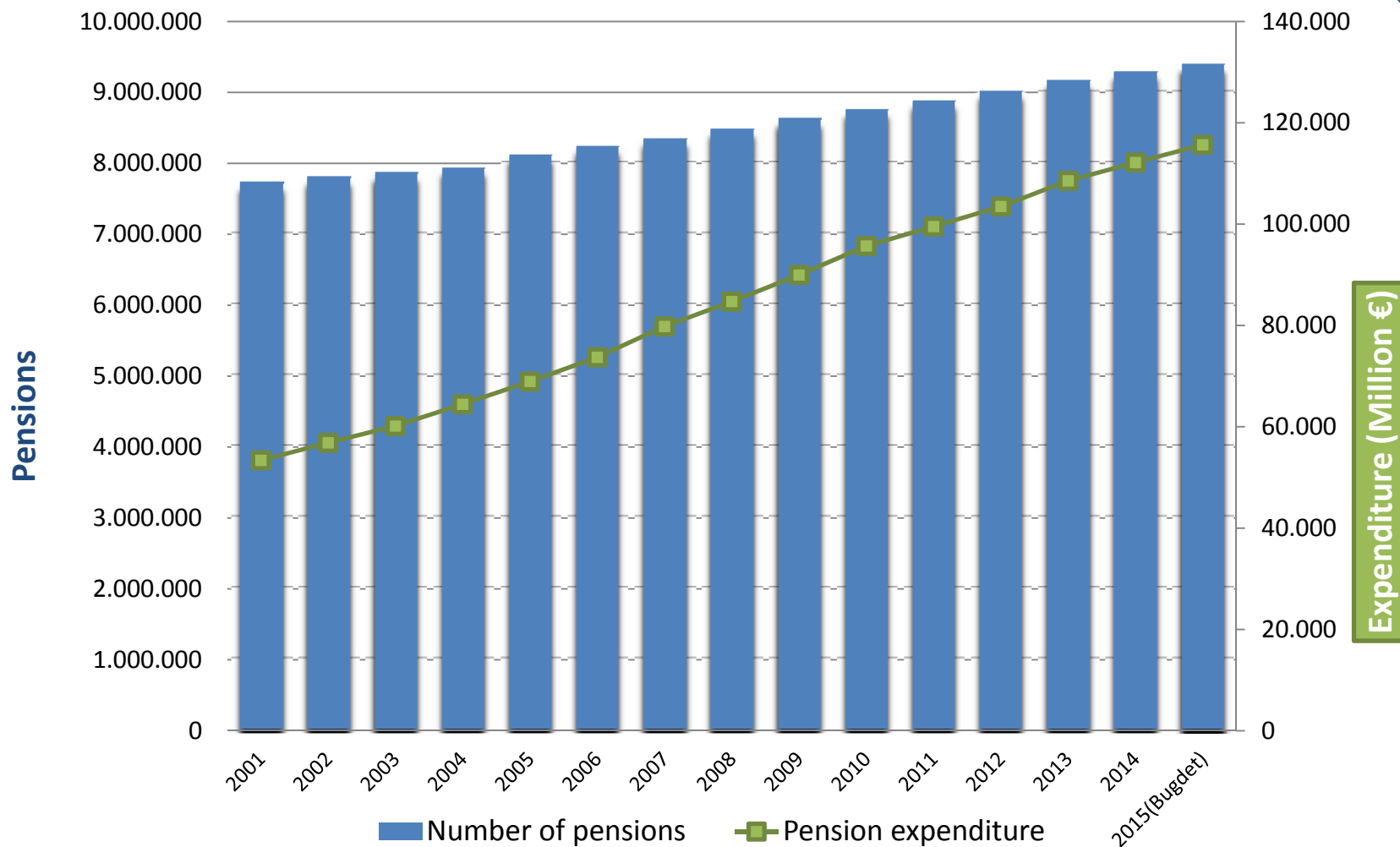


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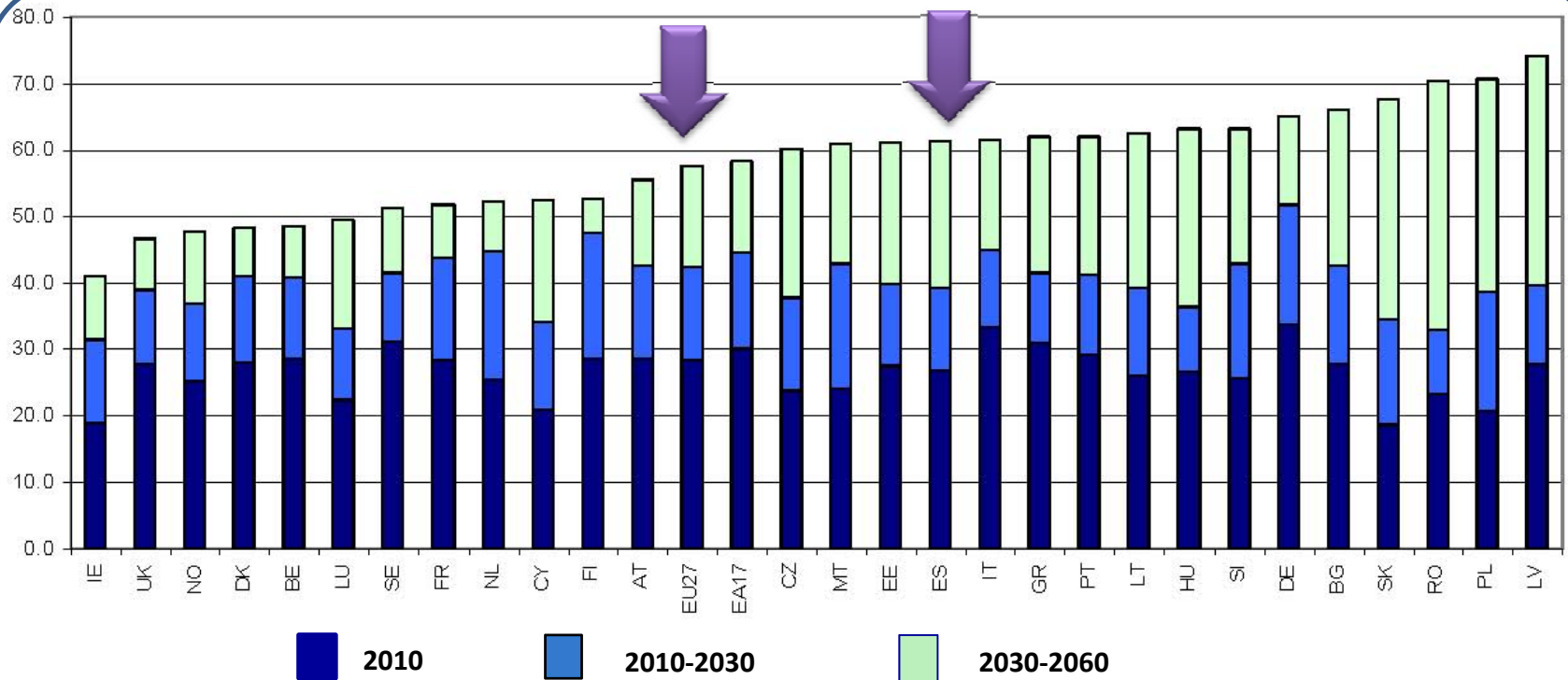
Déficit/ Superávit (%PIB)



Public Pensions trends



Spanish Social Security is nowadays deeply hit by the crisis and in the future by the aging population.

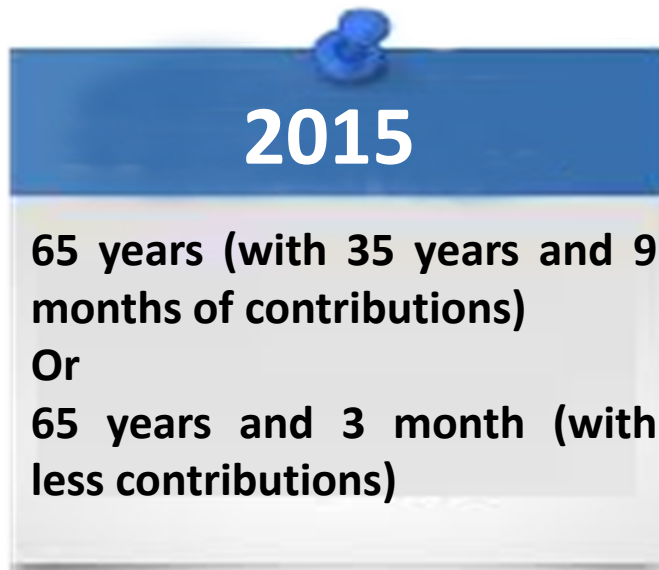


The Old-age Dependency Rate will increase in all EU countries, although there are important differences between countries. In Spain, the rate will grow from the current 27% to 40% in 2030 and will reach 60% in 2060.

Source: Commission Services, Eurostat, EUROPOP 2010.

The 2011-2013 reforms of the social security pension system

- Legal retirement age is **“increasing”**



2015

65 years (with 35 years and 9 months of contributions)
Or
65 years and 3 month (with less contributions)



2027

65 years (with 38 years and 6 months of contributions)
Or
67 years (with less contributions)

- The requirements for early retirement are being **tightened gradually.**

Retirement pension formula

$$P = Br * (\% \text{ contributed years}) * FS \leq \text{Ceiling amount}$$

Br

(Regulatory Base)

- 50% with 15 years (it's required at least 15 contributed years)
- 100% (increasing from 35 years in 2012 to 37 years in 2027)

FS

(Sustainability Factor)

After 2019

€ 35,852.32
in 2015

$$B_r = \frac{\sum_{i=1}^{24} B_i + \sum_{i=25}^{216} B_i \left(\frac{I_{25}}{I_i} \right)}{252} \text{ in 2015}$$

The **Regulatory Base** is the average of the last years of contributions. The period used will gradually increase from the last 15 years in 2012 to 25 years (by 2022).

The **Contribution Base (Bi)** is the earned income in a range between the minimum salary €9,079.20 /year, and the ceiling contribution amount, equal to € 43,272.00/ year in 2015.

The *Bi* corresponding to the 24 month just prior to retirement are considered nominal values and the remaining *Bi* are up-dated according to the evolution of the Consumer Price Index.

... Promoting active aging. Late retirement

■ Late retirement

An increase in the accrual rate will be applied for each year of contributions after the legal retirement age:

For careers lengths

- below 25 years+ **2%**
- between 25 and 37 years.....+ **2.75 %**
- over 37 years.....+ **4%**

- ### ■ Active retirement: compatibility between retirement pension and active life.

Old age pensions are compatible with paid-employment and self-employment, regardless whether the work is on full-time or part-time basis, provided that the pensioner has reached the statutory retirement age. The pension benefit will be equivalent to half of the amount the pensioner would be entitled to, excluding minimum top-ups. (19,522 pensioners)

... Reinforcing the contributory aspect

Since 1994, the years taken into account in the calculation of the Regulatory Base of the retirement pension have been increased:

Until 1994
2 years

From 1994
to 1997
8 years

From 1997
to 2012:
15 years

From 2013
to 2021:
increase
from **15**
to **25**

From 2022
onwards:
25 years

...Sustainability factor

The Sustainability Factor (FS) is an automatic link between the amount of retirement pensions and developments in life expectancy of pensioners.

Minimum Pension ≤ Pension ≤ Maximum Pension

From
2019
onwards

Only applicable
to new Social
Security
retirement
pensions

Social Security
mortality
tables
(modelling
with EUROPOP
and INE)

...Sustainability factor

The **Sustainability Factor (FS)** is an automatic link between the amount of retirement pension benefits and developments in life expectancy of pensioners. The mathematical formulation of the Sustainability Factor:

$$FS_t = FS_{t-1} * e_{67}^*$$

*Pension = Regulatory Base * % years contribution * FS ≤ Maximum Pension*

Being:

$$FS_{2018} = 1$$

t = the year of the factor, taking values from the year 2019 onwards.

e_{67}^* is the annual change in a five year period life expectancy at age 67, according to the mortality tables of the population covered by Social Security, calculated using the following formula

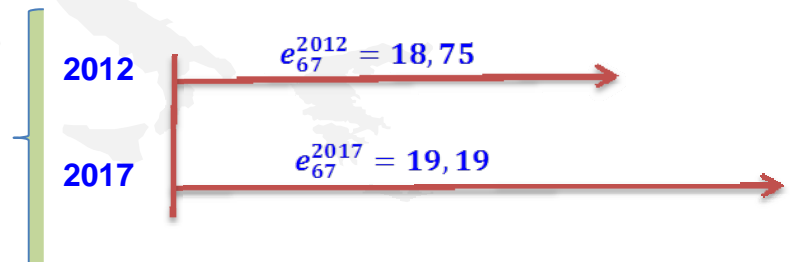
$$e_{67}^{2012-2017} = \left[\frac{e_{67}^{2012}}{e_{67}^{2017}} \right]^{\frac{1}{5}}$$

Fixed value applicable for the calculation of FS in the years 2019 to 2023 = 0.9953

$$e_{67}^{2017-2022} = \left[\frac{e_{67}^{2017}}{e_{67}^{2022}} \right]^{\frac{1}{5}}$$

Fixed value applicable for the calculation of FS in the years 2024 to 2028 = 0.9960

Link benefits to life expectancy



...Revaluation Pension Index

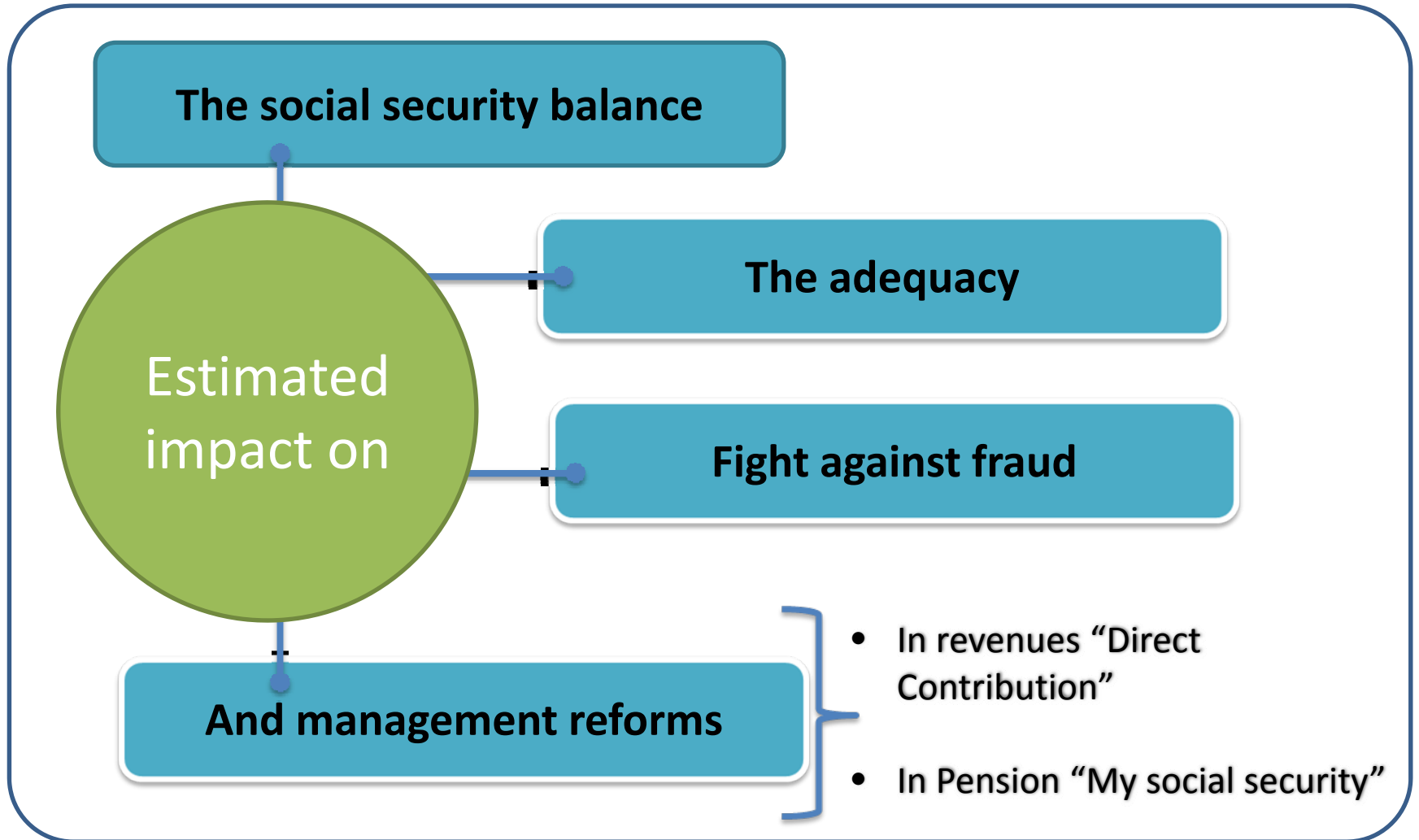
The yearly adjustment of the pensions system, IR , is established annually by the State Budget Act, according to the following mathematical formula:

$$IR_{t+1} = \underbrace{\bar{g}_{I,t+1}}_{\text{Indexation}} - \underbrace{\bar{g}_{p,t+1}}_{\text{Income variation of the system}} - \underbrace{\bar{g}_{s,t+1}}_{\text{Number of pensioners variation}} + \alpha \underbrace{\left[\frac{I_{t+1}^* - G_{t+1}^*}{G_{t+1}^*} \right]}_{\text{Substitution Effect Surplus distribution Deficit reduction}}$$

- **Centered means of 11 years**
- **A new indexation for the stock of pension**
- **All types of pension, not just retirement**
- **In force since 2014**

➔ **Minimum value of IR = 0.25**
Maximum value of IR = CPI + 0.50

Evaluating the effects of the pension reforms



The social security balance. New targets Indicators

Longer working lives

	Before reforms 2012	After reforms 2014 (Transitory period)
Increase effective retirement age	63.9 years	64.1 years
Decreases early retirement	42.2%	41.3%

Pension expenditure 2014-2015 will grow up less than 2012

Components of expenditure			
	2013 (%)	2014 (%)	2015 (%)
Average benefit without revaluations	1.7	1.6	1.6
Revaluations	1.5	0.25	0.25
Number	1.6	1.4	1.2
Total (%)	4.9	3.3	3.0

The social security balance

Social Security pension expenditure (%GDP)

- Future expenditure will be kept in a range of 10% - 11% GDP.

The social security reserve fund has covered the deficit in past years and nowadays

(First quarter 2015)	Million €	% GDP
Purchase price	42,014	3.9
Market price	49,156	4.6

The future surpluses and deficits are balanced with the reserve fund.

The adequacy. New targets Indicators

The effectiveness of the pension system is measured by their ability:

- ✓ To replace pre-retirement earned income and
- ✓ To prevent poverty risks

Indicators

- Although the increase of the average retirement pension amount is restrained, it is still higher than the CPI.

	2012 (%)	2013 (%)	2014 (%)
Retirement pension	3.5	3.4	2.1
CPI	2.9	0.3	-1.0

- The percentage of minimum pensions is declining due to fact that the amount of the new pensions is in most cases, higher than the minimum pension benefit.

Ratio minimum pension		
	2012	2014
Retirement	26.6%	25.5%

The adequacy. Minimum Pension Provision

- **Tax Financed** top-ups system for the contributory pensions.
- Pensions top-ups will be applied in all cases:
 - Full time or part-time workers. Temporary and indefinite contracts
 - All types of activities.



The adequacy. New targets Indicators

- Net Theoretical Replacement Rate is one of the highest in the EU.

	2013 (%)	2053 (%)
NTRR	96.2	86.8

- By law, the Government every five years will prepare a report, for its presentation to the Congress of Deputies and social partners about the reforms regarding the sufficiency and adequacy of the Social Security pensions.

Fight against the fraud

In Spain the Government has promoted the new Act project of Work Inspections and Social Security for more coordinated and effective inspection services.

A National Office for the Fight Against the Fraud is going to be created.

Fighting against fraud are currently giving returns in terms of lost contributions and it is expected to maintain the amounts raised in the future.

Management reforms

Raising social contributions

The new direct system of payment of social contributions will allow to take an active role in the enterprise's payment process , moving from a model of self-settlement to a new billing model.

The priorities are to minimize the mistakes in the implementation of the contribution rules, to compare the data in advance and to facilitate the payment of the contributions through telematic means.

The system will automatically apply the price increases and/or reductions, achieving greater legal security, and will give an individual calculation for each worker' contribution. In conclusion, the system will be guarantee against possible irregular situations in the income of contributions.

The system apply to 1,500,000 companies with 13,000,000 employees, and more than 3,000,000 self-employed.

Management reforms.

Informing the worker all his working life data

“Your social security” is a virtual space where citizens can access by digital signature to:

- Information about their working lives
- Make simulations of their future pensions
- Applications for benefits

New regulation for the citizens' right to access the information in regard to the Social Security system

Electronic Administration

Beyond pension reforms

After making the reforms described, the effort is focused on increasing financial resources:

For non contributory pensions:

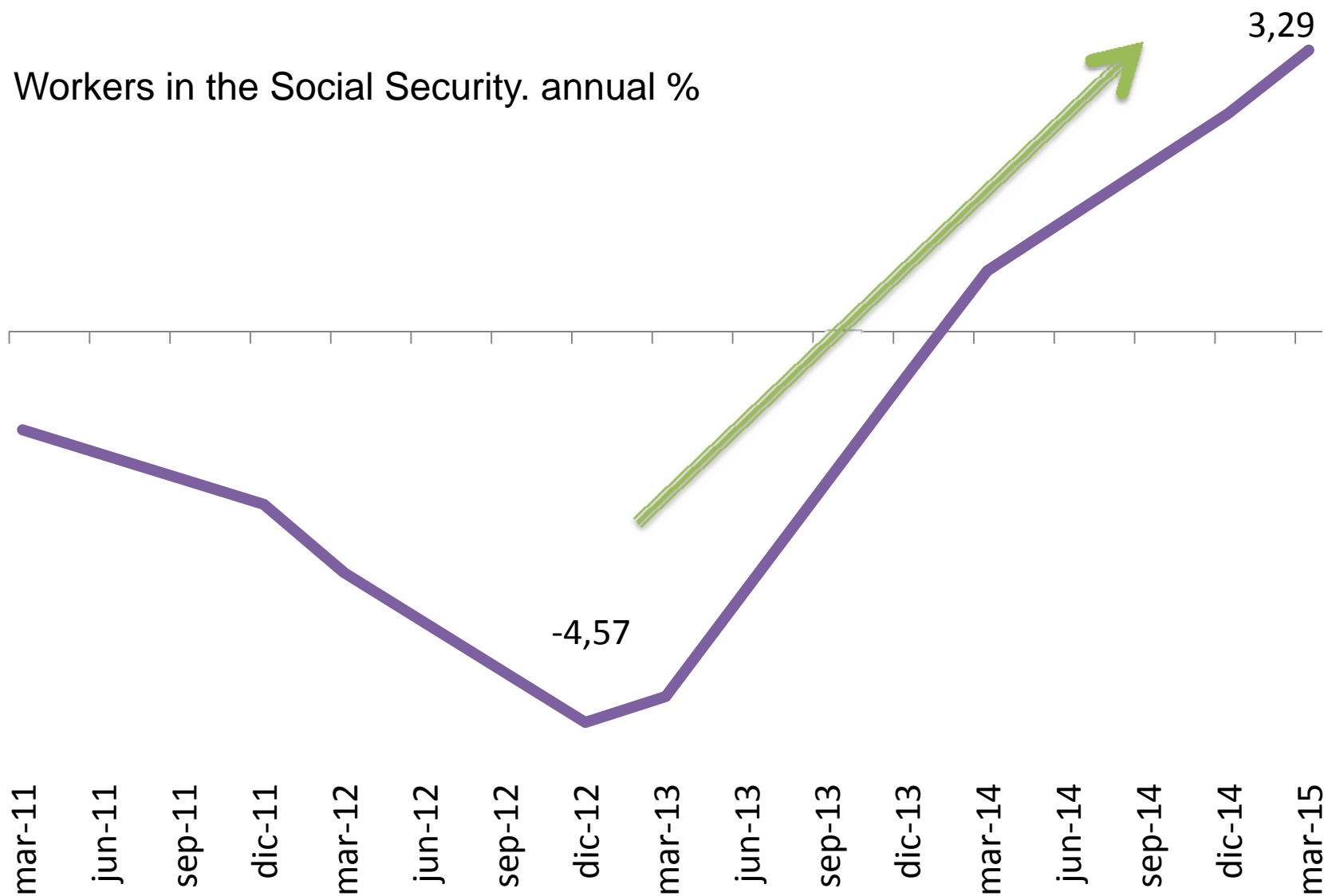
- Since 2013 the full amount of the minimum guarantee pensions are financed by **general taxation**. 7,600 million euros.

For contributory pensions:

- Increase employment rates .- After six years losing jobs, 2014 ended with **536.512** workers more, and in 2015 employment is growing at rates of **3%**.

A year of creating NET EMPLOYMENT

Workers in the Social Security. annual %





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www.meyss.es

www.seg-social.es