# ACTRAV's support for trade unions in the Caribbean: Promoting decent work and social protection to address economic, demographic and ecological transformations

- **Webinar 4 – Old-age, disability and survivors' benefits in light of ILO's pension policy**

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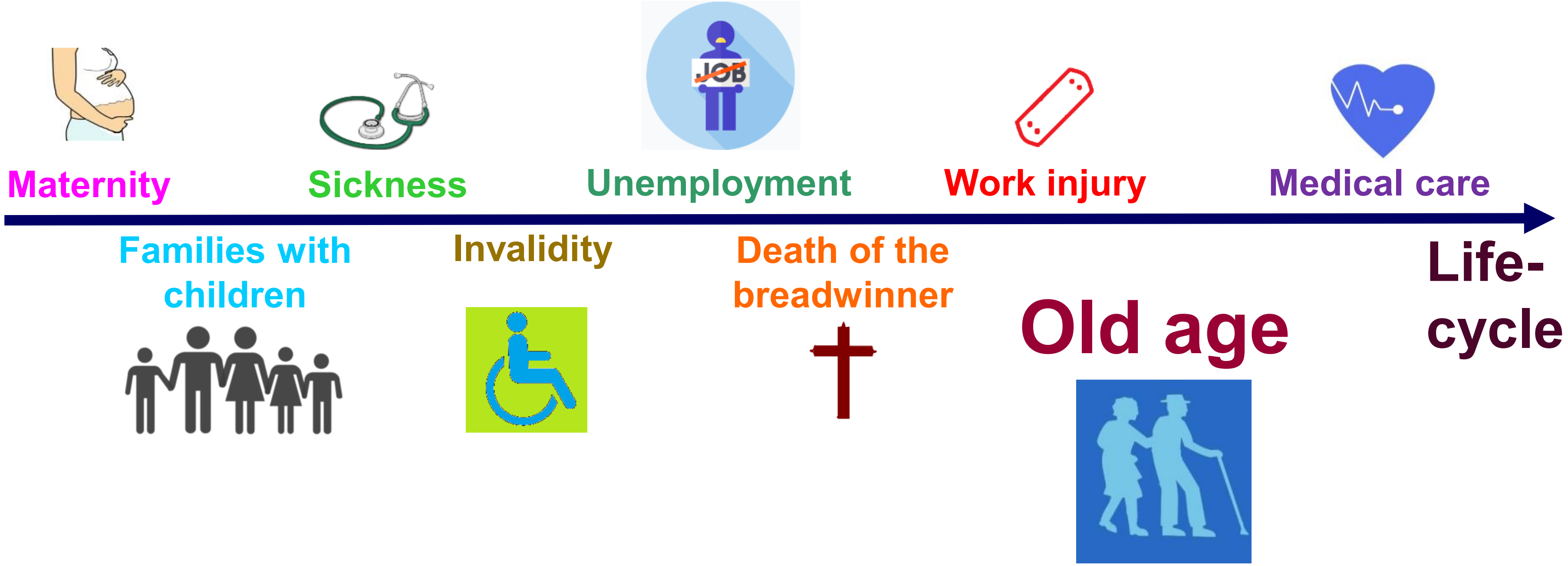
# What is social protection:
# 9 social security branches covered by Convention No. 102



# The relevant ILO social security standards for building and maintaining sustainable and universal pension systems as part of comprehensive social protection systems





## Social Security (Minimum Standards) Convention, 1952 (No. 102)

**Sets minimum standards for the nine branches of social security:**

- Minimum percentage of personal coverage;
- Minimum level of benefits
- Maximum qualifying period for the entitlement to benefits;
- Minimum duration of benefits

## Invalidity, Old-Age and Survivors' Benefits Convention, 1967 (No. 128) and Recommendation, 1967 (No. 131), Part III in conjunction with Part V

- Set higher levels of protection than C102 in terms of population covered and the level of benefits

## Social Protection Floors Recommendation, 2012 (No. 202)

- Provides guidance to member States in building comprehensive social security systems and complements the existing Conventions and Recommendations
- Provides for basic income security for persons in old age

# Minimum old-age benefit under Conventions No. 102 and No. 128, and Recommendation No. 202

| Contingency | Convention No. 102 | Convention No. 128 | Recommendation No. 202 |
|---|---|---|---|
| **Old-age** | ▪ 40% of former earnings after 30 years of contributions<br>▪ Reduced pension to be paid after a maximum of 15 years of contributions | ▪ 45% of former earnings after 30 years of contributions<br>▪ Reduced pension to be paid after a maximum of 15 years of contributions | ▪ Basic income security for older persons should ensure effective access to essential goods and services and allow life in dignity. Pensions should be adequacy and predictable |

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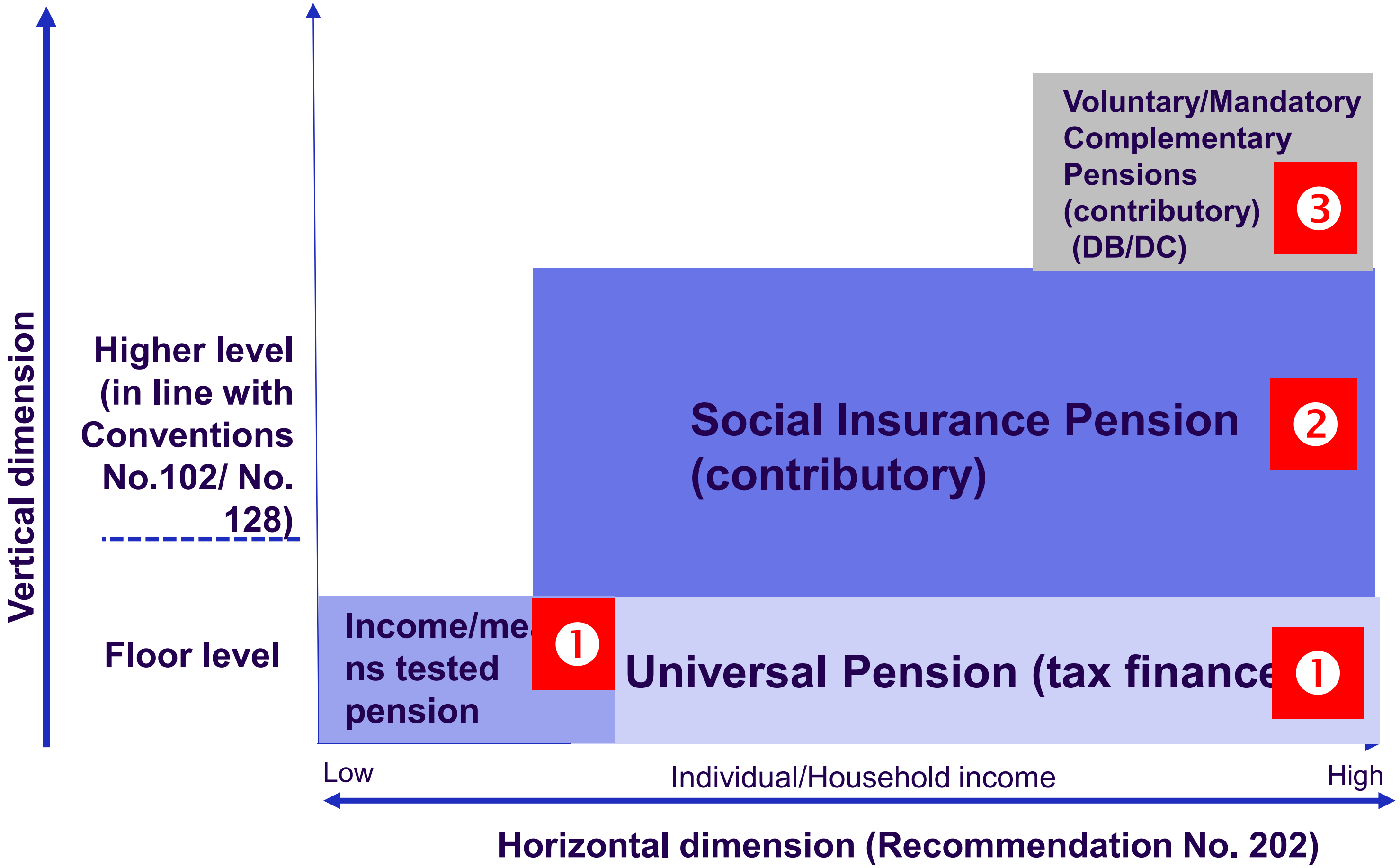
# The ILO's two-dimensional approach to pensions




**Pillar 1 – the pension floor:** The aim of this pillar is to establish a social protection floor for older people, through a non-contributory pension scheme and is financed from the general budget. This floor can either be universal or pension/means-tested ***(essential pillar of a national pension system)***.

**Pillar 2 – the social insurance pillar:** This pillar follows the typical design of social security pension systems, defined benefit and mandatory affiliation, financed through employer and worker contributions. It should provide higher levels of pension benefits so that people can maintain their standard of living after retirement. It should provide at least a minimum replacement rate of 40 per cent of former insured income to a person at retirement who has 30 years of contributions or employment, as well as a reduced pension for those who have contributed for at least 15 years. ***(essential pillar of a national pension system)***.

**Pillar 3 – the voluntary or mandatory complementary pillar:** Not all countries need to have this pillar. The complementary contributory component can be either voluntary or mandatory, employment-based occupational or non-occupational, and involve either defined benefits or defined contributions.

# What are the principles of ILO's social security standards to guide the organization and management of pension schemes?

- General responsibility of the State
- Universality
- Predictability of benefits defined by law
- Social solidarity and collective financing
- Adequacy of pensions
- Non-discrimination
- Transparency in management
- Social partners' participation
- Financial, fiscal and economic sustainability with due regard to social justice and equity
- Indexation of pensions in payment

## What is social solidarity

- Horizontal redistribution
- Vertical redistribution
- Intergenerational redistribution

# Extension of comprehensive pension coverage through universal social pensions or a mix of contributory and non-contributory provision

- A combination of contributory and non-contributory schemes is the most prevalent form of organization of pension systems in the world, appearing in 106 (54 per cent) out of the 195 countries for which data are available
- In 70 countries (36 per cent of the total), contributory schemes are the only mechanism providing old-age pensions – in most cases (67 countries) operating under a public social insurance scheme and covering mainly employees and self-employed workers, with the consequence that informal economy workers are often left out of these schemes
- In 14 countries, however, pensions are provided exclusively through non-contributory schemes. Of these, the majority (eight countries) provide universal coverage
- In a few countries, schemes do not offer pensions, but they do provide lump-sum benefits through provident funds or similar programmes. These are however not considered as adequate protection in old age by ILO social security standards, which require a periodical payment to be made throughout the contingency, i.e. until death

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# Classification of pension schemes

Defined benefit schemes

Defined contribution schemes

Notional defined contribution schemes

- **Defined benefit (DB) schemes** were at the origin of social security systems. Their financing is based on solidarity and pooling of risk and they provide benefits defined by national legislation:
  - **Social insurance pensions**: They are based on the principles of solidarity and collective financing established by ILO social security standards. The contributions paid on behalf of insured persons (share of income from work transferred to the pension scheme) are pooled in a common fund from which pensions are paid to pensioners based on a formula or methodology established by law, which can only be modified through a change in legislation.
  - **Universal and means/pension-tested schemes:** These schemes (non-contributory schemes) are usually financed from the general government budget. Benefits are paid either at a flat rate or as an amount that takes into account the beneficiary's means, and sometimes also the means of his or her family members
- **Defined contribution (DC) schemes:** Contributions are paid into an individual account for each insured person. They are invested in, for example, the fixed-income and equity markets, and the returns on the investments are credited to the individual's account. At the time of retirement, the balance of the savings plus the investment returns in the participant's account is applied to purchase a pension annuity. The pension paid depends on the amounts contributed and the investment earnings. As the future returns on the investments, and the future benefits to be paid, are not known in advance, there is no guarantee that a given level of contributions will translate into an adequate benefit level and provide income security.

# Defined Benefits vs Defined Contributions



## Many variations between pure DB and a pure DC schemes

Risk is assumed collectively.

Impact of risks is on contribution rate, instead of replacement rate (benefit).

This is much less volatile, because impact is assumed collectively and over very long period

**Defined Benefit (DB)**

**Pension level is defined**
(salary replacement ratio)

**Required contribution rate**

***Provides financial security***

**Defined Contribution (DC)**

**Contribution rate is defined**

**Resulting pension level**
(salary replacement ratio)

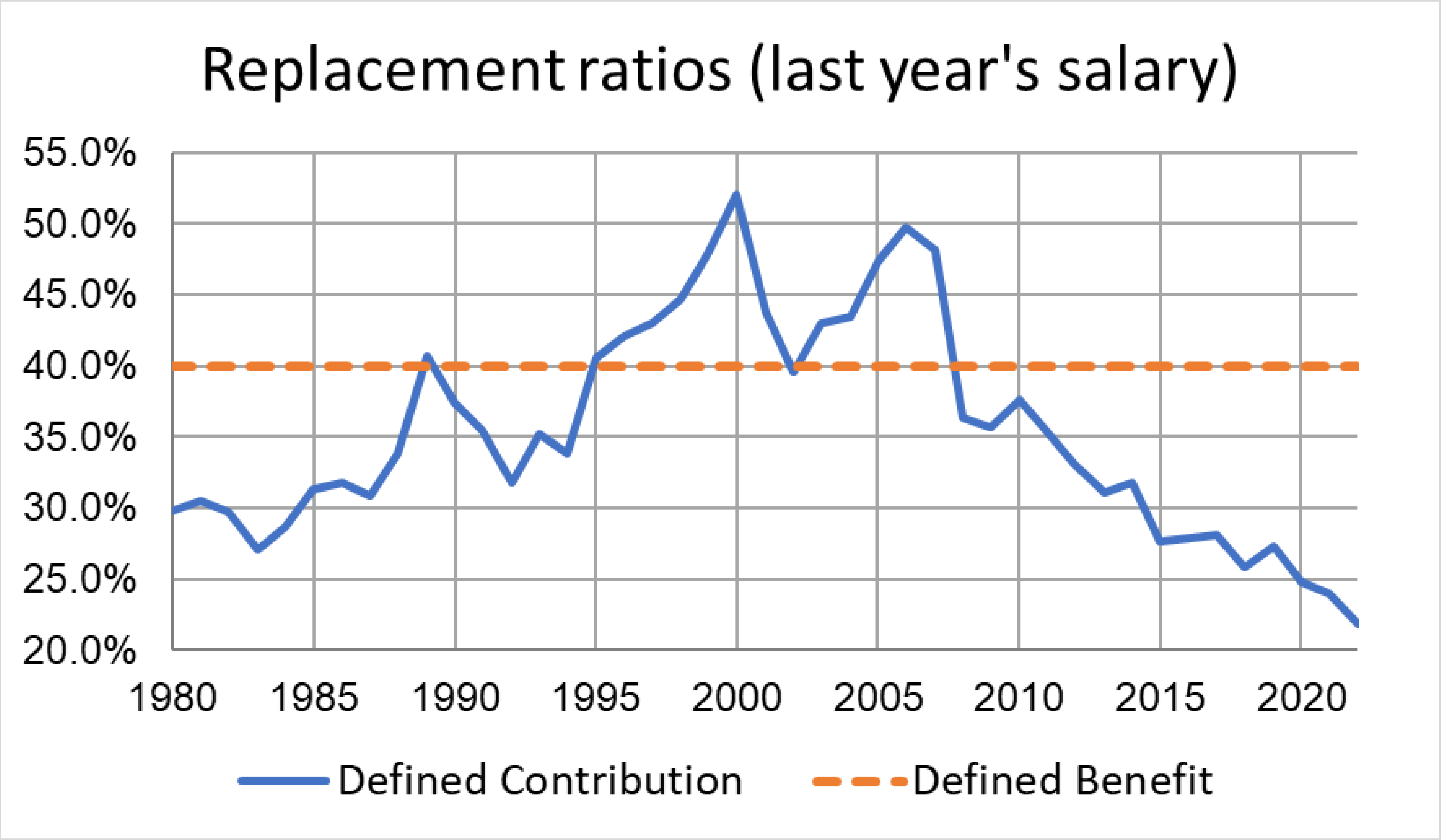
***Provides unpredictable revenue***

Risk is assumed individually.

Very high volatility of replacement ratios (benefit)

# Defined Contributions






Practical example based on actual Canadian historical economic cycles (salary increase, investment return, interest rates)

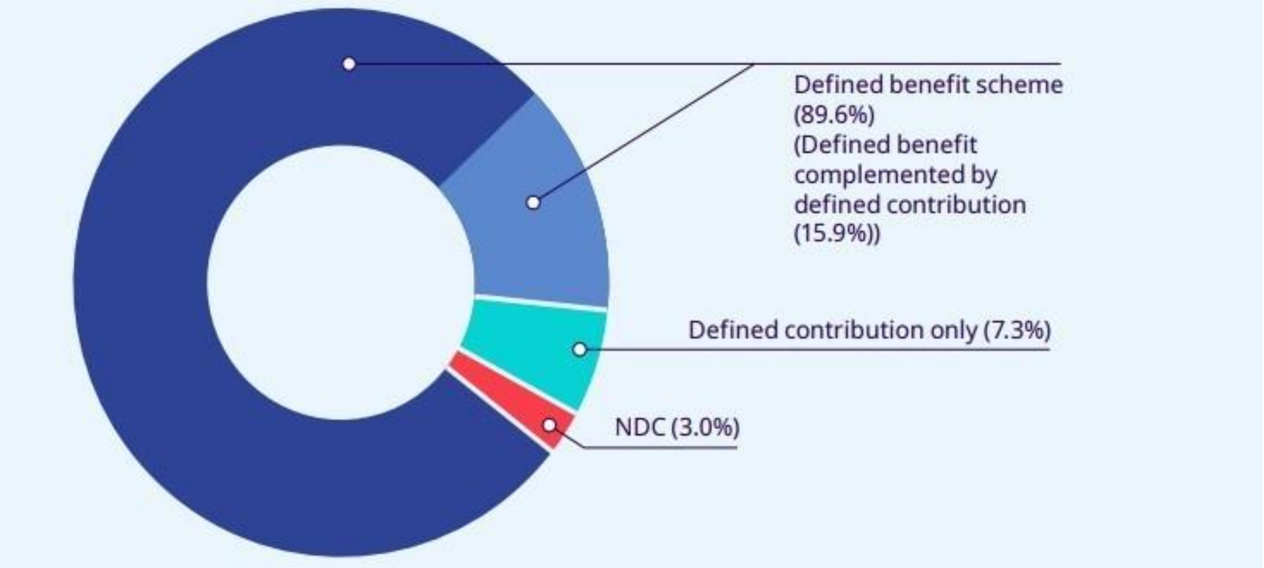
- ❑ 10% contribution rate
- ❑ 30 years of contribution
- ❑ 20-year life expectancy at retirement

Replacement ratios: pension at the date of retirement as a % of the last year's salary

Slide prepared by Andre Picard, Head, Actuarial Services Unit, Social Protection Department, ILO

# Which types of pension schemes are used around the world?

- DB schemes are the predominant schemes worldwide, being present in 89.6 per cent of countries. In one in six countries (15.9 per cent), DB schemes are complemented by mandatory DC schemes. Only 7.3 per cent of countries rely exclusively on mandatory DC schemes, based on individual accounts, and just 3 per cent have only NDC schemes



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# Pension privatization

## What is pension privatization?

**Pension privatization** is a simplified term used to describe a category of structural pension reforms involving three key changes:

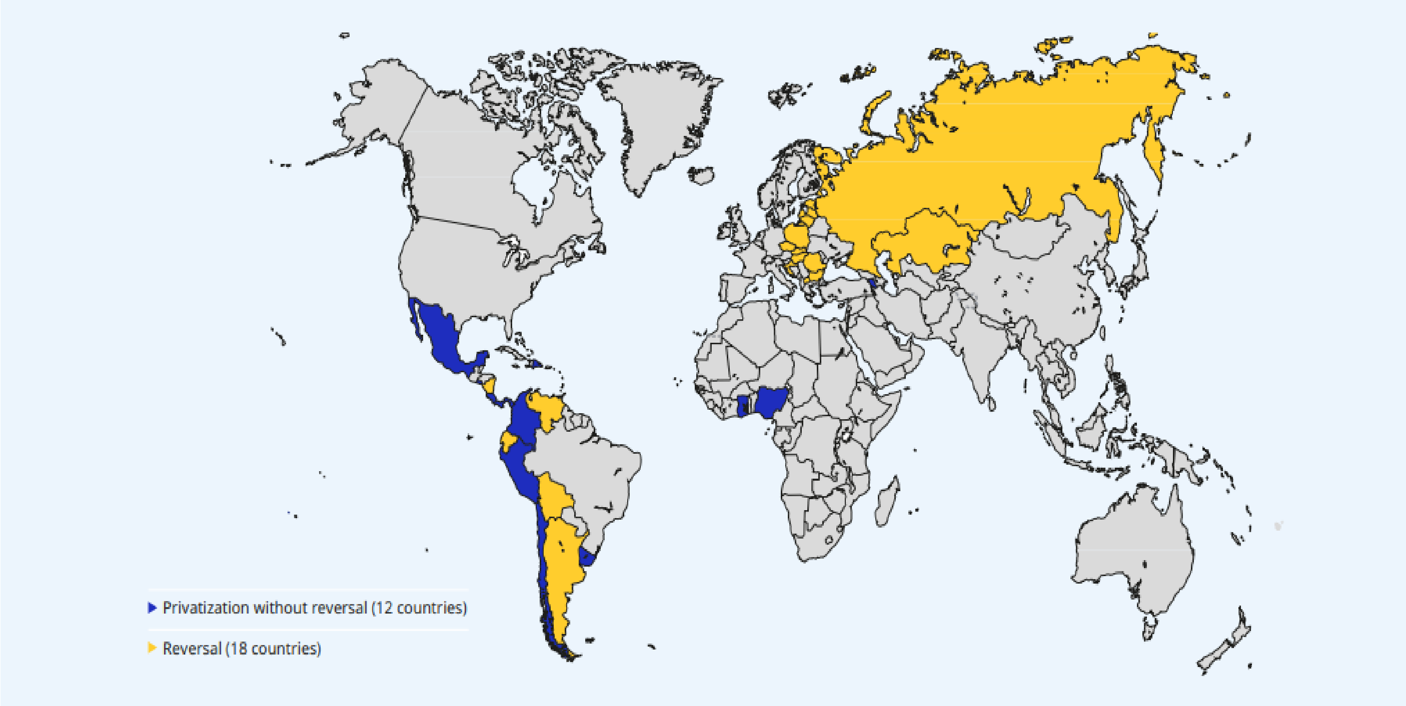
- A shift within the mandatory pension system from a **defined benefit** mechanism, in which retirement benefits are set in relation to working income, towards a **defined contribution** scheme, in which only the contributions are specified in advance, while benefits vary according to an individual's payroll contributions and the investment returns from those funds.
- A **shift from a pay-as-you-go financing method**, in which the payroll contributions of current workers are used to finance the benefits of current pensioners, **towards one in which old-age benefits are funded wholly by each worker's contributions to an individual account during his or her working life and the investment returns from those funds.**
- A **shift from public to private administration** of pension funds.

- Advocates of pension privatization claimed that whereas DB-based systems would lead to an unavoidable "social security crisis" or an "old-age crisis", privatization was a clear-cut solution to address population ageing and ensure the sustainability of social security pension systems
- It would not only enable higher pensions for future beneficiaries but also increase national savings and accelerate economic growth
- Additionally, a main objective of the privatization efforts was to mobilize people's savings so as to stimulate national long-term savings and develop capital markets

## HOWEVER:

- However, pension privatization policies did not deliver the expected results
- The reasons are multiple, ranging from high fiscal and administrative costs to low coverage and benefits, to the unpredictability of old-age income due to capital market risks
- During the 2008 global financial crisis, many pensioners had to rely on social support, as the value of their pension benefits had fallen to very low levels, often below the poverty line

# Pension privatization and reversal of reforms




- In Latin America, 10 countries undertook structural reforms, which replaced, in whole or in part, public systems with "private" systems
- Similarly, 14 countries in Eastern Europe and the former Soviet Union embarked on pension privatization
- Moreover, two African countries also privatized their public pension systems during the same period
  - By 2018, 15 countries had re-reformed and reversed pension privatization fully or partially, returning to public solidarity-based systems by terminating the individual accounts and transferring all funds to newly created or existing systems, or by merging the private pension funds with the public pension scheme, or by downsizing the volume of the individual accounts

# Different pension models from an ILO perspective: Which model complies best with ILO social security standards?

- Schemes based on defined benefits best fulfil the requirements set out in ILO social security standards and the key principles enshrined therein, for the following reasons:

  - ✓ State responsibility, investment risk and predictability
  - ✓ Collective financing and pooling of risks
  - ✓ Principle of solidarity and the purpose of redistribution
  - ✓ “One of the main lessons of the economic crisis has been the conclusion that, where the schemes were financed collectively and have been fully managed by the State, in particular through PAYG financing, the immediate impact has been small. In contrast, fully funded schemes, where individual savings have been invested in relatively volatile products, have sustained severe losses.” *ILO Committee of Experts on the Application of Conventions and Recommendations*

# How Can Trade Unions Contribute to the Achievement of Universal Pension Coverage?



## Workers' representatives can:

- Workers' organizations should make a vital contribution to informed discussions on pension reform policies and their implementation at the national level.

- To that end, they need to know which pension policy options are the best for their country, be aware of the various financing mechanisms and understand the implications of each option for social protection coverage and benefits.

- This requires in addition a high-level strategic vision and the ability to negotiate and generate consensus for the transformative changes necessary to fashion a better future that includes social protection for all

- Workers' representatives should insist on good governance of the social protection system. Board members of tripartite boards of directors of social security institutions are "trustees" for social security schemes and thus have to exercise a reasonable standard of care on behalf of all the beneficiaries of a scheme.

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# KEY RESOURCES:

## ACTRAV Social Protection Resource Package

### Workers’ guide:

- Workers’ guide to ILO Conventions concerning minimum standards of social security

### Four policy briefs on:

- Extending social protection coverage to informal economy workers: What workers’ organizations need to know
- Creating fiscal space for financing social protection: What workers’ organizations need to know
- Old-age pension models worldwide from an ILO perspective: What workers’ organizations need to know
- Closing gender gaps in social protection: What workers’ organizations need to know

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# Together we can achieve universal, sustainable and adequate pension schemes

## Thank you

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