

## SUSTAINABLE DEVELOPMENT: IS THERE A ROLE FOR THE PENSION FINANCING SCHEME?

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### Abstract

*The ageing phenomenon affects the entire world. The rate of elderly population is growing in all countries and the sustainability of public finance needs to be ensured. One of the most important instruments that absorb the ageing implication is the pension system, which varies from country to country. This article study the ways in which the design of the pension system in different countries can affect the sustainable development principle of “not compromising the ability of future generations to meet their own needs”, starting from the relation between the “pay-as-you-go” financing public pension system and sustainable development.*

**Keywords:** ageing, sustainable development, pension system, fiscal policy,

**JEL Classification:** Q01, J11, E62, H55

### 1. Introduction

The declared central objective of sustainable development consists in the idea that one generation should not affect another generation capacity to cover their needs, the consumption of a generation should not affect the consumption possibility of another generation (Nuta, F.M., 2011). In this context, the principle of financing, which is based Pillar 1 of the public pension system, can be interpreted as a clear violation of the concept of sustainable development, because in this pillar, the current generation of retirees affect the financing and consumption of future generation of retirees (equivalent to the current generation of employees) since the benefits are covered by current employee contributions.

On the other hand, sustainable development involves a stable population size, including in terms of population aging. Conclusions of economic analysis reveal that with increasing number of elderly population with changing dependency ratios, there are concerns about the long-term sustainability of providing income in this context.

In the specific literature cannot find approached this perspective on how are financed social benefits provided to pensioners, but rather the authors addressed the issue of sustainability of the pension system in terms of the existence or lack of financial resources to cover the needs of the system.

### 2. Pension systems characteristics and the impact on sustainable development

The novelty of this paper is generated by the connection of the sustainable development content with the choice of pension system structure from one country or another, ultimately demonstrating that a pension system that is based essentially on the idea of "pay-as-you-go" will affect the sustainable development potential of that country.

In the European Union countries the pension scheme is administered mainly by the state, which generated mandatory public pension scheme that offers income to elderly persons either as a single, centralized, either as alternatives according to business areas. Also, the studies (national reports) show that these public pension systems generally provide a "minimum pension" those who do not qualify to receive a pension based on income obtained throughout life, which in some cases is a particular case of social assistance.

In the EU the diversity of pension systems is caused by different levels that are the reforming process of the pension system, based mainly on defined contributions or benefit system, pension point system, but there are pension schemes that provide a flat rate pension, which can be increased through participation in the occupational or other parallel system (Denmark, the Netherlands, Ireland and the United Kingdom).

Thus, in the Member States there are 16 states with the public pension system are based on the principle of defined benefit (DB), 5 states that offer public pension system on the principles of defined contributions (DC), 3 states that offer pension on the principle pension point (PS) and 4 states that provide public pension system that combines all

elements mentioned above (fixed rate and defined benefit or defined benefit in combination with point system), according to the table below:

**Table 1: Pension systems in the EU-28**

	Countries	Pillar 1		Pillar 2-Mandatory (individual capitalized savings)	Pillar3-Voluntary	Occupational scheme
1	Austria	DB, financed by social contributions	PAYG, “statutory pension system” (“Gesetzliche Pensionsversicherung”)	-	DC from 2003	Mandatory
2	Belgium	DB	PAYG, including the „Silver Found” covering the pension since 2030	- DC from 2003 (Act on Supplementary Pensions)	Saving schemes	Voluntary
3	Bulgaria	DB	PAYG	DC from 2002, two types of funds: occupational funds and universal funds	DC from middle 90 and Pillar 4 din 2007	Voluntary
4	Czech Republic	DB	PAYG (Pension Act, 1995)	-	DC from 1994 (Supplementary Pension Insurance)	-
5	Cyprus	DB		- Law of 1984, private sector	-	Mandatory/Voluntary
6	Denmark	DB, public	(the national old age pension, 1956-folkepension)	- 1964: ATP scheme (Arbejdsmarkedets Tillægs Pension) and 1990: labour market pensions-(Supplerende arbejdsmarkedspension for førtidspensionister)	DC, Individual pension savings	Mandatory
7	Estonia	DB	PAYG, 1999, State pension scheme	Compulsory funded pension scheme, DC from 2002	Voluntary funded pension scheme, DC from 1998	-
8	France	DB+PS	PAYG and régimes complémentaires obligatoires	-	Voluntary, PERP – Plans d’épargne retraite populaires, 2003	Voluntary, PERCO – Plans d’épargne retraite collectif, 2003
9	Finland	DB	PAYG	-	Voluntary	Voluntary
10	Germany	PS	PAYG, 1957	-	DC from 2001	Voluntary
11	Greece	Flat rate + DB	PAYG	-	Voluntary	2002, Voluntary
12	Italy	NDC from 1995	PAYG	-	Voluntary, 1993	Voluntary, 2005
13	Ireland	FR+DB	PAYG	-	DC	Mandatory-public and Voluntary-private
14	Luxembourg	DB	PAYG	-	Voluntary	Voluntary
15	Latvia	NDC	PAYG, from 1996	DC from 2001	DC from 1998	-
16	Lithuania	DB	PAYG, from 1995	DC from 2004 and 2011 Voluntary	DC from 2004	-
17	Malta	Flat rate + DB	PAYG,	-	Voluntary	Mandatory-public, from 1979

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18	Netherlands	DB	PAYG, from 1956 Algemene Ouderdomswet or AOW	-	Voluntary	Mandatory
19	Portugal	DB	PAYG	-	Voluntary	Mandatory/Voluntary, 2008
20	Poland	NDC	PAYG from 1999	DC from 1999, otwarte fundusze emerytalne, OFE	DC	
21	United Kingdom	DB		-	Voluntary	Voluntary
22	Romania	PS	PAYG	DC from 2007	DC	-
23	Spain	DB		-	Voluntary	Mandatory-public// Voluntary-private
24	Sweden	NDC		Mandatory	Voluntary	Mandatory
25	Slovakia	PS	PAYG	DC from 2005	DC from 1996 and 2007	-
26	Slovenia	DB	PAYG	DC from 1992- Voluntary	DC	Mandatory/Voluntary
27	Hungary	DB	PAYG, 1950	DC from 1998, Voluntary	DC from 2007	-
28	Croatia	pension = PP x PF x APV (personal points, pension factor, actual pension value)	PAYG (Pension Insurance Act) - financed through contributions and budget transfers	DC from 2002 (Act on Compulsory and Voluntary Pension Funds)	DC from 2002 (Act on Pension Insurance Companies and Pension Payments)	
29	Norway	NDC		-	Voluntary	Mandatory

*Source: Countries reports ASISP 2013 European Commission, DG ECFIN, The 2012 Ageing Report: Economic and budgetary projections for the EU27 Member States (2010- 2060), pag. 87-90*

Note:

DB: Defined benefit system

DC: Notional defined contribution system

PS: Point system

FR: Flat rate

The decision to reform public pension systems in countries such as Bulgaria, Estonia, Latvia, Lithuania, Hungary, Poland and Slovakia, Romania, who turned the public pension system in two-pillar pension, mandatory public and mandatory pension with private administration is an important step for ensuring the sustainability of pension systems in those countries, including the principles of sustainable development regarding the provision of resources for all generations.

Most public pension systems provide financing on the principle of pay as you go, system which requires that the resources generated by social contributions imposed on employees and employers are used to cover the financing needs of current pensions in the public system, which generates the idea that pensioners are people assisted by the state in terms of financial support, eliminating the idea that these people contributed a lifetime, before retirement, to the system for ensuring their financing at this stage.

In this regard, we argue that PAYG system affects sustainable development, thus creating conditions for deteriorating future generations financial situation, especially considering the current and future evolution of ageing phenomenon.

Thus, given that the decision makers who manage public pension system does not realize this, the conditions for sustainable development will be irreparably damaged, the pressure on public systems become more intense, with the possibility that these systems lead to consistent public financial imbalances.

### 3. Conclusions

One of the most important measures to provide financing of the future generations based on own resources system contributions transferred to the state is that of boosting private system development, the second pillar pension, by increasing the contribution percentage that supply the individual funds, on the one hand, and, on the other hand, granting tax incentives to encourage saving as a way of providing the resources necessary after the moment of their retirement.

Thus, in essence, encouraging current employees for the establishment of funds that would ensure future revenue is the most important objective of the decision-makers. A further reason is the fact that the population of Europe is aging in the world with a percentage of 23% population aged 65 and over at the moment, estimated to maintain in the first place in 2050 when the percentage will be 34%.

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