Appendix 2 - Changes in the pension system

In accordance with the provisions of *the Act of 25 March 2011 on the amendment of certain act relating to the functioning (operation) of the social security system*, a *Review of the pension system* was published in June 2013, and on 4 September 2013, the concept of changes in the pension system to be introduced in 2014 was presented. Currently, a draft introducing changes in the pension system is being prepared, which will be forwarded for public consultation in the first half of October, and its assumptions include:

- **transfer of part of the pension rights of the insured, expressed by The State Treasury bonds, from the Open Pension Funds (OFE) to the Social Insurance Institution (ZUS)**
  - transfer of assets for a total amount equal to 51.5% of the assets of each pension fund (as of 31 December 2012) and saving pension rights resulting from the transferred assets on a sub-account maintained by the Social Insurance Institution,
  - redemption of Treasury bonds transferred to the Social Security Institution;
- **establishing the rules for pension payments from funds collected in OFE and for transfer the pension rights of the insured from OFE to ZUS:**
  - launching of the so-called "security slider", i.e. a mechanism of gradual, starting 10 years before retirement, transfer of capital accumulated in OFE to the pension fund of the Social Security Fund, and accounting for the sub-account maintained in ZUS,
  - calculation by ZUS of the pension, based on the measures recorded on the account of the insured (first pillar) and the sub-account (second pillar);
- **establishing a new amount of compulsory contribution transferred to the OFE equal to 2.92%,** which corresponds to the 40% limit of OFE investments in shares, with the original amount of contribution transferred to open pension funds (7.3%). **The proposed change in the functioning of OFE** which allows the insured and those entering the labour market to choose the fund, to which the social contribution goes, **does not change the mandatory nature of this part of the pension system (as opposed to voluntary forms of retirement savings in Individual Retirement Accounts – IKE, Individual Retirement Security Accounts – IKZE or the Occupational Pension Schemes – PPE).** After the entry into force of the amendments, the insured will still not be able to opt out of paying the mandatory pension contribution as required, and they may only decide whether future pension contributions will be forwarded to ZUS or OFE. Currently, the insured choose one of the open pension funds operating in Poland. Now, the alternative will include a sub-account in ZUS;
- **stimulation of the third pillar - through changes in the functioning of IKZE:**
  - adoption of tax solutions providing real incentives to save in IKZE – i.e. the introduction of taxation of payments from IKZE and payments

to persons entitled by flat-rate income tax, instead of the current taxation of payments from IKZE according to the PIT scale,

    - introduction of a limit on payments to IKZE, common to all, in the amount similar to the current maximum annual contribution limit for IKZE account, i.e. about PLN 4000;

- **removal of the minimum rate of return and the marketing of investment principles,** including:
    - prohibition on investments in the State Treasury debt instruments and debt instruments guaranteed by the State Treasury,
    - change in investment limits in various OFE investment categories,
    - increase in the limit of foreign investment, in connection with the judgment of the Court of Justice of the European Union in case C-271/09;
- **review of the system of fees and remuneration of pension funds:**
    - halving fees payable to the ZUS for the transfer of contributions to OFE;
    - halving the maximum contribution fee to 1.75 percentage points.

The impact of changes in the pension system on public finances

The establishment and functioning of OFE in the current formula makes it necessary to finance additional borrowing needs of the State Budget, resulting from covering from the State Budget the loss of pension contributions transferred to OFE since the beginning of the pension reform (i.e. since 1999) and expenditure on additional debt service in this respect. According to the Ministry of Finance, the total debt of the State Treasury in respect of the financing of additional borrowing needs relating to the establishment and functioning of OFE stood at the end of 2012 at PLN 279.4 billion, which accounted for 17.5% of GDP. This means that the debt due to OFE accounted for over 30% of the total debt.

The effect of the changes in the pension system will be an abrupt reduction of public debt in 2014, resulting mainly from the one-off effect of the redemption of the State Treasury securities purchased by the Ministry of Finance. According to preliminary estimates, assuming that half of the insured goes to ZUS, the public debt-to-GDP ratio will decrease as a result of changes in pensions by about 7 percentage points, and the ratio of the general government debt by about 8 percentage points. Therefore, after the entry into force of the **changes to the pension system, it is planned to adequately (by 7 percentage points) reduce the public debt thresholds on which the Stabilizing Expenditure Rule correction mechanism is based.**

The introduction of a "security slider" mechanism and a lower contribution to OFE, along with a lower number of insured in OFE will be conducive to lowering the borrowing needs in a sustainable manner in the coming years, and thus to the level of public debt.

According to ESA95 rules, the general government revenues will register a value equal to the amount of assumed pension liabilities, which is equal to the value of the assets acquired and redeemed. According to the ESA2010 rules, this transaction, as a rule, will be reflected in the financial accounts, without impact on the outcome of the sector.