Belgium: the end of the public pension reserve "Silver Fund"

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In 2001 Belgium created the "Silver Fund" as a means of front-loading the future cost of the pay-as-you-go pension scheme. Now (2016), 15 years later, although public pension reserve funds are a traditional financing instrument used in a number of countries, the government decides to abolish it.

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Description

In 2001, Belgium created the "Silver Fund" to safeguard the sustainability of public finances and the future of pensions. It was a form of pre-financing of the burden of future pensions (2010-2030). At the start the aim was to contribute annually up to a maximum of 1% of Gross Domestic Product (GDP), to be invested in government bonds. The fund could be drawn upon from 2010 onwards, when the first post-war baby boomers reached the age of 65, and provided that public debt was below 60% of GDP (Pacolet & Coudron, 2006).

Originally the Belgian High Council for Finance advised that any structural surplus in the public budget should be reserved in this Fund, reaching 0.7% in 2007 and up to 1.5% of GDP in 2011. In reality, financing of the fund remained fragmented from the outset, and from 2007 onwards no additional contributions were made, except for the capitalised interest on the investment portfolio. The portfolio is invested in Zero-coupon Treasury bonds. This was far below the original ambitions and the centre-right government decided to dismantle the fund in May 2016, arguing that it was no real additional fiscal reserve and that the future sustainability of pensions was guaranteed by more structural measures such as the increase of the legal pension age (Van Overtveldt, 27 May 2016).

From the very beginning the fund was criticised by economists, politicians as well as opinion makers, for being an "empty box", because the surpluses were invested in public debt, so that on balance no additional reserves were created. When drawing on the fund to finance future pensions, the state has to repay those bonds. Pensions, therefore, are being financed out of the general budget as the bonds are reimbursed. In reality the funds were however earmarked for future financing of the social security system, obviating the need for present spending and in the meantime facilitating the rest of the public debt.

Outlook & Commentary

In June 2016 the fund reached an amount of €21.9 billion (Zilverfonds, 2015). Between now and 2028 the capital and interest payments at maturity represent on average almost €2 billion a year. The question is how these funds will be used. The simplest solution would be for the state to offset its debt in "Silver Fund certificates" against the assets in "Silver Fund certificates" it owns via the "Silver Fund". An alternative would be to use the funds that will become available year after year to improve the level of social protection in Belgium. That would make it a real pay-as-you-go scheme, i.e. by using the yearly amount that comes available to finance yearly additional

expenditures for social protection.

The "Silver Fund" is not a unique example of public pension reserve fund. The OECD listed recently 25 such funds, of which the Social Security Trust Fund in the USA was the largest (OECD, 2016). In Europe public pension reserve funds exist also in Norway, Sweden, Finland, France, Spain, Portugal, Poland, Bulgaria and Bosnia-Herzegovina. In view of the fragmented financing track, and the size of the Belgium population (around 11 million inhabitants), the Belgian fund was not even disproportionately small. The "Silver Fund" (€21.9 billion) has already reached 53% of total public pension spending (€41.6 billion in 2014), which illustrates how it could contribute over some years to the financing of pensions, if that were needed. By way of comparison, the minimal level of the US Trust Fund for social security is 100%. In reality it is more, and of course there too pensions are really financed from the yearly revenue from contributions. The US Trust Fund is also invested in public debt.

At the moment when Belgium decided that the "Silver Fund" should be abolished, Germany had just launched a similar system. In 2015 a reserve fund for the long-term care insurance ("Pflegevorsorgefonds") was created. As well as increasing long-term care contributions, the government decided that each year 0.1 percent point of the contributions (some 1.2 billion per year for the moment) will be attributed to the fund. This fund can be used from 2035 onwards to boost financing of the German long-term care insurance. Similarly to the "Silver Fund", which could be drawn upon from 2010 onwards when the pension risk of the baby boomers materialises, the German long-term care fund can be depleted from 2035, when the German baby boomers reach the age when they may need long-term care services.

The Silver Fund is not the only public fund for social protection in Belgium. Since 2007, the Belgian health insurance has adopted a prudential approach by setting aside surpluses to compensate for future deficits. A "Future Fund" for the health insurance was created at that time. This front-loading of future costs stopped in 2010, but a contribution to the general equilibrium of the social security system was still possible, illustrating that there was still a margin within the growth targets for healthcare spending. With some €1.6 billion, the relative importance of the "Future Fund" compared to the current yearly expenditure was only 6.2% (Pacolet & De Wispelaere, 2015).

A more successful experiment was the reserve fund for the Flemish long-term care insurance ("Vlaamse Zorgverzekering"), also created in 2001. Here the front-loading of funding was even one of the basic characteristics of the insurance. In the first years of its existence, no less than 1/3 of the budget was used for capitalisation. In 2014 no additional funding was provided. Meanwhile the capital reached €898 million in 2014, or 2.7 times the yearly benefits from the Flemish long-term care insurance (Agentschap Zorg en Gezondheid, 2014).

Further reading

Agentschap Zorg en Gezondheid (2014), Vlaams Zorgfonds, Jaarverslag, Brussels

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