



Norway: Agreement on occupational pension reform in the public sector

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In March 2018, the Government and the public sector unions reached an agreement to adapt the public sector occupational pension schemes to the main principles of the 2011 National Insurance pension reform. With this agreement, the Norwegian pension reform has become fully effective also for the third of the workforce employed in the public sector.

Description

Since the late 1960s, Norway has had full coverage, with a homogenous and coordinated system of occupational pensions, for public sector employees (both the state and municipal sectors). The schemes have up till now been of the Defined Benefit type (i.e. promising a certain level of annual benefits), aiming to replace 66 percent of the final salary for employees with at least 30 years of service. Benefits from the first pillar National Insurance (NI) system are taken into account, so that the 66 percent replacement rate is reached by a combination of NI benefits and occupational pension benefits (so-called "gross integration"). While the benefit profile in the NI system is progressive, the benefit profile of the occupational supplement is regressive, resulting in a compound profile where total benefits are proportional to previous earnings. However, only annual earnings up to a ceiling set at NOK 1,162,600 (approx. €121,677) are replaced. Old age pensions can be drawn from age 67, but since the late 1980s a negotiated early-retirement scheme, *Avtalefestet* pension (AFP), has existed in both the private and public sectors, allowing employees to retire at age 62 without actuarial penalties.

In 2011, the reform of the NI system started to take effect. The reform entails the introduction of a Notional Defined Contribution (NDC) system for the accruing of benefits (i.e. a system

where a certain fraction of annual earnings is credited a pension account and where the accumulated amount is transformed into an annuity upon retirement), a mechanism for longevity adjustment of benefits, and an under-indexation of running pension benefits - 0.75 percentage points. It also introduces a flexible retirement age on actuarially neutral terms. The principles of the NI reform clash with the structure of the public sector occupational schemes, and in the 2009 wage bargaining round, the former (Stoltenberg) Government tried to negotiate a reform of the public sector occupational schemes to bring them into line with the NI reform. The attempt failed and the main features of the public sector occupational schemes were kept intact (the Defined Benefit formula with a 30-year rule for acquiring full benefits, and the gross integration with NI benefits). In addition, the public sector AP-scheme was kept intact as a subsidised early-retirement option between the ages of 62 and 67. By contrast, it had in 2008 been decided to completely transform a similar scheme in the private sector into a supplementary occupational pension scheme with a pension drawn on actuarially neutral terms – just like the reformed NI benefits.

The outcome of the public sector negotiations in 2009 was a serious setback for the overall pension reform. However, two important aspects of the reform (and the most significant

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retrenchment measures) were implemented in the public sector schemes as a result of the 2009 negotiations: the longevity adjustment to benefits and the under-indexation of running benefits (0.75 percentage points). As the years have passed, it has become increasingly clear to the public sector unions that these measures will gradually undermine the generosity of the schemes; benefits will become intolerably low for younger cohorts of public employees, without giving them the advantages of a flexible system to compensate for lower benefits by working longer.

Already in the Autumn of 2015 the public sector unions were in principle ready to renegotiate the 2009 outcome, but the process came to a halt because of procedural disagreements. In late 2017, a compromise was reached: pension negotiations were held separately from the 2018 wage bargaining, while unions were allowed to call a referendum among their members and to have a veto on the final outcome.

In March 2018 the negotiations were successfully completed, ending in an agreement that was later confirmed by an overwhelming majority of public sector union members. The agreement contains the following main elements:

1. The occupational schemes will be transformed into an NDC-framework equivalent to the reformed NI-system. Occupational pension rights will be accrued over the entire career with an annual accrual rate of 5.7 percent of earnings. For earnings in the range between the earnings ceiling in the NI scheme (set at NOK 681,600 [approx. €71,330]) and the ceiling in the occupational pension schemes (NOK 1,162,600 [approx. €121,677]), there will be an additional 18.1 percent accrual rate, adding up to a compound accrual rate of 23.8 percent.

Benefits can be taken out on actuarially neutral terms between age 62 and age 75, just like in NI. This new system will be applied to individuals born in 1963 or later, and will only start taking effect for new accrual from 2020. The former "gross integration" system will be entirely abandoned.

2. The existing AFP-scheme will be completely transformed, from an early-retirement scheme to an additional actuarially neutral, occupational old-age benefit scheme in line with the reformed private sector AFP scheme. Also, this pension accrual scheme will be an NDC scheme with annual accrual rates of 4.21 percent of earnings in the range covered by the NI scheme (up to NOK 681,600 [approx. €71,330]). By aligning the public and the private sector AFP-schemes, a serious obstacle to mobility between the two sectors has been removed.

3. For employees whose health and/or work-conditions make it difficult to continue working after age 62, a small transitory benefit was introduced offering benefits between the age of 62 and 67 of about 10 percent of the previous scheme.

Outlook & commentary

The agreement marks the completion of the Norwegian pension reform, that would otherwise have been seriously curtailed by only partly applying to public sector employees. The agreement is therefore important for the legitimacy of the overall reform, and the strong support shown for it in the union membership referendum was a significant victory for the social partners and for Norwegian tripartite negotiations.

Under the agreement, public sector employees have retained relatively generous occupational pension schemes that now apply principles of life-long accrual, and actuarial

neutrality with respect to the timing of benefit take-up. For public sector employees who have had short careers and who prefer or are forced to withdraw from work at age 62, the new system will clearly be less favourable than the old, but for those public sector employees who can take advantage of the actuarial neutrality by working longer, the agreement means that they will benefit from decent replacement rates, although the longevity adjustment will lower annual benefits in the decades to come.

The public sector unions managed to gain a symbolic concession from the Government – the introduction of a small new supplementary benefit targeted at employees who leave the labour market and take up benefits early at age 62. This new benefit breaks with the principle of actuarial neutrality, but it is very small and is scheduled to be gradually withdrawn for younger cohorts. In future negotiations between the Government and the public sector unions, a possible expansion of this scheme is likely to be on the agenda.

Further reading

Avtale om offentlig tjenstepensjon [Agreement on public sector occupational pensions]: <https://www.regjeringen.no/globalassets/departementene/asd/dokumenter/2018/pensjonsavtale-oftp-2018-03-03.pdf>

West Pedersen, A. (2017). ESPN Flash report 2017/06: [Towards a fully individualised pension system in Norway](#).

West Pedersen, A. (2015). ESPN Flash report 2015/57: [Employment protection age limit extended from age 70 to age 72](#).

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