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Kosovo* plans significant pension policy shift

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In November 2018, the Ministry of Labour and Social Welfare proposed a substantial reform of the existing 3-pillar pension system. A major element of the reform is the re-introduction of a Pay-As-You-Go (PAYG) pension. The objectives of the reform include ending the layering of the general tax-financed pensions benefiting powerful interest groups by establishing universal rules and increasing the income of ("average") pensioners.

Description

Unlike in other former Yugoslav entities, the Pay-As-You-Go (PAYG) pension system, in which current workers' contributions are used to pay for current pensions (contrary to funded systems where contributions are set aside in a fund and used after workers retire), was fully discontinued in Kosovo. In 2002, the "United Nations Mission in Kosovo" (UNMIK), which administered the territory between July 1999 and February 2008, established a 3-pillar pension system in line with the advice of the World Bank and other donors (Cocozzelli 2007, World Bank 2007). Originally, this system was organised as follows (for details on terminology, see Pension Adequacy Report 2018):

- Pillar I: A flat-rate basic pension for all residents aged 65 or above, paid from general taxation and connected to the cost of a minimal food basket (2,100 calories a day), i.e. only €75 per month in 2018.
- Pillar II: A statutory funded scheme, financed by minimum 10% of gross salaries paid equally by employers and employees and managed by the autonomous body Kosovo Pension Savings Trust (KPST). This is a mandatory individual pension savings scheme rather than a classical pension: After reaching pensionable age (65 years), an initial lump sum and a monthly payment no smaller than minimum wage are issued until the individual saving is used up. This income is generally low and spent after only a few years Thereafter, the pensioners should rely on the basic pension only.
- Pillar III: Personal pension schemes. Pillar III is underdeveloped, with only one existing fund which managed only 0.6% of all (€1.65 billion) pension savings in 2017.

Over time, in particular after Kosovo's declaration of independence (2008), the number of Pillar I pensioners has grown continuously since more schemes (beyond the flat-rate basic pension) have been created to cover specific and often powerful interest groups (e.g. former socialist workers and war veterans). There are now 13 Pillar I pension schemes covering different categories of individuals with different eligibility criteria and unequal payments, and more social groups are requesting similar schemes. As a result, more than 95% of all pension spending is financed through general taxation. Based on the findings of the Auditor General, 4.97% of all Pillar I pensioners were either working or receiving double tax-financed pensions - against the law – in 2017. Many veterans of war also exit work to become eligible for such pensions.

In November 2018, the Ministry of Labour and Social Welfare proposed a substantial reform of the pension system with a view to ending the layering of the general tax-financed pensions benefiting powerful interest

This designation is without prejudice to positions on status, and is in line with UNSCR 1244/1999 and the ICJ Opinion on the Kosovo declaration of independence.

groups by establishing universal rules and increasing the income of ("average") pensioners. The following are the main proposed changes:

- Former Pillar I, financed through general taxation, will be named Pillar Zero (0). Basic old-age pensions will be means tested to individual income and set at least at 20% of the median market individual income. For disability pensions, the rules that determine the level of disability for ordinary citizens will now also apply for invalids of war.
- In Pillar II, the old-age pension income will be calculated by dividing the overall saving for the average life expectancy after 65 (144 months in 2018). If the resulting pension income is lower than 60% of the median income (which corresponds to the income poverty threshold according to the EU definition), the basic pension (Pillar 0) will be added to it entirely or only to fill the difference. Pensioners with income equal to or higher than 60% of the median will not receive basic pension.
- Pillar I: A Pay-As-You-Go (PAYG) pension, in which current workers' contributions are used to pay for current pensions (contrary to funded systems where contributions are set aside in a fund and used after workers retire), will be reinstalled for the first time since pre-war (1999). Pillar I will kick in to finance the pension of retirees after they have spent their savings in Pillar II (that is, after 144 months), under the same terms they sustained in Pillar II, until death. Thus, if an individual used to receive €100 a month from Pillar II during 144 months, Pillar I will now continue to pay €100 after 144 months and until death. This will be financed from 3% contributions from employers (1.5%) and employees (1.5%). Pillar I will have a pension ceiling set at 2.4 x 60% of the median income. The reform also introduces Pillar I disability pensions for disability due to accident or occupational disease.

Relevant local actors, including political parties and worker unions, are in favour of the PAYG. Several political parties (such as the Social Democratic Initiative and the Social Democratic Party) and worker unions have even proposed to make PAYG the main pillar.

Outlook & commentary

Comprehensive pension legislation treating all citizens through universal or similar criteria would benefit Kosovo. The current expansion of specific pension schemes funded by general taxation is unsustainable (see IMF 2016, Kllokoqi 2018). As many groups have acquired rights in this way, pension inequalities will increase and pensions received by the average pensioner will remain low. The effectiveness of pensions in reducing income poverty and inequality will decrease as they are often targeted at those groups which are already well-off. Since around 85% of government revenues (2018) are collected from consumption taxation, the current social spending pattern without any reform will continue to increase the burden on the poor.

If the reform is endorsed by the Government, the pension coverage of old age population will remain 100%. However, the basic pension will now serve as a "guarantee pension" (rather than a universal one as it currently is) since it will be issued only to those with income under 60% of the median. This will spare some national budget.

At the same time, the reform document recognises the period of 1990s as "years of work contribution" for all former socialist workers who were removed from their jobs after the cancellation of Kosovo's autonomy in 1989. This will make thousands people eligible for pensions in the scheme of former contributors (Pillar 0). In addition, the reform document does not address at all the pensions of war veterans (Pillar 0), despite prosecutorial claims that hundreds have been falsely claiming the status of veterans. Bringing forward appropriate solutions for these two groups is essential, as it would ease considerably the short-term burden on the national budget and could contribute to decreasing inequality among pensioners.

Further reading

Cocozzelli, F. (2007), "Kosovo", in B. Deacon and P. Stubbs P (eds.) Social policy and international interventions in South East Europe. Cheltenham: Edward Elgar.

European Commission and Social Protection Committee (2018), Pension Adequacy Report 2018: current and future income adequacy in old age in the EU – Vol. I, Luxembourg: Publications Office of the EU.

IMF (2016), Kosovo technical assistance report - enhancing social protection cash benefits. Washington DC: International Monetary Fund (available here).

Kllokoqi, S. (2018), Reforma pensionale – rruga që duhet ndjekur? [Pension reform – the road forward?]. Prishtina: Institute for Development Policy.

World Bank (2007), The Kosovo pension reform: Achievements and lessons. Washington DC: The World Bank (available here).

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