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A new plan to reform part of the statutory pension scheme in Greece

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The Greek government plans to adopt a new reform of "auxiliary" pensions, which are part of the statutory pension scheme, introducing a transition from a pay-as-you-go notional defined-contribution scheme to a fully funded defined-contribution scheme. Debates are ongoing, while more details about the reform and its actual features will be made available with the adoption of the related bill by the parliament, expected in September 2021.

Description

The Greek government plans to adopt a new reform of the so-called "auxiliary" pensions, which are part of the statutory pension scheme. This reform is included in the National Recovery and Resilience Plan and is expected to bring about significant changes to the national pension system. Currently, pensions are based on a unified multi-tier (public) statutory pension scheme, which consists of four parts: i) a "national" (quasi-universal) non-contributory pension (financed from the state budget); ii) a compulsory contributory (primary) pension which operates under a defined-benefit pay-as-you-go scheme (an unfunded scheme); iii) a contributory auxiliary (secondary) pension based on a completely notional defined-contribution (NDC) scheme; and iv) lump-sum retirement benefits which are contributory, being provided under an NDC scheme. The reform envisages the transition of public auxiliary pensions from an NDC scheme to a fully funded defined-contribution scheme, financed by mandatory social insurance contributions paid by all employed persons. Auxiliary pensions will continue to constitute part of the first-pillar (public) statutory pension scheme.

In the post-reform system, every insured person will have an individual pension account of social insurance contributions; this will be invested, with the return on investment determining the amount of the auxiliary pension. The insured person will be able to choose to place their contributions into products of varying investment risk exposure (low, medium or high), while investments will be made by certified investment service providers, such as: financial institutions, insurance companies or asset management companies, operating under a strict framework of supervision and control. A new public organisation, the so-called "Hellenic Auxiliary Pensions Defined Contributions Fund (TEKA)", will be responsible for the management of social insurance contributions and for the payment of auxiliary pension benefits. The new levels of social contributions for the auxiliary pensions are expected to take effect from 1 June 2022 onwards: 6% for employees (3% paid by the employee and 3% by the employer) and €39, €47 or €56 for self-employed persons, depending on their chosen contribution category.

The system will also include a negative return guarantee to ensure that, whatever happens, the insured person will get back the amounts paid in social insurance contributions in real terms. This new system will be applied to those entering the job market from 1 January 2022, as well as, on a voluntary basis, to currently insured persons aged up to 35. As such, the reform is not expected to impose any change either to current auxiliary pensions or to the way in which auxiliary pensions are calculated for: i) insured persons aged 35+ on 31 December 2021; and ii) insured persons aged under 35 who do not choose to join the new system. It should be noted that the provision of survivors' and disability auxiliary pensions will be maintained; these will be financed by a special solidarity charge applied to the social insurance contributions paid.

According to the government, this reform is designed to address the negative effects of demographic developments on auxiliary pensions, and to strengthen public trust in the national pension system. At the same time, the government argues that this new system will further align benefits with contributions, thereby providing incentives for labour force participation while "disincentivising" undeclared work. In addition, the government expects that the reform will result in higher levels of auxiliary pensions. Finally, the government anticipates that this reform will increase savings and investments, which will, in turn, contribute to economic growth.

More details about the reform and its actual features will be made available with the submission of the related bill of Law to the parliament. The bill is expected to be adopted in September 2021, after public consultation, and will be accompanied by: i) an actuarial study; ii) a macroeconomic study; and iii) a public debt sustainability study. All three studies have already been published.

Outlook and commentary

The reform has brought to the forefront a long-standing debate about the introduction of fully funded defined-contribution elements into the national pension system. In this context, it is being heavily criticised by representatives of most opposition parties; they question the need for the reform, arguing that the negative effects of demographic developments on the pension system have already been mitigated by the 2016 reforms. Another main criticism is the high cost of the transition, which will extend over 60 years and involve the payment of auxiliary pensions to insured persons under the current system. According to the government, this cost will be covered by general taxation and the reserves of the "National Account of Social Solidarity between Generations (AKAGE)" as well as by additional resources expected to result from the economic growth. The exposure of auxiliary pension funds to market risk is also a major point of disagreement. Opposition parties refer to the experience of other countries which carried out similar reforms and, due to the negative effects of the post-2008/2009 economic and financial crisis on pension levels, were forced to cancel these reforms and return to pay-as-you-go pension systems.

The social partners stress the high risk to pension adequacy, and the extra financial burden that may potentially be placed on employed persons in an attempt to cover the costs of the transition. In addition, they claim that pensioners are more likely to receive lower auxiliary pensions, since the amount of the auxiliary pension is linked to fund performance, and thereby exposed to market risk. Finally, they raise questions about the impact of this reform on enhancing investments, and about the fiscal risk due to the high transition cost.

Undoubtedly, the reform will bring about a system for auxiliary pensions that will not be affected by demographic changes and their impact on the ratio of employed persons to pensioners, as auxiliary pension benefits will be determined by the assets accumulated in individual pension accounts. Yet it is questionable whether future auxiliary pensions will be higher: they will be exposed to market risk and will therefore be vulnerable to financial market shocks.

The potential positive outcomes advocated by the government are uncertain and, even if they do occur, it will be a long time later. In addition, the government needs to ensure that critical elements (such as: adequate organisational and administrative capacity, sufficient personnel, specific procedures, etc.) are properly in place for the implementation of this reform.

At present, it is hardly possible to provide an ex ante evaluation of the implications of the reform, given that its actual provisions have not yet been specified. In any case, any reform of the pension system must comply with the constitutional obligation on the State to guarantee the provision of social insurance benefits, while safeguarding social justice between the generations by fairly distributing the transition costs between them.

Further reading

Bun INE GSEE (2020) *The transition of the Greek economy to a new model of growth - An alternative proposal to the Pissaridis Report*, *Athens: Labour Institute of the Greek General Confederation of Labour (INE GSEE) (in Greek)*

Greek Government (2020) *Strategic directions of the National Recovery and Resilience Plan*, Athens: Ministry of Finance.

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