

Providing social security for the elderly

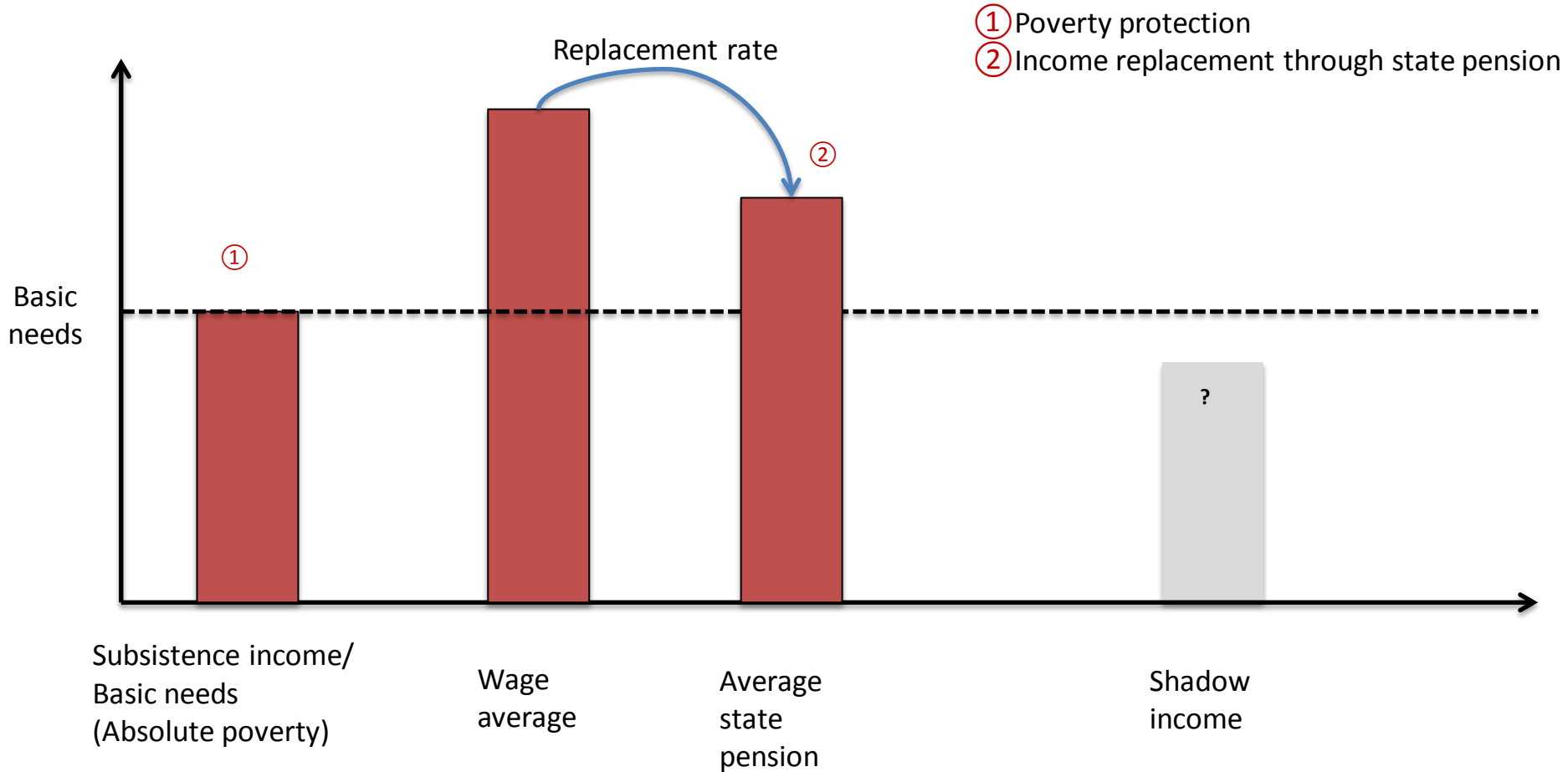
- An assessment of existing social insurance and assistance measures -

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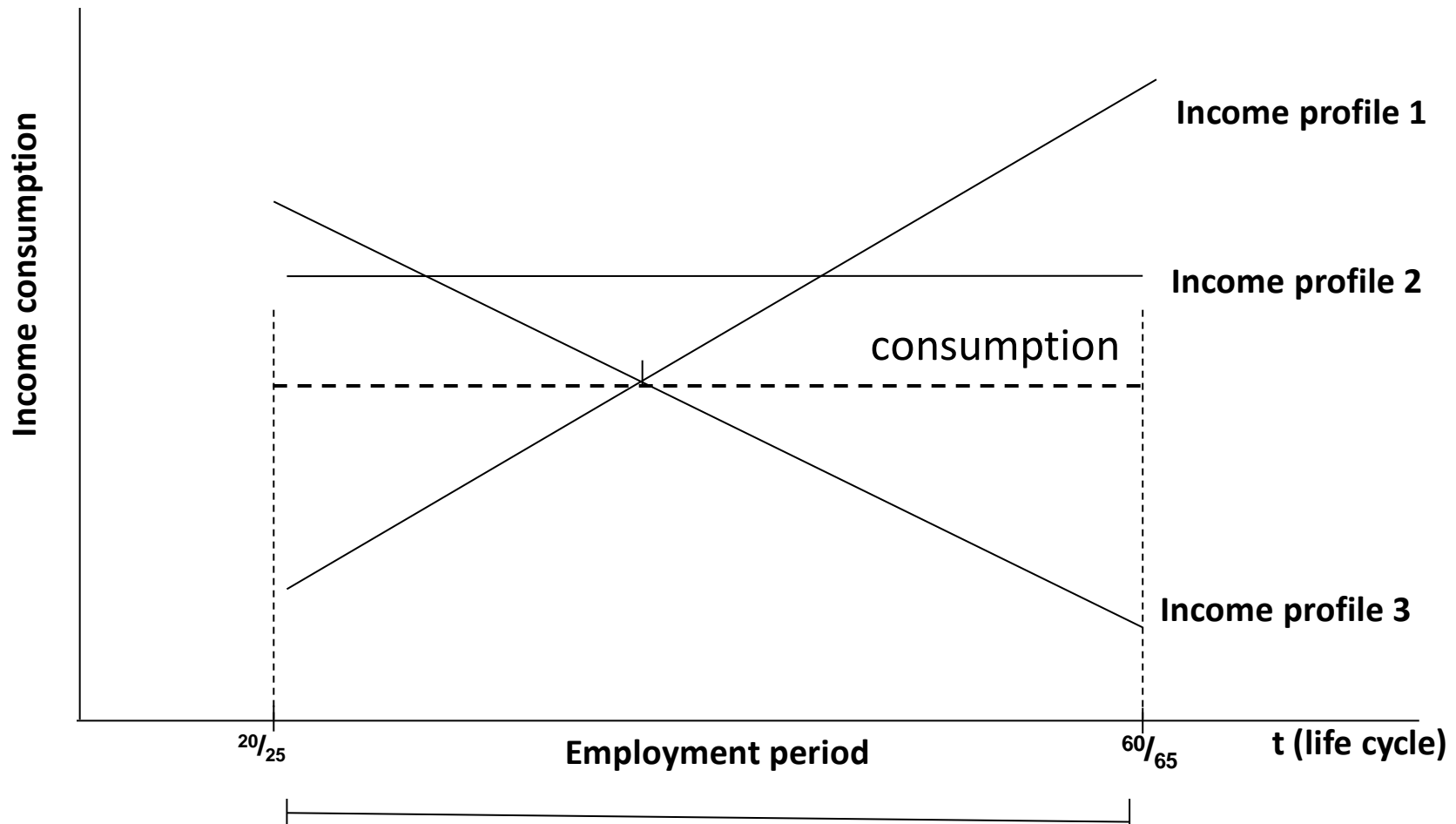
German Economic Team Moldova in cooperation with INCE

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Objectives for poverty reduction and state pension



Poverty prevention during the life cycle



Main objectives of social security (for the elderly)

1. **Poverty prevention:** individual has enough income to meet basic consumption needs (subsistence minimum)
2. **Income replacement:** upon retirement state pension sufficient to replace significant share of work income (replacement rate)

Question of this policy briefing

- How to ensure social policy is able to meet both objectives?

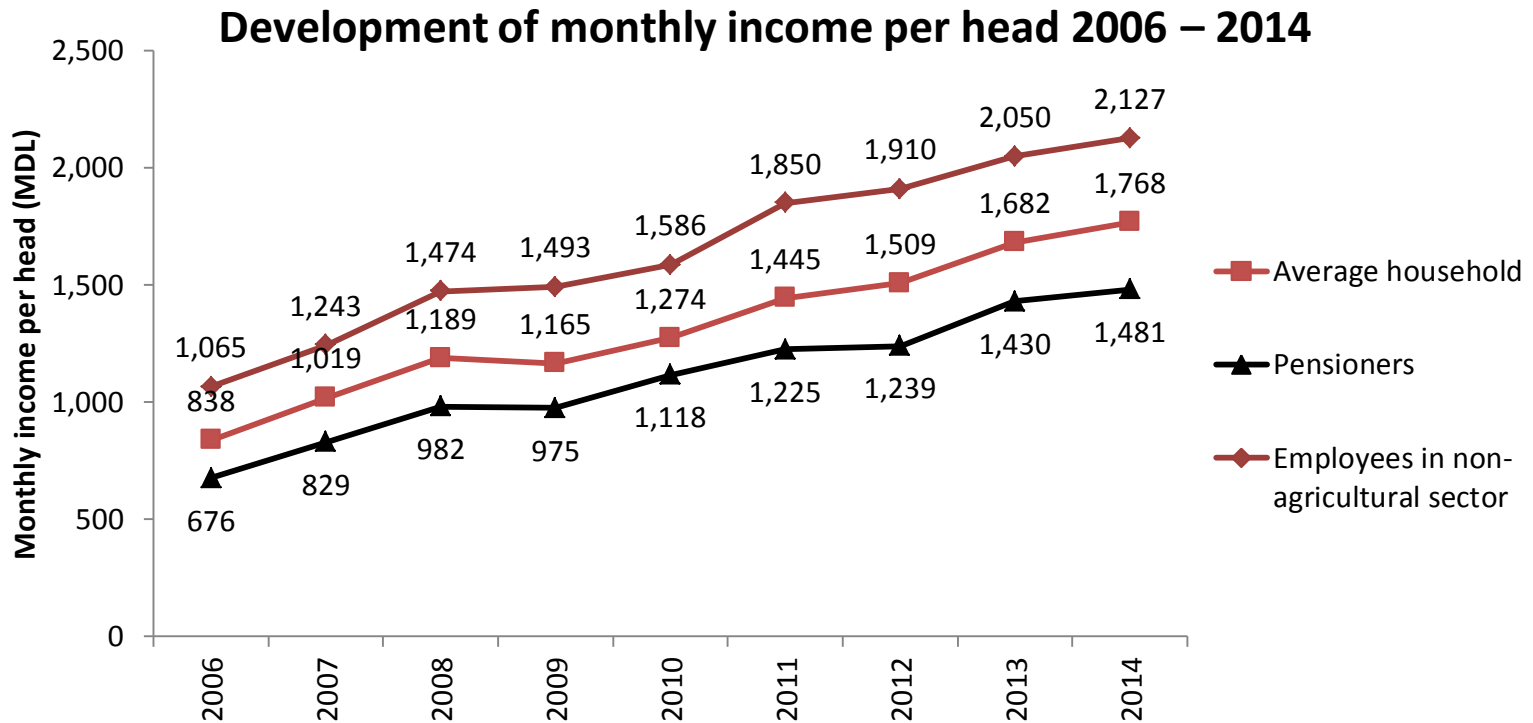
Structure

Part 1: Income distribution and poverty risk of the elderly

Part 2: Assessment of the existing social insurance and social assistance measures

Part 3: Recommendations for policy reform

Income developments pensioners vs. average household

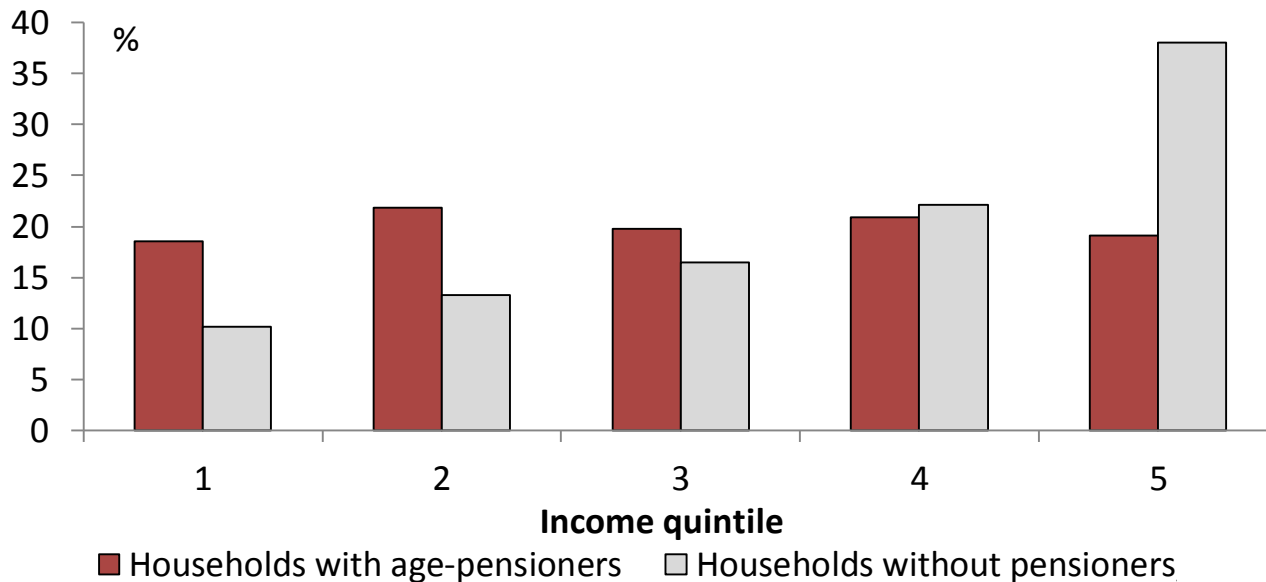


- Total income of pensioners (pension plus social transfers, wages, remittances, etc.) averaged ca. MDL 1500 in 2014 vs. MDL 1800 for all households
- Income situation better than average pension suggests
- Note: Numbers need to be treated with caution as especially wage income significantly underreported

Source: Office for National Statistics

How is total income of the elderly distributed?

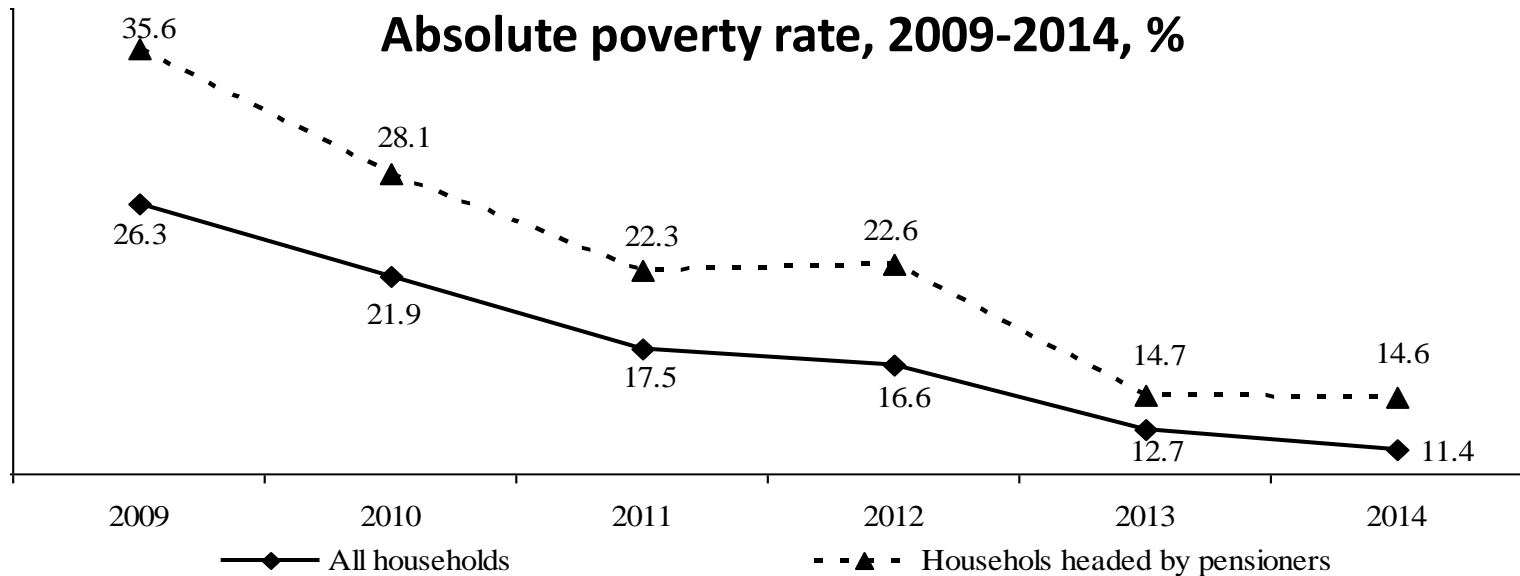
Distribution of income per head



- Total income (including pension, social assistance, wages, remittances, etc.) of people with old age pension rather equally distributed

Source: own analysis based on HBS

What is the poverty risk? – Absolute poverty



- Absolute poverty rate: Share of people with incomes below officially defined poverty line of MDL 1,257
- 14.6% of households with pensioners below absolute poverty line
- In comparison: Absolute poverty rate for population as a whole was 11.4%
- Falling trend of poverty risk for both groups

Source: own analysis

Poverty risk – Relative Poverty

The level of relative poverty of household members by area in 2014, %

	Total country	Big cities	Small cities	Villages
All households	6.7	1.2	3.6	10.0
Households with pensioners	7.0	2.0	4.1	9.6
Households with <i>old-age</i> pensioners	8.9	1.1	4.7	12.7
Households without old-age pensioners	5.9	0.8	3.8	9.1

Relative poverty: Share of people that can afford to consume less than 60% of the average (medium) consumer spending

- According to this rate, 8.9% of households with old-age pensioner live in poverty
- In comparison relative poverty rate of all households was 6.7%

Conclusion: Poverty rate of households with old age pensioners moderately higher

Source: own analysis based on Household Budget Survey

Income distribution and poverty risk among the elderly

Findings:

- Average incomes among the elderly remain low
- Yet incomes are much higher than average old age pension level suggests, elderly seem to be able to draw on various other income sources
- Statistics suggest a relatively low poverty risk for the elderly
- However, poverty line is set at a very low level

Conclusions:

- ① Existing social insurance and social assistance instrument quite good at preventing outright poverty among the elderly
- ② However, a large share of the elderly are „almost“ poor

Structure

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Description of existing major social security measures

Social insurance

mainly financed through Social State Insurance Budget (SSIB)

(Regular) retirement pension:

- Conditional upon
 - Retirement age (women: 57, men: 62)
 - Minimum contribution period of 30/32 years
- Pay as you go
- Partial retirement requires at least 15 years of contribution

Minimum pension:

- Requires at least 30/32 years of contribution for compensation up to MDL 760 (agricultural sector) or MDL 860 (rest of economy)

Top-up:

- If (any) pension is below MDL 1500, an additional lump-sum of up to MDL 180 is granted

Social assistance

mainly financed through the state budget (SB)

State social allowances:

- Socially deprived groups
- Covers old-age population with no entitlement to retirement pension

Social Aid:

- Tops up monthly income for low income households if income below guaranteed minimum income

Cold Season Support Allowance

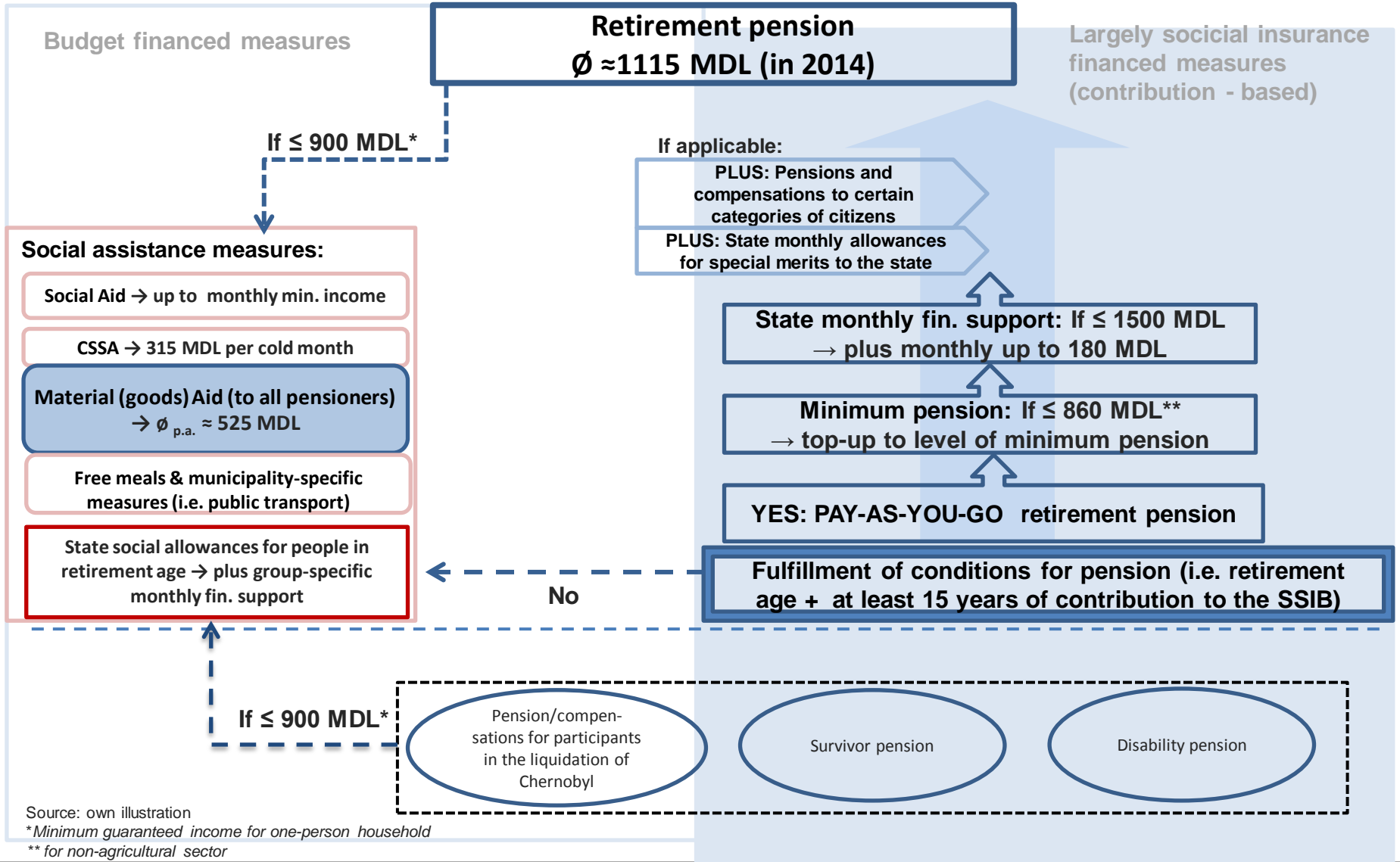
- CSSA during the heating season for low-income families

Material Aid

- Material aid (money/goods) provided once per year to any pensioner or person in despair

PLUS: Other (smaller) support measures including through local authorities

Social security system for the elderly



Is the current system able to meet its objectives?

Question: Is the current system suitable to meet the two objectives:

- (1) Poverty prevention and
- (2) income replacement?

Assessment:

Current system good at preventing outright poverty but not able to provide sufficient income replacement.

Problematic aspects of the current social security system

Problematic aspects

1. No clear division between income replacement and poverty prevention
2. State pension system (especially minimum pension) used mainly as a tool to prevent poverty – objective of income replacement neglected
3. Too much money redistributed, pension system cannot fulfil its actual purpose of income replacement for those who contributed towards a pension
4. **Lack of fairness:** pension of those who earned a regular pension on average only hardly above minimum pension level
5. Very **low incentives** for workers to earn a regular pension, much better to stop after minimum pension is earned
6. Too many overlapping and conflicting social assistance measures aimed at the elderly
7. Poor targeting of some social assistance measures – may also benefit pensioners with high income
8. Nevertheless social assistance level not high enough to cover basic needs

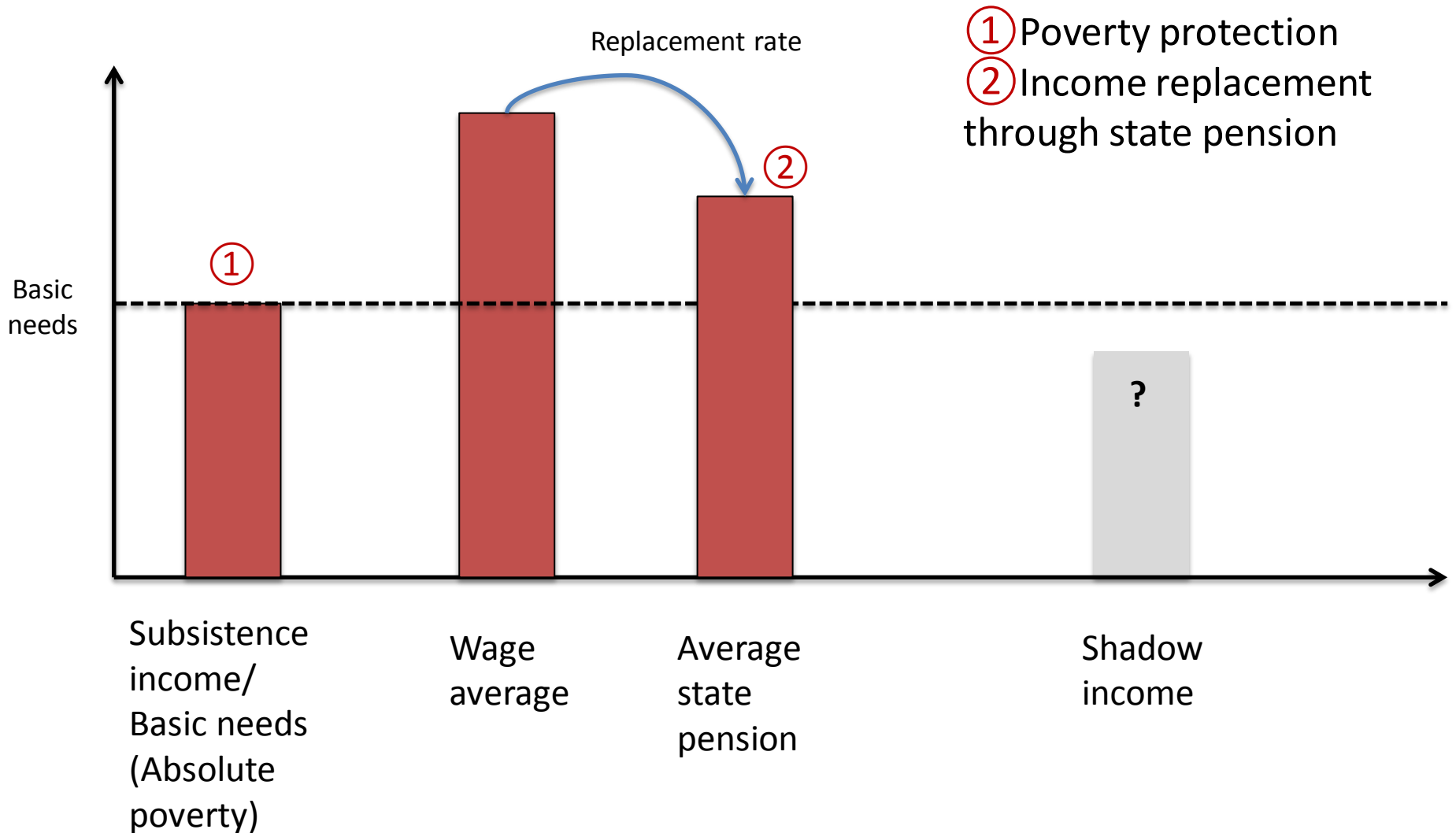
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Objectives for poverty reduction and state pension



How to achieve both objectives?

Objective	Pillar	Target group			Characteristics	Participation (contribution)	Funding collateral
		Life-time poor	Informal sector	Formal sector			
Elderly poverty protection	0	X	x	x	“Basic”/ “Social Pension” (assistance, universal or means-tested)	Universal/residual	Budget/general revenue
Elderly poverty protection & income protection (“consumption smoothing”)	1			X	Public pension plan, publicly managed, defined benefit or notional defined contribution	Mandated	Contributions, perhaps w/ fin. reserves

Source: own illustration based on World Bank

Overall strategy

Objectives:

- ① **Poverty prevention** – ensure a minimum subsistence income for the elderly to protect them from outright poverty
- ② **Income replacement** through a state pension system which provides an old age pension based on their life long pension contribution

Strategy for reform

- Strict separation between poverty prevention and income insurance
- Poverty prevention for the elderly to be incorporated in general social assistance
- State pension system will be reformed to achieve a gradual increase of the replacement rate

Poverty prevention through social assistance

- ① **Poverty prevention** – ensure a minimum subsistence income for the elderly to protect them from outright poverty

Specific measures to prevent poverty in old age:

- Instead of minimum pension provide a **guaranteed minimum income**
- Should be delivered through existing social assistance instrument
- If regular pension and other incomes of *household* too low, top up through Social Assistance (means-tested)
- *State Social Allowance* and *Cold Season Allowance* should be included in existing Social Assistance instrument
- Gradual increase of the level of Social Assistance (minimum guaranteed income) to ensure basic needs can be met

Result:

- **Social assistance ensures a decent minimum income for those of the elderly who do not have a sufficient income – and only those**

Income replacement through state pension

- ② **Income replacement** through a state pension system which provides an old age pension based on their life long pension contributions

Specific measures to ensure replacement rate of state pension is sufficient:

- Gradual increase of minimum contribution periods and pension age
- Valorization of past earnings
- Abolish existing fixed amount pension top-up and use the free funds to increase replacement rate of pensioners who receive a regular old-age pension
- Budget savings from means-testing of minimum pensions should be used to increase regular pensions
- Assess options for a budget-financed increase of the replacement rate for those (and only those) who contributed to a regular pension

Result:

- **Gradual increase of old-age pension and the replacement rate which provides incentives for people to contribute to state pension system**

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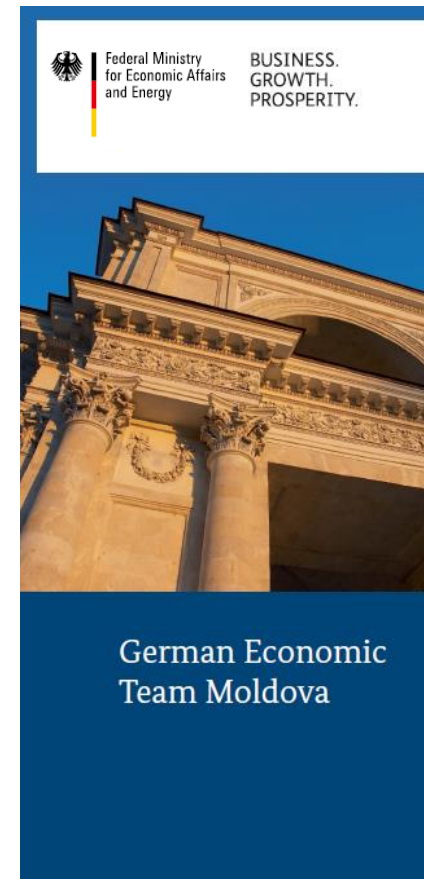
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Annex 1: Social security for the elderly: typical cases

Case 1 - “Social assistance only (single household)”

- Represents the case for an elderly individual that is not entitled to receive a retirement pension and thus only receives social assistance measures

Case 2 - “Minimum pensioner”

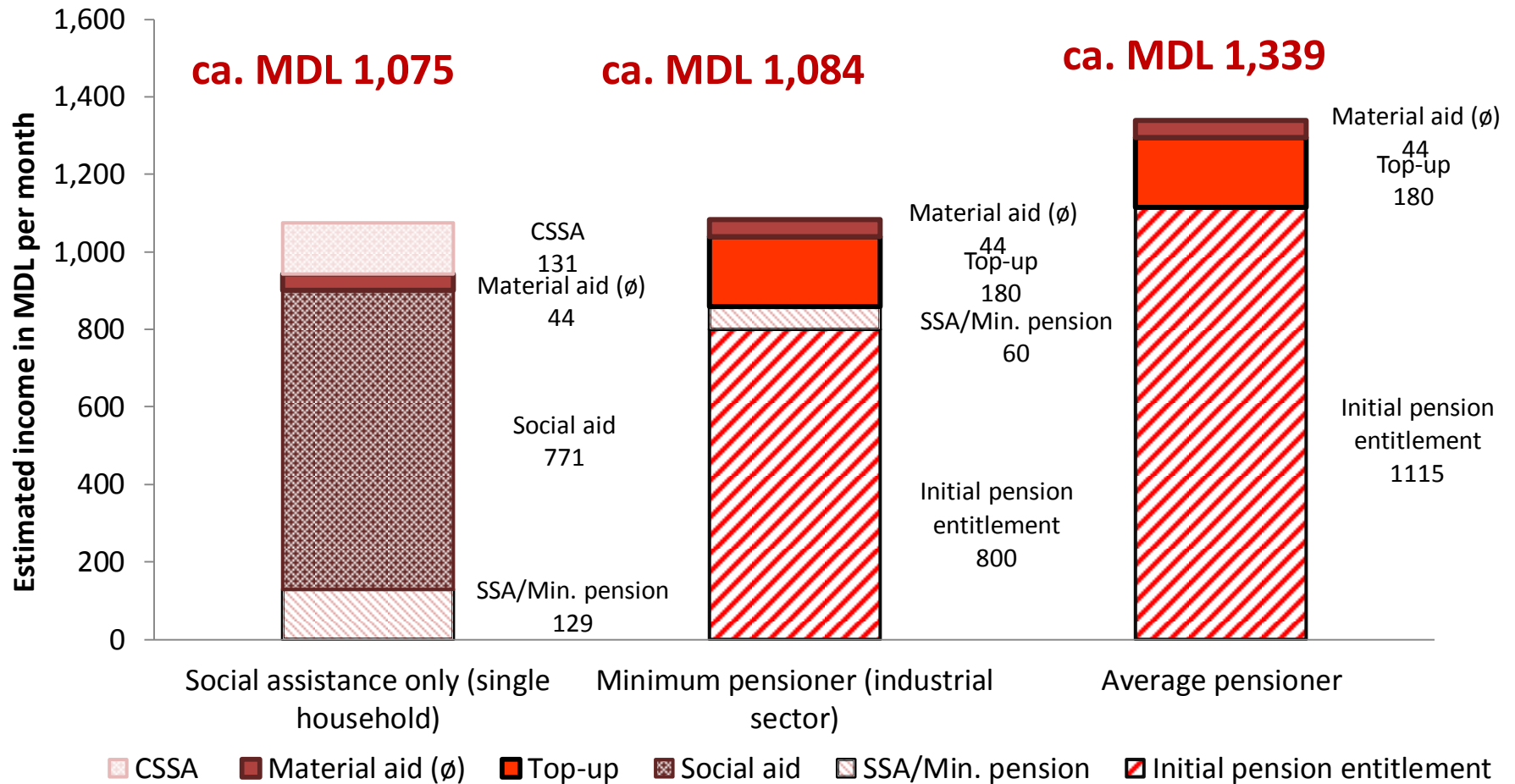
- The individual who receives a top-up amount so the pension reaches the minimum level of MDL 860 as his regular pension entitlement would have been below 860 MDL minimum pension level

Case 3 - “Average pensioner”

- The “average pensioner” receives a regular old age pension of about MDL 1115 in line with the average pension in 2015

Question: What is the combined income for each of the three cases from social insurance and assistance measures?

Annex 2: Comparison of incomes for the three cases



Source: own illustration based on National Institute for Economic Research (NIER)

Conclusion: Income from social aid or minimum pension almost as good as from regular pension. No incentive to earn a regular pension