



Support to the State Social Protection Fund on the introduction of funded element within the insurance-pension system, establishment of non-state pension funds and development of legal framework for regulating their activity  
Twinning Project AZ/13/ENP/SO/24



**ANNEX 33**

# **Pension system of Latvia. Comparison of the state funded elements.**

**Sandra Stabiņa**

**July, 2015**



Gesellschaft für  
Versicherungswissenschaft  
und -gestaltung e.V.



# Persons covered by compulsory social insurance/pension system

All employed and self-employed persons, at the age of at least 15 are subject to social insurance

## Contribution rate

- total – 34.09%
- for employer – 23.59%
- for employee – 10.50%

**earmarked for the public old-age pensions: 20% of wage**

# Branches of state social insurance in Latvia

State pensions insurance

Social insurance against unemployment

Social insurance against work injuries and occupational diseases

Disability insurance

Maternity and sickness insurance

Parental insurance

# Pension System

**1st pillar:** Notional defined contribution pension scheme – NDC PAYG (since 1st January 1996)

**2nd pillar:** State mandatory funded pension scheme – FDC (since 1st July 2001)

**3rd pillar:** Voluntary private pension scheme (since 1st July 1998)

# 1st pillar: Notional defined contribution pension scheme (NDC PAYG)

solidarity principle – PAYG

cover all employees

based on contributions made (20% minus rate for 2nd tier)

recorded in notional individual account

pension capital is accumulated during working life

indexation of pension capital

minimum savings period – 15 years (20 years from 2025)

retirement age for both sexes – 62 years and 6 month (in 2015)

an early retirement - 2 years before the statutory retirement age (60 years 6 month in 2015)

minimum pension

pension indexation (from 2014 with CPI and 25% wage sum growth)

special supplement

possibility to receive pension in working period

pensions are subject to taxation (except granted before 1996)

pensions granted before 1996 were not revised according to the rules of the NDC

# Old age pension formula

$$P = \frac{K}{G}$$

P – annual pension

K – pension capital

G – life expectancy at retirement

**in transitional period:  $K = K + K_s$**

K - pension capital after 1996

$K_s$  – pension capital until 1996 what is estimated by individual average wage 1996-1999

pension capital after 1996 is directly dependent on contributions made, interest rate of notional capital is related to the growth of contribution wage sum

pensions granted before 1996 were not revised according to the rules of the NDC scheme

persons with insurance record less than 15 years , when exceeding the qualifying age for old-age pension by 5 years, are entitled to the state social security benefit, paid from the state basic budget

# Other social insurance pensions

disability pensions are granted to disabled persons with an insurance record not less than three years. Old age pension granted instead of disability pension when person reaches retirement age (disability pensioners, who reached the retirement age before 1996, continue to receive a disability pension)

survivors pensions are granted to children and persons below 24, if they are full-time students at secondary, vocational or higher educational establishments

the same rules for indexation apply for all social insurance pensions.

# 2nd pillar: the state mandatory funded pension scheme – FDC

based on redistribution of contributions  
contribution rate - 5% in 2015, 6% from 2016

participation - mandatory (voluntary during a transition period)

private management

individual flexibility

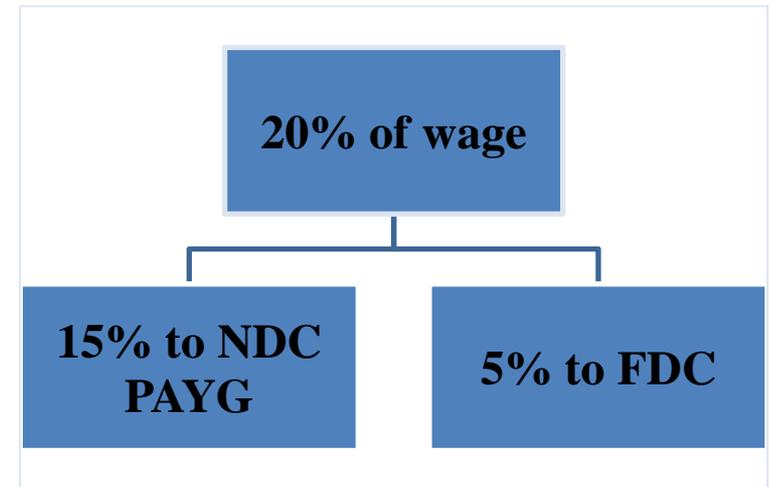
life annuity or PAYG pension

no guaranteed rate of return

capital is inheritable after retirement

*coverage - about 90% of economically active population*

*actual rate of return in last 10 years: + 4*



# 3rd pillar: Voluntary private pension scheme

voluntary contributions made by the employer or individual private management

types of funds - Open/Closed-ended private pension funds

minimum retirement age – 55

capital is inheritable or transferable to beneficiary

tax incentives for both – employers and individuals

no guaranteed rate of return

coverage about 22% of economically active population

actual rate of return in last 10 years: +4.04%

# Projected gross pension spending and contributions (% of GDP)

	2013	2030	2060	Change	
				2013-2030	2013-2060
<b>Expenditure</b>					
Gross public pension expenditure	7.7	5.5	4.6	-2.2	-3.1
Private individual pensions	:	0.3	2.2	+0.3	+2.2
<b>Contributions</b>					
Public pension contributions	7.0	6.2	6.2	-0.8	-0.8
Private individual pension contributions	0.9	1.7	1.7	+0.8	+0.8

# Comparison of State Funded tiers

Latvia	Azerbaijan – defined in draft law
<b>Participation</b>	
mandatory/voluntary	voluntary
<b>Scope of participation:</b>	
all contributors taking into account cohorts limits legislated for transitional period – the same for men and women	participants to NDC scheme taking into account age limits for new participants
<b>Individual accounts - contributions:</b>	
redistribution of social insurance contributions between the NDC and FDC schemes	additional contribution rate by individual
<b>Contribution rate:</b>	
legislated – 6%	legislated – 4%

Latvia	Azerbaijan- defined in draft law
<b>Minimum period/continuity of participation</b>	
no minimum - until retirement	3 years
<b>Pay - out</b>	
life annuity or to PAYG pension	to PAYG pension or lump sum (for small amount accumulated)
<b>Inheritance</b>	
Coinsurance person indicated after retirement in case of life annuity	capital is inheritable until retirement
<b>Rate of return</b>	
no guaranteed rate of return	no guaranteed rate of return
<b>Retirement age</b>	
Old age	Old age
<b>Asset management</b>	
private	state + private

**Thank you**