Civil-service pension schemes

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Axia Economics

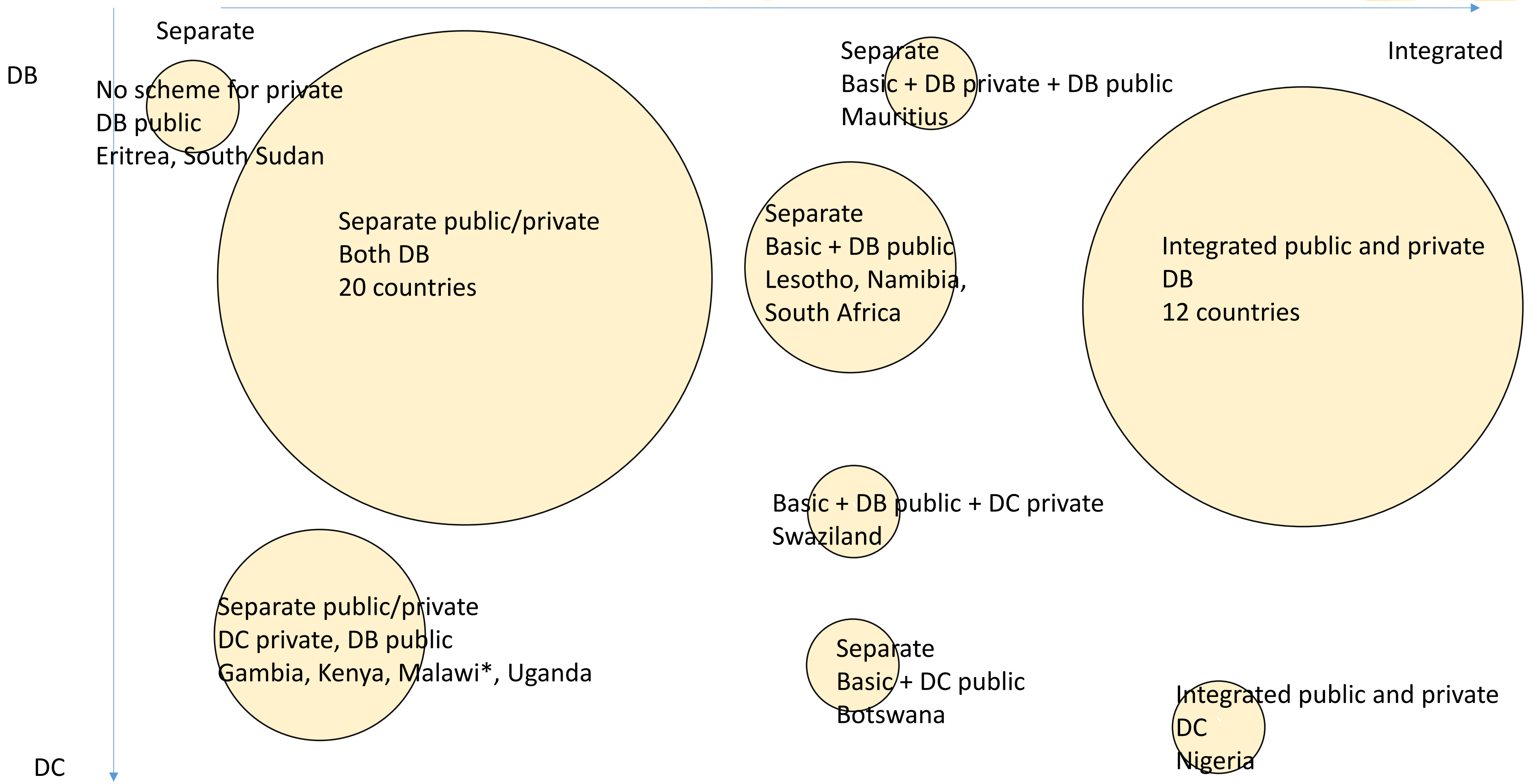
Origins

- Civil-service pension schemes usually set up before national programmes
  - independence of civil servants
  - make working for the public sector attractive
  - shift the cost of remunerating civil servants into the future
- Separate schemes then often persisted after national schemes established: ‘dualism’

Institutional arrangements

Fully integrated	Institutionally separate with similar benefits	Fully integrated with top-up arrangements	Partially integrated with top-up scheme	Entirely separate institutions and benefits
Chile	Denmark	Australia	United Kingdom	Austria
Czech Republic	Finland	Canada		Belgium
Estonia	Iceland	Ireland		France
Hungary	Israel	Italy		Germany
Mexico	Netherlands	Japan		Greece
Poland		New Zealand		Korea
Slovak Republic		Norway		Luxembourg
		Slovenia		Portugal
		Spain		Turkey
		Sweden		
		Switzerland		
		United States		

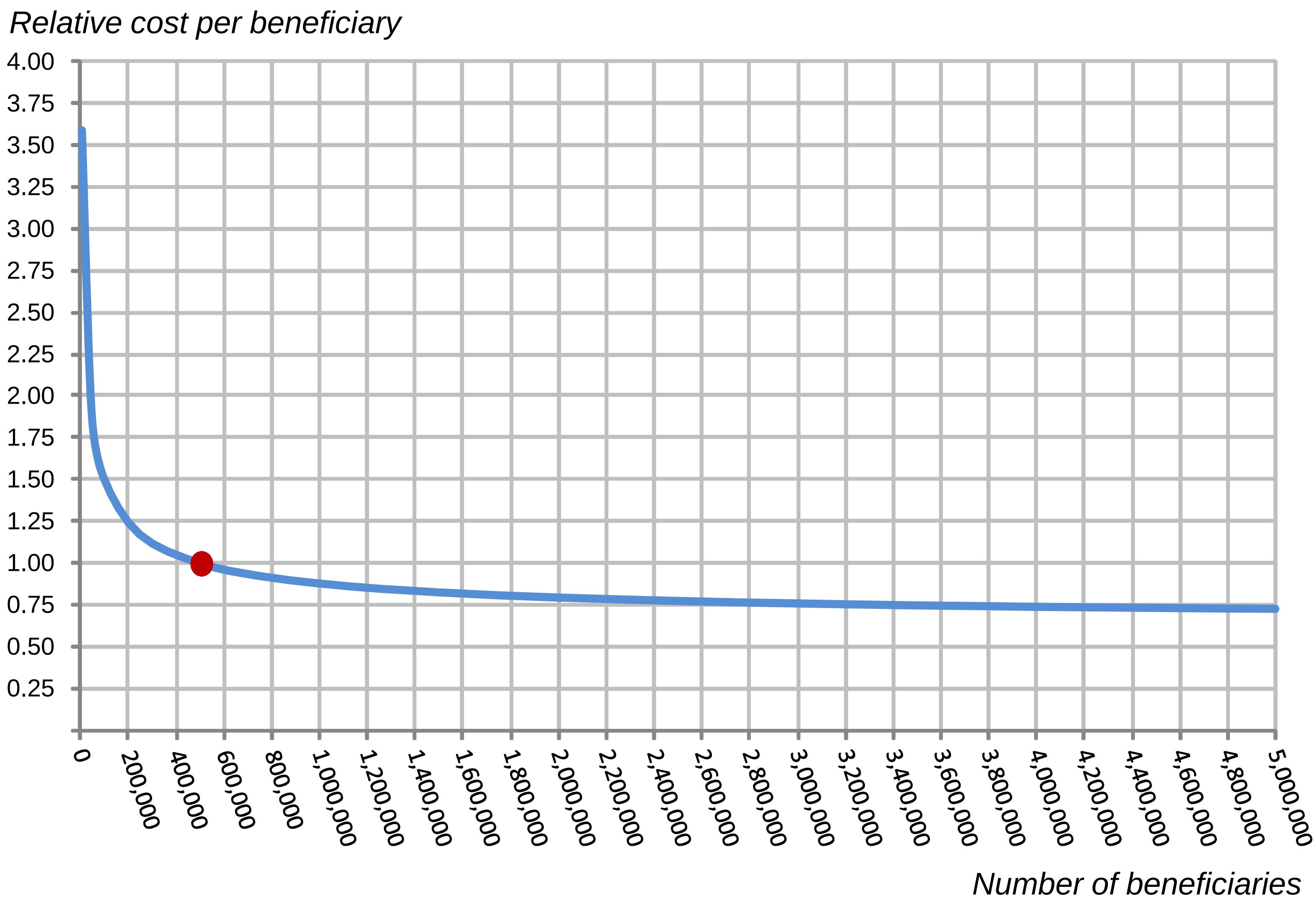
Institutional arrangements



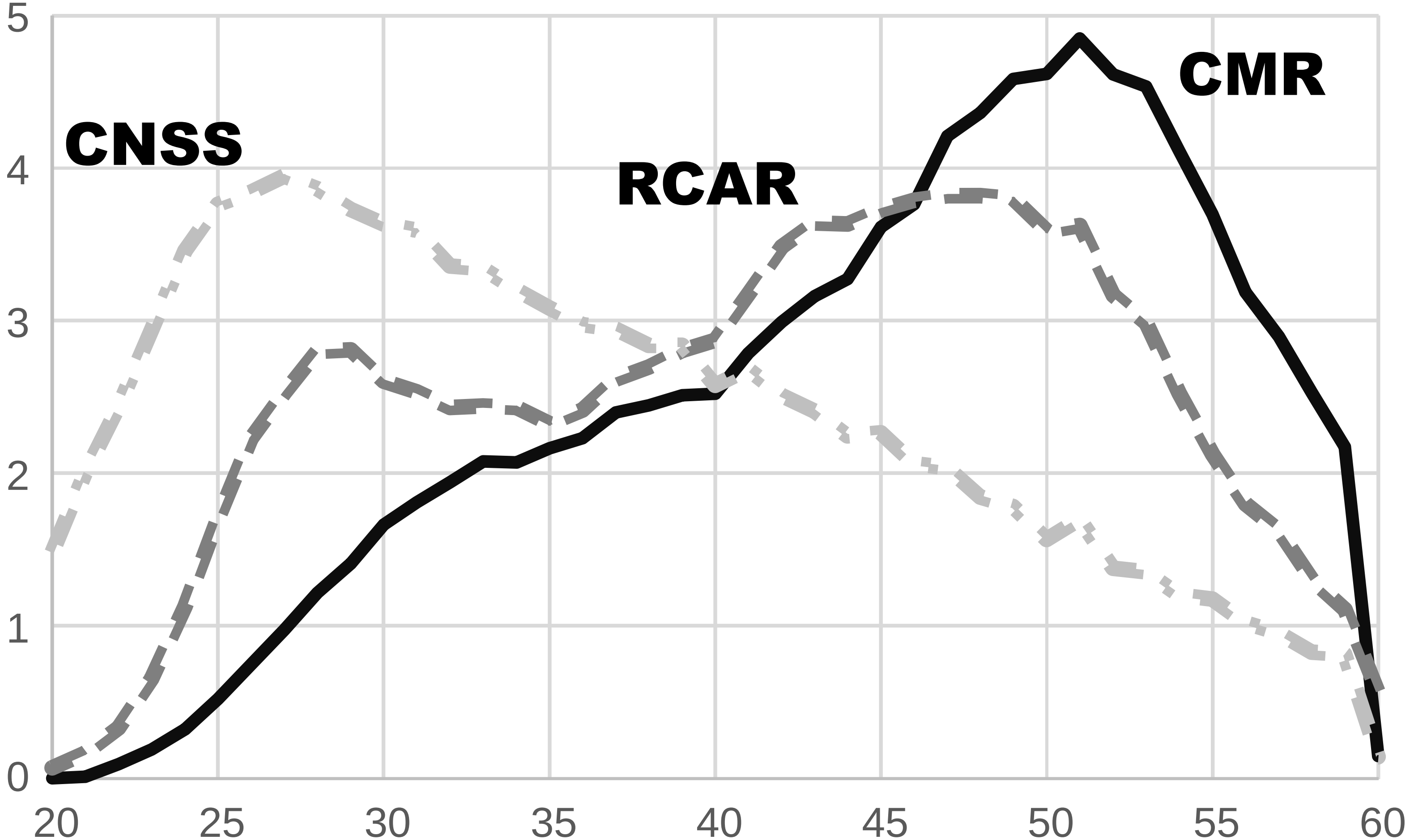
Dualism

- Arguments against
  - Integration gives civil servants direct, personal interest in the plan being well managed
  - Economies of scale
  - Mobility and portability
  - Equity
  - Transparency
- Long-term goal should therefore probably be integration of civil-service and national pension plans

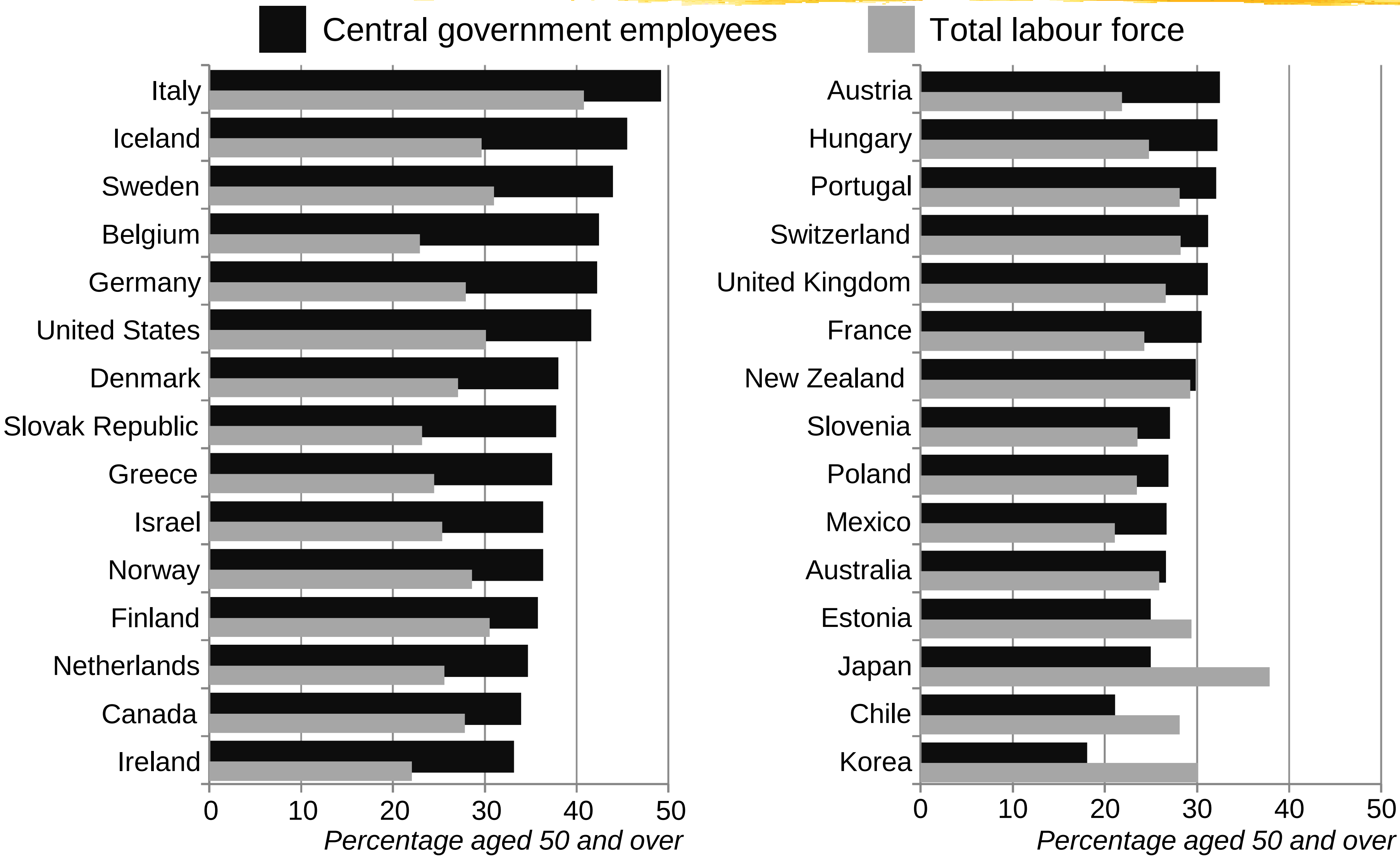
Economies of scale



Example: Morocco



Labour-force demographics: central government vs population



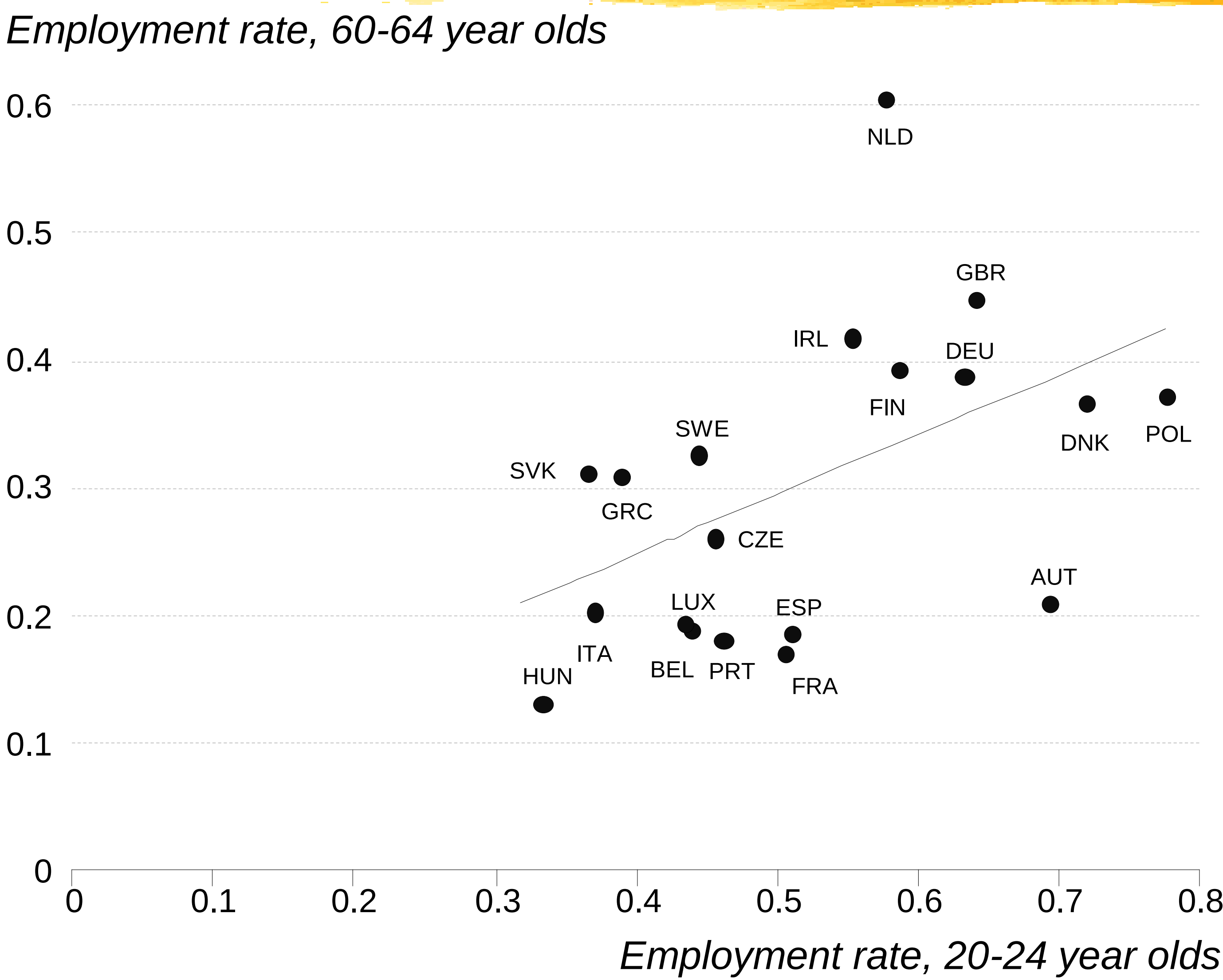
Reform options 1

- ‘Parametric’ reforms to defined benefit plans
  - reduce replacement rate
  - index pensions in payment to prices rather than civil-service earnings
  - introduce/increase member contributions
  - raise pensionable age
  - extend averaging periods for ‘final’ salary
- ‘Systemic’ reforms
  - introduce new system for new civil servants with some element of pre-funding of obligations
- Any reform must take account of all aspects of civil-service terms and conditions

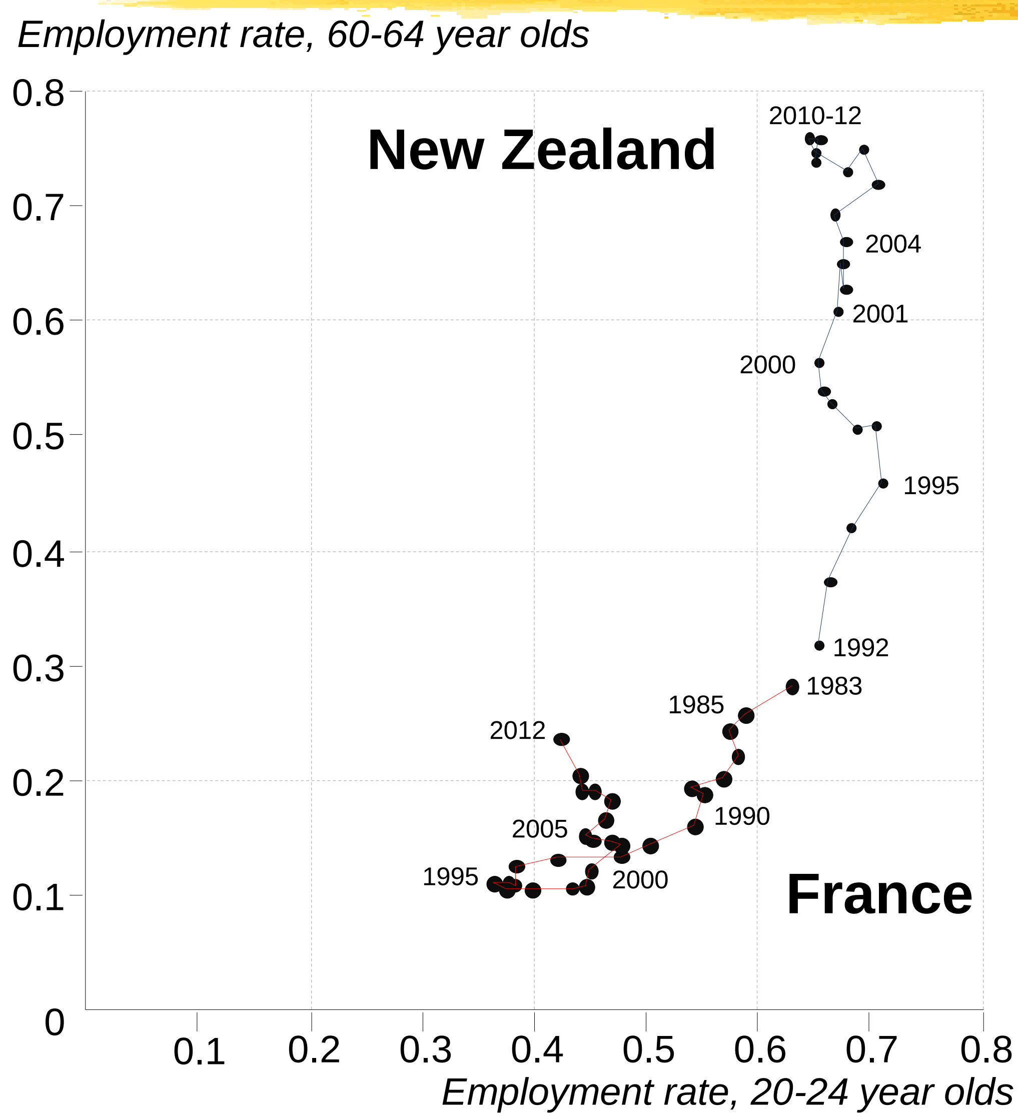
Reform options 2

- Increasing contributions:
  - employer contributions are just re-labelling, unlike national systems
  - employee contributions may have an effect on wages or productivity
- Increasing pension age:
  - civil service schemes are 'closed' systems
  - so increasing retirement age has different effects than it does in national schemes: labour supply effect in national schemes
  - increase in retirement age cuts duration of benefit payments, but
  - without downward adjustment of accrual rates to compensate, benefit values increase
  - people might retire on higher pay if earnings continue to grow with age
  - affects both pay and pension bills

Lump-of-labour fallacy across countries



Lump-of-labour fallacy over time



Flexibility and portability

- Civil service schemes are inflexible: ill designed to deal with people without full careers
- But flexible schemes are increasingly important
  - ‘revolving doors’: cross-fertilisation between public and private sectors
  - transfer of employees due to privatisation or contracting out

Reforms to improve portability

- Shorten vesting periods
- Preserve pension rights of early leavers
- Extend averaging period for ‘final salary’
  - career average uprating eliminates the mobility problem
  - also deals with problems of incentives for abuse
  - but requires improvements in record-keeping
- Introduce a defined contribution scheme
  - fully portable

Conclusions

- Reform of civil-service pension schemes is important in low- and middle-income countries
  - often, larger expenditure than national schemes and similar coverage
  - crowds out important social programmes
- Many options to put civil-service pension schemes on a sustainable footing
- Structural issues as important as fiscal ones
  - single national scheme would be more administratively efficient, equitable and increase labour-market flexibility
  - equity and efficiency also improved by longer averaging periods for earnings, shorter vesting periods, preservation for early leavers, DC option