Occasional Paper N.7:

THE PENSION SYSTEM REFORM IN MACEDONIA

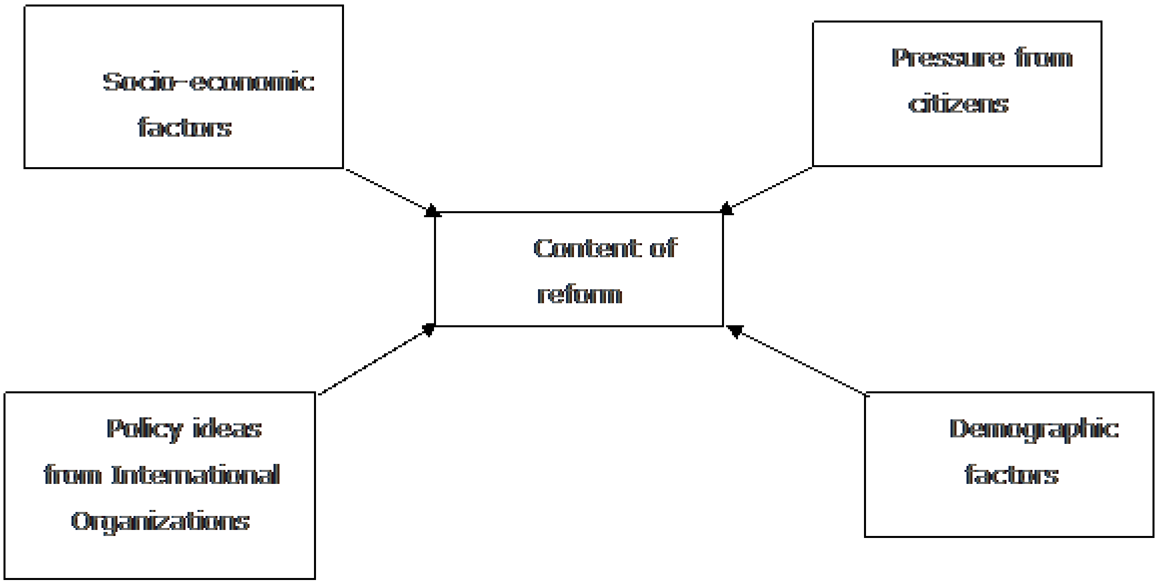
The Macedonian pension system exists for 50 years. The system was created at earlier stage when the population was younger and was developed to redistribute the income among generations of employed citizens by providing mandatory pension and disability insurance for all of them. For 40 years the pension system, financed on pay-as-you-go basis[1], has been successful. Just when the Macedonia's pension system has begun to mature, the conditions[2] conducive to a successful pay-as-you-go scheme, started to disappear. Population growth started to stagnate, fertility rates began to fall and life expectancy continued to increase. At the same time, due to the transition from command to market economy, the employment rate went down. As a result, today the country spends more on pensions and creates more public deficit then before. Consequently, the enormous public deficit and other global economic forces that affect the structure of the working pattern influenced the slow wage growth. Therefore the reform of the pension system is high on the political agenda of the last two Governments of Macedonia.

1.1. The purpose of the reforms of the pension system in Macedonia

A larger part of old persons in the total population means an increased number of retirees, while an increased life time expectancy causes longer use of pension. On the other hand, the unfavorable economic conditions: the high unemployment accompanied by the decrease of the fertility rate, impact on the contributors number in a long term period. The ratio between the contributors and retirees is very important for a PAYG system, because the benefits for the current retirees are paid with the contributions from the current contributors. Contributor's decline and the raise of the number of pensioners strongly impacts on the sustainability of the traditional pay-as-you-go funded scheme and influence the debate about the urgent need of reform of the pension system. Thus in this chapter we focus on the reasons why the pre-transition Macedonian pension scheme had to be reformed, what were the challenges to the old system and how they influenced the design of the new pension system.

For more precise identification of the forces involved in the process of pension reform in this paper the framework-conceptual map of reform provided by Pollitt and Bouckaert is used. It can be noticed from the diagram that four factors strongly influence the content of pension reform in Macedonia. These are: socio-economic factors, demographic factors, pressure from citizens and policy ideas from International Organizations (World Bank).

Figure 1



Adapted from Pollitt and Bouckaert, "Public Management Reform", 2000, Oxford University Press

The key factors that explain why Macedonia decided to reform its pension scheme is summarized in line with the previously mentioned division of forces that have a strong impact on the content of reform presented in Figure 1.

A. **Socio-economic factors:**

- **Loss-making companies, workforce redundancy and bankruptcy procedures**. The transition from command to market economy led to an increasing number of enterprises that work with a loss, to workforce redundancy and to a growing number of bankruptcies. According to the official data, 43 public companies are making losses, thus 30 860 workers were made redundant and unpaid contributions to the pension fund amounted to EUR 77.115.604[3]. Furthermore, 339 companies declared bankruptcy, which also had an impact on the difficulties and the deficit in collection of contributions.
- **Raising unemployment.** In the same time the unemployment rate went higher. It went up for 30 % in 7 years. Compared with all the countries, analyzed in the

Augusztinovics's economic survey of Europe, the Republic of Macedonia has the biggest employment drop throughout the period from 1991 to 1998. In 1998 almost 35 % of the population was unemployed.

· **Raising number of pensioners.** As a result of the aging of the population, rise in life expectancy and favorable retirement eligibility criteria, the number of pensioners went high. The data from the Pension and Disability Fund show that merely in ten years (1990-2000) the number of pensioners went up for 69%.[4]

· **Decline in the number of contributors.** The number of contributors fell and benefits payments increased, creating a widening financial gap. While the number of scheme contributors declined by 30 per cent in Bulgaria, 45 per cent in Latvia, and over 60 per cent in Albania[5], in Macedonia the ratio between contributors and pensioners according to the official statistics was the following:

Table 4. Ratio between contributors and pensioners in Republic of Macedonia

Year	Employed in public sector, private sector and farmers	Pensioners	Number of pensioners per 1000 contributors	Ratio contributors to pensioners
1990	571.419	166.224	291	

3.4

1991

534.887

180.749

338

3.0

1992

531.083

193.294

364

2.7

1993

503.010

210.537

419

2.4

1994

468.632

216.834

463

2.2

1995

427.658

219.307

513

2.0

1996

403.820

222.726

552

1.8

1997

381.723

227.099

595

1.7

1998

370.869

232.216

626

1.6

1999

374.025

235.839

631

1.6

2000

366.906

240.221

657

1.5

2001

351.009

247.200

704

1,4

2002

332.728

249.421

750

1,3

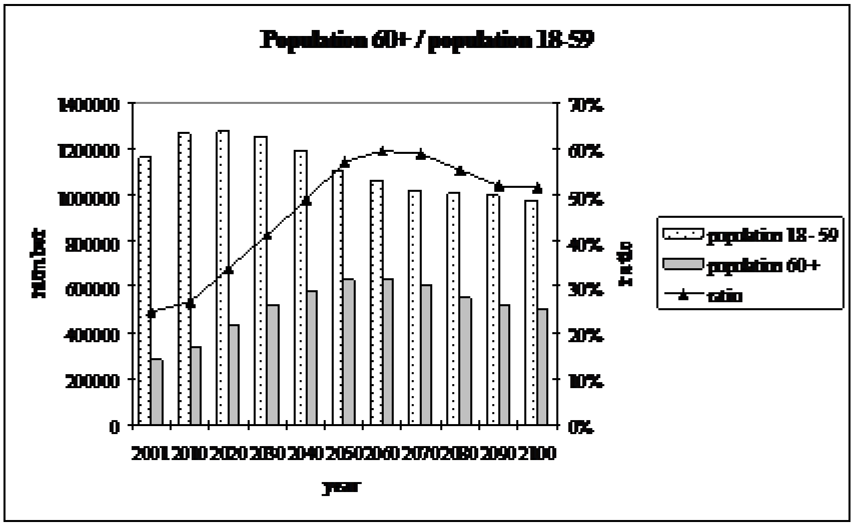
Source: Pension and disability insurance fund of Republic of Macedonia, Presentation overview, Skopje 2002

From the table above, one can notice that the ratio between contributors and pensioners has decreased from 3.4 to 1.5, which portrays a very serious situation where one and a half employed person from his/her salary is paying the pension of one pensioner. The international standard for sustainable pension scheme is to have at least three people that pay the pension of a pensioner, but every system strives for even bigger ratio, i.e. in Sweden the ratio between contributors and pensioners goes up to 7.

· **High pension expenditures.** 30% of the Government's expenditures in 1997 are used for pensions, which makes pension expenditures in Macedonia to be among the highest in the region, primarily due to the high replacement rate and generous eligibility and benefit structure.

B. **Demographic factors:**

a. Demographic shifts. Macedonia is regarded to be a "young country" because 30% of the population is under 20, but estimations say that the elderly will increase over 70%, from roughly 13 to 23% of the population in just 20 years.[6] The ratio of the group of working age of population rises from current 24.6% to 59.6% in 2060 and than decreases to 51.8% in 2100.



Source: Pension and disability insurance fund of Republic of Macedonia, Presentation overview, Skopje 2001

From the graph above, we can notice that the number of working age population increases in the first 20 years of projection, and than continuously decreases as a result of the low rate of fertility. On the other side, the old age population continuously increases during the 60 years and than slowly decreases. This is a result of the extension of the life time of people due to improved life conditions, the progress of the medicine, improved medical services, etc.

C. **Pressure from citizens:**

- **Sustainability.** In 1993 there was the largest delay of pension payments of about two pensions, which made the public more aware of the need of a more sustainable pension system. Political forces that shaped the decision making process, put the focus on reform of the pension scheme due to the pressures from citizens because more than 40% of the voters are either pensioners or about to be pensioners.
- **Fairness.** Pension benefits for retirees often varied greatly. Because old-age benefits were based on a worker’s 15 highest earning years, two Macedonians with equal lifetime incomes who had paid equal amounts of taxes could receive very different pension benefits. This formula discriminated in favor of higher paid white-collar workers

with peak-earning years at the expense of blue-collar workers with relatively stable earnings.

1.2. Process of pension reform- the impact of the World Bank

The serious financial situation in which the Pension Fund has found itself in 1993, and the constant decline in the ratio between contributors and pensioners in R.Macedonia has rushed the state officials to search for alternative solutions to these problems and eventually to start with a reform of the pension system. The financial institutions (World Bank, IMF etc.) were anxious to help Macedonia in the process of reforming the pension system, since it is closely linked to the overall balance of the state's financial expenditures. In terms of pension reform, the most obvious source of assistance was the World Bank, an institution that put strong and visible pressure on Macedonia as in the rest of the CEE and SEE countries. This fits into the model of division of forces that influence on the pension reform in R. Macedonia as a forth factor-policy ideas from international organizations- that was left out from the previous chapter.

At first the existing pension system was criticized by the World Bank as too broad, as giving too little to too many, as being not sustainable and as failing to conform to sound actuarial principles. The real propagandizing activity of the Bank started in 1993 when the Macedonian pension system was faced with the most serious crises caused by the delay in paying the pension benefits to pensioners for two months. That is when the IMF and the World Bank pressured the Government to make macro financial balance of the expenditures and start up the so called parametrical reforms of the pension scheme. The parametrical reforms were undertaken in order to accommodate the difficulties in sustaining the traditional PAYG system. In the period between 1993 and 1998 many typical solutions were enforced to respond to the increased fiscal pressure by stepping up the contribution rate and by increasing the retirement age. At the end of 1993 the contribution rate increased from 18% to 20%. With the Law for pension and disability insurance that entered into force on January 1 1994 several restrictive measures were undertaken regarding retirement eligibility criteria, the most significant of them being: increase of the retirement age, i.e. from 60 to 63 years of age for men and from 55 to 60 years of age for women; estimation of the pension base as an average during the whole career, instead of the 15 most favorable ones; lowering of the percentage for pension determination from 85% to 80% of this average; repeal of the possibility to "buy" years of contributions as an option for fulfilling the eligibility criteria for retirement, etc. Other restrictive changes were introduced in 1995 that continuing the decrease of social elements of the system.[7] All these have been in line with the monetarist approach that the World Bank and IMF have taken in most of the transition countries in Central and South Eastern Europe. Abandoning solidarity and privatizing pension schemes has been the heading under which the Bank's philosophy was enforced in the transition democracies, and the above mentioned measures were just a first phase of the comprehensive approach that the World Bank has in the process of pension reform in R. Macedonia.

According to many reports of the World Bank, unlike Latin American reforms, which are heavily focused on a funded pillar, transition economies are increasingly likely to end up with mixed systems that balance advantages of intergenerational solidarity with advantages of long-term individual mandatory savings. Thus the World Bank in R. Macedonia, as in the rest of the CEE and SEE countries pushed for a multi-pillared pension system that encompasses both the public and fully funded (privately) financed and managed pillars of a pension scheme, accompanied with additional insurance for those who require it. This model of mixed pension systems can be regarded as embedded policy strata of the Bank at the level of the region. In the context of an ageing population, in OECD countries the fully funded pension schemes also constitute a viable alternative to pay-as-you-go pension schemes.

Recognizing that the World Bank has a strong impact and a role of an important actor in this area, we must identify the key policy diffusion mechanisms that it is using in the Republic of Macedonia and in the region and determine the type of policy transfer that occurs in the process of pension scheme reform.

The World Bank and other supranational organizations that have an interest in this policy area are 'vulnerable to being portrayed as facilitators of a new colonialism based upon foreign capital' -as argued by Held (1992:69) - therefore they do not impose policy but influence and disseminate 'good practice'. This is achieved by informal networks reinforced by meetings and forums provided by the international organizations. The World Bank, being the agent of policy transfer in the Macedonian case of pension reform, generates a 'high quality information' flow about its three-pillar pension scheme to participants at seminars, conferences, study trips, held in the country and abroad, for the Steering Committee of the Macedonian Government empowered to manage the reform of the pension system. Joint seminars and study trips that the Bank organized for Government officials, representatives of the pension fund, financial experts and other stakeholders in the Macedonian pension reform, and other participants coming from every country in the region[8] were "designed specifically to promote homogenization of the participants at the forum around the policy discussed there, rather than discussing opportunities for policy exchange"[9]. However, the key assumption here is that policy learning by any state is voluntary, not enforced.

Another mechanism of policy transfer employed by the World Bank is the persuasive power of reform rhetoric. This fits into Dolowitz and Marsh's category of perceptual transfer. This is where policy learning is triggered by perceptions of 'falling behind' or failing to be part of an international consensus. These perceptions may be especially caused when participating in a forum with states where the reform is already ongoing, such as the seminars and conferences organized by the World Bank and mentioned above. Arguably, the most appropriate model for Macedonia came from countries with similar levels of economic and social development-the countries from CEE and SEE that transit to democracy and market economy and have already adopted the World Bank's model of pension scheme. Therefore, voluntary and coercive transfer cannot be neatly dichotomized when one examines the activities of the World Bank. There are instances where the Bank appears to be more coercive in its approach to disseminate ideas and practice. The Bank needs to be ensured that the 'best practice' will be implemented rather than merely encouraging the state for implementing the favored idea, model, or practice. Thus, the Bank provides substantial funds for the whole process of designing, enforcing and implementing the model promoted by the World Bank. The two financial arrangements that were most often given to transition countries, including R. Macedonia, in the process of reforming pension systems are the following:

· Investment credits = given to the government if certain conditions are reached and the money can be used only for implementation of a detailed design of policy matrix; the money is transferred in two or more installments and for each of them 'no objection' approval must be received from the Bank

· Adjustment operations credits = given for direct support of the budget; income transfer program based on means-tested eligibility criteria; usually given in the form of technical assistance for capacity building of the institutions of the country-client of the Bank

Both the IMF and the World Bank have given 'structural adjustment loans' to Macedonia, but much less is known by researchers about the conditions of the loans of the IMF, than those of the Bank since they are handled confidentially. As discussed above, these financial arrangements are 'designed to ensure execution of a *contract*' and in many respects are coercive in their nature. This fits with the Dolowitz and Marsh's category of conditionality. In the Macedonian case of pension reform we can say that a certain degree of conditionality occurs when particular steps in the reform process are incorporated in the loan conditions (see below). Still, the loan conditions do not determine which model of pension scheme the country should eventually adopt. This leaves the Government with a degree of freedom to choose voluntarily the version of pension policy best suited to the situation in Macedonia.

The problem for recipient countries is that the consequences of coercive policy transfer can be negative. By following the prescriptions of the international organizations, the result for transition countries may be an 'inappropriate pension scheme' based on an "expatriate model which has been developed in the context of big business, industrial society and metropolitan government…."(Smith 1992:17). Furthermore, Held (1992:72) acknowledges the perils of coercive transfer when he says that "it should be a question of learning rather than of direct transplanting: differences in political culture, levels of economic development, country size and bureaucratic capabilities will determine which reforms are feasible." Even the World Bank in this respect advocates certain adjustments in the model promoted by its officials. Retirement age, replacement and contribution rates are some of the characteristics under which the pension schemes differ in different countries in CEE and SEE. But the readiness of the economy to embrace and the stability of the market to sustain the newly designed pension schemes are still some of the issues that worry experts in the region. In Macedonia particularly, trust in the banking system is rather low and the new second pillar of the pension system envisages personal saving accounts in private pension funds. Furthermore, only banks and insurance companies are empowered by law to establish private pension funds. Therefore the success of the new pension system is seriously put into question. This fits in the category of inappropriate policy transfer as discussed by Dolowitz and Marsh. The possibility for uninformed transfer (another category of policy failure that fits in the Dolowitz and Marsh's model of policy transfer) to occur in the Macedonian case of pension reform is very small. The Steering committee of the Macedonian government, empowered to manage the reform, has looked into the cases of Latvia, Croatia, Bulgaria, Poland and Hungary, and "made thorough analysis of their new pension systems, which itself drew lessons not to adopt some of the drawbacks of their legislative framework."[10] And finally, knowing that the three-pillar pension system is fully worked out program it is hard to believe that some of the elements that made the new system successful elsewhere may not be transferred in Macedonia. "We have followed all the prescriptions of the World Bank in combination with the recommendations of our consultants and it cannot lead us to an incomplete transfer." [11]

But the source of coercion may not be the World Bank. As Onimode (1999:30, quoted in Richard Common's "Public management and policy transfer in Southeast Asia", 2001) points out that 'the Bank and the Fund claim that they do not impose anything- countries run to them and invite them to become involved in their economies', as is the case with the Macedonian pension system reform. The Macedonian government has requested assistance for the reform of the social sector programs which has been included as an integral part of the World Bank's Country Assistance Strategy (CAS). The broad goals of the strategy are to stimulate economic activity through the consolidation of fiscal gains and the promotion of private sector development. In accordance with various documents of the Bank, a reform of the social sector programs, particularly pension reform, will improve long term viability of the pension fund and will move to a fully-funded (private) pension pillar, which is identified by the CAS as critical for achieving the above mentioned objectives. These goals are in compliance with both the

‘Washington consensus’ and the Bank’s philosophy for marketization and privatization of the pension policy.

The technocratic elites within the countries- clients of the Bank- can also act as a source of pressure for policy reversal and thus are given ‘crucial international backing from the IMF and the World Bank’ as it is argued by Biersteker (1995:186, quoted in Richard Common’s “Public management and policy transfer in Southeast Asia”, 2001). “Domestic structures mediate, filter, and refract efforts by transnational actors and alliances to influence policies in various issue areas”.[12] Transnational actors need to gain access to the system and then contribute to winning policy coalitions in order to have policy transferred. The state still retains considerable power to decide whether or not transfer should occur, but this depends on the relative strength of the domestic state structure and the levels of influence that the technocratic elites have in the process of policy decision-making. But, as might be noticed, the World Bank and other transnational actors can primarily win or create, educate technocrats with a strong belief in their policy and then support them through the process of transferring and implementing the policy in question. In the Republic of Macedonia the World Bank has started its involvement in the pension reform through giving adjustment operation credit for building evaluation capacity within the Government and Pension and Disability Fund. This resulted in establishing the Actuarial Unit in 1995. The Unit, using an actuarial model makes short-term and long-term projections of revenues and expenditures of the Fund, under the projected demographics and economic development trends and their variations, within the different assumptions for the pension policy. These projections are used for the aims of the pension system reforms, which are undertaken by the Ministry of Labor and Social Policy and by the Pension and Disability Insurance Fund of Macedonia. The first projections of the Unit, portrayed crises in the long run and required immediate action. This crisis approach drew attention to problems with the existing scheme and created the will to address them. Thus, we can say that the projections, done by the Actuarial Unit of the Pension Fund, which has been trained by experts from the World Bank, had a great impact on the very decision for starting more fundamental structural reform of the public pension system. On the basis of the reports and the recommendations from both the Bank and the Actuarial Unit of the Pension Fund, ‘even though all measures undertaken in a period 1993-1998 had positive effects’[13] in a direction of the financial consolidation of the Pension Fund, in 1997 the Government required and the World Bank gave a new adjustment credit (Social Sector Adjustment Credit) for designing a pension reform program, including the actuarial forecasting and economic planning of the reform and drafting the legislation required to underpin the reform. So the World Bank created its own pro coalitions within the institutions of the state and thus got support for the implementation of their goals by the technocratic elites.

The World Bank and other international organizations will only have influence within a state if they are invited by the political elites. What often appears to be an example of coercive policy transfer can be quite the opposite. Thus the role of international organizations in policy transfer is an ambiguous one. States retain considerable autonomy in deciding whether or not they will allow themselves to be influenced by them. However, when the states are faced with a huge public debt and an unsustainable pension scheme, the credits and loans provided by IMF, World Bank and others seem to be very appealing and confirmation with the global strategy of these transnational actors in the area of pension policy do not seem to require big efforts. In Macedonia the governing elites adopted the legislation that regulated the new pension scheme with relatively little question. The Steering Committee which managed the reform was firm in its position that no other alternative program than the three-pillar pension system was possible. By the time that the Labor Union and other interest groups started to oppose the new system, the Macedonian blueprint had been adopted by the Parliament. This development is a result of the non-corporatist approach of the interest groups in the country and the weak civil society that is characteristic for every transition democracies. The Labor Union is the only contra coalition objecting to the abandoning of the solidarity elements of the pension system. Thus the Union negotiated the implementation of the newly adopted pension system to be postponed for another year.

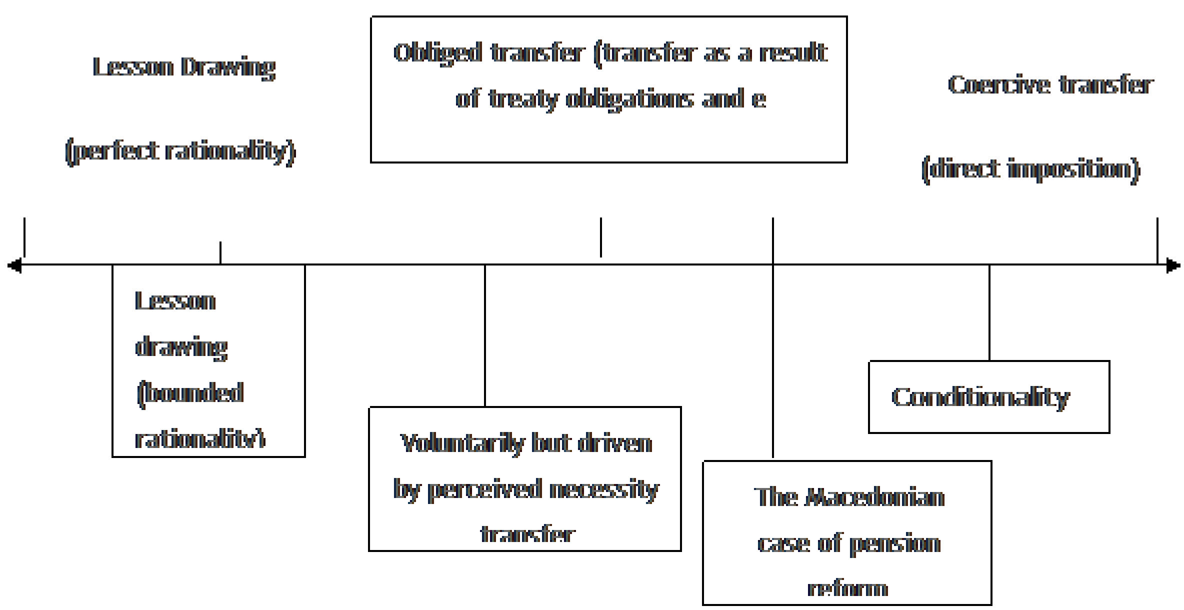
Finally, key policy diffusion mechanism is the activity of external agents, consultancy firms, think-tanks and other members of the epistemic community which are guiding the change in pension policy in the countries that transit towards democracy in CEE and SEE. Consultancy firms and think-tanks may be very influential because they can bring professional expertise, opinion, knowledge and recommendations to the Government and at the same time can remain independent from the policy ideas of international organizations and foreign governments. The presence of the epistemic community in the process of pension reform in the region, as well as in the Republic of Macedonia, has been dominant, due to the lack of capacity within the government officials to conduct the reform process on their own. In Macedonia experts and consultants gave various kinds of technical assistance to Government and Pension Fund officials in every stage of the process. It must be noted that all engaged in the reform process have been selected and appointed by the Steering Committee for the reform of the pension system from the list of consultancy firms and experts provided by the World Bank. "When international organizations, such as IMF and the World Bank get involved in the policy transfer, they often recommend that particular consultants be hired."[14]The consultants and experts hired in the course of the reform have been paid from the financial assistance that the Bank gave to the Government of Macedonia, thus one can argue about their independence from the global policy strata that the Bank has in this policy area, though, to an extent, they can also make different policy recommendations.

So, if we say that in the process of reforming the pension scheme in the Republic of Macedonia policy transfer has occurred, than the World Bank is the agent of the policy transfer. Since the Government requested financial assistance and invited the World Bank to give its recommendations and policy ideas in the process of reforming the pension system, the transfer can be perceived as a combination of voluntary and coercive actions. The coercion is especially noticeable in the conditionality of the arrangements that the Bank offered to the Government of Macedonia, where detailed steps of how the reform will develop are regulated. However, the Government remained free to choose the policy design itself. Nevertheless, the applied model was chosen as a result of the perception that the country is lagging behind the rest and was as much an effort to homogenize the pension systems in the region. Thus the transfer can be regarded to be mainly voluntary and perceptual, with some indirect coercive elements incorporated in the loan conditions of the Bank.

To establish simple a distinction between voluntary and coercive transfer is to oversimplify the process of pension reform. Therefore, Dolowitz and Marsh has conceptualized transfer as lying along a continuum that runs from lesson drawing to direct imposition of a program, policy or institutional arrangement. The process of pension reform in Republic of Macedonia starts with lesson drawing, scanning programs in effect in the rest of the CEE and SEE countries. But as a result of the Bank's involvement in this reform process, by giving technical assistance and giving loans with specific conditions, the reform of the pension system in Macedonia is placed further from the lesson-drawing end of the continuum. Adapted continuum of the process of pension reform in Republic of Macedonia shows that the transfer in this case involves voluntary, perceptual and coercive elements.

Figure 2

Application of the Dolowitz and Marsh's concept of policy transfer continuum: Policy transfer continuum- from lessons drawing to coercive transfer



2. <u>What is being transferred? – Three pillar pension system</u>

The pension reform in the Republic of Macedonia was officially initiated in 1997, when a project for pension system reform was set up within the Ministry of Labor and Social Policy. The project was managed by a Steering Committee consisting of representatives from the Macedonian Government, in particular the Ministry of Labor and Social Policy, experts from the Pension and Disability Fund, representatives from the Ministry of Finance and the National Bank of Macedonia. The project for pension system reform was financed through the financial assistance programs of the World Bank, the Dutch Government and USAID. The Committee was given an objective to reduce the financial requirements of the public system and to introduce a fully-funded scheme. With the new pension scheme it was intended to empower individuals to take greater responsibility for their own retirement, but at the same time, to sustain the government's important role in the statutory pension system. Government must provide a basic "safety net" pension and set up an effective regulatory mechanism. The social protection of retired persons is simply too important for the government to leave pension arrangements to the prudential behavior of individuals and market forces. To make the system sustainable means to reduce dependency on, but not to eliminate the strength of intergenerational solidarity. Thus, the central feature of the reform program is the funded pillar, which coexists with a reformed PAYG pillar.

The project was divided into several phases:

· **Development of an exact design of the pension reform program**. The Steering Committee for pension reform was entitled to develop the ultimate design of the reformed pension system. This involved identifying steps that need to be taken towards a full reform of the pension system. "For the public system design issues involve retirement age, age exclusive retirement, penalties for early retirement, separation of the disability system and indexation. For the privately managed scheme the issues involve eligibility, contributions, retirement benefit options, retirement age, guarantees and taxation"[15];

· **Development of an actuarial capacity to inform the selection of the pension reform design.** Actuarial capacity to model or simulate financial implications/costs for a transition to a fully-funded pension system under particular demographic and economic scenarios had to be developed;

· **Development of an action plan for transition.** The transition to a funded system has to be financed. Thus different financial options had to be developed. This involved full assessment of the financial and insurance capacity of the Pension Fund, the surplus that the Fund could gain under alternate scenarios of economic growth and evaluation of the Government potential to finance the transition process;

· **Development of a public information campaign.** An essential part of the reform strategy is to mobilize public support. Thus it necessary to design, test and implement a public information campaign in order to explain the objectives and implication of the overall reform program;

This project was set up in coordination with the World Bank, and financed through its Social Sector Adjustment Credit, approved in 1997. Within the project the Macedonian Parliament adopted legislation that regulated the new design of the pension system. The World Bank also coordinated the financial support and the technical assistance coming from other donors, like the Dutch and the Japanese governments. Every stage of the project was required to get 'no objection' approval from the Bank. "If the conditionality set by the World Bank was not met, subsequent trenches of the credit would not have been transferred."[16] Since the content of the project signed by the World Bank and the Macedonian Government, described the steps in details one can argue whether the Steering Committee was independent in the process of decision-making or was just implementing the prescriptions written in the project.

What was the content of the message that has been spread? In a World Bank working papers: 'escaping the fatal logic of the pay-as-you-go monopoly and moving to a system that allows taking advantage of capital market developments—without, at the same time, eliminating pay-as-you-go advantages' has been identified as crucial for the Macedonian reform of the pension system. Thus, in March 2000, the new law that regulates the reformed pension system was adopted. The new system was introduced under the heading of "three-pillar pension system" and consists of:

· The first pillar, compulsory and financed on PAYG basis

· The second pillar, compulsory and fully funded

· The third pillar, voluntary and fully funded

According to this scheme, eligible for a retirement benefit are contributors with 64 years of age (for men), i.e.62 years of age (for women) and minimum 15 years of pension service. The employers provide funds for the pension and disability insurance rights and the persons insured under Pension and Disability Insurance Law. The contribution rate is 21.2% of the gross salary for contributors who will remain in the mono-pillar system. Those who will choose or by law belong to the two-pillar system are going to contribute with 14.2% of the gross salary for the PAYG pillar and 7% of the gross salary for the second, fully funded pillar. This means that the contribution rate of 21.2% is just divided between the two pillars.

The contribution of 14.2% of the gross salary will be collected and managed by the public Pension and Disability Insurance Fund, which will use the funds for paying the pensions to the present and future pensioners. This corresponds to the very definition of the pay-as-you-go technique of financing: current pension benefits are paid out of current revenues from a tax, in the Macedonian case, a payroll tax. These funds are going to be used for paying the family and disability benefits, as well as part of the old-age pension. The additional 7% of the contribution rate will be initially paid to the public Pension and Disability Insurance Fund, which is responsible to transfer the funds to the private company for pension fund management. Every individual will have her/his own personal investment account operated by afore mentioned private companies and audited by the Agency responsible for providing security for the funds in the second pillar. Contributors will also have the right to transfer funds from one into other company for pension fund management.

The third pillar is designed to provide additional protection for people who want more income and insurance in their old age. It consists of personal savings plans managed by a private company and fully funded by the persons deciding to become contributors in this financial and administrative arrangement. Thus, the third pillar operates on a voluntary basis without a defined contribution rate and depends on the decision of every individual.

Table 5. Model of the new Macedonian pension system

Country

Type of scheme

Financial system

Administration

Participation

Macedonia

Mixed

Defined benefit

Defined contribution

Undefined contribution

Mixed

Pay-as-you-go

Funded

Funded

Public

Private

Private

Mandatory

Mandatory

Voluntary

Macedonia decided to mainly proceed with the traditional defined benefit pension scheme. With the defined benefits scheme, the pension formula is defined in advance, and the rest of society takes the risk if the economy does not do well, as opposed to defined contributions scheme, where contributions are specified and ultimately determine future benefits, even though there is uncertainty about future rates of return. Thus, this scheme depends on the market in great extent and is characteristic for the second pillar of the Macedonian pension scheme. A further observation is that the contribution rate for the public pension fund (gets 14,2% of the contributions) is higher than the one that flows into the two private pension funds (7% are transferred there). This leads to the conclusion that Macedonia, in the process of pension reform was not strongly favoring a fully-funded, privately-managed pension scheme. Is it because Macedonia is still transiting from a command to a market economy and does not have a fully developed private sector, capital markets and trust in the banks?

The system mirrors the approach of the World Bank to build mixed pension schemes in the region. It cannot be argued that the Macedonian pension system is identical with the rest of the schemes employed in Bulgaria, Croatia, Poland, Hungary etc., since all of them differ with regard to the replacement and contribution rates, the retirement age and the transition mechanisms. The systems are rather similar and in general have the same design, the design that has been promoted by the World Bank in its publication "Averting the old age crises" published in 1994, but we cannot speak of policy convergence. Convergence theory is "the idea that whatever their political economies, whatever their unique cultures and histories, the "affluent" societies become more alike in both social structure and ideology".[17] Globalization increases the likelihood of convergence, but important differences remain between the ways in which states respond to the policy problems created by globalization.

The World Bank continued to contribute to the process of pension reform in the Republic of Macedonia. It gave credit for a pension reform technical assistance project, which aimed to building the capacity within the Ministry of Labor and Social Policy and the Pension Fund. The project was set up to ensure that the achieved outcomes[18] from the project financed through the Social Sector Adjustment Credit can be sustained and the future reforms carried out in a professional and organized manner. The project was implemented through technical assistance from a team of international experts and through training and involvement of foreign and local consultants, including lawyers, economists and media specialists. "During the course of the project foreign consultants were able to transfer a great deal of knowledge about principles and options for reforming pension systems. And as a result of that, the financial plan developed by the Actuarial Unit was accepted by the Government and the World Bank, which demonstrates the increased capacity of the Ministry of Labor and Social Policy and the staff of the Pension Fund."[19]

The new Macedonian pension system was designed to be operational on 1 January 2004. But the implementation process has not started yet. The World Bank has approved and made effective a new investment loan (Social protection investment loan) in 2004 for supporting the implementation of the design of the afore described pension scheme, so delays in its enforcement can be expected. The World Bank has interest in ensuring that the design, developed under the two previous projects of the Bank, will be functional. Therefore, “financial assistance for the transition period will be provided to the Macedonian Government and further support in terms of technical assistance to the staff of the Pension Fund will be given”.[20]

So, if the message of the World Bank in the process of pension reform in the Republic of Macedonia was to escape from the pay-as-you-go monopoly and to favor marketization and privatization of the pension scheme, than the three pillar pension scheme is a thorough answer of the Macedonian Government to the requirements of the Bank. However we cannot say that the model applied in Macedonia is copied from the World Bank’s report promoted in 1994, but has been designed according to the political and economic reality of the state. Thus if we discuss the degree of the policy transfer, one can argue about emulation and not copying of the policy idea. The Macedonian Government accepted that the three pillar pension system, applied in almost all other countries in the region, provides the best standard for designing legislation at home, but rejected transplantation of the model in every detail. Even though authors argue that copying and combining of the policy programs can be applicable in the process of policy- making, in the process of pension reform in Republic of Macedonia the emulation is crucial not only in the agenda-setting but also in the policy formulation and implementation stage of the policy-making process.

[1] Pay-as-you-go (PAYG): in its strictest sense is a method of financing whereby current outlays on pension benefits are paid out of current revenues from a tax, in the Macedonian case, a payroll tax

[2] The two crucial variables for pay-as-you-go pension systems are: population growth and real wage growth

[3] Source: Pension and Disability Fund, Overview of the loss making and bankrupted companies, last updated 30.06.2003

[4] Source: Pension and disability insurance fund of Republic of Macedonia, Presentation overview, Skopje 2001

[4] R.Palacious, M.Rutkowski and X.Yu, "Pension reform in transition economies", World Bank, Washington D.C., June 1999

[5] R. Palacious, M. Ritkowski and X. Yu, "Pension reform in transition economies", World Bank, Washington DC, June 1999

[6] E. Fultz and M.Ruck, "Pension reform in CEE: An update on the restructuring of national pension schemes in selected countries", ILO, 2000

[7] Changes included revoking: the right to a money allowance for care and support of others; right to using social standard funds by the beneficiaries and the right to the funds for improvement of the protection of the disabled; providing resources for cash benefits on the basis of remaining working capacity by the employer; adjustment of the pensions according to the increase of wages in non-economic sector in the country; transferring the expenses for payment of the pensions to be covered by the beneficiaries etc.

[8] like the seminars held in US(1998, 2002), Poland(1998), Latvia(2000), Croatia(2002), Bulgaria(2003)

[9] as argued by Risse- Kappen 1995, p.31

[10] Zorica Apostolska, Director of the Agency for supervision of the fully funded pension scheme, Interview taken in July 2003

[11] Liljana Poposka, Financial Director of the Pension and Disability Fund, Interview taken in July 2003

[12] as argued by Risse- Kappen 1995, p.25

[13] i.e. lowering the imbalance between its current revenues and expenditures

[14] David P. Dolowitz and David Marsh, "Learning from abroad: the role of policy transfer in contemporary policy-making", Governance: An international journal of policy and administration, Vol. 13, January 2000

[15] World Bank, Project appraisal document for Social Sector Assistance Credit for FYROM, 1997

[16] Rajna Krtova Cemerska, Social Sectors Program officer, World Bank Office Skopje, Interview taken in July 2003

[17] Richard Common, Public management and policy transfer in Southeast Asia, 2001 " Is policy transfer analysis a useful mode of enquiry in political science? p. 10

[18] the legislative framework for the new pension scheme and the financial plan for the transition towards fully funded pension system

[19] World Bank, Implementation completion report for Pension reform technical assistance project for FYROM, 2002

[20] Rajna Krtova Cemerska, Social Sectors Program officer, World Bank Office Skopje, Interview taken in July 2003

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