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PUBLIC MANAGEMENT REFORM: MODERNIZING PENSION SYSTEMS IN SWEDEN AND MACEDONIA; POLICY STUDY N.2

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PUBLIC MANAGEMENT REFORM

MODERNIZING PENSION SYSTEMS IN SWEDEN AND MACEDONIA

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1. Introduction: An Unlikely Comparison?

Ageing populations are global phenomenon. Ageing and its inevitable effect on the future liabilities of the State are the same for every country. The level of pension development, however, differs significantly from country to country. As might be expected, the transformation of Central and Eastern European (CEE) countries and South Eastern European countries (SEE) from command to open market economy has placed pension reform on the top of their agendas. However public pensions have also attracted much attention in Western Europe, due to ageing and stagnating productivity. Though, all countries follow one general pattern of reform, many universal, as well as local factors, influence on developing reforms that differ significantly from one country to another. They include: "changes in the age structure of the population; fundamental structural changes of the employment situation linked to globalization processes; integration of the former socialist countries into the world distribution of labor; and rapid changes of the financial markets"[1].

The considerable differences in the economic conditions and political development of East and West European states suggest that comparisons of policy-reform are nonsensical. So the postwar division of Europe remains as prominent today in policy research as it did ten years ago even though many scholars of Western Europe have taken an interest in Eastern Europe since 1989.

Today, in some parts of Central and Eastern Europe, the transition is over and the period of consolidation of democratic institutions and market economies is well underway. In other parts the transition is still an ongoing process. But differences in the political and economic conditions in Eastern and Western Europe persist.

[1] W. Schmahl, "Fundamental decisions for the reform of pension systems", International Social Security Review, Vol.52.3/99

2. General framework

In this paper the process of pension reform in Sweden and Macedonia is being studied in comparative perspective. The approach used here examines the factors that influence the policy reform and the transmission and diffusion of policy alternatives. International organizations and transnational experts play a key role in understanding why Sweden and Macedonia should be considering similar measures at a time when their structural circumstances vary markedly. Therefore this paper begins with describing the pension schemes that needed to be reformed, the challenges they were faced with and the purpose of reforming pension schemes in the two countries. The following section of this paper seeks to find out the role of the international organizations in enforcement of their pension policy schemes across different countries. The nature of the transfer (diffusion), the actors involved in the process, their divergent ideas, as well as the process of policy transfer (diffusion) itself is analyzed here. And at the end an overall comparison of the process of pension reform in both countries is made.

Thus the objective of this paper is to see why pension schemes are modernized, who is involved in the reform, what is the role of international organizations, think-thanks and consulting firms, how the process is conducted as well what designs have been chosen by the two governments. Therefore, in line with this objective, the main question in this study will be how similar or different is the reform of the pension systems in Sweden and Macedonia is?

We would expect that the policy alternatives in Sweden and Republic of Macedonia would diverge in important ways. Republic of Macedonia has made important progress, but the country's standard of living, foreign debt and unemployment rate is far away from Scandinavian levels. The working assumption in policy analysis is that different conditions lead to different solutions. And yet as this comparison of recent pension policy reform proposals in Sweden and Republic of Macedonia demonstrates, the range of solutions to current problems facing aging populations and "social security programs, which no longer appear affordable, at least in their present form"[2] in these two countries are curiously similar. How can we account for this convergence? The central thesis of this paper is that in the process of modernizing pension schemes the theory of policy transfer can be used as a theoretical framework that could explain the global diffusion of fully funded scheme applied world-wide in different pension systems.

This provides further evidence of Blyth's (2001) argument about the primacy of ideas in shifting policy systems. International institutions (OECD, World Bank, and IMF) have reinforced this primacy of economics over politics, providing models and advice that governments may have greater or lesser freedom to follow, as argued by Jacoby (2001). The combination of these two perspectives provides important insights into the dynamics of policy reform in both Eastern and Western Europe in the new millennium.

2. Pension schemes reform in general

As we grow old we work, produce and earn less and therefore need a secure source of income to see us through life. Societies and governments have developed mechanisms to provide income security for their older citizens as part of the social safety net for reducing poverty.

In the societies where the old make up a small part of the population, informal family-based arrangements are protecting the elderly. In other societies where life expectancy is high, formal arrangements are created to prevent poverty in old age. But since pension schemes are dependent on socio-economic developments, increasing life expectancy, and changes in the working pattern, regular modifications are needed. In recent years, the theme *reform of public pension schemes* was implying to the fundamental structural changes to statutory systems of public pensions rather than modifications to the existing schemes. The challenge of the reform is to devise a new system and a transition path that is acceptable to the old, who have been led to expect more, while also being sustainable and growth enhancing for the young.

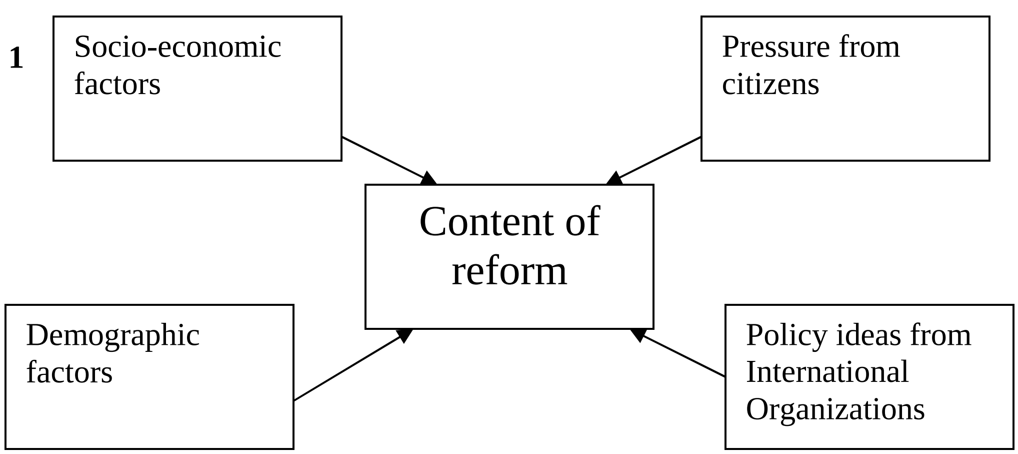
[2] International labor organization, Working paper no.21, 1997

Pension schemes have three main functions: saving, redistribution, and insurance. In practice the newly designed pension systems address the before-mentioned functions through three different financing and managerial arrangements:

1. *Public pay-as-you-go plans*: the government has the responsibility to finance, manage and insure public pensions. It offers defined benefits that are not actuary tied to contributions and usually finances them from payroll tax.
2. *Occupational plans*: privately managed pensions offered by employers to attract and retain workers. They are facilitated by tax concessions and regulated by the government.
3. *Personal saving and annuity plans*: are fully funded defined contribution plans. Workers save when they are young to support themselves when they are old. Since benefits are not defined workers bear the investment risk on their savings.

Which of these plans were adopted in the selected countries, why, and who was involved in the process will be some of the issues that concern me in this paper. Thus, for identifying the forces involved in the process of pension reform I will use the extremely useful framework-conceptual map of reform provided by Pollitt and Bouckaert. Though it must be mentioned that the diagram of forces is modified, in order for the trajectories of modernizing pension systems to be clearly understood. The diagram shows four factors that strongly influence the content of pension reform in both countries. Those are: socio-economic factors, demographic factors, pressure from citizens and policy ideas from International Organizations (OECD, World Bank).

Figure 1



To look at the similarities and differences in the process of modernizing pension systems in the selected countries the concept of trajectories will be also used. The trajectory of reform leads from a starting point α (alpha) to a future state of affairs Ω (omega). Every reform is projected in a scenario of the reform, which consists of initial state, the trajectory and the future state. It is surprising to see that the process of pension reform in Sweden and Macedonia involves a fully worked out scenario unlike in other areas of public management reform. To prove that we would proceed with over viewing the starting point of the reform in firstly Sweden and following Macedonia.

4. The old pension systems

While Sweden has a long tradition of social insurance[3], being the first nation to implement a mandatory government retirement system for all citizens[4], Republic of Macedonia has a 50 years old pension system.[5]

Sweden's former pension system (which still determines benefits for older workers and retirees) dates from 1962 and was a tax-financed, pay-as-you-go entitlement program. The system had two components. The first part was the basic pension (FP), which was available to everyone regardless of contributions paid. In addition, a second, earnings-related supplementary pension (ATP) was available. The supplementary pension provided old-age benefits linked to each worker's earnings history. To finance these benefits, the government imposed two separate payroll taxes on workers: a tax of nearly 6 percent for the basic benefit and a tax of 13 percent for the earnings-related portion of the program. The government also used general revenues to help finance the basic benefit.

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3 For more information, see Social Insurance in Sweden, 1999, available at *www.rfv.se/english/pdf/bokeng.pdf*. Additional information on the Swedish pension system may be found at *www.pension.nu* , *www.ppm.nu* , *www.saf.se*, or *www.rfv.se*.

4 Marten Palme and Ingemar Svensson, "Social Security, Occupational Pensions, and Retirement in Sweden," National Bureau of Economic Research *Working Paper* No. 6137, August 1997.

5 In order to provide continuity in the pension system, the Government of Republic of Macedonia after declaring independence developed a Law on Pension and Disability Insurance (PDI Law) in December 1993 ("Official gazette of the Republic of Macedonia" num. 80/93). The intention was to independently regulate relations and rights in the sphere of the pension and disability insurance.

The basic characteristic of pre-transition pension scheme in **Macedonia** as in other CEE and in SEE countries was the state's large role in providing retirement benefits: "pensions were major responsibility of the government, which mandated, financed, managed and insured public pensions"[6]. Pensions in Republic of Macedonia were financed on a pay-as-you-go basis through transfers of funds from state-owned companies to a social-security budget within the state budget. The second characteristic was the retirement ages, which in Macedonia and other transition countries were lower than those in OECD: male workers retired at age 60 with 25 years of service, while women retired at 55. The third characteristic was the calculation of benefits, which commonly were calculated as a fixed percentage of a worker's reference income for a minimum number of years, often with a flat rate component and/or a benefit maximum. The government financed the pension system from payroll tax that was defined on 21% of the gross salary. This scheme was created to redistribute real income both across and within generations.

5. The main factors that influenced the pension reform in Sweden and Macedonia

Just when the Sweden's pension system has begun to mature, the conditions conducive to a successful pay-as-you-go scheme[7], started to disappear. Population growth started to stagnate, fertility rates begun to fall and life expectancy continued to increase. In the same time due to the enormous public deficit and other global economic forces that effect on the structure of the working pattern, wage growth was slowing dramatically, thus the Swedish government decided that they had to reform the Swedish old-age pension system.

On the other hand the Macedonian pension system was created at earlier stage when the population was younger. Also due to the transition from command to market economy the employment rate went low. As a result today the country spends more on pension and creates more public deficit then before. Therefore reform of the pension system is high on the political agenda of the last two Governments of Macedonia.

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[6] World Bank, "Averting the old age crisis", Policy research report, Oxford University Press, 1994
[7] The two crucial variables for pay-as-you-go pension systems are: population growth and real wage growth

However the key factors that explain why both countries decided to reform their pension schemes is summarized in line with the previously mentioned and presented in Figure 1 division of forces that have strong impact on the content of reform.

In Sweden:

1. Socio-economic factors:

- **Long-term deficit.** The unfunded pension system liability in 1996 was nearly $500 billion, roughly equal to 200 percent of Sweden's economic output.

- **Future tax increases.** Payroll tax rates already were high—nearly 20 percent—but they would have had to rise even more to keep the existing system in balance. According to Swedish government estimates, the tax rate would have needed to be as high as 36 percent by 2025.

- **Economic impact.** The system's high tax rates discouraged output and employment. The adverse effect on work incentives was particularly severe because of a weak relationship between the taxes workers paid into the system and the benefits they expected to receive. In other words, workers had an incentive to work less and to underreport their income since increased pay simply meant higher taxes without an accompanying increase in future pension benefits.

2.Demographic factors:

- **Decline in a number of the working people.** In 1950, there were more than five working-age people for each person over age 65. Now there are fewer than four, and the ratio eventually will drop to three working-age people per retiree.[8]

[8] www.heritage.org/research/social

3. Pressure from citizens:

- **Fairness.** Pension benefits for retirees often varied greatly. Because old-age benefits were based on a worker's 15 highest-earning years, two Swedes 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.

In Macedonia:

1. Socio-economic factors:

- **Raising unemployment.** "In 1995, the average unemployment rate was 12.5 per cent in CEFTA and Southeast Europe. In CEFTA countries, the percentage decline in employment was greater than that in output (with the exception of the Czech Republic), while in other countries the drop in unemployment was less, reflecting hidden unemployment in the form of shorter working hours or unpaid leave. The situation in Macedonia was very serious. In 7 years the unemployment rate went up for 30 %. In comparison with all other countries analyzed in the Augusztinovics's economic survey of Europe, Republic of Macedonia has the biggest employment drop throughout the period from 1991 to 1998. In 1998 almost 35 % of the population was unemployed.

- **Decline in number of contributors.** For the Macedonian pension scheme, the above -mentioned developments had negative impact: 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[9], in Macedonia

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

the ratio between contributors and pensioners according to the official statistics was the following:

Table 1. 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	6.57	1.5

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

3. Demographic factors:

- **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.[10]

3. Pressure from citizens:

- **Sustainability.** The delay in payment of the pensions in 1993 made the public awareness for more sustainable pension system bigger. 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 of 40% of the voters are either pensioners or about to be pensioners.

6. Policy transfer- theoretical framework for explaining the policymaking

As it could be noticed the fourth factor that influences pension reform in the selected countries was not mentioned in the previous chapter. The reason for that is the role of the International Organizations in the decision-making process in the area of pensions. Therefore the international organizations will be separately examined in this chapter. The factors addressed earlier explained why the capacity of both pension systems declined and have to be reformed, but it were the ideas of the OECD and the World Bank that carved the new pension schemes.

In recent years there is a growing interest in studying the role of international organizations in policy making, which resulted in developing different concepts of policy transfer- "a process in which knowledge about policies, administrative arrangements, institutions etc. in one time and/or place is used in the development of policies, administrative arrangements and institutions in another time and/or place"[11].

Dolowitz and Marsh are the authors who led the efforts to develop a model of policy transfer. They have drawn together a general framework of heterogeneous concepts including policy diffusion, policy convergence, policy learning and lesson drawing under the umbrella heading of policy transfer which mainly draws on the work of Rose (1991, 1993), Bennett (1991a,b), Robertson (1991) and Wolman (1992).[12] Policy transfer is thus used as a generic concept, which encompasses quite different understandings of the nature of policy development.

Dolowitz and Marsh have provided an extremely useful framework- a map of the process of policy transfer. That framework is designed to incorporate every form in which policy transfer occurs, thus the following classification is made: 'voluntary', 'perceptual', and 'direct' or 'indirect' coercive policy transfer. These classifications were

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[10] E. Fultz and M.Ruck, "Pension reform in CEE: An update on the restructuring of national pension schemes in selected countries", ILO, 2000
[11] Dolowitz and Marsh, "Who learns what from whom: a review of the policy transfer literature, Political studies 1996, p.344
[12] Mark Evans and Jonathan Davies, "Understanding policy transfer", Public Administration Vol.77, No2, 1999, p.363

made in order to explain why country *a* would want to transfer policy *b.* According to Dolowitz and Marsh (1997), "voluntary transfer' implies that rational, calculating actors desire a change and actively seek policies to satisfy their needs. Coercive transfer on the other hand occurs when policy makers are forced by the actions of outsiders to engage in transfer".[13] Dolowitz also differentiates 'perceptual transfer' based on 'feelings of being left behind' when policy makers perceive themselves as having fallen behind the international community. But when involved in policy transfer actors have different options to chose. As Rose identifies, there are different degrees in policy transfer: copying, emulation, hybridization, and synthesis. Countries could incorporate policies or programs by copying without any changes; but countries could reject copying in every detail and accept that the particular program elsewhere provides the best standard for designing legislation at home. Hybridization and synthesis involve combining elements of programs found in two or more countries to develop a policy best suited to the emulator.[14]

Table 2. A model of Policy transfer (adapted from Dolowitz and Marsh)

Why transfer?	Who transfer?	What is transferred?	Where from?	Degree of transfer?
Voluntary Coercive Perceptual	Bureaucrats Elected officials Consultants Policy entrepreneurs	Pension schemes	Other countries International organizations	Copying Emulation Inspiration Mixtures

Source: Richard Common, Public management and policy transfer in Southeast Asia, 2001 " Is policy transfer analysis a useful mode of enquiry in political science? p. 30

Globalization strongly affects the ability of individual states to make policies that are appropriate to their particular political, economic and social contexts. Governments struggle with their new environments and face problems that are linked to every other problem, which makes the policy transfer even more appealing because it offers a 'short cut' or a 'quick fix' to those problems. International Organizations, such as the OECD,

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

G-7, IMF, World Bank, UN and its various agencies, are increasingly playing a role in the spread of ideas, programs and institutions around the globe. These organizations influence national policy-makers directly, through their policies and loan conditions, and indirectly, though the information and policies spread at their conferences and reports. That makes the International Organizations agents of coercive policy transfer.

Even though the main objective of the International Organizations is policy diffusion among the member states, in the case of modernizing pension systems, one can argue about both policy diffusion and policy transfer. Policy transfer is the conscious adoption of a public policy from another state, organization, agency. Ideas and policies may be diffused, but to transfer to occur they must be adopted and implemented.

The central thesis in this paper is that in the process of modernizing pension schemes the theory of policy transfer can be used as a theoretical framework for explaining the global diffusion of fully funded pension systems. Thus the policy transfer is used as an independent variable to explain the policy outcomes in reforming pension systems in Sweden and Macedonia. OECD and the World Bank are regarded to be agents of the coercive policy transfer that took place in both countries.

Analysis of pension schemes and recommendations for their reform has been on the top of the agenda of international organizations in recent years. Although pension policy is an integral part of the social policy mandate of the International Labor Office (ILO), and the International Social Security Association (ISSA), one can notice the recent involvement of the World Bank and International Monetary Fund (IMF). The Organization for Economic Cooperation and Development (OECD) traditionally is concerned about the social policy in its member states, but comprehensive and fundamental statements on pension reform are new department.

Whereas the OECD encourages exchange of ideas and programs among the member states, the World Bank focuses on programs of concern to developing countries. The World Bank report ”Averting the old age crises: Policies to protect the old and

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[14] R. Rose, “What is lessons-drawing?” 1993, p.21

promote growth", presented at the annual World Bank meeting in Madrid 1994, made the organization's worldwide involvement in the issue of old-age provision into a much-discussed and sometimes controversial subject.[15] The report favors a three-pillar model of old-age provision. According to this model, the functions of income protection and income redistribution should be separated in both administration and financing. The income distribution should be taken over the public system financed taxes or contributions, while the old age saving should be done under the second pillar, which should be funded and privately managed. The third pillar should allow anyone who wants further protection to accumulate capital privately to provide for his or her old age.

The OECD approach is different from other international organizations since it is a research body which analyses economic issues and formulates policy recommendations, but does not give credits or finance projects, unlike the World Bank. Because "it does not enter into any financial risk, the OECD, does not have to specify all the details of a reform project and negotiate them with the borrower".[16] In early 1998, the OECD published its study "Maintaining prosperity in an ageing society" in which the organization stresses the need to contain the expenditure of statutory social security systems. According to OECD 's calculations, the balance of financing of statutory pensions in most member states will go into a sustained deficit in about ten years' of time. Thus, a legal framework within which alternative provision options can operate must be established. Here OECD 's recommendations coincide with those of the World Bank, advocating for a second pillar of fully funded old age savings. That also explains the convergence between the pension schemes adopted in Sweden and Republic of Macedonia.

[15] World Bank, "Averting the old age crisis", Policy research report, 1994
[16] Monika Queisser, "Pension reform and international organizations: from conflict to convergence", International Social Security Review, Vol.53 2/2000, p.41

7. The process of reform

Despite the long time horizon of pension schemes, the need for major reform has been portrayed as a crises requiring immediate action.[17] Perhaps this crises approach was necessary to draw attention to problems with existing schemes and create the will to address them. With the new pension schemes the desire was to empower individuals to take greater responsibility for their own retirement, but in the same time, to sustain the government's important role in statutory pension systems. 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 government to leave pension arrangements to the prudential behavior of individuals and market forces.

Thus, both Sweden and Macedonia approached the reform of the pension system, during which process these four features received greater attention:

1. Type of scheme: defined benefit or defined contribution
2. Financial system: pay-as-you-go or funded
3. Administration: public or private
4. Participation: mandatory or private

These features will be also used as crucial variables for a comparative analysis of the process of pension reform in the selected countries.

A national pension scheme involves transfer of resources from active to retired persons. No matter how they are financed, pensions are simply transfers of resources from active to inactive persons. Under the pay-as-you-go (defined benefits) system, the transfer is direct, through taxes or contributions paid by workers. Under the defined-contribution system, pensioners liquidate assets, which they have accommodated by selling them to workers. In both cases, workers' disposable income is reduced by the amount of resources transferred to retired persons.

[17] Warren Mc Gillivray, Pension reform: where we now?, International Social Security Review, Vol. 53, 1/2000

The former national pension scheme of both Macedonia and Sweden was defined benefit, financed on pay-as-you-go basis, administered by a public pension fund and the participation was mandatory for all working citizens. In order to address all three functions of pension schemes: saving, redistribution and insurance the new systems were designed to encompass multiple financing and managerial arrangements.

7.1. The Swedish case

Sweden is now one of the world's leaders in the global shift to private pension systems. Being an archetype for consensual democracy characterized by slow decision-making in the area of public policy, Sweden has initiated the present pension reform 20 years ago. In that period various parliamentary and government's commissions considered different issues, but the debate mainly took place within the Government's special Commission for reforming the pension scheme. All actors in the reform process, members of political parties, representatives of the: Government, Parliament, employer's organizations, trade unions, OECD, consulting firms and social groups affected by the reform itself, composed the Commission. It was this Commission, which in 1994 proposed a reconstruction of the system, but was finally presented to the Parliament in 1998. The first pensions under the new system were paid in 2001.

The new Swedish pension system consists of three parts, the first two being of the type Defined Contributions (DC). The three parts are:

- The 'Income pension', funded through the defined contribution DC system
- The 'Premium pension', funded trough the DC/fully funded system
- The 'Guarantee pension', funded through the defined benefit and PAYG system

The Income pension is a notional funded system. Contributions to this system are added to the personal notional accounts, and the yearly pension is determined from the total holding at retirement. The yearly contribution for an individual is defined as 16% of her/his 'personal income'. The account is increased each year by an "interest", which equals the increase in the National Income Index.

The Premium pension is a funded system. Each individual in the system has her/his own account. The yearly contribution for an individual is 2.5% of her/his 'personal income'. The individual has to choose how the money shall be invested. The investments are administered by the PPM, the Premium Pension Authority. At the moment PPM offers 800 funds and an individual can choose at most 5 funds and can change funds free of charge. For those who do not make an active choice, the money is invested in a government default fund.

The general tax revenue finances the Guaranteed pension. Those with low lifetime incomes that will accumulate limited notional and financial capital, from age of 65 will be entitled to a supplement guaranteeing her/him a minimum pension. The guaranteed pension share of total pensions is indexed by the change in the Consumer Price Index.

Beginning at age 61, a worker can retire, and the government uses the money in these notional accounts to calculate an annuity (annual retirement benefit) for the worker. The new pension system adjusts retirement benefits for inflation, although the adjustment may vary according to real wage growth. This provision creates a direct link between the growth of labour force income and the taxes paid on that income, and the benefits paid to retirees. This ensures that the system is financially sustainable.

7.2. The Macedonian case

In **Republic of Macedonia**, the pension reform was officially initiated in 1997, when a project for pension system reform was set up within the Ministry for labor and social policy. The project was a joint venture of the Macedonian Government, experts from the Pension and Disability Fund, consulting firms, Labor union and other groups that were affected by the reform. It was financially supported by the World Bank, which financed the pension reform design, the legislative framework and the management of the project. In the period between 1993 and 1998 a lot of other measures were undertaken in order to accommodate the difficulties in sustaining the traditional PAYGO system. Thus, the Government enforced many typical solutions to respond to the increased fiscal pressure by stepping up the contribution rate and by increasing the retirement age, i.e. from 60 to 63 years of age for men and from 55 to 60 years of age for woman; in regard to the pension base, derived from the average of all wages of all pension service, instead of the 10 most favorable years it was decided to decrease the percentage for pension determination from 85% to 80%, etc.

However, it was only in March 2000, when 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 is consisted of:

- The first pillar, compulsory and financed on PAYGO basis
- The second pillar, compulsory and fully funded
- The third pillar, voluntary and fully funded

The system will be operational on 1 January 2005. According to this scheme eligible for a retirement benefit are contributors with 64 years of age (for man), i.e.62 years of age (for woman) 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 PAYGO 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. 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 keep the rights 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 is consisted of personal savings plans managed by a private company and fully funded by the ones who will decide to become contributors in this financial and administrative arrangement. Thus, the third pillar operates on voluntary basis without defined contribution rate and depends on the decision of every individual.

7.3. Comparing the two cases

Much more clear picture of the Ω (omega) point of the reform trajectory or the designs chosen by the Governments of Sweden and Macedonia can be obtained if the information from above is put together in one scheme. By using the variables: type of scheme; financial system; administration and participation we could easily see the differences and the similarities of both systems.

Table 3. A comparative view on the two models

Country	Type of scheme	Financial system	Administration	Participation
Sweden	**Mixed** Defined contribution Defined benefit	**Mixed** Funded Pay-as-you-go	 Private Public	 Mandatory Mandatory
Macedonia	**Mixed** Defined benefit Defined contribution Undefined contribution	**Mixed** Pay-as-you-go Funded Funded	 Public Private Private	 Mandatory Mandatory Voluntary

It is obvious that the models applied are combination of different financial and managerial arrangements. Sweden and Macedonia appear to adopt systems that combine public managed pension plan designed to meet the basic needs with a privately managed personal saving accounts to satisfy the high demand of middle-and upper-income groups. Both systems are created to provide the three basic functions of a pension scheme: redistribution, saving and insurance. The redistribution is obtained through the publicly managed pension plan, funded on a pay-as-you-go basis. The saving is enabled through the personal saving accounts, privately managed and fully funded. And the insurance is provided jointly by all pillars, but secured with the third voluntary pillar in the Macedonian case. So, these schemes separate the redistribution from the saving function by introducing the two pillar system where the main theme in both cases is that they are mandatory regulated, meaning that in future will still require government management or regulation. Therefore public management and financing are clearly needed to address the redistributive side of old age security programs. But saving and insurance could be addressed through private plans that are mandated and regulated by the Government.

The main difference between the two cases is that whereas Sweden gave preference to a defined contribution pension scheme, Macedonia decided to mainly proceed with the traditional defined benefit pension scheme. To what do we account this divergence? In a defined contributions scheme, 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 extend. On the other hand, 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. Further more the defined contribution plans are by definition fully funded, though it is possible for the defined benefit plans to be funded also. This brings me to the conclusion that the Swedish government was more in favor for the fully funded, privately managed, pension scheme, than the Macedonian government. Why is that so? Is it because Macedonia is still transiting from commend to open market economy and doesn't have developed private sector as Sweden has? Or is it because of sustaining the money in the public pension funds, which are often required to invest in government securities or the securities of state-enterprises in order to strain its capabilities?

The strong orientation to privately managed pension systems of the Swedish government could be also seen from the scheme bellow where it is shown that 16% of the contribution rate goes to private funds whereas only 2,5% are flowing into the public pension fund. In comparison the Macedonian public pension fund gets 14,2% of the contributions and only 7% are transferred to the private funds.

As we know pay-as-you-go pension schemes are often described to be vulnerable to demographic shifts. There are many projections, which show that the proportion of the elderly will increase by a third in many currently demographically "young" countries, and that especially refers to Macedonia, thus it could be noticed that by increasing the retirement age the government wanted to accommodated the problems that could derive from the severe demographic shifts. The Swedes remain liberal here and define only the earliest retirement age at 61 without giving the upper ceiling.

And of course at the end we should not forget that while the Swedish pension system is fully operational from 2001, the Macedonian pension scheme is still in the process of implementation and it will be operational in 2005.

Table 4. Differences and similarities in the process of reforming pension schemes

Issues	Sweden	Macedonia	Converge	Diverge
Actors involved	Pol.Parties, Representatives of Gov., Parl., unions, OECD	Pol.Parties, Representatives of Gov., Parl., unions, WB	X	
Operationalization	2001	2004		X
Contribution rate	16%- funded 2,5%-PAYG	14,2%- PAYG 7%-funded		X
Retirement age	From 61 all men & women	60-women 65-men		X

However, the similarity, indeed the resemblance, of the two models of old age pension system with the ones proposed by on one hand OECD and on the other hand World Bank, is striking. Sweden being a leader between OECD member states to almost privatize the national pension system, literally applied the recommendations of the “research institute” in order to sustain its long-term solvency and protect the citizens. Macedonia not only applied, but also billed the World Bank for the system promoted by this transnational organization. Due to the convergence of the ideas of both OECD and World Bank for having a fully funded, privately managed second pillar, the new pension systems of Sweden and Macedonia also converge.

8. Conclusions

The purpose of this paper was to survey the present state of pension reform in Sweden and Macedonia. It was not intended to evaluate specific reforms. Pension schemes are long-term programs and a comprehensive assessment of the effectiveness of a particular system can be made only after a generation has completed its working and retirement periods, which means after 70 years or more. But the future of pension schemes is evolving very rapidly and as we have seen from the examples of Sweden and Macedonia, often pension systems do not live up to 70 years in order to be evaluated. However, that does not prevent governments to design programs that appropriately address the challenges with which their systems are faced.

Two alternative pension designs are currently being implemented with a desire to split certain risks. The **first** design consists of financing retirement incomes from a range of different sources in particular a mixture of defined benefit and defined contribution schemes. This design comprise number of tiers (pillars):

- A bottom anti-poverty tier, pay-as-you-go defined benefit tier, mandatory and publicly managed, which will provide 50% of lifetime average earnings and which is fully indexed;

- A second tier, defined-contribution based, mandatory and privately managed, which will provide pension by means of annuities;
- A third tier, defined-contribution based, voluntary and without ceiling, privately managed.

This design is promoted by the World Bank and fostered by many, if not all, developing countries, especially the transition countries from Central and Eastern Europe, including Republic of Macedonia.

A **second** alternative is a notional defined contribution scheme. The structure of such a scheme is very similar to a defined contribution scheme: a notional account is accumulated during the working life based on contributions and the (notional) interest obtained on them, which could be converted in pension at retirement by means of an annuity. The main difference is that the interest rate applied is not the market rate of interest but some other indicator. This designed is promoted by the OECD and fostered by several member states, led by Sweden, which adopted this system first.

Sweden and Macedonia were studied here because the pension reform in both countries and the designs they have chosen illustrates thoroughly the fierce debate between the positions of the International Organizations, particularly OECD and the World Bank. But as it could be seen from the selected cases their approaches and the models they promote converge markedly even though there are bound to be differences of opinion because of different perspectives and mandates of the various organizations.

One single conclusion stands out: there is no single design, which fits all countries and all circumstances. The question of what is the most appropriate design has to be weighed against other factors, and need to provide universal coverage and good governance. These will determine not only what is feasible and what is not, but also where the most desirable balance lies. Even though different conditions lead to different solutions, the international organizations as global actors in the policy decision-making influence greatly the policy outcome.

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