

The Icelandic Pension System

- some regulatory aspects & effect of increased longevity

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The Icelandic Pension system

- Small in absolute terms : ~ 14.500 million Euro*
- Big in relative terms : ~126% of GNP (pillar II)

- DB funds closed to new entrants **6**
- DB funds open : **2**
- DC funds : **20**

- (* FME yearly report 2012)

The Icelandic Pension system

- Mandatory membership for ages 16-70
- Benefits lifelong pension from no later than 70 years + invalidity, widow(er), childrens benefits
- Minimum premium 12% of all wages,
- General cover from 1969, agreement on the labour market for creating funded pension system w mandatory membership as an addition to pillar I
- Regulated by law set in 1997 (prev. 1980, 1974)
- Optional premium up to extra 6% payments for additional DC (pillar III)
- After 1997 pension reform funds accepting new members are to be fully funded

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Regulation of financial position

- Closed DB funds are exempt from this type of control
- If liabilities exceed assets by more than 10% of liabilities in one year or more than 5% in five consecutive years the fund must react (law from 1997)
- This control has been in active use, in recent years after the financial crisis most DC funds have had to reduce accrued benefits by 10% up to 30%

Calculation of financial position

(From yearly accounts 2012, Söfnunarsjóður lífeyrisréttinda)

	Áfallin skuldbinding	Framtíðar- skuldbinding	Heildar- skuldbinding
Eignir:			
Hrein eign til greiðslu lífeyris	106.413.520	0	106.413.520
Endurmat verðbréfa miðað við 3,5% vexti	3.952.112	0	3.952.112
Fjárfestingakostnaður	(2.672.885)	0	(2.672.885)
Núvirði framtíðariðgjalda	0	39.917.372	39.917.372
Eignir samtals	107.692.747	39.917.372	147.610.119
Skuldbindingar:			
Ellilífeyrir	88.071.567	33.519.627	121.591.194
Örorkulífeyrir	7.313.685	4.854.370	12.168.055
Makalífeyrir	12.287.209	2.067.661	14.354.870
Barnalífeyrir	53.015	501.348	554.363
Rekstrarkostnaður	1.587.940	1.191.932	2.779.872
Skuldbindingar samtals	109.313.416	42.134.938	151.448.354
Skuldbindingar umfram eignir	(1.620.669)	(2.217.566)	(3.838.235)
Í hlutfalli af skuldbindingum	(1,5%)	(5,3%)	(2,5%)

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Calculation of financial position

- Assets are shown at cost prices
- Liabilities are valued at 3,5% real rate of interest
- Assets with fixed income are revalued at 3,5% real interest rate
- The Icelandic Actuarial Association (FÍT) has the task of publishing the life- and invalidity tables to be used for valuation

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Life tables for valuation

- Going back to 1960 life tables have been published by FÍT every 5 years based on 5 years experience with population data
- In recent year tables have been published every 3 years
After 1997 pension reform funds accepting new members are to be fully funded
- The tables do not include any prognosis of improving mortality

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FÍT Life tables –life expectancy

Life expectancy at birth / 67

	Male	Female	Male	Female
ISD0711	79,5	83,6	16,8	19,1
ISD0408	79,1	83,2	16,5	18,9
ISD0105	78,6	82,9	16,1	18,9
ISD9903	77,9	82,2	16,0	18,3
ISD9600	76,9	81,7	15,2	17,9
ISD9195	76,2	81,1	14,9	17,6
ISD8690	75,0	80,6	14,6	17,5
ISD7680	73,6	80,2	14,5	17,2

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Response to increased longevity

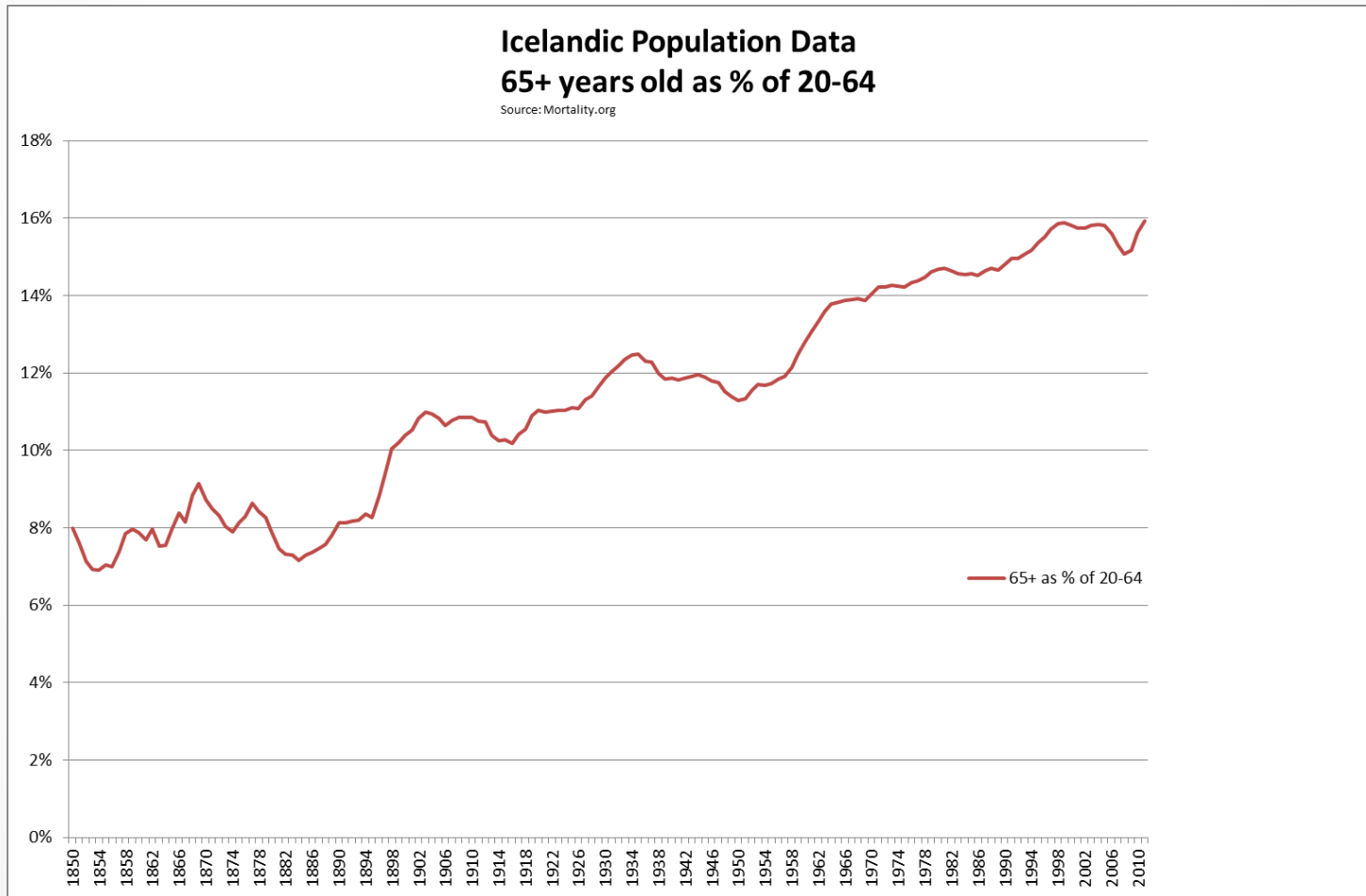
- Due to the pressure from increased longevity premiums were raised to 11% in 2005 and then to 12% in 2007
- Increases in life expectancy have continued
- With a view to future expected increases in lifespan it is clear that the current premium / benefit levels will not be tenable
- Valuations made with life tables including expected future improvements in life expectancy show significant effect on the financial position of funds

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Response to expected future increases in life expectancy

- The Icelandic Actuarial Association has set down a working party with the task to prepare life tables with a built in prognosis of expected future increases in life expectancy – to be concluded this year
- The Association has been reluctant to introduce such tables unilaterally
- Discussions in the pension fund community and the association of actuaries have mainly focused on meeting the future increases in longevity by raising the retirement age rather than by further increases in premiums
- Generally the way forward is seen as raising the retirement age to at least 70 in steps over the next 20 to 30 years, not by increasing premiums

Increase in longevity



Increase in longevity

- Decrease in fertility can further add to financial burdens of the future working generations
- Decrease in mortality before retirement cannot offset the increase in time lived after retirement for a fixed retirement age
- Increasing premiums is really more moving the problem, not solving it

Increase in longevity

– how serious a problem ?

- „Far and away the best prize that life has to offer is the chance to work hard, at work worth doing. ”
(Teddy Roosevelt)
- A fixed retirement age is an artificial construction of fairly recent date
- If the proportion working in the population can be increased the size of the problem can be reduced
- This calls for a flexible labour market which accepts the elderly willing and able to work
- The labour market rather than any financial solution might be the best venue for handling future increases in longevity