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Pension system of latvia: Case study approach

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Abstract

The current paper offers a case study approach for testing several options and hypotheses. The need for Pension Reform in Latvia has been the result of a steadily increasing aging of the population. By 2001 a new three-level pension system was introduced in Latvia aiming to reduce the effect of demographic risks and demonstrating the country's intention to provide an optimal public or private compound in old-age provision. Nevertheless, the demographic prognosis of European Commission estimates that by 2060 the population in Latvia will reduce from 2.2 million to 1.7 million people, and the number of elderly people will almost double. The potential impact of demographic change on the age structure and the size of population is dramatic and still the main problem that cast the doubt on the ability of state mandatory pension scheme to provide the appropriate pension level. Personal financial planning, personal investments are important. The objective of this research work is to investigate whether the existing Pension system in Latvia is working effectively under changing economic environment. It also analyzes the role of Private voluntary pension scheme and the current demographical situation with a flow of emigration. The research work aims at offering several options for the improvement of the situation.

Keywords: Economic development, Demography, Pension Levels, Private voluntary pension scheme, Solidarity, Retirement.

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1. Introduction

According to the public research work carried out by the international finance service company Allianz in 2014, the pension system of Latvia is the 9th sustainable pension system among 50 countries. To elucidate Pension Sustainable Index and to determine sustainability of each country's pension system, 50 countries were evaluated according to different criteria. Basing on the research work carried out the highest Pension Sustainable Index can be observed in Australia, Sweden and New Zealand. Special methodology has been worked out to determine Pension Sustainable Index and it is always observed in the research work process. The main criteria are the residents' age structure, public finances, pension age, reforms of the implemented pension system, etc. (Allianz, 2014). The new pension system was started in 1995 in cooperation with the World Bank, hence, the existing pension levels have been introduced in the country:

- 1 level - mandatory extra-fund pension scheme guaranteed by the state
- 2 level - funded pension scheme guaranteed by the state;
- 3 level - private voluntary pension scheme.

The existing pension system is organized so that the residents can participate in securing their own old age. The core principal of the pension system is the following: higher social insurance installments are deposited at the present moment, higher pension will be received in future. There are three main objectives lying at the basis of old age pension system:

- The principle of solidarity;
- The principle of justice;
- The voluntariness principle.

According to the existing legislation in Latvia, a definite pre-pension and pension age has been determined in order to receive pension due to the age. Raising the pension age has been one of the implemented tools to reduce the problem of aging. Starting from January 2014, by then the existing pension age 62 years, and adding 3 months per year and, thus, by January 2025 the pension age will be 65 years. So, starting from January 2025 a person will receive old age pension if his/her insurance standing is at least 20 years. (Law On State Pension, 1996)

The Law on State Pensions describes definite cases where the person has the right to receive old age pension prematurely; it is possible 2 years in advance of the legal pension age. In this case, according to the Law on Pensions, the insurance standing should be at least 30 years long. There exist definite restrictions if the person wants to retire prematurely: the person gets 50% of the calculated pension. Expected learning outcomes –working on this case will enable Bachelor's level students studying economics to acquire the expertise necessary for dealing with pension system problems in an environment of slow economic development, aging of population and migration. It should also enable students to understand the importance of financial literacy and necessity of planning personal finance for old age.

2. The Main Characteristics of Current Pension System

The reform of Pension System in Latvia has been initiated alongside with the rehabilitation of independence of Republic of Latvia. The aim of this reform was to restructure the existing pension system according to the present social-economic system in Latvia. The previous pension system did not conform to the conditions of market economics and, consequently, it was not able to function in the new situation. According to previous system reform the size of the pension did not depend on the amount of payment made, thus, the amount of the pension depended on average salary and the length of service. Such situation did not stimulate the workers to follow tax payments because the pension was

ensured even in such cases when tax payments were made according minimal wage set by the legislation of the country. So there might be a possibility in future not to have enough money to secure pensions. Another major task was to set up a financially sustainable system to reduce the risks of rapidly aging population. Oxford dictionary says that the term “pension” has the following explanation: pension is a regular payment made to the retired persons (or older) or to the physically handicapped persons, or to the widows (Oxford Dictionary, 2012)

Statistical bureau of European Communities defines the term “pension” as periodical payments with the aim to maintain receiver’s income after retirement ceasing paid employment at the normal pension age or to back the income of elderly people. (European Parliament's Employment and Social Affairs, 2010)

Organization for Economic Cooperation and Development (2003) defines pension as payments made to the participants of the pension fund (or to the dependent person) after retirement age. Basing on the above mentioned explanation the authors believe that pension is a periodical payment with the aim to maintain income after retirement ceasing paid employment at definite age.

Taking into account both dramatic decrease of birth rate and a negative demographical trend, it became clear in 1990-s that the state budget would not be able to ensure pensions in the long term. As a result of this, there was a need for the reform. Pension reform is based on the Concept of Pension System Reform worked out between 1994-1995. The reform envisages the introduction of three-level pension system, thus improving financial position of old age people and risk division between the state (future tax payers) and person’s savings in compulsory and voluntary pension scheme.

The main aims of the reform were the following (Verje, 2006):

- To form a three-level pension system which would allow to divide the state and every individual’s responsibility towards their financial means in old age;
- To create a safe state pension system in which the pension amount depends on their social contribution rates ;
- To set up the financial system which can be administered efficiently;
- To increase the retirement age, thus ensuring the ratio decreases between the employed and the retired, as well as reducing the burden of social security system;
- To stimulate the development of the state economic system, ensuring the opportunities to invest the savings in the economy, thus developing a financial and capital market.

Two different kinds of financing pension system have been mentioned:

- 1) Defined Benefit (DB) – pension system which guarantees pension payments of definite volume not taking into account mandatory or voluntary paid social insurance contribution
- 2) Defined Contribution (DC) - pension system at the basis of which lies pension contribution directly dependent on the paid social insurance mandatory or voluntary contribution into personal pension accounts.

The principles of the above mentioned two pension systems (DB and DC) were transposed into pension system of Latvia. Basing on the justice principle, pension contributions in Latvia are directly dependent not only on social insurance mandatory and voluntary contribution, but also on the length of service and on the profitability level of the chosen funded pension plan. Alongside with the mandatory social insurance contribution every person has the possibility to enlarge his/her personal pension fund paying voluntary contribution into private pension funds.

Pension Level 1 was introduced in January 1996, it includes generation and gender equal treatment principles. Generation equal treatment means that working population social security contributions are being used in order to pay old age pensions to the current retirees. Gender equal treatment

means that the same pension period applies in case of their retirement to both women and men. According to the European system (PAYG) it is the type of pension which is subjected to huge demographical risks.

Pension Level 2 was introduced on 1 July, 2001. Since that period a part of social security contributions that have been made, are being invested in financial markets and pension accruals are being made in each Level 2 personal account. Pension Level 3, that is, private voluntary pension scheme was introduced in July 1998. Pension Level 3 envisages a free choice for every individual to set up additional accruals for their pension by making contributions into Private Pension Funds. Private Pension Fund is a licensed finance body, which accepts their own private contributions, as well as those made by the third party. They organize their management in order to ensure accruals for those persons in old age.

Taking into account the above information, the major success of pension system reform in Latvia is creating Pension Level 2, which is compulsory to the majority of population; it also helps to reduce the effect of demographic risk on pension. However, this Pension level is being subjected to many other risks, which the population of Latvia must take into account when deciding the appropriate Pension Fund. (Law On State Pension, 1996)

In accordance with the State funded pension law, each individual has the right to choose how to organize the payment of his funded pension capital. When the individual has reached the retirement age, he can

- 1) Add the accrued funded pension capital to the non-funded pension capital and recalculate old-age pension in accordance with the state's legislation system
- 2) Obtain life assurance policy (life pension) (Law on State Funded Pension, 2001)

In September 2013 JSC "SEB Dzīvības apdrošināšana" started to offer life pension policies. At present three insurance companies offer such kind of service. Members of state-funded pension schemes can sign the agreement about obtaining life pensions if

- The individual is of retirement age or has the right to retire in advance
- Accrued funded pension capital has reached definite volume of set by the insurance companies.

The aim of the state implemented Pension Reform is to create a financially stable and efficient pension scheme that is based on individual social security contributions which in turn will ensure such amount of pension that depends on the contributions made over the previous period, as well that will facilitate the increase of social security contribution growth.

The need for Pension Reform was the result of a steadily increasing aging population, instead of keeping the current retirement age. Life expectancy has been gradually increasing. As a result, every year we see the growth in costs for pensions from social security budget.

The task of the developed pension system is to increase the compensation level under the condition that the person takes part in all three Pension Levels at the same time.

(See Figure 1). Compensation in this case is the expected pension ratio against their salary.

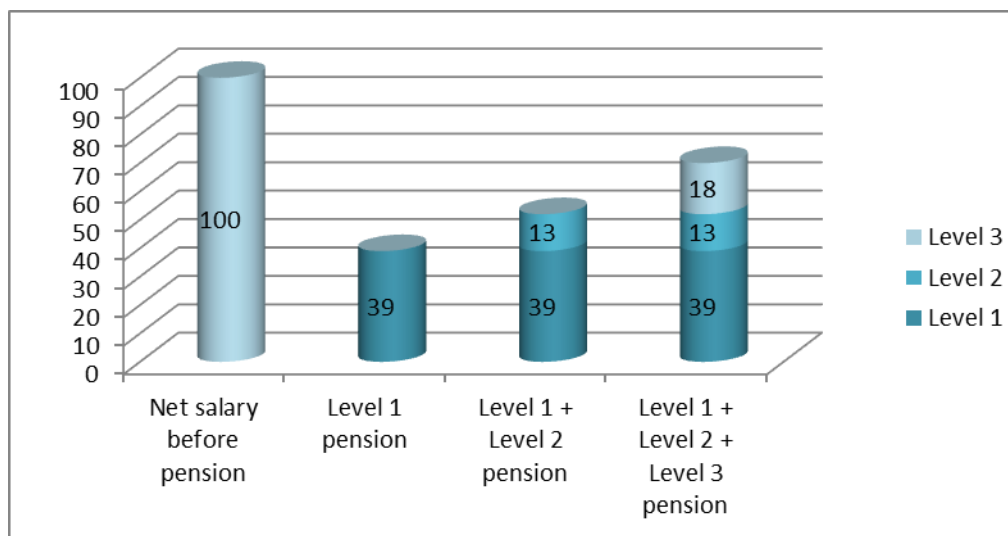


Figure 1. Compensation volume in case of participating in one of pension levels expressed in percentage.
Source: compiled by the authors

Figure 1 reflects compensation volume taking into account several conditions: if the person was born in 1976, in that case, the person since 1976 receives average salary that has been determined by the Central Statistical Bureau, private pension fund 10% contribution and the person will retire at the age of 65. In the case of being the participant of all three pension levels at the same time, he or she might receive salary compensation in the amount of 70% from his/her salary during the retirement period.

Additional **accruals** to their pensions are formed in Pension Level 2 from their personal savings registered in pension capital which in turn is being invested in stocks, bonds and other securities, as well as bank deposits. Investment is being carried out by an intermediary- licensed wealth manager. Thus, pension capital accrues much faster than inflation and the average salary in the country. 15% of state social insurance contributions were channelled to the 1 pension level in 2015. Due to this, solidarity principle has been secured where participants of the first pension level secure the pensions to the present pensioners.

Nowadays Pension Level 2 participants can choose their own wealth manager either state or private. Private wealth managers offer to invest pension capital into corporate bonds, stocks and foreign securities. The participants have full rights to change the manager once a year, but they are allowed to change investment plans twice a year. The work of private wealth management is supervised by Financial and Capital Market Commission. The work of State Treasury is being supervised by the Ministry of Finance.

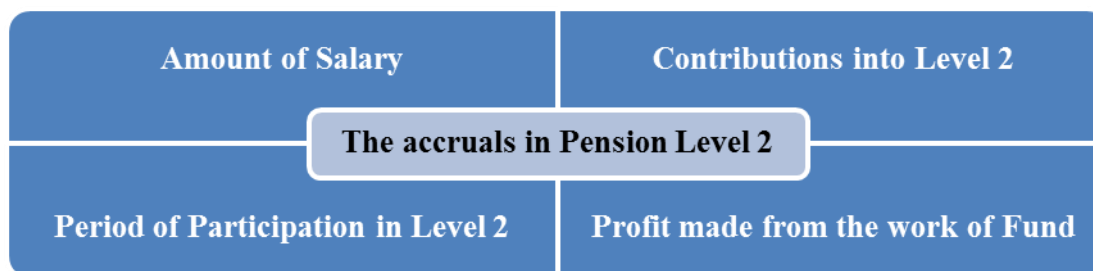


Figure 2. Factors affecting the accruals in Pension Level 2. **Source: Mavlutova & Titova, 2014**

There are 4 factors affecting the accruals in Pension level 2. The first factor “the amount of salary “affects total social **security** contributions. In relation to pensions, the sum equal to 20% of gross salary goes into Pension Level 1 and Pension Level 2. As a result, the amount of gross salary directly affects taxpayers’ amount of pension.

Second factor is “the amount of contributions made into Level 2” which depends on pension division ratio between Level 1 and Level 2. The participants of Level 2 do not have to make additional social **security** contributions. The increase of ratio from contributions made into Pension Level 2 is one of the methods how to decrease demographic risk.

Table 1. Total redistribution of pension capital contributions between pension system 1 and 2 in percentage.

Source: SSIA, 2015

Years	Level 1	Level 2
2001 - 2006	18%	2%
2007	16%	4%
2008	12%	8%
2009	18%	2%
2010	18%	2%
2011	18%	2%
2012	18%	2%
2013-2014	14%	6%
2015	15%	5%
2016	14%	6%

As can be seen from Table 1, the government of Latvia changes regularly the ratio between Pension Level 1 and Pension Level 2 contributions due to the economic situation of the country. As it was previously mentioned, the first level PAYG (pay –as- you- go) system is the system in which taxes **are paid by the** economically active population, the payments are being made to the current retirees. Pay –as- you-go System (PAYG) envisages that the current retirees are being paid from the contributions of today’s working population. It is believed that such a system reduces the savings amount, because the working population is not interested to make additional savings (Bode, 2003).

The major drawback of this system is its changeable ratio between the working population and the retirees. As the number of working people decreases and the number of retirees increases, the tax revenue might not be sufficient in order to pay pensions. According to the research data carried out by Deutsche Bank and AEGON Global pensions research, the envisaged reforms were meant to reduce this risk. Such reforms were carried out in the United States and Western Europe, further they were introduced in Central Europe, as well as in Eastern Europe (Life in European Union, 2012). The reforms are being introduced also in Asian countries.

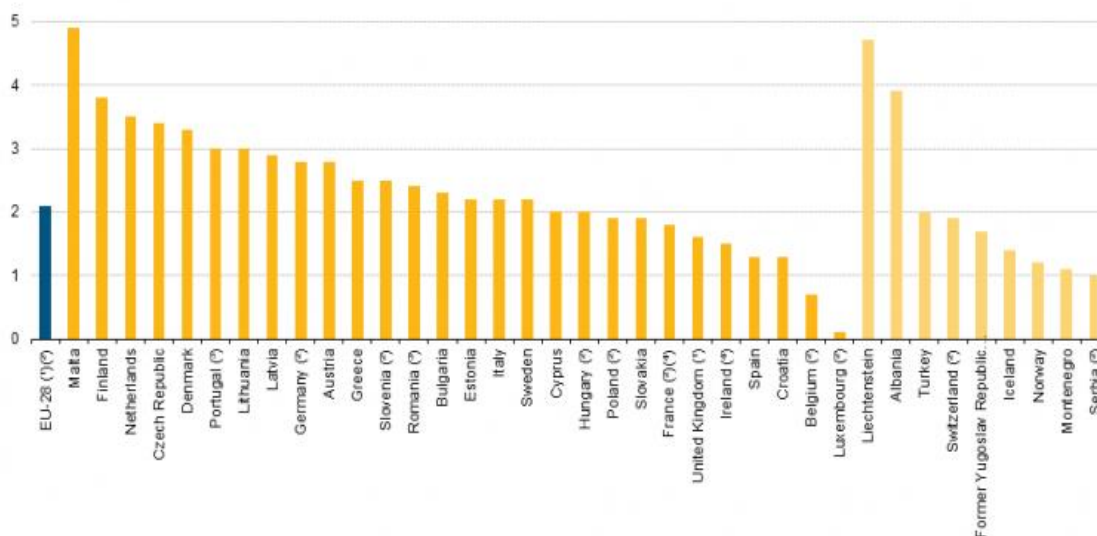
Pension reforms are needed in every country in order to reduce the risks, however, they are carried out taking into account different conditions and limitations which are affected by demographic situations. Germany and Southern Europe, namely Italy, Portugal and Spain are affected by the most severe demographic problems. As to the UK and France, this problem does not have such an impact on the population due to higher birth rate (Borsch-Supan et al, 2005). In case of Latvia, the demographic situation is extremely important. Not only the ratio between birth rate and death rate is negative, as it was mentioned above, but also the so called “envelope salaries”, unemployment and migration to other countries influence pension system as the revenue from taxes reduce, thus making less contributions to the pension fund. As a result, the state is forced to raise taxes, which slows down the economic development.

Since 2010 **the** employment rate has been dropping leading to the unemployment growth in the country. It was followed also by the decrease in salary, thus affecting the amount of tax **being paid into the** state budget. The Republic of Latvia acted appropriately by increasing contributions into Pension Level 2. The first solution was to increase **the** retirement age because life expectancy of the population also has grown, so it was necessary not to allow the fast growth of the number of retirees. Initially the aim of Pension Level 2 was not only to increase pension capital, ensuring full value pensions in future, but it was meant to facilitate the development of national economy.

3. Environment of Latvian Pension System.

The previous model of pension system was politically damaged. Additional allowances for pensions and allowances to parents were included into social security budget. In 2006 additional pension allowances were set up which were not envisaged for initial pension model. Thus, in 2008, the so called child benefits were transformed from state basic budget to social budget, it partly affected also sick leave payments which were covered by employers (State pension special budget, 2012). At present after enhancing economics, there is enough money in social budget for raising pensions, but, due to the worsening the relationships between the EU and Russia, the basic budget won't be fulfilled.

The number of population in accordance with Population census of 2011, in March 1, 2011 constituted 2 067887. Since the previous population census carried out in 2000, the number of population has decreased by 309 thousand or by 13%. The decrease of population has been due to natural population movement (the death rate increased the birth rate), as well as because of international migration.



(*) Provisional; estimate.

(*) Break in time series in various years between 2004 and 2014.

(*) Estimate.

(*) Provisional.

Source: Eurostat (online data code: demo_pjanind)

Figure 3. Increase in the share of the population aged 65 years or over between 2004 and 2014 (percentage points) Source: Eurostat, 2014

Economists claim that such a ratio, in which there are so few employees and so many dependants, especially pensioners, cannot sustain for a long term. According to the above described data we can

see that Latvia, like the whole EU (see Figure 3), undergoes significant demographic changes and this process influences structural changes in the number of the inhabitants. The negative changes of structure and number of the inhabitants are explained by the low birth rate and comparatively high death rate on 1000 inhabitants of Latvia. During the last seven years the situation has not improved and every year negative natural increase is created and that means that the death rate is higher than the birth rate.

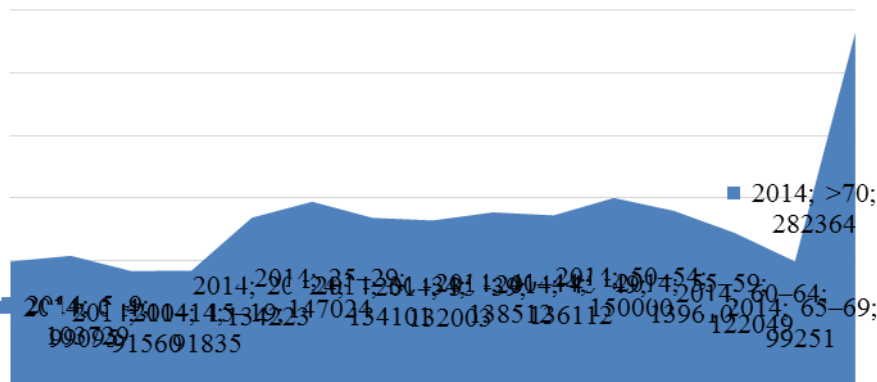


Figure 4. The age structure of the inhabitants in Latvia (2014) Source: CSB, 2015a

When studying the age structure of the inhabitants in Latvia in 2014 (see Figure 4), the authors have come to the conclusion that the number of children up to age 15 is considerably lower than the number of the people who have reached the employment age in Latvia. This means that the demographic situation in Latvia over the last years is worsening and thus, the demographic load is increasing.

The biggest worry is that the number of workers who can pay for the retirement benefits of an ever-growing number of retirees will not be able to do that. One retired person is supported by less than two workers in Latvia. There will be slower economic growth in Latvia as a result of internal and external factors (see Table 2).

Table 2. Economic development key indicators in Latvia, 2011- 2015 Source: Economic development of Latvia,

	2014				
	2011	2012	2013	2014	2015f
(Growth, in comparison with the previous year, %)					
Gross domestic product	5.0	4.8	4.2	2.3	2.0
Private consumption	2.9	3.0	6.2	2.6	2.4
Public consumption	3.1	0.4	2.8	3.1	1.8
Formation of total equity capital	24.2	14.5	-5.2	0.1	-3.0
Exports	12.0	9.8	1.5	1.7	0.7
Imports	22.0	5.4	0.3	0.3	-0.8
Consumer prices	4.4	2.3	0.0	0.6	0.5
(% of GDP, unless indicated otherwise)					
General government sector balance	-3.4	-0.8	-0.9	-1.4	-1.0
General government debt	42.7	40.9	38.2	40.0	35.0
Changes in the number of employed	1.3	1.6	2.1	-1.1	0.2
Unemployment rate	16.2	15.0	11.9	10.9	9.8

The quality of life for older people will decrease. That is why everybody needs to start thinking about his pension already now. Respectively, in order to improve the situation positively, the birth rate should increase twice **from what** it is today.

The average monthly old-age pension in Latvia was 259 EUR in 2013, which, in comparison to the average pension benefit in 2009 had been raised by 26,7 EUR (10%), and it constituted 278,65 EUR in 2014. The distribution of all pension benefit almost had not been changed for the period from 2009-2012 due to the fact that pensions have not been indexed. The inhabitants with the length of service less than 10 years, have been insured with the state social security allowance. The state social security allowance is guaranteed 64.03 EUR.

Now the government of Latvia is highlighting that everyone needs to start thinking about their pension themselves. It is done during disadvantaged time, because in a period of boom, when everyone had high incomes, no one spoke about that. Today when the situation with the government budget is negative, they start thinking about that. People do not understand and think that it is not fair to give a lot of their income to pensioners now and at the same time they need to save money for themselves.

By implementing Pension Level 3, Latvia started to go into the right direction, because people have the possibility to increase their pension and take care of it themselves. In Latvia there are now seven private pension funds which offer 27 different pension plans you can invest into, the biggest insurance companies also supply Pension Level 3. (Law On Private Pension Funds, 1998)

The investment has been done according two strategies:

- Active pension plans – the strategy of investing entities. Great part of assets is invested into shares and other securities and they are more subjected to price fluctuations within a short period of time, but in the long run could bring higher income.
- Integrated pension plans envisage to invest assets into secure state, local authority and commercial associations securities and term deposits of credit institutions, which ensure stability of income.

54.52% from the representatives of Public pension funds have chosen Active pension plan by 31.12.2014. Whereas, Integrated pension plan was chosen by 45.48% representatives of public pension funds. By the beginning of 2015 contributions of pension plan representatives reached 12.7 m EUR, which in its turn exceeded the total volume of contributions made at the beginning of 2014 by 72% or by 5.3 m EUR. Average private pension capital yield of one individual rose by 6% or by 67 EUR and it has reached 1262 EUR. The average age of the individuals has remained the same – 46 years – at the start of 2015 (The Association of Commercial Banks of Latvia, 2015)

Currently the money is invested in short term deposit savings where its profitability is much lower than inflation, so money loses its value. Bonds accumulate money for **the** state budget which goes to consumption but not into state investments in the long term. Part of the money is being invested into shares or other securities. Thus profitability of private pension plans is very attractive (see Table 3)

Table 3. Profitability of private pension plans (%). Source: The Association of Commercial Banks of Latvia, 2015

Plans	1 year	3 years	5 years	10years
Balanced pension plans	4.91%	5.32%	4.40%	4.19%
Active pension plans	6.62%	7.33%	4.97%	3.40%
All pension plans average profitability	5.33%	6.00%	4.83%	4.04%

The problems that Latvia is facing today and will face over the future ten or twenty years such as migration, low birth rate, aging of society and the changes in national economy and economy in general, as a result of the crisis, leads to the fact that the burden on the social security budget will keep growing.

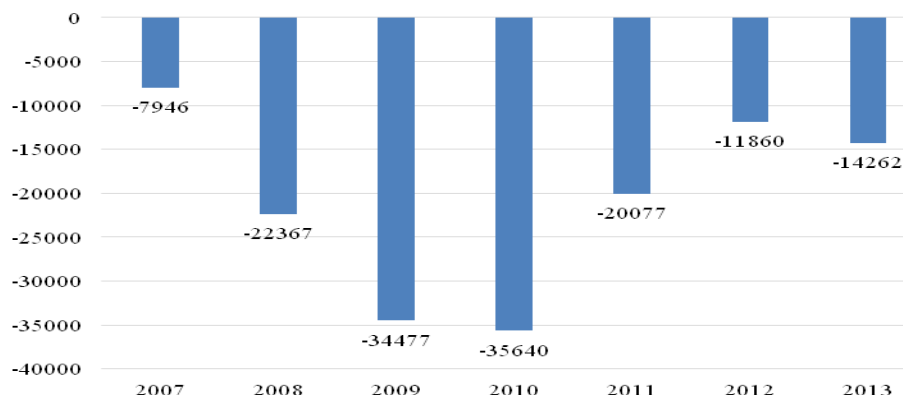


Figure 5. Immigration saldo of the inhabitants in Latvia (2007-2013). Source: CSB, 2014

The generation that in 5- 10 years could be economically active citizens and become tax payers is very small in number. Demographers of Latvia point out the unwillingness of the government or their inability to tackle the problem.

Latvia has a favourable geographical location, so it will not stay empty, that is why the flow of immigrants could be the only way out of the situation for the future pensioners. It is obvious that the government is not capable of solving this problem.

4. Interest Groups and Opinions

One of the international partners that takes part in reforms is the World Bank. The chief executive advisor is Inguna Dobraja who consulted the government of Latvia during the previous pension Reform in 1996, admits that the increase of the retirement age is obvious due to the fact that the life expectancy has increased and the society ages much faster. In her view, the pace of retirement age increase is quite moderate. As to special rules that allow several professions to apply for early retirement, in her opinion cannot be justified.

The existing generation solidarity pension system is not honest and will crash. The opinion was put forward by DNB bank economical expert Peteris Strautins on business portal "Nozare.lv" during the discussion related to social budget. He has pointed out that the current pension system is a good instrument in order to reduce the poverty in old age. However, at the same time it is a huge obstacle to economic incentives.

Economists P. Strazds considers that the population of Latvia thinks that children raised by others will earn pensions for them, thus reaching redistribution from people with several children towards those who do not have children. According to his views, the distortion created by the system cannot be removed completely, but it is possible to try to balance them, so that larger amounts are allocated to facilitate birth rate. If people were aware of the fiscal consequences in the long term for demographic trend and the impact on their own interests, they would be more interested in higher birth rate. It is one of the most stable ways how to secure old age.

Financial literacy and personal planning is the subject which has not gained large popularity in Latvia. It is also proved by the Financial and Capital Market Commission in 2015. Sociological research carried out by Financial and Capital Market Commission in cooperation with investigation centre SKDS on finance literacy of inhabitants in Latvia proved the participation level of the inhabitants in using financial services. According to FCMC chief Kristap Zakulis (2014), the knowledge and activities related to various financial questions also have been clarified.

Edmunds Rudzītis, an expert from SEB bank admits that the habit to save for future is more developed in Lithuania and Estonia. Lithuanian people traditionally are regarded as saving nation. 39% of the inhabitants make investments for their future. But Estonian people have greater possibility to save because the level of income is higher than in other Baltic countries. 27% of the respondents are saving for the old age, but in Latvia – only 18%. That means that the ostrich policy is used or people rely on different alternatives which might give additional income to their pensions – continuing work after reaching the retirement age or relying on children or other relatives’ support. But it cannot guarantee adequate income level in retirement.

The pensioners who retired during the last two years and who had received the so-called “envelope” salary confess that they have felt a significant decrease of their income. If we compare the pre-pension income to the pension volume, then, according to the director of SSE Riga business center Arnis Sauka, the average drop in income constitutes 52%. That means that these retired persons should live on small income, accordingly, every fifth inhabitant of Latvia supports financially elderly relatives by allocating 138 EUR monthly. If the illegal economy does not decrease, not forming long-term savings of a proper volume and the population still going older, then, in future, state budget might significantly experience certain pressure on it.

(Sauka & Putnins, 2015). This is obvious from Table 4.

Table 4. Average old-age pension and average salary in Latvia 2007-2014 (EUR) Source: CSB, 2015b

	Old-age pensions	Increase	Average salary	Increase
2007	158		566	
2008	200	27%	682	20%
2009	233	16%	655	-4%
2010	250	8%	633	-3%
2011	254	1%	660	4%
2012	257	1%	685	4%
2013	259	1%	716	5%
2014	266	3%	765	7%

In 2014 the average salary in Latvia was 2.8 times higher than the old-age pension. According to the collected information in the table, the average increase of old-age pension was within the limits of 1% - 3% in the time period 2011 -2014. But the average salary in the country diminished in 2009 and 2010 due to the experienced crisis in the country. Starting from 2011 a moderate increase in average salaries has been noticed in Latvia. If the number of the employed continues to diminish and the average salary does not grow, in the long-term the presently employed won't be able to support the retired people.

Across almost all European Union countries there is tendency that benefit ratio which shows the ratio between the average gross public pension benefit and the average gross salary will decrease. As it is clearly seen from Figure 6 it is especially important for Latvia, which has already the lowest benefit ratio from all the countries and is predicted to become even smaller. These ratio tendencies show that in future the supplementary pension, for example, private pension funds will become even more important in order to keep the high life quality.

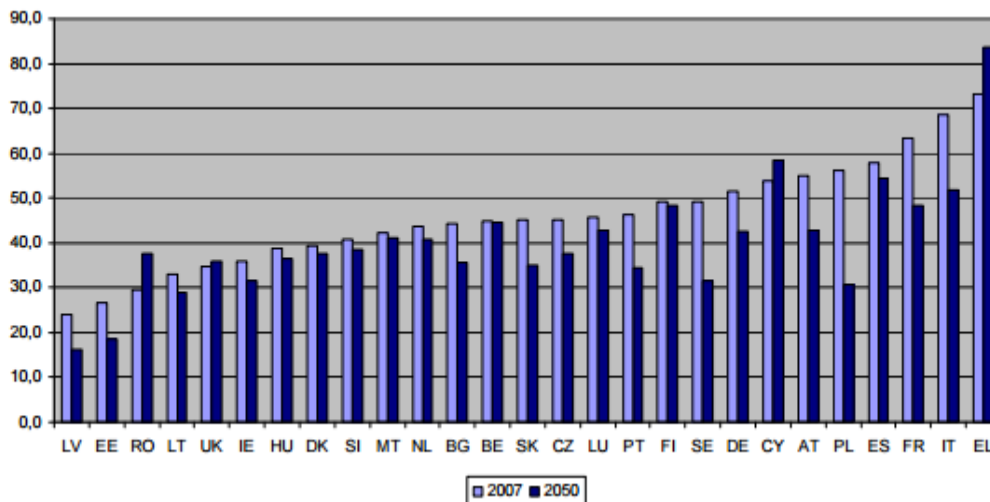


Figure 6. The benefit ratio (average gross public pension benefit divided by average gross wage) in 2007 and 2050. Source: Eichhorst et al., 2011

The growing importance of participation in 3rd level Pension schemes is the main reason why the authors chose to analyze the 3rd level pension funds in Latvia. The money that the individual regularly pays into the fund is being invested in various financial instruments depending on the chosen investment strategy. The aim of private funds is not only to save the money for the retirement but also to gain additional value. In order to encourage individuals to invest in third pillar pension funds, government grants possibility to obtain a refund for the overpaid income tax from the amount person has paid to Pension Level 3.

According to the current pension system and due to the demographic situation, the working people of today will receive lower pensions. The problem remains because the current demographic situation means that the number of retirees will grow, but the number of working people and taxpayers will continue to reduce. The pension system in Latvia has been formed in accordance with the principles of classical finance pyramid. It works well when new participants grow, that is, the number of tax payers increases and the country experiences a huge economic growth.

5. Proposals for decision making

5.1. Option 1

The problem is that due to the current demographic situation, the number of retirees will continue to grow, but the number of working people and taxpayers will continue to reduce. Major solutions for economical structure are also related to demography. It is necessary to facilitate birth rate and employment of young people.

5.2. Option 2

It is necessary to consider seriously migration issues (immigration and emigration) policy, so that it contributes to a qualified workforce and enhances economic growth. They help in covering state subsistence costs, but it is unlikely that they will be able to create added value to economy. High level of unemployment, the lack of job places for young people has led to the situation that the majority of jobless people are looking for jobs outside Latvia.

5.3. Option 4

To introduce relevant life-long learning system for elderly people in Latvia so that these people could be in the labour market and could secure adequate income level for themselves.

5.4. Option 5

As regards gradual growth of pension age, it is necessary to facilitate the system and availability of health care. It enables the pensioners to take care of their health and to be able to work effectively. It includes the necessity to have mandatory health checks every year.

5.5. Option 6

The government in collaboration with Financial and Capital Market Commission should provide information campaign about benefits, opportunities of investments and the 3rd Pension Level future role. The present situation shows that people don't trust the state and do not believe in sustainability of Latvian pension system.

5.6. Option 7

The social tax should be decreased gradually by motivating people to apply for the Pension Level 3. The accumulation system should be introduced when working people make contributions into private pension funds and receive pension later from these savings.

5.7. Option 8

For the persons close to the retirement age and who have made contributions in pension funds it is essential to lower the level of risk to lose a part from their savings due to short-term market fluctuations by introducing state guarantees like it is the field of insurance.

5.8. Option 9

It is possible to set up Pension Level 4, which is based on the solidarity principle in society within the family. Family traditions play an important role. For instance, during pre-war period families in Latvia had many children, parents did not make social contributions or they were very low. The earned money went to education of their children. In old age children took care of their parents.

5.9. Option 10

The mandatory participation in the third level pension schemes in Latvia should be introduced for employees with income starting from 1000 EUR and up.

5.10. Option 11

To open closed pension funds for employees of state structures and companies with a state capital in order to promote this activity. To offer fund management tools on closed funds establishment and operation based on practical experience of the biggest Latvian companies - VAS "Latvenergo" and "Lattelecom", that established the only existing closed pension fund - "Pirmais Slēgtais Pensiju Fonds" in Latvia.

6. Key Questions for problem solving

6.1. Value – based questions

- Is the current pension system able to survive, thus the retirement age increase will allow to solve the lack of financial means?
- What is the role of the case to improve macroeconomic indicators and to influence the factors of further development of national economy (GDP, workforce, employability, innovations, technological process, investments in economy)?
- How could migration policy help to solve the lack of pension funds? Should the government give benefits to young people to motivate them to stay in Latvia and start their own business or to offer them tax relief, as well as to set up the courses for young entrepreneurs free of charge.

6.2. Practical – led questions

- Are finance literacy questions fully integrated during different subjects taught at schools? Are they easily understood and related to real life situations? To introduce the finance literacy, the teachers should simply be creative and think how to link their subject to the questions from the field of finance. They should teach how to calculate the existing examples from the adequate information supplied by the banks. The teachers should work on methodological materials for acquiring the practical skills.
- The Latvian government has to indicate the specific future for the Pension Level 3 system in the country, so that people will start to believe in it? Currently, there are seven private funds in Latvia. The Pension level 3 also supplies insurance companies.
- Today people are not aware in which funds or projects or finance instruments their Pensions of Level 2 are invested. Is it possible to receive improvements in economic development and pension security, if Pension Level 2 savings were invested in more profitable finance instruments in Latvia?
- Taking into account high level of illegal economy in Latvia, how will the right instruments to struggle against illegal economy influence the effectiveness of the Pension System?

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