The Social and Economic Impact of the State Pension

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Abstract

When a person reaches retirement age he wants to have the same standard of living as before retirement.

The fundamental social function of the pension system is to ensure universal coverage, to provide decent pensions for retires, for those suffering from accidents at work or people who became ill and could no longer work.

Achieving these goals is difficult due to many factors that influence each person's living conditions differently and applying the same conditions to everyone is often unfair and wrong.

The main source of income that a person will have when he reaches the legal retirement age is the state pension. This will represent up to 50% of the income that the person had before retiring. There are countless factors that influence its level: gross income, contribution period, retirement conditions, economic situation, number of employees, number of retirees and legislation in the field.

This paper will present general questions relating to social security, social insurance type, authorized institutions, and their evolution over the last years.

Key words: pension system, social insurance, contributions,
J.E.L. classification: H55, G24, G51

1. Introduction

The Mercer & CFA Institute published in 2015 a study showing how important a diversified pension system is, so that any employee, during his active life, can choose between several possibilities. Each country can have its own pension system that takes into account the economic, legislative, political environment, the level of development and the social environment.

In Romania, the pension system is a complex one because it includes two categories. The first category refers to the state pension, and the second category refers to the privately administered pension.

The state pension, also called the first pillar of the pension, is collected by a person only if during the period in which he was employed with legal forms he paid the contribution to the social insurances. This contribution is mandatory and is deducted from the employee's gross salary income by the employer each time the salary is paid. The contribution to the social insurance fund is 25% of the gross income made monthly by an employee. The contributions of all existing employees in the economy constitute income to the social insurance budget and are immediately redistributed for the payment of pensions related to existing pensioners. These contributions go to a fund that ensures the payment of monthly pensions. If there is a large number of employees who pay their monthly contributions, the state will have sufficient resources to pay pensions.

2. Theoretical background

According to the American economist Peter Diamond, pensions depend primarily on the history of each individual rather than on the level of taxes collected, and age plays an important role in determining the level of each person.

The idea of dividing the burden of the financial future into pillars was suggested by the World Bank and adopted by several European countries. Some countries, such as the Czech Republic and Slovenia, introduced this measure late or substantially modified the mandatory private pillars. Hungary and Poland have implemented this measure but abandoned it when the pressure on public debt was too great. In Croatia, Bulgaria or Romania, the rule for each person to compose their pension from several sources, including a mandatory pillar, privately administered, is still in force.

The pension value depends primarily on the income obtained by each individual (for example salary income as the basis for calculating the contribution to the social insurance fund) and the the number of years of contribution to social insurances. Gross pension income will also be determined based on the calculation systems used at a given time.

In Romania, pension systems include three components. The first component is that of the public pension system, the second consists of universal privately administrated pension funds (still in the project stage) and the third component consists of facultative pension plans. These plans are mainly aimed at people with higher incomes and those who want higher pensions than those guaranteed by the first two mandatory systems. The purpose of these schemes is to allow their participants to have flexible savings plans that can be adjusted according to their preferences and needs. There are different types of schemes such as: individual pension plans and others alike.

There is a close interdependence between these three components of the new pension system. The first two are based on the collection and distribution of contributions collected by the National House of Public Pensions. The components based on capitalization and private administration (Pilar II and Pilar III) operates under the authority of the Supervisory Commission of Pension Companies.

3. Research methodology

The paper analyses a segment of the Romanian pension system based on the official results reported by National House of Public Pensions (CNPP), National Institute of Statistics (INS) and ASF (Financial Supervisory Authority). The data were analyzed and interpreted from an economic point of view, the values being expressed in euros.

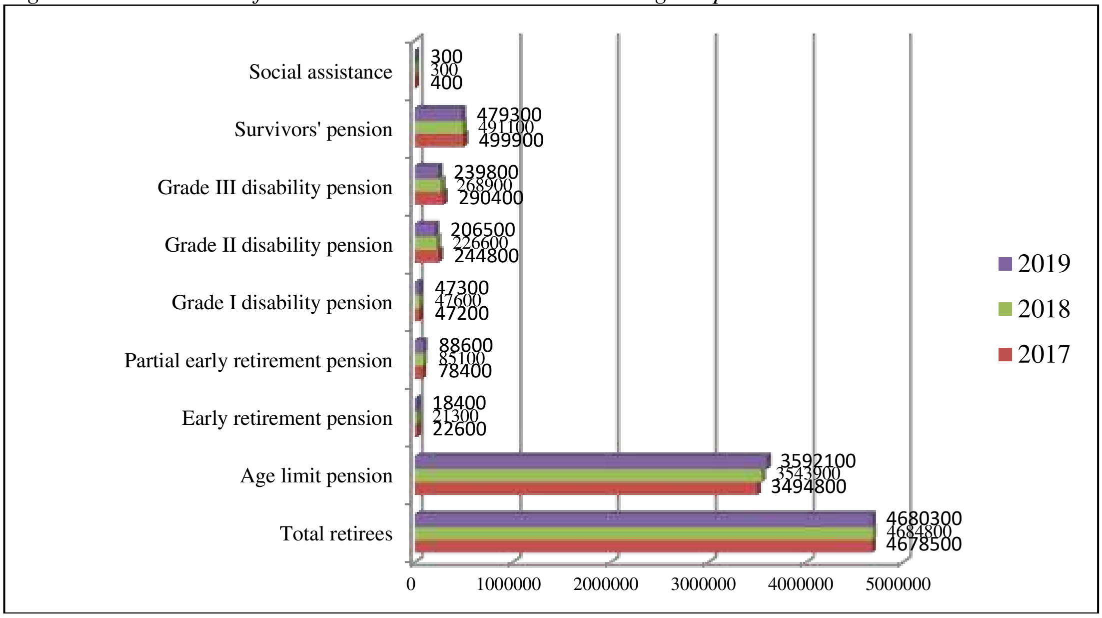
4. State pension system - Pillar I

From a demographic point of view, there is a decrease in the population due to the declining number of births and the increase in life expectancy of the population.

The pension system currently accounts for about 9% of P.I.B. and about 26% of our country's public expenses. Recent generations, born after 1989, will retire late to improve the aging trend of Romania's population.

According to the data published by the National House of Public Pensions, the number of retirees had the following evolution in the period 2017 - 2019. The statistics data included in the figures are related to December of each year.

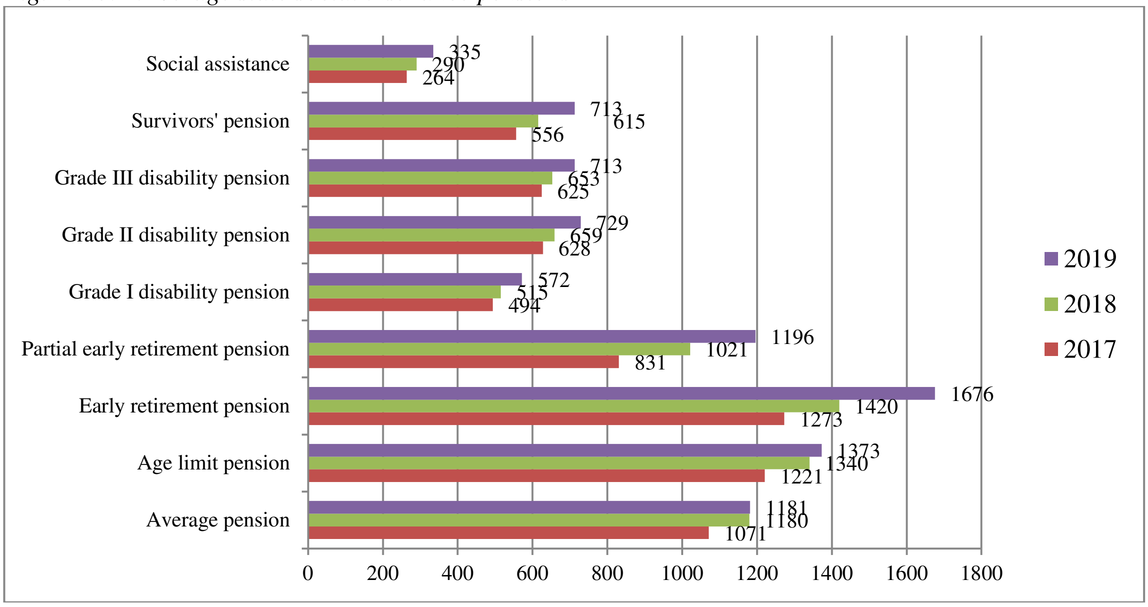
Figure no. 1. Number of state social insurance retirees during the period 2017-2019



Source: National House of Public Pensions, 2020

In figure 1 we can see that at the end of 2019, according to reports by the National House of Public Pensions, the total number of retirees increased to 4.684 million people, with 1,900 more retirees than in December 2017. It can be seen that the total number of retirees remained relatively constant throughout this period and that the largest number of retirees is those retired at the age limit (over 70%).

Figure no. 2.Average state social insurance pensions



Source: National House of Public Pensions, 2020

In figure 2 we can notice the increase of the average pension by types of pensions existing in the state system in the period 2017 - 2019 (lei), as a general average and as an average for each pension category.

It can be seen that the average pension reached 1,181 lei per month in February 2019. It can be seen that the average pension reached 1,181 lei per month in February 2019. In 2018, the highest increase was registered by the average old age pension, reaching 1340 lei. The average pension for all categories of pensions granted in 2019 reached 1181 lei, exceeding by 10 per cent the year 2017.

According to the Romanian legislative framework, the following **types of pensions** are granted:

- *The age limit pension.* This can only be achieved if women have reached the age of 63 and men have reached the age of 65. This is not a sufficient condition because a minimum contribution period is required, which is regardless of gender, of 15 years during the entire active period. If the person has contributed to the pension system for less than 15 years, he / she cannot retire.
- *The early retirement pension.* A person can retire with a maximum of 5 years before reaching the standard retirement age if he has contributed to the pension system for a minimum of 43 years. It is a great contributory period, but possible to achieve by people who started working very early. This pension can become an old-age pension on reaching the standard retirement age, and the pensioner's pension will be recalculated.
- *The partial early retirement pension.* For this type of pension, the contribution period is shorter, but penalties also apply. The person can retire up to 5 years before reaching the standard retirement age if he has contributed to the pension system between 35 and 43 years.
- *Survivor's pension*. If the deceased was retired or met the conditions for obtaining a pension, they are entitled to a survivor's pension: children and surviving wife/husband.
- *Invalidity pension.* All policyholders who have lost all or at least half of their working capacity as a result of accidents at work, occupational diseases, tuberculosis, common illnesses, and other accidents unrelated to work are entitled to an invalidity pension. Retirees with disabilities are subject to regular medical check-ups, at intervals of 6 to 12 months, until reaching the standard retirement ages. The pension is then being recalculated. If the retired does not show up, for reasons attributable to the retired, the medical examination the fact that the retired will cease to receive his pension starting with the month following the one in which the medical examination was provided or, as the case may be, the cessation of the pension payment.

5. Conclusions

If we analyze the existing pension system in Romania, we can observe that there is an aspect that can be improved. The government must set clear targets for the entire pension system. In order for the pension system to be more transparent, the method of calculating the pension should be able to be understood by each employee through the possibility of creating simulations through which to know the potential level of the pension he will receive. Fiscal facilities can also be offered to encourage the population to make savings.

The total administration and investment costs of each pension plan must be made public because clients can make comparisons between the administration funds.

A flexibility of the voluntary pension system is needed, as participants may be in different situations before reaching the legal retirement age.

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