THE OVERALL CHALLENGE FOR ALL GOVERNMENTS WILL BE TO MAKE A GENUINE EFFORT TO PROMOTE GREATER UNDERSTANDING OF RETIREMENT SECURITY ISSUES, OPEN A REAL DEBATE, ENGAGE THEIR CITIZENS IN FINDING AND AGREEING TO SOLUTIONS, AND TO CLOSE THE GAPS BETWEEN THE CURRENT SITUATION, THE FUTURE OUTLOOK, AND THE PREFERENCES AND EXPECTATIONS OF THEIR POPULATIONS.

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# Table of Contents

Introduction 1

Opening Remarks 7

Panel I
Public Pensions: A Comparative Look at Reform—Approach, Implementation, Impact 20

Panel II
Private Pensions: Risk, Uncertainty and How it Affects Individuals 30

Keynote Speeches 42

Panel III
Long-Term Care: Services and Support—What it Means for Retirement Security 56

Panel IV
Health Care: Financing and Its Impact on Government, Employers and Individuals 66

Closing Remarks 78
MODERATOR NORM ORNSTEIN, RESIDENT SCHOLAR, AMERICAN ENTERPRISE INSTITUTE PROVIDES REMARKS PRIOR TO THE FIRST PANEL SESSION.
INTRODUCTION

Many countries are re-evaluating their retirement income and social insurance systems to better deal with the consequences of population aging, low birth rates, and other demographic trends. The resulting system changes often alter the relative risk borne by workers, retirees, families, government, and employers.

This conference examined efforts by several developed countries to balance the risk in their retirement and social insurance systems. Four policy issues held center stage in the panel presentations and ensuing discussions:

- Reforming and stabilizing public pensions;
- Meeting the growing need for long-term care in aging populations;
- Strengthening occupational, or employer-sponsored, pensions; and
- Providing for adequate health care in the face of growing demand and increasing costs.
OPENING REMARKS
BILL NOVELLI, CHIEF EXECUTIVE OFFICER, AARP EXPLAINS THE FINDINGS OF THE AARP INTERNATIONAL RETIREMENT SECURITY SURVEY DURING HIS CONFERENCE OPENING REMARKS.
Good morning and welcome to our discussion of Reinventing Retirement: Balancing Risk. A question we’ve been asking ourselves at AARP for quite some time is “Can America Afford to Grow Old?” And, can we do so with intergenerational fairness—that is, without sticking our children and grandchildren with the bills? We see this as one of the most important issues of our time.

This is not a question just for us here in the US. It is a question for the world. In fact, it is perhaps an even more urgent question for Japan and many European countries than it is for us here in the US. They are older and aging faster.

As the largest nongovernmental organization in the US representing the needs and interests of persons age 50 and older—with nearly 36 million members—we are focusing considerable attention on reinventing retirement. Through our Global Aging Program, we have organized a series of events under the title of “Reinventing Retirement” which revolve around the issues of the changing nature of retirement and retirement security in developed countries.

We began this series last year in London with an international conference on Retirement Strategies for an Aging World. Today, our focus is on risk in retirement systems. We will look at the pillars of retirement security—public and private pensions which include savings, and health and long-term care insurance. We have a superb group of experts from the US, Europe, Canada, Japan and other developed nations who will address the relative risk borne by government, individuals and employers in their countries for the various pillars of retirement.

As we explore these issues, the first question we have to ask is, why has retirement security become such a critical issue internationally? I think we all know the answer. It’s the coming together of several factors all at the same time. The general population is aging and longevity is rising. The working age population is shrinking or slowly growing, and public pension systems are under stress. Likewise, economic forces such as rising health care costs also have an impact.

Increasing life expectancy and people exiting the labor force at relatively early ages are resulting in longer periods of time spent in retirement. For individuals, longer retirements mean stretching savings over more years. For society, they also mean that public pension and health benefits must also be paid for more years. This creates a significant international public policy challenge in ensuring that individuals have sufficient income security to live comfortably throughout their retirement years.

We wanted to improve our understanding of attitudes and behaviors surrounding personal and national retirement issues, and to assess the public’s confidence in having sufficient income to retire comfortably, attend to their health and long-term care needs, and live securely after leaving the workforce.

To explore these issues across various countries, we designed an International Retirement Security Survey. It examines key issues in retirement security across ten developed countries selected for their varying emphasis on the three potential sources of retirement income: public...
funding, designed to guarantee—through governmental transfers—a minimum income standard during retirement; employer-provided pensions and private savings.

These sources provide the income that, along with health-care benefits and long-term care, foster economic security in old age. With this survey, we examine opinions about retirement security in the United States, Canada, Australia, Japan, Germany, France, Italy, the United Kingdom, Sweden and the Netherlands. Slightly over 4,000 respondents were included in this telephone survey—approximately 400 in each country—which was administered for AARP by Harris Interactive, an international research organization with field offices in each country used in this study.

This morning, I would like to share the key results of that survey with you.

Key Results

Attitudes toward retirement among the majority of adults across all ten countries are characterized by five primary factors: Guarded optimism; limited thought given to retirement issues; a feeling of being less than fully informed about retirement; a lack of confidence in what government can provide in the future; and a belief in shared responsibility in providing for retirement.

Guarded Optimism About Retirement

When respondents were asked about their general optimism about retirement, in the aggregate we found guarded optimism to be the predominant outlook, with only 16% very optimistic, two out of five (41%) at least somewhat optimistic, and two in five (39%) somewhat or very pessimistic. The results, however, varied by the following demographic factors:

- Employment status: Those who are already retired express the most optimism (65% somewhat or very optimistic), followed by those who are employed (56%). Less than half of those who are not working express optimism toward their retirement (49%).
- Income: Respondents with higher incomes are, not surprisingly, more optimistic toward retirement than those with lower incomes (67% who earn $40,000 or more per year are optimistic, versus 55% who earn less than $40,000 being optimistic).
- Age: Respondents ages 45 to 65 are more optimistic than respondents ages 30 to 44 (59% versus 53%).
- Marital status: Those who are married show more optimism about their retirement than those who are not married (60% versus 50%).
- Education: Individuals who have obtained at least a college degree are somewhat more optimistic than those who do not have a college degree (61% versus 55%).
- Optimism toward retirement also varies quite substantially by country. With the exception of Japan, countries that are higher on the aging curve have lower optimism compared to those lower on the aging curve. In the United States, Canada, the United Kingdom, Australia and Japan, at least six in ten are optimistic about their retirement. Australians and Canadians are the most optimistic, with over three in four (77%) saying they are optimistic when they think about their retirement. By contrast, in Germany, France and Italy, only slightly over one-third say they are optimistic about retirement.
**Thinking About Retirement**

More than half of individuals across all countries (58%) have given retirement at least some thought, and one in four (25%) have given it a great deal of thought. However, nearly one in five (17%) have given no thought at all to retirement. Significant differences are also evident by employment status—only half of those who are currently not working have given retirement at least some thought.

How much someone has thought about retirement also varies dramatically by country. In the US and Germany, 44% have given retirement a lot of thought—and 73% have given retirement at least some thought in these two countries. But in Italy and Sweden only 12% of respondents have thought a lot about their retirement and less than half have given retirement at least some thought.

It’s important to understand that thinking about retirement does not necessarily correlate with expectations. Interestingly, Americans and Canadians have given their retirement more thought and are also relatively optimistic, whereas Germans have also thought about it a great deal yet report significantly lower levels of optimism about their retirement.

**Information About Retirement**

On the whole, respondents do not feel very well informed about the things they need for a happy and successful retirement. Only one in four (25%) rate their level of information at an “8” or more on a 10-point scale, where 10 represented “extremely well informed” and 0 “not at all informed.” The average rating for how informed people are about what they need for a happy retirement is a lukewarm 5.7 out of 10.

These results vary by employment status: current retirees more often say they feel informed (mean of 6.2) than do the employed (5.7). Those not working are even less likely to feel informed (5.0). Perceived information levels also vary by country. In the US, 40% rate their information level at an “8” or higher on a ten-point scale. Canadians feel nearly as well informed, with 37% rating their information level at an “8” or higher. Residents of Japan, Sweden, France, and Italy report being much less informed, with less than 20% of individuals in these countries providing ratings of “8” or higher. Notably, in Japan, only slightly more than one in ten respondents (11%) provided these high ratings when asked how informed they are about retirement issues.

**Expected Sources of Income in Retirement**

Despite the current and anticipated financial and demographic pressures on public pension systems in many developed countries—and the prospect that these systems in their current forms may not be financially sustainable—residents of these countries have high expectations regarding the public pensions.
The public pension systems are seen as a critical retirement income source, with 42% of the respondents expecting them to be a major source of their retirement income and another 39% expecting them to be a minor source of income. In sum, over four in five individuals (81%) are counting on a public pension as a source of income when they retire.

After public pensions, employer-provided/occupational pensions (28%), earnings from employment (26%), workplace retirement savings programs (26%) and other personal savings (25%) are most commonly expected to be major retirement income sources.

Notably, our results show that few believe inheritance (7%) and family support (4%) will be a major income source when they retire.

Some variations in income sources by country are also evident. In four countries—Germany, Italy, Netherlands and Sweden—public pensions are expected to be the primary retirement income source. In the US, UK and Australia, however, workplace retirement savings programs are seen as primary by more people. In no country do more than ten percent of the residents see family support as a major source of income, nor is inheritance expected to play a major role.

In response to a related question, which asked which source will provide the largest share of income in retirement, public pensions were again rated the highest, with 34 percent saying they would. No other option was selected by more than 14 percent of respondents.

Retirement Income Adequacy

People in the developed countries are living longer than ever before. For example, in the eight European and North American countries surveyed—France, Germany, Italy, Canada, The United States, The United Kingdom, Sweden and The Netherlands—the average life expectancy at 65 ranges from 18-21 years for women, and from 14-17 years for men. The fact that these are average life expectancies means that many persons will live well beyond. Moreover, advances in health care and living standards likely will continue to increase these life expectancies in the future.

This means that to assure adequate income for retirement—with many people retiring in their early 60s if not earlier—people should be planning for living 25 or more years after they retire. How confident are people that they can live comfortably for these years?

Our study shows that confidence in the adequacy of retirement income is very limited. More than two in five respondents (43%) are not confident that they will have enough money to live comfortably in retirement for at least 25 years. Conversely, a mere 15% report that they are very confident they will have enough money for a comfortable retirement. These figures match closely those dealing more generally with retirement optimism; as we noted earlier, only 16% report being very optimistic about their retirement.

Confidence about having enough money for retirement varies by country. In Canada, fully 71 percent are somewhat (46%) or very (25%) confident that they will have enough money to live for 25 or more years after retirement, followed by The Netherlands (70% somewhat or very confident), the US (at 68%), and Australia (at 64%). However, in half the countries surveyed—
Germany, France, Italy, Sweden and Japan—those who are confident are in the minority. Italians are the least confident, with only one in three stating that they will have enough money to retire comfortably for 25 years or more.

Interestingly, when we asked respondents if they were ahead of schedule or behind schedule in saving for retirement, 55% said they were either ahead or on track compared to 41% who reported being behind schedule. So why aren’t people saving? Those who feel they are behind schedule reported the top reason as being they just don’t have enough income to save. Surprisingly, educational expenses were the second reason even in countries where the cost of higher education is free or minimal.

**Current Health Status**

Now, let’s turn to health. One’s overall state of health and access to affordable, quality health care are also important factors contributing to confidence about retirement and quality of life in retirement.

Many respondents feel good about their health status, with 50% rating it either excellent or very good, and another 31% rating it good. As with the economic indicators, these percentages vary by employment status and by country.

Employed individuals show significantly higher self-reported ratings of their current health status than the retired and non-working, with nearly nine in ten (87%) rating their health at least “good”. At most, seven in ten of the retired and non-working say their current health status is at least “good”.

Age and income are also factors when it comes to self-reported health. One-quarter of the residents ages 45 to 65 in the 10 countries consider themselves to be in “fair” or “poor” health, compared to only 13% of the younger cohort. Additionally, those with higher income ($40,000 and over) report that they are in better health than those earning less than $40,000.

Comparisons across countries also show differences in self-reported health status. Australians provide the highest ratings (83% reported their health as being excellent/very good), followed by Canada (62%), the US (61%), and the UK (56%). The French (39%), Germans (38%), and the Japanese (38%) are significantly less positive about their health. And the Italians (17%) are the least positive.

**Health Care Concerns in Retirement: Paying for Long-Term Care**

All ten countries in our study have a national health-care insurance system for retirees. And, not surprisingly, all ten share similar concerns about rising health-care costs. This is especially noteworthy in the wake of changing demographics, where people are living longer and thus increasing the probability that they will require healthcare and long-term care in their retirement years.

In this study, respondents generally express some confidence in having access to quality health care in retirement (64%), being able to pay for medical expenses (70%), being able to pay for prescription drugs (71%), and expecting good health throughout their retirement (65%).
In comparison, fewer feel they will be able to pay for long-term care (55%) such as nursing home or home health care should they need it during their retirement.

The lack of confidence about having enough money for long-term care can be found across all of the countries surveyed. In three countries in particular—the UK, Germany and Italy—fewer than half of the respondents express this confidence. In fact, in all ten countries, the level of confidence expressed regarding ability to pay for long-term care is the lowest of the five health-related questions presented in this general category.

Sources of Health Care Financing

As was the case with retirement income, respondents believe that government-sponsored health-care programs will play the primary role in funding their health-care costs during retirement. Almost half of all respondents (47%) feel these programs will pay for all or most of their health care in retirement, with only 17% seeing no role for this funding source.

Nonetheless, about one in three respondents (35%) believe that most or all of their health-care costs during retirement will be paid from their own savings. In line with the previously reported low rating of family as a major income source in retirement, very few believe that their family or a caretaker would pay all (5%) or most (7%) of their health-care costs in retirement.

Again, this varies by country. Italians and Germans are most likely to see government sources paying some or all of their health-care costs during retirement (71% and 58%, respectively), whereas few Americans (29%) believe the government will pay most or all of these expenses.

Surprisingly, nearly one in three Americans (31%) say that government-sponsored health care will pay none of their health-care costs in retirement, despite the presence of Medicare and Medicaid and the role these programs play in covering current health-care costs of older persons in the US.

Confidence in Government

Despite the expectation of at least some government support for retirement income and health care, residents of all ten countries are consistent regarding their lack of confidence in the ability of their governments to provide these benefits in the future.

With regard to health care, there is low trust in the government’s current ability to provide even current retirees with health-care benefits. The overall rating of trust in the current system is at an average of 4.5 on a 10 point scale (with 10 representing “total trust” and 0 representing “absolutely no trust”). Trust is even lower when it comes to covering future retirees’ health care benefits. This received an average rating of only 3.8 on the 10 point scale, a drop of 1.2 points.
Trust in government’s current ability to pay the public pensions of current retirees is only slightly higher (an average rating of 5.0), but trust in its ability to pay public pensions in the future declines to an average of only 3.9 (a drop of 1.1 points).

While there are differences across countries, respondents in every country have less trust that their government will be able to pay retiree health benefits or public pension benefits to future retirees. The survey also suggests that people who reside in countries that have undergone substantial reforms may have less trust in their government’s ability to pay retiree benefits than people in countries that have not experienced such changes.

Moreover, public pensions are not regarded as providing a very adequate retirement income. This finding is consistent from a public policy perspective, given that in many instances public pensions are designed to serve as only one of the three major sources of retirement income and security.

Our study found that a large percentage of individuals (42%) expect public pensions to be a major source of their retirement income. Can retirees live comfortably on these pensions? The feeling is a resounding no—only 20% feel the public pensions in their countries enable people to live comfortably in retirement. In contrast, over three in four respondents (77%) say that retirees cannot live comfortably on public pensions. 90% of Japanese, 85% of Americans, 83% of Italians and 81% of those in the UK feel their public pension is not a sufficient source of income to live 25 years in retirement. These opinions are held regardless of income, age, marital status, or level of education.

**Work and Retirement**

So, how do people reconcile this? One way is to continue working. While retirement is typically viewed as a time to stop working completely, less than one out of three respondents (31%) across all countries in this study plan to do that. Italians (53%) are the most likely to say they expect to stop working; in fact, Italy is the only country in which a majority plan to stop work completely.

The US has the lowest percentage of individuals who plan to stop working completely when retired—only 14%. The most frequently mentioned retirement activity for US respondents is working part-time (34%). When looking across all countries, the majority view some amount of work as part of their so-called retirement. The more frequently mentioned options include working part time (19%), alternating between periods of work and leisure (16%), and volunteering (17%).

Why do people wish to continue to work after retirement? Interestingly, money is not the prime motivator, coming in third among four options presented—only four in ten (37%) rate “money” as being “very important” in their post-retirement employment plans.

The primary reasons people expect to work after retiring is that they want to stay involved and connected (45%) and they enjoy work (43%). These reasons for working after retirement are of
nearly equal value to employed individuals, those who are not currently working and current retirees.

**Policy Solutions to Retirement Challenges: An Emerging Consensus**

All of these findings point to a major international political challenge in determining how countries will adapt their current income security and health insurance systems to meet the needs of future retirees.

- Is saving for retirement an individual responsibility, or is there an essential role for employers and government?
- Who is responsible for supporting those who are retired?

When we asked about this, we found that an overwhelming percentage overall (94%) believe that government programs have at least some responsibility in supporting retirees: 43% contend government has the primary responsibility, and 51% say that it has some responsibility.

About one in three (34%) say that individuals themselves should bear the primary responsibility for supporting themselves when retired, followed by one in five (19%) who feel that employer-based programs should bear this responsibility. Interestingly, there is no difference in these opinions by retirement status—nearly identical percentages of the retired and employed believe that government programs should bear the primary responsibility for supporting retirees.

We also find consensus across all countries that government programs, employer-based programs and individuals have a shared responsibility—all should bear at least some responsibility for supporting the retired. In Italy, Sweden, Japan, France and Germany the prevailing opinion is that government should be primarily responsible. In the remaining countries, respondents are more likely to believe that government should bear some of the responsibility. Nonetheless, government programs still receive the highest ratings across all countries.

**Policy Solutions**

This really leads us to the question of balance and risk. Countries need to re-examine policy options and have a national discussion about what people want from their government and how much they are willing to pay.

In our survey, we wanted to examine public opinion about various options that would ease the stress on public pension systems. So, we presented a list of options and asked respondents to choose which ones they found acceptable, and to what degree they would be acceptable.

By a substantial margin, raising the taxes of higher paid workers is generally seen as the most acceptable choice for the government to make in order to maintain public pension funds—two out of three respondents (68%) rate this alternative at least “somewhat acceptable”. Perhaps not a surprise.

In the aggregate, increasing the size of the labor force by allowing more immigrants into the country to work (49%) and shifting to private savings accounts (49%) are also moderately
acceptable. The least acceptable choice is raising the retirement age required to qualify for public pensions. Only one in three (33%) said this alternative is at least somewhat acceptable.

These findings vary significantly by country:

- The United States and France are least open to increasing the size of the labor force through immigration—less than one-third in these countries find this option acceptable (32% in US and 30% in France). Conversely, more than four in five Swedish respondents (78%) say this option is acceptable.

- Increasing the retirement age required to qualify for public pensions is not acceptable to the majority of respondents in any of the countries surveyed, with fewer than half in any country reporting that this alternative is acceptable. Germans, however, find this to be a more acceptable option (48%) than residents of any other country.

- Italians and the Japanese are the least open to increasing future retirement benefits at a lower rate than currently provided for. Less than a third in each of these two countries find this option acceptable, compared to slightly over one half in the US (55%) and the Netherlands (52%).

- Shifting to private savings accounts was rated as at least somewhat acceptable most often by France (61%) and the US (56%), and least often by Australia (35%) and Italy (38%).

Education level is also a factor in explaining the acceptability of different policy options. Respondents who have college degrees are far more likely to accept allowing more immigrants into the country to work (62% of those without college degrees). And, they are also more likely to accept raising the retirement age required to receive benefits (40% versus 30%), shifting to private accounts (55% versus 47%), and raising taxes for everyone in the workforce (43% versus 35%).

**The Public Challenge to Policy Makers**

Our results show a disturbing lack of confidence across countries government’s ability to pay public pensions. While a large percentage of our respondents expect to rely on public pensions as a major source of income during their retirement, the overall level of trust that they have in their government’s ability to pay public pensions to current and future retirees is greatly lacking. Overall, only 17% of the total respondents rated their trust in the government’s ability to pay benefits to current retirees as an “8” or higher on a ten-point scale. Only seven percent of total respondents rated their trust in their government’s ability to pay future pensions as “8” or higher.

This lack of confidence has been found not only among the general public, but also among opinion leaders. A recent AARP study of opinion leaders in G7 countries found that over half (56%) of the leaders surveyed do not feel their nations’ public pensions/retirement benefits will enable the average retiree to live comfortably in retirement. Opinion leaders in Italy, Canada, and the UK were the least confident that retiree’s pension benefits would be sufficient for an older person to live comfortably.
In conclusion, global increases in longevity and rising health-care costs mean that government spending for retirement and health programs will put increasing pressure on government budgets. The findings of this survey show that people in ten developed countries view their retirement with guarded optimism. A surprising number, however, have given their retirement little or no thought, and a large proportion do not feel very well informed about the things they need for a happy and successful retirement.

Many persons polled in the study also expect that public pensions and health-care benefits will play a primary role for their retirement security. Yet, they lack confidence that their governments will be able to provide these benefits in the future. Therefore, many are not confident that they will have enough money to live comfortably through retirement.

While attitudes toward retirement differ considerably from country to country, there are some areas of consensus regarding the challenges, which are substantial. However, the findings also suggest potential remedies. Large percentages of adults in all countries expect some level of work to be a part of their retirement years, so increased opportunities for the employment of older persons could benefit both older persons and the economies in which they work.

Respondents also see more taxes from higher income persons to support public pension systems as an acceptable remedy to the fiscal strains these systems face. Of course this may not be an easy policy to implement. And finally, the lack of information noted by many respondents represents an opportunity for public education to help individuals better prepare for their retirement.

The overall challenge for all governments will be to make a genuine effort to promote greater understanding of retirement security issues, open a real debate, engage their citizens in finding and agreeing to solutions, and to close the gaps between the current situation, the future outlook, and the preferences and expectations of their populations.

While the citizens in these countries do not view government as the sole source of support for the elderly, they still expect government to be a significant source of support in their old age. Combining the views of the public found in this International Retirement Security Survey with those of Opinion leaders in the 2004 G7 survey, governments in developed countries need to take appropriate actions and build confidence that they will meet their future commitments by preparing now for their rapidly growing aging populations.
EDWARD TAMAGNO, JEAN-MARIE LE GUEN AND JUDITH FEDER DISCUSS STRATEGIES FOR PROVIDING ADEQUATE AND AFFORDABLE HEALTH CARE TO AGING POPULATIONS.
PANEL I

PUBLIC PENSIONS: A COMPARATIVE LOOK AT REFORM—APPROACH, IMPLEMENTATION, IMPACT
Germany, the United Kingdom, and the United States are three countries with similar problems, different approaches, and, possibly, different prognoses. Germany is the oldest of these countries, with nearly one in five people ages 65 and older. The US is the youngest, with just over one in eight in this age group. The UK holds the middle ground.

The effects of increasing longevity. Increased longevity, a tribute to medical advances and high living standards, is an important social achievement for developed societies. However, increased longevity creates retirement income policy challenges; a longer life must also be a financially sustainable life. Rising longevity increases a country’s dependency ratio, defined as those within a population under the age of 15 or over the age of 65, compared to those between 15 and 65 years of age. Rising dependency ratios have propelled Germany, the UK, and the US to rethink their pension programs.

Germany. In 2000, two workers supported each pensioner. By 2050, the ratio of pensioners to workers is projected to approach one-to-one, and, under pessimistic forecasts, could rise to as much as 1.25 to 1. In the latter case, every four workers could be supporting five pensioners. This demographic stress is much greater than that forecast for many other countries, particularly the US. One reason Germany’s dependency ratios are rising so quickly is that the country is experiencing the world’s fastest transition from a large baby-boom generation of workers to a small generation of their children. The latter generation is about half the size of its parents’ generation.

Another reason for fast-rising dependency ratios is greater longevity. When people live longer after they retire, the pressure on the smaller generation that must finance their benefits is increased. In 2000, a German’s remaining life expectancy at age 65 was three years longer than in 1970, and is projected to increase another 3 years by 2030. These increases will raise total spending on retirement benefits by 50 percent.

United Kingdom. Preparing for demographic changes in the UK has been hampered by the retirement income system’s complexity. With five components of the public system alone—and several private retirement income options as well—neither policy makers nor the public always understand how the components work together.
By the 1990s, it was clear that the number of UK public pension recipients would rise by 50 percent over the next 50 years. Yet there were no plans to increase spending on public pensions. Making things worse, contributions to occupational and personal (IRA-type) pensions have been level for a number of years. Thus, private pension benefits may not be able to make up for the declining value of government pensions and the increasing costs of longevity. “[This imbalance] was realized too late,” said Alison O’Connell, Director of the UK’s Pensions Policy Institute.

United States. The US also faces a demographic imbalance. Average life expectancy at age 65 increased by 4 years between 1940 and 2005. But between 2005 and 2080, it is projected to increase by 5 years, or 25 percent more than over the previous 65 years. “We just can’t stand still on that dimension,” warned Larry Thompson of the Urban Institute.

At the same time, however, the US faces less-immediate problems than many OECD countries. The US population is expected to age less rapidly than most OECD countries over the next fifty years and the labor participation rate among older workers is higher in the US than in many OECD countries. According to the OECD, in 2003 over three-quarters of Americans age 50-64 were employed, compared to about two-thirds of those in the same age cohort in the European Union.

When to retire. The retirement age is probably the easiest retirement income parameter for the average layperson to understand: the early retirement age is the soonest I can claim my benefits; the normal retirement age is the longest they can make me wait. Other than this understanding, however, nothing else about retirement ages in public pension programs is simple.

Germany. “[E]arly retirement is damn expensive,” argued Prof. Axel Boersch-Supan of the University of Mannheim. Early retirement can impose costs on both workers and retirees. Workers have to pay higher payroll taxes as more retire early, while retirees typically have to accept reduced benefits. A 1972 reform made the retirement age very flexible in Germany. As a result, the typical retirement age has dropped from 65 to 60. Early retirement adds to the pressure brought by demographic changes, all of which make the system unsustainable, he added.

However, discouraging early retirement requires more than publishing a new early or normal retirement age. “Retirement age in a country where you can retire earlier or later is essentially meaningless,” stated Boersch-Supan. Actuarial adjustments to benefits are the way to reduce the costs of early retirement and encourage workers to delay claiming benefits. If the normal, or full
benefit, retirement age moves to age 67 from age 65, for example, benefits payable at the early retirement age 62 will have to decline to reflect the fact that a person retiring at age 65 will now collect benefits for two additional years. The new retirement age is just the reference, or "pivotal," age against which their benefits will be calculated, according to Boersch-Supan.

**United States.** Raising retirement ages is also "...the only realistic way..." to deal with the US Social Security system's long-term demographic gaps, according to Thompson. If future benefits are projected as if the retirement age had been raised, however, Social Security's long-term replacement rates as a share of average earnings are projected to drop precipitously. Under such reductions, the retiree's lifetime benefit remains unchanged, but the annual or monthly benefit is reduced to reflect the longer period over which benefits are received.

**Retirement contributions and benefits.** Public pensions are generally intended to serve as only one of the three major sources of retirement income and security, with employer pensions and private savings making up the remainder.

**Germany.** Germany has been debating capping its high payroll tax contribution rates for retirement income and other transfer payments. As early retirees swell the beneficiary population, such a cap means cuts in future benefits. But benefit cuts must be rational and understandable, and must be politically feasible to command a Parliamentary majority, Boersch-Supan believes. To maintain retirees' living standards in the face of benefit cuts, public policy should also aim to offset these cuts with increased benefits from occupational pensions and private savings.

**United Kingdom.** In the UK, the value of public pensions is eroding due to indexing practices (see Indexing, on page 23). As in Germany, lower public pension benefits will have to be offset by higher private pension benefits to maintain the living standards of future retirees. In the UK as in Germany, however, making sure that this transition takes place will not be easy. "[W]e seem to have hit a glass ceiling in how much private pensions can deliver," stated O'Connell. But unless private pensions increase, future retirees face the risk of being caught with lower public pension benefits and nothing else to make the difference.

**United States.** Future US retirees face many of the same risks as do those in Germany and the UK. If future Social Security benefits decline, the bottom 60 percent of retirees risk having inadequate retirement income. The top 40 percent will generally have employer pensions, and the top 20 percent will have substantial asset income.

Since housing is most Americans’ single most valuable asset, many US workers believe that the value of their home will compensate for a lack of pension saving. But, Thompson pointed out, "...[I]t's people... who have a pension who also have a house. ... [P]roperty is [not] going to save a great number of people if they don't have a pension."
But Social Security benefits will constitute the principal source of retirement income for the bottom 60 percent—or more—of retirees. Optimistic expectations about the future role of private pensions in this group’s retirement income are not supported by long-term projections, Thompson believes. Cuts in Social Security benefits will hit this group hard, because Social Security is all they will have.

**Indexing.** Indexing increases public pension benefits over time to maintain their value to pensioners. Once benefit levels have been set, policymakers must solve the difficult problem of determining how to index them going forward.

**United States.** Initial US Social Security benefits, as well as those in many other countries, are indexed to average wage levels, while annual cost-of-living-adjustments (COLAs) are indexed to prices. Under wage indexing, retirees’ living standards improve at the same pace as those of the average worker. Price indexing, in contrast, allows retirees to maintain their own living standards, but does not permit them to share in the economic growth of the nation as a whole.

One indexing option the US has considered is price indexing of initial benefits on a progressive basis. Under this option, initial Social Security benefits would be indexed to prices for high-income earners, while low-income workers would continue to have their initial benefits indexed to wages. Middle-income earners would be subject to a mix of price and wage indexation. Higher earners—those earning 1.6 times the average wage—could lose 42 percent of their initial benefit. But this option could also mean a reduction in benefits for the average earner, whose benefit could decline to as little as 17.5 percent of the average wage after other projected reductions are considered and after deducting Medicare insurance premiums.

**United Kingdom.** In the UK, the indexing technique applied to the Basic State Pension—the foundation of the retirement income system, has changed over time as the structure of public pension benefits has changed. In 1980, the UK added the State Earnings Related Pension Scheme (SERPS) to its public pension system. SERPS was intended to be both an earnings-related supplement to the flat-rate Basic State Pension, and an alternative to occupational pension plans for the majority of private-sector employees who were not covered.

At the time SERPS was introduced, the Basic State Pension was indexed to the higher of changes in average wages or changes in prices. Once SERPS was introduced, however, indexing for the basic pension was changed to price indexing alone. This change in indexing was a “culprit for UK pension problems,” according to O’Connell, who believes the change in indexing was caused by the existence of SERPS.

In the U.K, as in most other developed countries (but not the US), the poverty level is defined in relation to average wages. Accordingly, the change to price indexing for the basic pension...
meant that it would fall steadily below the poverty level, which is typically defined as income that falls below 40 or 50 percent of average income. Before price indexation was adopted, the basic pension stood at one-quarter of national average earnings. After 25 years of price indexing, it has declined to less than one-fifth, and now stands at just over half the maximum means-tested benefit available to retirees. Half of all persons over the state pension age are now eligible for means-tested benefits, and this proportion is projected to rise to 70 percent over time.

The shift to price indexing has increased risk for many individuals who now must depend on means-tested benefits. The means-tested system is not as firmly set in legislation as the pension system; eligibility conditions and benefit levels can be changed at short notice. Moreover, “… put plainly, British people just don’t seem to like means-testing,” added O’Connell.

Germany. Boersch-Supan suggested that aging countries should index public pension benefits on the basis of demographic changes. The purpose of demographic indexing is to keep constant the burden of paying for pensions on active workers. Under demographic indexing, any increase in the ratio of pensioners to active workers would be subtracted from the cost-of-living index otherwise payable to pensioners.

For example, suppose that average wages rise by 1.5 percent in a given year. If pension benefits were indexed to wages, benefits would also rise by this amount. But under demographic indexing, the change in the ratio of pensioners to workers would have to be subtracted from this increase. Suppose this ratio increased by 0.3 percent in the same year. The cost-of-living increase payable to pensioners in that year would be the difference in these two values, or 1.5 percent – 0.3 percent = 1.2 percent. Pensioners would lose 1/5 of the increase based on wage indexing, or 0.3 percent/1.5 percent.

Selling reform to the public. Reforming public pension programs requires far-reaching, long-term changes that have to be stable even after a change in government. Stability makes long-term planning easier, and reduces risk for workers, retirees, employers, and the government. For pension reform to work, therefore, it is necessary to have a “grand coalition” across political parties, as well as between employees and employers. Germany, the UK, and the US each face different challenges in making the case for reform.

Germany. Raising the retirement age is important to public pension reform in most countries, but Germany faces special barriers in accomplishing this task. The country has a high unemployment rate. Many Germans believe that raising the retirement age would raise unemployment further as older workers began to compete for jobs with younger workers.

“That argument is wrong,” said Boersch-Supan. The process works exactly the other way around; countries where workers retire early have high unemployment rates, while those with
later retirement have lower unemployment rates. Early retirement increases unemployment rates because it has to be paid for by payroll taxes levied on workers. Higher payroll taxes increase the cost of labor. High labor costs, in turn, reduce employment.

Public pension reform is thus also a matter of economic growth. This is particularly true for the demographically older countries—Japan, Italy, and Germany—but more broadly for many European countries as well. The German public seems to understand that high taxes reduce prosperity. As result, the country may be more ready for true reform than appearances suggest.

**United Kingdom.** One problem in selling reform to the British public has been the multitude of legislative changes governing the public pension system over the last 30 years. “Government works best when it can offer a simple, reliable, and honest message on the future retirement income an individual can expect from the state,” said O’Connell. If the public has confidence in the foundations of the system, it will be prepared to build on those foundations.

**United States.** “The US has witnessed one of the most nonproductive debates [over Social Security reform] imaginable,” said Thompson. Social Security reform needs consensus to move forward, but the recent debate has been based on partisan politics, on both sides. There is a dilemma in carving private accounts out of the system, but most people don’t understand it, he believes. Philosophical assertions have dominated a good deal of public understanding on this issue, setting the Social Security reform debate back “a decade or two.”

**Policy Options Going Forward.** Caps on payroll tax contributions for public pensions loom large in policy discussions in these three countries.

**Germany.** Germany’s new pension reform caps payroll tax contribution rates for retirement income and other transfer payments (see Retirement contributions and benefits, on page 22). But these caps may not be sufficient to solve Germany’s long-term pension problem. Three additional options include making the cost of early retirement clear through appropriate actuarial adjustments; understanding that increasing the retirement age does not increase unemployment; and adopting demographic indexing of pension benefits. Increased coverage under private pensions will also take pressure off the public pension system.

**United States.** Unlike Germany, the US is discussing raising the cap on earned income subject to the payroll tax as one way to shore up the Social Security system’s finances. In 1937, over 90 percent of all labor earnings were subject to the Social Security payroll tax. This share is currently at about 85 percent. Many proposals would raise the tax base to about 90 percent of earnings, or from a maximum of about $90,000 to about $140,000. Such a change could increase payroll tax payments by $5,000 or more per year for both the employee and the employer. Higher-income workers, in short, would face a substantial tax increase. Progressive indexing (see Indexing, on page 23) has also attracted some support.

According to Larry Thompson, other possible policy options include raising payroll tax contribution rates and raising retirement ages. These ideas, however, “…currently lack measurable support,” Thompson noted. President Bush has rejected the idea of a tax rate increase, though he has left open the option of raising the cap on earnings subject to the payroll tax. Germany
and the UK have enacted requirements that all employers offer at least a 401(k)-type of pension plan. These requirements are relatively new—both were enacted in 2001—but some encouraging increases in coverage are emerging.

**United Kingdom.** The UK faces a different set of policy problems and hence, different policy options. Concerns about the declining real value of the basic pension and the resulting increase in elderly poverty are widely shared. Consequently, a consensus is building that coverage, benefits, and indexation of the basic pension need to be improved. The pension should also be simple. In the UK, over 100 parameters determine an individual’s government pension benefits. Complexity makes it difficult for workers to predict their future benefits and make decisions about work, saving, and retirement based on such predictions.

As in Germany and the US, UK policymakers would like to increase the role of private pensions in retirement income provision. In the UK, 88 percent of public sector workers contribute to a non-state pension, while only 44 percent of those in the private sector contribute to a non-state pension. There is some concern that private pension coverage is suffering from over-regulation, and that greater simplicity would help in the private sector as well. “Government should... create an efficient environment in which individuals and employers can develop their own future [pension] provision in the way they choose,” stated O’Connell.

Fairness is another issue in UK pension reform debates. In addition to the differences in occupational coverage between government and private-sector employees, gender equality has also become an issue. Sharp differences in pension outcomes between men and women have emerged. These differences have made equality of pension rights a central point in the pension debate for the first time in the 60-year history of the pension system.

Finally, inadequate savings or public or private pensions—as well as the desires of many older workers—may bring the issue of continued work to the foreground. The AARP International Retirement Security Survey found that only 14 percent of Americans expect not to work after reaching retirement age. More Americans expect to work than in the other nine countries surveyed, but a majority in all countries viewed some amount of work as part of their retirement. Respondents want to work to stay active and involved—and many will need the money.

Many would like to phase out of their current job gradually, work part-time at a new job, or alternate periods of work and leisure. Phased retirement can be an option for some workers, who could gradually reduce their hours in their “career” job. However, the workplace culture may have to change for retirees to be able to merge retirement and work in the way they want without becoming second-class workers to their employers and their colleagues.
LARRY THOMPSON, ALISON O’CONNELL AND AXEL BORSCH-SUPAN DISCUSS PUBLIC PENSIONS DURING THE FIRST PANEL SESSION.
PANEL II
PRIVATE PENSIONS:
RISK, UNCERTAINTY
AND HOW IT AFFECTS
INDIVIDUALS
Workers face several risks in private pensions. One is the risk of having no private pension. Another risk is that if the worker has a private pension, it may not work very well. And even a good pension can be lost if the plan fails. The UK, Ireland, and the Netherlands face a varied set of issues related to individual risk in private pensions.

**Coverage.** The three countries differ in private pension coverage and trends.

*United Kingdom.* The UK has experienced a long-term decline in employer pension provision. “It’s continuing rather oddly at a time when government, up until recently, placed a lot of focus of their pension policy on developing private provision,” according to Bryn Davies of Union Pension Services, in the UK. (For background on the public-sector components of the UK retirement income system, see “Public Pensions: A Comparative Look at Reform,” on page 20.)

*Ireland.* Ireland had no agreed-upon national pension policy until the late 1990s. Ireland is a young country—ten years younger than the next nearest European country. “Being young meant Ireland had time to plan,” said Anne Maher, Chief Executive of the Irish Pensions Board.

Pension policy, as well as policy on all matters related to pay and employment, is made by a social partnership group that meets every three years. This group is composed of government representatives, employers, and trade unions, as well as the pension industry. The partnership operates by consensus, so all parties agree to the risk inherent in policy decisions. Accordingly, pensions are not a political or partisan issue. “And I hope that it is going to remain a nonpartisan issue,” said Maher.

The Irish retirement income system has two pillars: the state universal basic pension and private voluntary supplemental pension coverage. The first pillar is a flat benefit, currently 32 percent of average industrial earnings, and projected to rise to 34 percent. It is an anti-poverty benefit and intended for the lower 30 percent of the workforce by pay level. This benefit is funded on a pay-as-you go basis and is generally sustainable over the long term.

The National Pensions Reserve Fund supports the first pillar. This fund is in some ways analogous to the US Social Security trust funds (see further discussion in *Pension risks and investment standards*, on page 35). The Irish government has a statutory commitment to support the first pillar pension by paying 1 percent of GDP into the National Pensions Reserve Fund each year.
The second pillar includes occupational schemes, personal plans, and Personal Retirement Savings Accounts (PRSAs). PRSAs are a new product, available to almost all adults, that function much like an individual retirement savings account.

There was an extensive debate in the late 1990s concerning whether the second pillar should be made mandatory. A voluntary system was judged to provide better benefits if coverage could be raised to adequate levels. The private system currently covers 52.4 percent of the workforce and 59 percent of those over age 30. The aim of pension policy is to raise this share to 70 percent. The remaining 30 percent of the workforce would be served by the social welfare system, including a noncontributory pension for those not qualifying for the basic state pension on a contributory basis.

Pensions in the public service (civil service) sector function as a measure of the success of government policies toward private pensions. As in many countries, Irish public servants have extremely generous benefits, and almost universal coverage, noted Maher. These pensions are funded on a pay-as-you go basis, supported by some funding from the National Pensions Reserve Fund, which also supports the state basic pension.

Public-sector pensions are becoming a social issue in Ireland because there is no pension risk for public servants—all risk is borne by taxpayers. At the same time, private-sector employees see themselves as paying steadily more for pensions that are getting worse.

The Netherlands. The first pillar of the Dutch retirement income system was implemented in 1957. It is flat-rate pension with a universal entitlement, and is intended to provide a minimum standard of living. All participants begin to receive benefits at age 65.

The roots of the second pillar, or the employer pension system, go back further to the period immediately after World War II. As in the UK and Ireland, private employers in the Netherlands provide occupational pensions on a voluntary basis, though once the employer offers a plan, the employee is required to participate. Unlike the case in the UK and Ireland, however, some 95 percent of all workers are covered under employer plans. The third pillar consists of voluntary individual savings that, like contributions to occupational pensions, benefit from tax incentives.

Plan types. All three countries are seeing some movement away from the primacy of the traditional defined benefit retirement plan and towards both defined contribution and hybrid plans, plans that combine elements of both defined contribution and defined benefit. This movement seems to be most pronounced in Ireland and the UK, but is also observable in the Netherlands.

The shift from defined benefit to defined contribution plans shifts investment risk in private pensions from the employer to the employee. The defined contribution plan participant also
bears longevity risk, default risk of insurance companies or other providers, political risk that the pension system might be changed, and earnings risk, according to Maher.

**Ireland.** In Ireland, there are two defined benefit plan participants for every defined contribution plan participant. However, if participants in civil service plans are excluded, the ratio drops to 1:1. “There’s a big shift from defined benefit to defined contribution plans,” said Maher, “[though] our defined benefit schemes have survived considerably better than in the UK.”

Employers in Ireland would like to shift more of the risks inherent in pension plans to employees. However, because the Irish workforce is more unionized than in the UK, this shift has been less pronounced in Ireland.

**United Kingdom.** Over the last 10 years, the UK has seen a significant change from defined benefit to defined contribution plans. Prior to that time, most employees who had a pension were covered by a defined benefit plan. More recently, however, many defined benefit plans have been closing to new entrants, and some even to future accruals. “There are even some who argue that defined benefit schemes are in terminal decline,” notes Davies.

**The Netherlands.** “Netherlands is still a defined benefits country,” said Nijssen. Occupational plans are experiencing changes, however. There is a “careful shift” toward defined contribution plans. There is also a search for alternatives. One alternative or hybrid could be a combination plan that provides a defined benefit to a basic level and a defined contribution benefit above that level.

**Benefit levels.** Many of the changes in pension plans can reduce the benefits some workers can expect in retirement.

**Ireland.** As the shift to defined contribution plans continues, employers may cut their plan contributions, leaving workers responsible for providing a larger share of their retirement income. Thus, the shift to defined contribution plans can result in inadequate contributions and benefits. In Ireland, the average contribution to a defined contribution plan is 5 percent of pay each for the employer and the employee. “That is simply not enough if it is not started in time,” said Maher.

**United Kingdom.** In the UK, many defined benefit plan formulas that based benefits on final pay are being replaced by formulas that base benefits on career average pay. To the extent that an employee’s earnings rise over the course of his or her career, a plan that bases benefits on career average pay can yield lower benefits than one based on final pay. Cash balance plans, a hybrid between defined benefit and defined contribution plans, are also emerging in the UK, but have not yet taken a substantial hold.
Similar concerns over benefit levels have emerged in the UK as in Ireland. Defined benefit plans are being replaced by defined contribution plans that are “almost invariably significantly worse”—in terms of expected benefits—than the plans they are replacing, argues Davies.

**The Netherlands.** Pensions in the Netherlands are calculated on a variety of bases. About two-thirds of private pensions base benefits on final pay; benefits in the remaining third are based on career average pay. The goal of most plans is that all participants should have a retirement income equal to 70 percent of final pay or career average pay, depending on the plan. This replacement rate would include first-pillar statutory old age pension benefits, and would be achieved after 35 to 40 years of contributions.

A public-private partnership is necessary for long-term sustainable pensions in the Netherlands, according to Jan Nijssen of the ING Group. “Occupational or employer-sponsored pensions are the backbone of pension systems,” he notes. He sees it as crucial that occupational pensions expand to provide one or two times the benefits available through the first retirement income pillar.

**Public-private mix.** Countries vary considerably in the degree to which they rely on public and private sources for retirement income, noted Nijssen. In the Dutch system, the first (public) retirement income pillar provides about 50 percent of retirement benefits; the second (occupational) pillar provides about 40 percent; and the third (private savings) pillar provides about 10 percent. Nijssen believes that these proportions constitute a balanced retirement income system.

The UK and Switzerland are examples of countries that have a similar balance among pillars. In contrast, larger countries such as Spain, Germany, France, and Italy depend more on the first, or public, pillar for retirement income, and are thus less balanced based on this approach.

**Benefit security.** The security of private pension benefits is an issue in all three countries, but it has surfaced differently in each country.

**United Kingdom.** For much of the past 30 years, legislation in the UK has tended to shift pension risk away from the participant and toward the employer and the plan. With the decline in defined benefit plan coverage and the increase in defined contribution plans, this shift has tended to reverse. Despite the cumulative effect of 30 years of legislation, the last decade has seen a shift of risk from employers and plans, back again to workers. According to Davies, “…the whole point of a defined contribution scheme, apart from any reduction in the level of benefits, is to reduce the risk that is placed on the employer.”

In an effort to reduce the risks facing defined benefit plan participants, the UK has taken an important step to guarantee benefit security to participants in defined benefit plans that may be terminated. Beginning in 2005, British defined benefit plans are covered by the Pension Protection Fund (PPF), which functions much like the Pension Benefit Guaranty Corporation...
(PBGC) in the US. The fund covers defined benefit plan terminations when the plan is under-funded and the employer is insolvent. The fund will provide 100 percent of prospective benefits for pensioners and 90 percent of prospective benefits for members not yet at retirement age.

The PPF is only in its beginning stages, so its long-term prospects are not yet clear; however, Davies stated, “I think the theory is that we’ve learned from [US] mistakes and will rise above them.” In particular, he hopes that risk-based levies on pension plans will provide positive feedback to plans that could affect the PPF’s stability.

The PPF is supported by compulsory payments levied on defined benefit plans. These payments are currently based on plan membership, but will change to a risk basis in 2006. The legislation establishing the fund has also tried to address the issue of moral hazard. The new regulatory authority is charged with ensuring that funds are sufficiently well funded to minimize calls on the fund. In particular, the fund has broad powers to compel payment by employers who may have terminated an insolvent plan if the fund’s board decides that the employer manipulated the plan’s finances to avoid liability under the plan.

The PPF could face problems in ensuring pension fund stability, however. Beginning in September, 2005, European pension plans gained the ability to register across borders when the European Union directive on pensions comes into force. “There are suggestions that some of the UK plans will register in Ireland in order to avoid the Pension Protection Fund,” noted Maher. This is not something Ireland would welcome, she stated, but it could happen.

In addition to implementing the PPF, the UK relies on accounting standards to ensure benefit security. Accounting standards are intended to ensure that investors and company managers are aware of the level of potential liability on the company that sponsors a defined benefit plan. Such standards can ensure that the plan’s status is correctly represented on the company’s financial reports. Finally, actuaries are becoming more cautious in terms of the assumptions they are willing to make with respect to funding and plan liabilities.

The Netherlands. Views on the current state of benefit security in the Netherlands are mixed. Foreign observers have a good deal of admiration for the Dutch pension system. “They think it’s solid,” observed Nijssen. He believes the international perspective is valid, because the Netherlands has the highest amount of pension assets per capita. Pension participants must receive their benefits in annuity form at retirement and may not withdraw lump sums.

On the other hand, confidence among the Dutch themselves is not quite as high. “There’s a lot of internal criticism and distrust in the system,” said Nijssen. Participants see benefits declining as contributions increase. People also see an increase in the retirement age as a benefit reduction.

Ireland. Benefit security is also an issue in Ireland. The Pensions Board supervises private pensions and advises the government on pension policy. Ireland has a very stringent pension funding standard. Under this “wind up” standard, pension plans must have enough assets to meet their liabilities if they were to wind up, or terminate, tomorrow. “[O]ver 40 percent of defined benefit schemes, which we supervise, have deficiencies in meeting our funding standard,” stated Maher.
The public supports the funding standard, but the standard causes concern among employers. To meet the standard, many employers have had to pay out large sums of money to make up for the investment losses that occurred in the early 1990s. “Ireland is a small open economy,” noted Maher, “so employer competitiveness is important to us.”

As in the UK, accounting standards are also intended to promote benefit security in Ireland. The accounting standards in Ireland require disclosure in the company’s accounts of the assets and liabilities of the pension funds, with the assets measured at current market value. This requirement is affecting the equity values of the companies themselves. Employers are also concerned about the level of pension costs and the volatility of these costs.

**Pension risks and investment standards.** Both defined contribution plans and defined benefit plans are exposed to financial market fluctuations. The UK and Ireland are framing different policy responses to such fluctuations.

**United Kingdom.** Financial market fluctuations increase the risk and cost to employers of providing defined benefit pension plans. As real investment returns decline, the employer’s own back-up liability for promised benefits increases. And with fewer new, younger employees entering the defined benefit system, the UK private pension system is maturing. Consequently, a larger share of pension assets is considered to be dedicated to projecting the interests of pension beneficiaries.

In the face of these developments, the UK is seeing a debate over how pension fund assets should be invested. Some observers argue that, because of their long-term nature, pension funds should only invest in bonds and should not hold equities at all. The contention is that liabilities for pensions in payment are best matched by investments in bonds.

This view does, indeed, appear to influence pension plan investment decisions. Between 1996 and 2003, the share of pension assets invested in bonds increased fairly consistently, rising from about 18 percent in 1996 to about 27 percent in 2003. The share invested in index-linked bonds has also been increasing. “One of the problems in the UK is a lack of updated statistics,” Davies said, “but it is clear that the trend [toward fixed-income investments] is well-set and probably has accelerated in the last two years [from 2003 to 2005].”

**Ireland.** Ireland is taking a different tack in its management of the National Pensions Reserve Fund, which provides funding for the first-pillar pensions. While the US Social Security trust funds hold only special-issue federal government securities, the National Pensions Reserve Fund is operated in much the same way as private pension plans. The fund is managed independently—managers even include foreign experts. The fund holds 80 percent equities (40 percent in Europe and 40 percent outside of Europe) and 20 percent bonds and is invested almost entirely...
PANEL II

in overseas assets. Because this fund is the “ultimate long-term fund,” it cannot be touched until 2025, when the demographics start to change, Maher pointed out.

The World Bank has been watching this fund with interest, because not many such funds have a track record yet. The Norwegian fund, which is funded with oil revenues, has been successful. Ireland has been looking at the Canada Pension Plan with interest. New Zealand and France have also set up similar funds, but those funds are more recent. At the present time, the National Pensions Reserve Fund amounts to 10 percent of GDP. By the time it is intended to be used, however, it will total about 40 to 50 percent of GDP. “At that stage, it will be a dangerously large sum of money if we have any other [economic] problems,” Maher said.

Pension education. Pension education can be an important tool for expanding private pension participation as well as individual savings.

United Kingdom. The UK government is committed to engaging the public in a debate over the evolution of pension policy. Most of the public debate over pensions concerns second-tier, or private pensions (see Policy options going forward, below).

The UK is also seeing a need to educate the population on how the changes to pension policy specifically affect their own work and retirement decisions. “People in my country have been hammered over the head for 30 years [about retiring] as early as possible because that’s good for the younger generation,” said Davies. Now that pension policy has reversed course toward encouraging longer work careers, there is a need for public awareness of how the system is changing, and what steps individuals can take to shore up their retirement security.

The Netherlands. In the Netherlands, as in the US, most people do not understand how much they will need for retirement, or the financial risks they face in retirement, according to Nijssen. These risks include investment risks, inflation, and longevity, all of which contribute to the risk of outliving their retirement assets. Individuals need to be properly advised about such matters as the need to save, asset mix, life cycle funds, and the effect of inflation on purchasing power. More awareness and communication about retirement risks is needed, he concluded.

Ireland. The Irish private pension system is supported by a national pension awareness campaign run by the Pensions Board. The campaign is aggressively run in an effort to attract public attention to and raise pension awareness for pension and savings issues in the country. “The government very much accepts… a responsibility for pensions,” said Maher. The government is not trying to shift responsibility for the system to employers or individuals.

Maher believes that public messages about pensions and savings have to be kept simple. She cited a recent savings incentive as an example. To encourage private saving, the government instituted a plan that said for every 4 euros an individual saved, the government would add one more in five years. “Everybody could understand that,” she said. As a result, 1.2 million persons out of Ireland’s population of 4 million invested in the program.

Policy options going forward. Policy makers in all three countries are considering revisions to their systems to contain costs and ensure adequate retirement income for aging populations.
United Kingdom. The UK is in the process of developing reform proposals for the second tier, or occupational pensions. “With basic pensions, everyone but the government is clear about what needs to be done,” said Davies. However, with respect to employer-sponsored pensions, there is only a consensus that reform is needed; there is no consensus about how that reform should look.

A three-person Pensions Commission representing the stakeholders in the pension system is reviewing the issues and developing policy recommendations. The government has no legal obligation to respond to this report, but has committed itself to do so. As the debate continues, there will presumably be legislation that could come into effect as early as 2008. “[T]hese are exciting times for pensions in the U.K,” concludes Davies, “but what’s not clear is where this is going.”

Ireland. Ireland is considering a number of reform models: enhancing the current voluntary private pension system; mandating supplementary private pensions; mandating a supplementary state defined contribution plan; mandating a state supplementary earnings-related plan; and enhancing the first pillar pension with continued voluntary provision of private supplementary plans. Not all these options may have equal chances of implementation, however. The voluntary supplementary system is “fairly enshrined” in Ireland. Enhancing the first pillar pension, in turn, would assign substantial added fiscal responsibility to the state at a time when other countries are attempting to reduce this responsibility, notes Maher.

Ireland is also examining a number of related issues. One issue is the amount of risk participants should be free to bear with respect to their own retirement income. Should they be allowed to take benefits in lump sum at retirement and possibly spend these benefits on non-retirement purposes, or should they be required to purchase annuities to ensure a lifetime stream of income?

The Irish government could also become involved in private pension provision by sponsoring an annuity fund, stated Maher. The state might be able to provide annuities more cheaply than private providers because, unlike private providers, it would not be subject to solvency requirements, nor would it have to make a profit.

The current level of state support for pension-related tax incentives is another issue facing Ireland. Are these incentives adequate, should they be reduced or increased, and are they spread fairly? Like the UK, Ireland is also facing issues concerning adequate retirement outcomes for women. Finally, governance issues are important to the extent that they affect pension coverage and benefit adequacy.

Ireland expects to face all these concerns with an agreed pensions strategy supported by the government, employers, unions, and the pensions industry. Pensions are not an issue of party poli-
Netherlands. “Winds of change blow in the Netherlands,” stated Nijssen. A new type of third-pillar account, called the lifetime savings account is to become effective in January 2006. It is intended to be a flexible savings instrument to supplement, but not replace, employer-sponsored or individual pensions. Funds are to be withdrawn only for specific purposes: early retirement, sabbatical leave, extended maternity leave, or study time. The expectation is that people age 50 and older will use it for early retirement, as that has been abolished. But “… for people under 30, the question is, are they going to use it at all?” according to Nijssen. And for people between 30 and 50, the question is whether they will use the account as a flexible instrument.

Disability benefits. Public retirement systems may include benefits for disabled persons. The UK, Ireland, and the Netherlands face different policy environments with respect to this issue. In Ireland, disability and retirement benefits are provided through separate programs. “[A] strong disability lobby … is doing quite well in getting fair benefits,” stated Maher. Retirement and disability benefits are also provided separately in the UK. The disability benefit is “a very hot topic at the moment,” according to Davies. The government is in the process of developing policy proposals for changes in this benefit, she added.

Nijssen noted that the Netherlands is starting to perceive a number of social benefits—including those for disabled persons—as “a little bit too generous against the context of an aging population.” He believes that a solution to this problem can lie in an expanded partnership among the three pillars of retirement income security.

Issues related to the European Union. Members of the European Union (EU) will face particular pension policy challenges. As economic integration among the European Union members proceeds, coverage issues among member countries will become more complex. European Union Directives promote harmonization of pension laws across member countries. “The big companies … are looking to provide benefits to their employees on a cross-border basis,” he noted, “but that’s still very difficult in Europe.”

The United States leading the way? As developed countries reform their private and public pension systems, Nijssen believes “…it is very much up to the United States to show that it can be the role model … in … voluntary second pillar systems, [since] there are not that many in the world.” First, the US must maintain a sustainable first pillar, he believes. Then, it is necessary for the US to stimulate voluntary savings in the second and third pillars as strongly as possible. To this end, the US should promote annuities and hybrid defined benefit/defined contribution plans. Perhaps even multi-employer defined contribution plans for some groups should be considered. “In the great tradition of America,” these problems and issues can probably be resolved by product innovation, particularly in the insurance arena.

Nijssen believes the US should also consider new work and retirement patterns in response to social trends. “It’s no longer 100 percent work, 100 percent retire,” he stated. Increases in longevity should be split between work and retirement, not added to retirement.
JAN NIJSSEN, BYRNE DAVIES AND ANNE MAHER DISCUSS PRIVATE PENSION ISSUES DURING THE SECOND PANEL DISCUSSION.
KEYNOTE SPEECHES
I’m grateful to have been invited by AARP to speak today at this conference and I am delighted to be here.

I took up my current job following the UK General Election in May, but I have been Pensions Minister before. That was in 1999. It is interesting returning to these issues six years on. It was before the dot com crash and the fall in world stock markets—and before we had fully grasped the scale of increasing longevity. Pensions then was a much quieter topic, but today pensions reform has become one of the biggest challenges we face. Setting the right balance in sharing risk—between individuals, employers and government—is one of the key judgments we have to make.

Employers have been switching from defined benefit to defined contribution schemes. And many point to the balance sheet risk from defined benefit schemes as the decisive consideration. Optimizing the allocation of risk is key to continuing the provision of long-run, sustainable pensions.

But the answer is not easy. If a large employer feels unable to bear the risk through the vehicle of a defined benefit scheme, surely an individual is even worse placed to bear that risk? Should individuals bear it to allow essential flexibility when fundamental parameters such as life expectancy change? Perhaps there could be a role for the government in managing risk—maybe through the provision of longevity bonds? Employers, individuals and government—all are in the frame.

As the Pilgrim Fathers knew well, where there is risk, there is also opportunity. And I want to focus today on the opportunities of an aging society.

The life expectancy of a man aged 65 in the UK has risen by three months every year for the past twenty years. For women, the increase has been three months every two years. These are wonderful developments, transforming all our prospects, and there is no sign of the trend slowing down. We need to plan, in order to make the most of them.

The perspectives of the next generation of retired people will have been shaped by very different experiences to those which have shaped today’s generation. They will be more numerous and likely to live longer. They will have lived through technological revolutions rather than World Wars. They will have had to cope with the smart card rather than the ration book. They’ll work for longer, be more independent, enjoy better health and be making very different demands of their politicians.
The challenges of an aging population include how to organize savings to provide adequate incomes in retirement. But they go much wider. They include employment, healthcare, discrimination and access to public services. Governments will have to think much more carefully and broadly about how to meet the needs of older people: from sports centers to care homes; from transport to the workplace.

We need to change fundamentally the way we think about aging. It’s increasingly about activity rather than dependency. More often today, older people give support to others, as carers and grandparents, rather than being dependent on care themselves. They need to be enabled to exercise choice. We need to encourage and support them in playing an ever greater and more active role in our society. “Reinventing Retirement” is about how our whole society is changing, and whether we can make aging an opportunity for all of us, rather than a threat. We have to plan now for an aging population. Muddling through will not be enough for success.

There’s no single magic solution. Each country has to find the right mix of policies. But we can explore options together, learn from each other’s experience and expertise—as we are doing at this conference—and help each other to plan actively for an aging community.

In the UK, an important part of our reforms, helping ensure sustainability of state pension provision, has been to target new resources at the least well off pensioners, as those who need help the most. Pension Credit, introduced two years ago, offers a guarantee that every pensioner will be able to obtain a minimum level of income to avoid poverty, and above that, up to an income threshold, it rewards pensioners for having built up modest savings.

In combination with measures such as Winter Fuel Payments, and increases in the Basic State Pension, the new arrangements mean that the least well-off third of pensioners are some £2,000 a year—$3,400—better off than would have been the case if the 1997 system had been retained. The proportion of pensioners whose income after housing costs is less than 60% of the median for the population as a whole has fallen from 27% in 1997 to 20% today—and that at a time when median earnings have grown sharply through Britain’s recent economic success. Periods like the one we have enjoyed of economic success have tended in the past to be marked by a decline in the relative position of retired people, but we have been able instead to improve their relative position.

It led the Institute for Fiscal Studies in London to declare recently that, for the first time, people in retirement in the UK are now no more likely than anybody else to be poor.

But maintaining that desirable position will not be easy. The challenge of rising lifespans poses more fundamental challenges still. Our Pensions Commission, chaired by Adair Turner, will produce its final report in November, and the Government will need to respond with proposals for long term reform.

“Governments will have to think much more carefully and broadly about how to meet the needs of older people.”
Some have suggested that we should raise the State Pension Age at which it is possible to draw a state pension on the basis of past national insurance contributions. At present the age is 65 for men in the UK and 60 for women, but the age for women will be raised step by step from 2010 until it is also 65, as for men, in 2020. We may have to consider increasing it further, although it will be hard for some, but part of the challenge that we face in the UK at the moment is to help people to work up to the current State Pension Age, let alone setting a higher one. Over a third of men in the UK are outside the labour market by the age of 60; and over half before the state pension age of 65.

Our State Pension Deferral policy increases the rewards for choosing to work for longer—introducing an enhanced state pension or a lump sum of £20,000 to £30,000 for typical individuals who decide to take their State Pension at 70 rather than 65.

And our tax simplification measures taking effect next year also mean that, for the first time, it’s possible to carry on working for the same employer whilst drawing an occupational pension.

Last November, we passed a Pensions Act that is a landmark in securing and strengthening private pension provision. The Act created the new Pension Protection Fund whose remit is comparable to the Pension Benefit Guarantee Corporation, and which is greatly strengthening protection for members of defined benefit pension schemes.

The Act will also help employers to provide pensions in the first place. It strips away layers of regulation that have built up over the years, and it complements the radical tax simplification taking effect next year which replaces today’s eight separate tax regimes with one single regime.

Another key dimension is giving individuals the information they need to make good decisions about saving for their retirement. We need to encourage workers to take advantage of employer supported pension provision that is already available—too many, who could, are not doing so at the moment. Some 4.5 million people have access to company pension schemes in the UK but have not joined them. Where an employer makes a contribution to the scheme, these individuals are missing out on a significant employee benefit.

If we could put that right, we would go a long way towards addressing the current problem of under-saving for retirement. So we have been examining options such as auto-enrolment—where employees are included unless they opt out, rather than being excluded unless they opt in. I know this has been very successful in the US—with evidence suggesting that it can double participation rates—and I’m very keen to explore this further in the UK. We published guidance last week to encourage employers to practice auto-enrolment and to address the anxieties they have about it.

A key element of the response to longer lives must be making it easier for people to choose to work longer. Older people are a valuable part of the labor force, and yet many retire early.
because they are compelled to stop work rather than because they want to. Avoiding the cliff edge between work and retirement must be a government priority, together with breaking down the wasteful barriers—often self imposed—which prevent employers from accessing the skills and talents of older workers.

One barrier that can stop older people working longer is discrimination on the grounds of age. We gave details last week of the legislation we propose to address age discrimination in employment from next year.

Can it be right that people can lose their jobs for being 65? It does not seem right. But mandatory retirement ages can be a management tool for companies—so we need to tread carefully in changing the rules. There were calls for us to abolish mandatory retirement ages altogether, but we have announced that, instead of that, from next year, mandatory retirement ages below age 65 will be unlawful unless, exceptionally, a lower age can be objectively justified. And employers will have to give consideration to requests from employees reaching retirement age to work on.

Age-related discrimination is not the only problem. Older women face serious problems with pensions and employment which add a gender dimension to the challenges. Our culture needs to change, to break down these barriers and enable individuals to realize their ambitions of entering and staying in work, and to give better opportunities to older workers.

We can’t afford to allow discrimination to deprive the economy of the skills of an entire cohort which could contribute to the pool of labor available to meet the growing challenges of an aging population.

But the challenge goes much further than simply achieving adequate incomes for retirement. We recently published *Opportunity Age*, our cross government strategy on aging, which highlights the importance of independence and dignity. It recognizes that the aging of our population demands new kinds of collaboration from agencies within government and across society as a whole. We need to work more effectively together.

The provision of care for those who need it is an important topic. In the past in the UK, there have been a variety of sources of help for people requiring help—financial help, and services provided through local authorities and others. We want to explore instead giving the person who needs the care the funding which is providing the care, and let them decide how to spend it to meet their needs best. We shall be piloting these individual budgets for care from later this year.

At the heart of our strategy is the conviction that the later decades of life should be as fulfilling as the earlier ones. That retirement should be invigorating and fulfilling rather than a period of decline and isolation. It means prolonging good health by keeping mentally and physically fit in retirement.

It’s about more than just health. We must think about meeting the growing demand of older people for leisure services and transport. And we need to tackle the fear of isolation by encouraging and supporting older people to contribute to the wider local community. Only a quarter of over-60s in the UK feel that they can influence local decisions.
The proportion of older people who live alone is likely to increase in the next 20 years. Tackling a sense of exclusion is crucial if we want to bring about real cultural and social change. We need to encourage and help older people to build networks of support and interest—for example, through social clubs and activities.

Delivering these changes means working in effective partnerships across different government departments, and outside government with the private sector and community organizations, and at local and community levels.

Our aim is that the engagement of older people will now be a key part of the system of Comprehensive Performance Assessment for local authorities that is operated by the Audit Commission. Nationally, Government departments must join up to deliver an ever greater collective package, closely examining, for example, how science and technology or sport and culture are meeting older people’s needs.

So we are confident that, by acting now, we can plan successfully to make the most of the opportunities of an aging population. Governments must show leadership, and have the courage to convey difficult messages, and to act to ensure that they shape the cultural and social changes which can allow our society to maximize the gains from what is unquestionably one of the greatest advances of our time—namely that we can all look forward to longer lives. Given the right planning, we can look forward also with confidence to aging actively. I hope we can work together to maximize the chances of our succeeding.

OLD-AGE SECURITY IN GERMANY—CHALLENGES, ANSWERS, IMPACTS

HEINRICH TIEMANN, STATE SECRETARY AT THE FEDERAL MINISTRY OF HEALTH AND SOCIAL SECURITY OF THE FEDERAL REPUBLIC OF GERMANY

Thank you very much for giving me this opportunity to tell an expert audience how Germany intends to meet the challenges of old-age security for its population.

First of all I would like to give you some basic data on old-age security in Germany. Then I will briefly outline the previous structure of the statutory pension insurance in Germany. Starting with the challenges that our old-age security systems have to cope with, I will then talk about possible reform alternatives — some of them were rejected, others are being implemented. For ‘dessert,’ I will present you first results of our reforms and all that remains to be done.
Facts on old-age security

Let us first talk about the facts. In Germany there are about 82 million citizens, of whom approximately 20 million are pensioners. At the same time another 51 million people are insured under the statutory pension insurance scheme, that means contributions are being paid for them at present or have been paid in the past, but they do not yet draw a pension today. Consequently, the statutory pension insurance scheme in Germany covers more than 80 percent of the German population. Such a large extent of insurance coverage has financial consequences. In 2004, the total expenditure of the statutory pension insurance was 235.5 billion Euro, that is more than 280 billion USD. To guarantee these payments in the long run is a Herculean task.

Basic structures of the statutory pension insurance

Now the interesting question is: What can our pensioners expect, how much is the amount of their pensions and who is going to pay for it all?

Well, the statutory pension insurance provides, above all, old-age pensions. But it also protects people against the consequences of reduced earning capacity and pays pensions to survivors. Last but not least it also offers rehabilitation. That means it ensures that the earning capacity of sick and disabled persons will be restored if possible. In my presentation, I am going to focus on old-age security.

Following a minimum period of coverage, an application for pension may be filed not before the age of 60 years. It is true that the standard retirement age is 65 years, but when further prerequisites are fulfilled and pension deductions are accepted, the pension may also be claimed before.

In Germany, a so-called standard pensioner—that is a fictitious person with an average income and 45 years of coverage—receives a pension of 1072 Euro per month (about $1280 USD). In reality these amounts are lower, because not everybody can accumulate 45 years of coverage. On an average, a man receives 987 Euro and a woman 482 Euro per month—converted to US dollars that is about $1180 and/or $575 USD. What is decisive for the pension level is the remuneration received during the entire period of insurance coverage. As a rule, the benefits granted under the statutory pension insurance in Germany depend on the amount of contributions paid.

Since January 1, 2003 the contribution rate has been 19.5 percent of the gross wages or salaries, but only up to the level of income that is liable to contributions, the so-called contribution assessment ceiling. Employers and employees both pay half of the contributions. This has been so since the introduction of the statutory pension insurance in 1889 under Bismarck. Since 1957 the pension system has been financed by the insured active persons in the so-called pay-as-you-go system. This is what we call the contract between the generations. It means that the currently paid pensions are financed by the incoming contribution revenue. The receipts from the contributors are used for paying the expenses for pensioners.

Challenges for old-age security in Germany

And now we already come to the two big challenges which the statutory old-age pension in Germany has to face. The first one—in the short term—is the dependence of contribution rates
on earned income and thus finally on the economic situation. The second one—in the long term—is the dependence on the ratio between the number of contributors and the number of pensioners. In the end, it is a question of demography.

As far as the economic situation is concerned, if a pension system is financed equally by employees and employers—as it is in our case—a high unemployment rate will destabilize the revenue basis and we cannot deny it. We are currently facing an unemployment problem in Germany. In May 2005, Germany counted 4.06 million unemployed persons, according to the standards of the International Labour Organization, which is an unemployment rate of 9.5 percent. Therefore it is necessary to create more jobs. For this purpose we need economic growth, and this depends on the labor costs of enterprises. And the contributions to the pension insurance are to be seen as non-wage labor costs that add to the burden. The essential goal of reform efforts in Germany is a limitation of non-wage labor costs.

And now a few remarks about demography: a pay-as-you-go pension scheme is based on the concept that the gainfully employed persons are paying the pensions of the current pensioners. Therefore, it is important to always have a sufficient number of young people for the labor market. When the pay-as-you-go system was introduced in 1957, the then Federal Chancellor Adenauer is alleged to have said: “Having children is what people will always do.” This was a classical misjudgment. Our problem is that the number of our children is continuously declining. That means in the foreseeable future, the number of persons in the labor market will decline as well. Nowadays a German family has 1.4 children on average, but 2.1 children would be necessary to reproduce the parents’ generation. Yet the increasing life expectancy has increased the pension term by 7 years during the past 40 years.

For the future, all this means that if currently only 23 percent, or almost one quarter of our population are 60 years or older, it will be more than one third already by 2050, that is 36 percent. The ratio between contributors and pension recipients is also becoming a financial problem for old-age security, just as in other industrialized countries. In addition to that, a disproportionate share of elderly people require care and also cause higher MT sickness-related expenditure. Consequently, the demographic development is a long-term challenge, not only for statutory pension insurance but also for health insurance and long-term care insurance alike.

Alternatives of reform

Weak economic growth, high unemployment, coping with the impacts of the German reunification and an unfavorable demographic trend required answers that guarantee old-age security in Germany in the long run.

What have been the alternatives that presented themselves to us? Which options did we choose, and why exactly these ones?

We did not opt to have the statutory pension insurance tax-financed. We think that in old-age security systems the contributions and benefits should be directly related to each other. Considerable tax revenue has already been poured into the general pension insurance scheme in the form of Federal subsidies, because on social grounds also benefits are granted which are not
based on contributions. These Federal subsidies amounted to 54 billion Euro in 2004, that is almost one quarter of the revenue. Any further increase in these subsidies would drive the Federal budget to its financial limits.

We did not follow the proposals to switch from the pay-as-you-go system to the fully-funded system in statutory pension insurance. This would have placed a double burden on today’s generation of contribution payers. On the one hand, they would have been obliged to continue paying contributions to finance the current generation of pensioners; but on the other hand, they would have been forced to build up a capital stock to provide for their own pensions. A complete change of system would be too expensive.

**The Federal Government’s pension reform**

Now I have outlined what pension reforms we did not implement. What have we done instead? It is a mix of several components, and the most important of them is the introduction of a so-called sustainability factor to the pension adjustment formula. Thus the ratio between pensioners and gainfully employed persons is taken into consideration. The result is that the aging of the population slows down the pension adjustment. Consequently, pensions will continue to increase and follow the development of wages; however, their rise will be lower than before.

What is important is to increase the effective retirement age. This particularly includes the consistent reduction of incentives for early retirement. For the age cohorts from 1946 onward, we are raising the age limit for the earliest possible retirement from 60 to 63 years. Moreover, with its labor market reforms within the scope of the “Agenda 2010” program, the Federal Government is also working towards an increase of employment opportunities for elderly persons. This policy bears fruit. Last year the employment rate of elderly employees rose to 41.2 percent, and at the same time the average pension age went up to 63.1 years, from just about 62 years in 1997.

And as the income situation of today’s generation of pensioners is comparatively positive on an average, we could ask them to shoulder more personal responsibility. Since 2004, the pensioners pay their contributions to the social long-term care insurance in full. Before, the statutory pension insurance had paid half of the contributions. This new regulation takes account of the fact that, during their working life, today’s pensioners did not, or only for a short period of time, pay contributions to finance the long-term care insurance. For this insurance was introduced only in 1995.

With these and a bunch of further measures the Federal Government has been able to stabilize the contribution rate for the statutory pension insurance at 19.5% of the gross wages. Also, in the long-term, the contribution rates will remain considerably lower than they would have been
without these reforms. They will not exceed 20% by 2020 and 22% by 2030. At the same time, the statutory pension will not fall below a certain level. The minimum replacement rate, that is the ratio between the standard pension and the average earnings, both before taxes, will be at least 46 percent by the year 2020. Our objective is to guarantee a higher re-placement rate than 43 percent also beyond 2020. What is more, the Federal Government made sure that the long-term trend of declining statutory pension levels may be compensated for by additional forms of old-age provision. This is one of the issues that is to be discussed at this congress, too: how much private pension savings will be expected of our citizens for their old-age security in the future?

Since 2001, Germany has been specifically supporting the establishment of supplementary—occupational and private—pension schemes in this area. In this way we have launched a paradigm change. It is true that the statutory pay-as-you-go pension insurance will remain the most important pillar of the old-age provision. But for the relief of this first pillar, the second and the third pillar—that is the private and the occupational pension schemes—will have to make a larger contribution. The future of old-age pensions is based on a reasonably balanced mix between an affordable statutory pension and a supplementary fully-funded occupational and private pension provision. This is the only way of guaranteeing a high level of benefits in old age.

Support of supplementary old-age provision

This is the reason why the German Federal Government launched the establishment of a voluntary fully-funded supplementary old-age pension scheme already in 2001 by providing state incentives in the form of massive financial support. Since that time, certified private pension products are substantially supported by highly attractive allowances and tax savings. In this way, persons with low incomes and families can also afford to build up a supplementary old-age provision. Moreover, the occupational pension schemes were backed up by an extensive catalogue of measures. In our opinion, the occupational pension schemes which are strongly influenced by the collective bargaining policy of trade unions and employers is a driving force for the continued expansion of supplementary old-age provision. At the final stage of reforms, as of 2008, 12.5 billion Euro will be made available every year for the support of supplementary old-age pension schemes.

All employees subject to social insurance (as well as civil servants) are entitled to support for private provision. At the final stage of the support, in 2008, 4 percent of the previous year’s income must be saved every year. The government contributes to these savings by granting an amount of 154 Euro for every adult and 185 Euro for every child. In addition, the amounts invested may also be declared as special expenses and deducted from one’s taxable income in 2008 up to an amount of 2,100 Euro. In the field of occupational pension schemes, every employee subject to compulsory statutory pension insurance can now request his or her employer to put parts of his or her future earnings in an occupational pension provision.

Together with further measures, this helped the occupational pension scheme to overcome the decades of stagnation and their partial decline. The percentage of employees in the private sector who are entitled to an occupational pension increased from 30% to 46%. This growth by 8 per-
percentage points took place in a period of only 30 months. This means that, about 15.7 million employees in Germany are entitled to an occupational pension. This corresponds to about 59 percent of all employees subject to social insurance coverage.

But also the private supplementary pension provision, the support of which is still in its initial stage, is showing a positive development. Up to the month of March 2005 4.3 million of the so-called “Riester Pension” contracts were concluded. We will continue supporting this trend in additional old-age pension provision. We want to do this by a continuous improvement of the framework conditions. We have, for instance, considerably extended the immunity from taxation and exemption from social contributions for that part of one’s remuneration which is invested in an occupational pension scheme. Since January 1, 2005, the conditions for private and occupational old-age provision were rendered much more attractive and citizen-oriented. In connection with the “Riester pension,” for example, a permanent application for state support was introduced so that in the future it will no longer be necessary to file an application every year. In occupational pension schemes, a new regulation was introduced, enabling employees to transfer their accrued occupational pension rights when they change their employer; thus, the needs of the mobile society and the changes in career patterns were taken into account. Since 2005, the employees may progressively deduct their contributions to the pension scheme from taxes. In this way they are given scope for supplementary pension provision.

Future need for action

Nevertheless, we still have a lot to do. It is currently being examined whether the statutory standard age limit of 65 years has to be raised after all. In 2008, the Federal Government will be obliged to report on whether today’s knowledge and assumptions concerning the future demographic trends and the development of the labor market are still valid. It will have to say whether it might be necessary—having due regard for the general economic climate—to introduce legislative measures for raising the retirement age. Moreover, in 2005, we will still have to examine whether the supplementary old-age provision is sufficiently widespread. We have to change attitudes—not only in the companies but also among employees—in order to win over wide sections of the population to supplementary pension provision.

Conclusions

With its pension reform measures, the German Federal Government has rendered the statutory pension sustainable and reliable. With the help of the supplementary private and occupational provision, the standard of living in old age can be maintained in the future. In this way, we have efficiently responded to the challenges of an aging society. Our measures ensure a well-balanced distribution of the demographic burden between contributors and pensioners. This is—and I think you will agree to that—the decisive criterion when answering the question: “How do we manage the demographic challenges of the future?”
PANEL III
LONG-TERM CARE:
SERVICES AND SUPPORT—
WHAT IT MEANS FOR
RETIREMENT SECURITY
Even generous pensions may not be enough to meet the need for long-term care, and pensions in many developed countries are not generous. Many older persons need at least some assistance with the ordinary activities of daily living, and others need skilled nursing care for extended periods of time. Increased longevity, advances in medical care for older people, and demographic changes mean that many families will not be able to provide long-term care directly to those family members in need. Consequently, the financing of long-term care and the share of this financing borne by retirees and their families affect retirement security.

The Organization for Economic Cooperation and Development (OECD) has studied the long-term care systems of 19 countries that, together, represent most of the different models of long-term care currently in use. These models are strongly influenced by each country’s attitudes toward social assistance in general and by the institutional structures that provide this assistance. The experiences of these 19 countries, plus an in-depth look at long-term care arrangements in Japan and the Netherlands, show what long-term care looks like in developed countries today.

Defining long-term care. The definition of long-term care varies to some degree from country to country, but there is generally a continuum from home care for those able to live in the community, to various types of assisted-living arrangements for those who need more care, to nursing homes for the frailest older adults or clients with disabilities. A more expansive definition would also include support to informal carers—family, friends, neighbors, and volunteers—in the form of respite care.

While the experiences of individual countries may differ from overall trends, one trend seems to be common in most developed countries; the boundaries between home care and institutional care have become blurred by such care models as continuing care communities. “Then the question is where would institutionalization start and where would home care end,” says Manfred Huber, of the OECD’s Directorate for Employment, Labour, and Social Affairs. “This doesn’t make it any easier [to track trends] for us statisticians … [but] clients can profit from [the greater flexibility of] these models.”

OECD countries. The number of countries with universal public long-term care coverage is growing, and includes Austria, Germany, Japan, Luxembourg, and Netherlands. Other coun-
tries such as Sweden and Norway effectively provide universal coverage through public services.

An alternative to direct provision is to provide through financial payments rather than through direct services. Australia, Austria, Germany, Luxembourg, Sweden, the UK, and the US are among the countries developing at least limited consumer-directed care arrangements. Under these arrangements, clients receive cash allowances that permit them to make their own choices regarding services and providers. The US is conducting limited experiments with such payments, only in some states and for a limited number of clients.

Japan. Japan has defined long-term care coverage as the third pillar of its social insurance system, after universal health care coverage and universal public pensions. One of the forces behind the development of this program was that Japan has one of the world’s fastest-aging demographic structures. “The share of the population age 65 and older is increasing by 1 percent every 2 years,” noted Naoki Ikegami of Keio University, Japan. “This is on the mind of every Japanese person.”

Yet the program was developed primarily for the benefit of the care-givers, and secondarily for those receiving care. The argument that provision of in-home care was an intolerable burden for women fell on sympathetic ears. Moreover, some long-term care was already being provided through the health care system, since there were no caps on the length of hospital stays. But this approach to the provision of long-term care was considered inefficient and ad hoc.

Japan restructured certain health and social services as the long-term care program was being designed. The Japanese system transferred the provision of a number of support services out of the health care budget and into long-term care insurance. This shift relieved some of the burden on the health care system. The long-term care program incorporated such health care services as visiting nurses, physical therapy services, day care, intermediate care, and some long-term care hospitals. From the social welfare system, in turn, the long-term care system took home help, day care, nursing homes, loan of wheelchairs and other devices, and the funding of home improvements such as ramps and handrails.

This shift of resources seems popular. Noted Ikegami, “[T]he general public would prefer to spend more… on … long-term care [premiums] than on health insurance. Health insurance premiums are seen as an increase in physicians’ incomes. Long-term care premiums, in contrast, are believed to result in the tangible benefit of increased staffing and availability of care.”

The Netherlands. In terms of services provided, the Dutch definition of long-term care is one of the more expansive definitions among developed countries. “… [W]e pay for all sorts of welfare

“The Organization for Economic Cooperation and Development (OECD) has studied the long-term care systems of 19 countries that, together, represent most of the different models of long-term care currently in use.”
services out of our health care budget,” said Jan van de Kasteele of the Dutch Ministry of Health, Welfare, and Sport. Social insurance coverage for nursing home care and home care were implemented during the economic good times of the 1960s and 1970s. This becomes very expensive because while income-related copayments are charged, means testing is not allowed in the national social insurance system.

Like Japan, the Netherlands is now redefining where health care services end and social welfare services begin, and shifting the responsibility for the social welfare content to municipalities. This shift is expected to improve both efficiency and cost containment. Social welfare services shifted out of the health care budget can be combined with services for which the municipality is already responsible, thereby increasing efficiency. Cost containment, in turn, can be enhanced because municipal services, unlike those provided through social insurance, can be means-tested and targeted to those most in need. “…[W]e no longer want to organize everything by way of [a] social insurance ‘right’,” stated van de Kasteele.

Who pays; how much. One measure of a government’s involvement in the provision of long-term care—or any other spending program—is spending in relation to Gross Domestic Product (GDP). GDP represents everything a country produces in a given year, so this relationship tells us how much of its resources a country devotes to a given program.

Most countries profiled in the OECD study spend between 0.5 percent and 1.0 percent of GDP on public long-term care programs. Spain, where far more care is provided informally, spends less than 0.25 percent of GDP on these programs. In contrast, the Netherlands, Sweden, and Norway—where the social commitment to long-term care is more extensive—spend between 1.25 percent and 2.75 percent of GDP on these programs.

The structure and availability of long-term care services is related to social, economic, and cultural norms. “Often countries make similar choices in long-term care that they make in other social applications, for example in health care,” noted Huber.

Countries that spend less on health care, for example, or those with a more fragmented system of health care, tend to have fewer long-term care services in place.

Countries differ in the extent to which they use either targeting or means-testing as ways to achieve efficiency and fairness. Under the new Japanese system, long-term care is a universal entitlement, with a 10 percent copayment required of most users, and less for those with low incomes. Services are targeted to those most in need of help through the intake and care man-
agrement process (see How care is provided, on page 59). The Dutch system also combines universal eligibility with targeting of services according to need. Sweden likewise prefers to maintain a universal entitlement, but with strict targeting to those most in need of services.

Other countries, in contrast, employ both targeting and means-testing to keep costs under control and maintain a fair balance between public and private spending. For example, Australia, New Zealand, and the UK are increasing targeting, but also accept means testing as a fair way to set the personal contribution.

Quality of care. Like long-term care itself, the quality of care means different things in different countries. In Japan, “Quality monitoring is mainly restricted to structure: whether workers have licenses, preventing fraud and abuse, etc.,” according to Ikegami.

In countries such as Sweden and Norway, where spending on long-term care is high, the definition of quality is more expansive and includes the social right to have privacy in a nursing home. Accordingly, over 80 percent of nursing home residents in Norway live in single rooms, compared with 10 percent in Japan. Other amenities in institutional care also differ widely among countries. In short, concludes Huber, “[Quality] measurement issues remain, in particular for home care and informal care.”

How care is provided. Long-term care is provided both formally and informally. The OECD found that at least 2/3 of all long-term care is informal care, provided by family members, friends, or neighbors. Problems can arise if the supply of informal care shrinks, or if informal carers lack needed support.

There are many differences among countries in what the family is expected to do for its older members or those with disabilities. In some countries, family care has been a cultural norm that is only now starting to shift to a belief that long-term care is a state responsibility.

OECD countries. In most developed countries, deinstitutionalization of older adults has been an important policy goal. While quality of life issues figure prominently in this decision, costs also play a role. The OECD study found that even though far more people receive home care than institutional care, institutional care accounts for up to 75 percent of government spending on long-term care services. Among the countries included in the OECD survey, the US devotes the second-smallest share of public long-term care spending to home care, reflecting the heavy emphasis on nursing home care financed through the Medicaid program.

Japan. Japan’s new program is causing a realignment from mostly informal care—provided in the home by daughters and daughters-in-law—toward formal care provided through home health agencies, various types of assisted living facilities, and nursing homes. This shift was already taking place before the new program was implemented, and the new program is accelerating the pace of change. “[T]here’s sort of a myth that there’s an Asian tradition that

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NAOKI IKEGAMI discusses the long-term care needs of Japan’s aging population.
the elderly are venerated,” states Ikegami. Instead, what is respected is status and position, which do typically accrue to older people. But the parent who becomes dependent loses status and position. Institutional living then becomes attractive to older adults.

The new system operates on a managed care model and, as in the Netherlands, is centered at the municipal level. Nurses or social workers manage client intake, while care managers assess clients’ needs, develop care plans, coordinate services, and advise their clients. Clients can change care managers or care manager agencies as they wish.

As part of this process, Japan has identified 5 levels of care. Services to be provided are based on the client’s ability to perform ordinary activities of daily living, as well as on cognitive performance. Level 1 clients require only minimal assistance to stay in their own homes, while level 5 clients need extensive assistance that may require placement in an institution. Level 1 care is the most prevalent service mode provided under the new system.

Unlike the case in other developed countries, nursing home care has become popular under the new program. Waiting lists stretch several years. Those on waiting lists often opt for assisted living arrangements, but then they must pay the residential costs, which are higher than the copayment required for nursing home care.

One consequence of the greater availability and use of formal care is a change in family dynamics. As older adults start to depend less on their children, they are less willing to leave their children assets, since they expect to need these assets for their own care.

The Netherlands. The Netherlands is experimenting with living arrangements that can improve older adults’ quality of life at the same time as they reduce the costs of providing care. People admitted to institutions become less self-reliant than those living in the community; experiments in the Netherlands have found that the level of formal care needed declined by 60 percent when clients were allowed to stay in their own homes rather than enter an institution.

And for those who need some level of institutional care, policymakers are rethinking the nursing home model. Care could be better delivered in smaller facilities than in large institutions.

Smaller facilities can be more home-like and more connected to their local neighborhoods, thereby reducing the cost of providing care.

Workforce issues. In all developed countries, women provide most long-term care, both formal and informal.

OECD countries. Women particularly dominate the long-term care workforce in countries that provide long-term care through cash allowances that the client can spend on whatever services he or she deems appropriate. In some countries, such allowances can be paid to family members who are not participating in the paid workforce. Many women working in long-term care are older, and have few other labor-force options. In other countries, such as Sweden and Norway, where care is provided directly
rather than through care allowances, women workers still predominate, but the care workforce tends to be younger.

Countries with universal systems have seen the growth of private provider markets. New organizations and workers are entering the market, and the role of for-profit providers is increasing in all aspects of long-term care. Some providers offer an integrated menu of long-term care services, ranging from home care to various levels of institutional care.

**The Netherlands.** If no reforms are made to the Dutch long-term care system, care provided and cost of care is expected to double by 2040. Finding the workers to provide such an increase in care would be difficult. Just as the Dutch are looking toward more means tested and targeted long-term care benefits to control costs, they hope this strategy will also lead to reductions in care needed and lessen the need for large increases in the long-term care workforce. According to van de Kasteele, “the government…will not try to provide some care to everyone, but...concentrate on giving good quality of care to the most needed.”

**Japan.** Japan does not face the same shortage of long-term care workers that plagues many developed countries. The adoption of universal long-term care insurance has opened up an entire new market for long-term care services. Care managers, for example, have become an established profession. Clients feel care managers are more accessible than physicians, and better able to solve clients’ problems. The long-term care market has also been able to absorb surplus workers from other sectors. For example, some former construction workers enter the care workforce because they are adept at such tasks as lifting patients.

But, noted Ikegami, “The problem of career advancement still remains.” Long-term care jobs may be dead-end or part-time positions. One way workers can make a satisfying career in long-term care may be to attend a professional training school for such workers; graduates are assured employment, which may not be case for other university education.

**Policy options going forward.** Developed countries will have to confront issues of access, affordability and quality of care.

**The Netherlands.** Countries that already have universal long-term care systems, such as the Netherlands, are facing fiscal pressures. “[W]e created…a beautiful, broad [long-term] care system [where] everything is collectively organized and most is collectively paid, but we have to privatize part of the system to guarantee the service in the future for the really needy,” says van de Kasteele. The expansive Dutch model of long-term care may have stretched beyond the country’s long-range capacity to provide this care.

**Japan.** Since the Japanese system is newer, it has not yet confronted the same problems as countries with more established programs. But as Japan expands the coverage and types of long-term care services available to its older adults, it will also need to address the long-term fiscal sustain-

“Many women working in long-term care are older, and have few other labor-force options.”
ability of a universal entitlement program in the face of a rapidly aging population, according to Ikegami. Financial constraints may require decreasing services in the future, but making eligibility criteria more stringent could be difficult since the program has become established as an entitlement and its transparent eligibility criteria have become popular.

To stave off cost and staffing pressures, policymakers in Japan and elsewhere want to ensure that publicly provided long-term care services complement, rather than supplant, informal care. Reliance on informal care will be influenced by demographic and medical trends. For example, improvements in health status and life expectancy mean that more older people are living with a spouse. The right mix of support services such as counseling and respite care will be essential as family caregivers themselves become older, and these services are not always in place.

**OECD countries.** Even as developed countries continue to age, demographic changes alone are not the most important factor driving long-term care costs. “Demography alone would probably add something like 1 percent of GDP [to long-term care costs],” Huber said. Rather than demography, he believes that improving quality will be the important driver of future long-term care costs.

“Examples of quality deficits [in long-term care] are numerous,” according to Huber. Consequently, governments are taking a more active role in improving regulation and assessing the quality of care. Every country participating in the OECD study cited staffing issues as the number one concern with respect to quality issues. Concerns about staff shortages suggest that current remuneration levels may have to be increased.

On the medical front, progress in dementia care could lead to substantial changes in the delivery of long-term care services. Such progress could reduce the number of people with intensive long-term care needs and allow more people who would otherwise have been institutionalized to live in the community.
JAN VAN DE KASTEELE, NAOKI IKEGAMI AND MANFRED HUBER ENGAGE IN A PANEL DISCUSSION ON LONG-TERM CARE.
PANEL IV
HEALTH CARE: FINANCING AND ITS IMPACT ON GOVERNMENT, EMPLOYERS AND INDIVIDUALS
An older population has higher health care needs. The American, French, and Canadian health care systems are different in structure and operation, and yet face similar problems. As their populations age, these systems may need to be redesigned to redistribute risks among workers, retirees, employers, and the government.

**System principles.** US Medicare, the French health care system, and the Canadian health care systems are driven by different sets of principles. These principles affect the way the systems operate; the outcomes for individuals, government, and providers; and the policy options available for solving the problems each system faces.

**United States.** US Medicare is the federal entitlement program, which provides health care coverage to virtually all older adults and some people with disabilities. The US is unique in that health care coverage is not universal, but it is linked to employment. Most people with health insurance receive it through their employers. US Medicare was created to ensure that people age 65+ have affordable and quality health care coverage. The program covers inpatient care in hospitals, helps cover doctors’ services and outpatient care and was just recently expanded to help cover prescription drug expenses. “...[t]he program is a first line of defense to provide these beneficiaries access to mainstream medical care,” states Judith Feder, Dean of the Georgetown University Public Policy Institute in Washington, D.C.

**Canada.** Unlike the US health care program of the same name, Canada’s Medicare system is a universal coverage system. It is based on five major principles: public administration, comprehensiveness, universality, portability, and accessibility.

Two features of the Canadian system are of particular importance to the comparisons with the US and France. Comprehensiveness means that the program must cover all medically necessary services. The definition of such services is renegotiated from time to time between the provincial and territorial governments and their respective colleges of physicians and pharmacists.
Accessibility is a key factor in Canada’s policy debates. Federal and provincial laws require that there can be no hindrance to accessibility based on fees. Fees include copayments, overall charges, and extra billing, or billing for an amount higher than the fee schedule for each service that has been negotiated between the provincial government and the medical providers. The principle of accessibility also prohibits any discrimination based on factors such as age, pre-existing medical conditions, or income. While both the US and the French health care systems make considerable use of copayments, in Canada these are strictly forbidden. Moreover, notes Tamagno, “Canadians are very committed to keeping the [health care] system the way [it is].”

**France.** In France, health care coverage is a social right, built on equality in access to health care and freedom to choose one’s health care providers. This coverage is based on the concept that society is the first insurer for certain measured risks in life. These risks cover retirement, family life, occupational accidents, and, especially health care.

“It is undeniable that the system does work well since most people have access to quality health care at low cost,” stated Jean-Marie Le Guen, M.D., a legislator and member of the Assemblee Nationale, France. He noted, however, that the cost is low for the population, but not for society.

**Coverage.** The health care coverage systems in all three countries are in many respects highly successful and enjoy high popularity. However, all three programs suffer from some coverage gaps as well.

**United States.** The US Medicare program is not a universal program, and, even with respect to its target group, has coverage gaps. The program only covers people age 65+ and people younger with certain disabilities or end-stage renal disease. Until Medicare’s prescription drug coverage program began its phase-in period on January 1, 2006, the program did not cover prescription drugs. The Medicare system caps beneficiaries’ out-of-pocket payments, so, in effect, it has provided coverage against medical catastrophes. Finally, the program provides virtually no coverage for long-term care. That gap is filled, for low-income older adults, through the means-tested Medicaid program.

The joint federal-state Medicaid program provides health care coverage for low-income people and for some children in modest-income families. Most other people with coverage receive it through employment-based plans. Depending on the definition of coverage used, up to 45 million people, or about 15 percent of the population, are without coverage.

**France.** Many countries finance and deliver long-term care services outside the health care system. In France, in contrast, long-term care is an emerging health care system issue. As the population ages, France is facing the need to guarantee care for people who need help with the activities of daily living. France decided to ask its citizens to work an additional day a year
Canada. Prescription drug costs are both a coverage issue and a pressing cost issue in the Canadian health care system. The system only covers prescription drugs administered in the hospital. Some 65 percent of all Canadians have supplemental coverage for prescription drugs, as well as dental or eye care services.

To fill the gap in public-sector prescription drug coverage, all provincial and territorial governments have “pharma care” plans that cover at least older adults, very low-income people, and people with disabilities. Thus, increases in drug costs affect provincial governments substantially.

An example of such a drug plan is that provided in Ontario. Virtually all residents age 65 or older qualify. The plan covers about 2,600 drug products, but not necessarily all available prescription drugs. Low- and moderate-income older adults face no deductible, but pay $2 per prescription. All other older adults pay a $100 annual deductible and $6.11 per prescription.

This program is considered fairly generous but is also expensive. There are also debates about covering the latest “wonder drug,” but provinces are reluctant to do this unless there are clear indications of savings elsewhere in the system. “We’re having big debates about that all the time,” said Tamagno.

Health care delivery. Canada, France, and the US are all regarded as having high-quality health care systems that deliver state-of-the-art care. But each country’s system delivers care somewhat differently.

United States and France. In both the US Medicare system and the French national health care system, private-sector physicians provide care. Care is delivered on demand, subject to ordinary scheduling needs of patients, practitioners, and hospitals and other facilities. Waiting lists for care—including elective (that is, nonemergency) surgeries—do not exist either in France or the US. On the other hand, emergency rooms can be overcrowded in both countries. In the US, emergency rooms may be overcrowded because they often function as primary care providers for people without health care coverage. In France, on the other hand, emergency rooms are often overburdened as a result of government budget cutbacks.

Canada. Waiting times for scheduling certain medical procedures have become a major policy concern in Canada. While no national statistics are collected on this problem, “…the waiting times for elective surgeries are horrendous, almost everywhere in Canada,” said Tamagno.

Waiting times vary considerably among provinces and by service. Waiting times for selected procedures in Ontario—Canada’s largest province—provide examples. Median waiting times for some surgeries particularly relevant to older adults include 24 weeks for hip replacements and
33 weeks for knee replacements. Waiting times for other procedures range from 29 days for mastectomies for breast cancer to 22 weeks for a magnetic resonance imaging procedure (MRI). It is also of interest to note that in the US, these procedures would generally not be considered “elective.” The only delays for these services result from ordinary scheduling issues facing the patient, physician, or hospital.

Waiting times stimulated a lawsuit that led to an important Canadian Supreme Court decision handed down in June 2005. Quebec, along with five other provinces, prohibits private insurance for services that are also covered under the public health insurance system. The suit charged that this prohibition, combined with lengthy waiting times for elective surgeries, constituted an unjustified violation of the patient’s rights to life and the security of the person. These rights are guaranteed both under the Canadian constitution and under the Quebec Charter of Human Rights and Freedoms, a law of the National Assembly that supersedes all other laws.

While two lower courts rejected this claim, the Supreme Court upheld it. The court’s decision means that waiting times, combined with the prohibition on private insurance that overlaps with the public system, are not justified. Many OECD countries have a system like Canada’s, where public and private insurance overlap. Accordingly, the court reasoned, overlap in benefits should not be expected to harm the public system. Rather, it is possible that expanded private insurance coverage could reduce waiting times by increasing the health care system’s capacity.

**Public-private mix.** Universal health care coverage—or even coverage under a government-sponsored plan—generally involves the participation of both the public and the private sectors. The mix of public and private delivery and spending differs considerably among France, Canada, and the US, as well as among other OECD countries.

**France.** In France, health care coverage is provided through funds managed by employers and trade unions. Everyone, including families, registers with the local fund. Self-employed physicians, dentists, and other practitioners in their own practices provide most primary and secondary care. Salaried hospital staff also provide some such care.

Most self-employed practitioners operate under national agreements negotiated between the insurance funds and the associations representing the practitioners. These agreements cover not only allowable rates but also certain conditions of practice. About a quarter of doctors covered by the agreements (those in what is called the “second sector”) are authorized to charge more than the negotiated rates. A small proportion of doctors are not covered by the agreements at all, and thus may set their own rates, but patients receive almost no reimbursement from the national health insurance system for such care.

“The mix of public and private delivery and spending differs considerably among France, Canada, and the US, as well as among other OECD countries.”
The compulsory component of the system reimburses on average 70 percent of costs, leaving participants with a 30 percent copayment. More than 80 percent of the population has supplemental insurance, often provided by employers. This insurance covers all or part of the remaining costs. In addition, individuals may purchase other coverage on their own, though in practice most supplemental coverage comes through the work place. Thus, for more than 96 percent of the French population, medical care is either entirely free (for low-income people) or is reimbursed 100 percent.

Canada. The structure of the Canadian system reflects the country’s governmental structure. “[W]e have the world’s most complicated federal system,” said Edward Tamagno, a policy associate at Canada’s Caledon Institute of Social Policy. Health care is a provincial responsibility in that the provinces decide how their systems are to be structured and what goods and services will be provided. In areas of provincial jurisdiction, the provinces are sovereign.

The federal government has only one constitutional power over the health care system, and that is the spending power. The federal government can provide fiscal incentives to the provinces to adopt particular policies, but such incentives can give rise to debates about abuse of the federal system.

Most people—even Canadians—generally believe that the Canadian health care system is entirely a public system. “This isn’t the case,” said Tamagno. The Canadian system, unlike the US Medicare system of the same name, is universal and covers all residents. The system is financed overwhelmingly from the general tax revenues of the provincial governments, along with federal contributions. Three provinces also impose earmarked payroll taxes that finance a small portion of the health system’s total costs.

But the Canadian system also relies substantially on private spending in the form of private health insurance intended to supplement government benefits and provide services not covered under the public system. Until the mid-1990s, about 3 out of every 4 dollars spent on health care was spent through the public system. At that point, reductions in government expenditures lowered the public share to about 70 percent, where it has remained since.

Most OECD countries have a similar public-private mix in their health care systems, with the Netherlands having a somewhat larger private share than Canada. As in many other health care system measures, the US anchors the scale, with a majority of health care spending—including out-of-pocket spending as well as private insurance—passing through the private sector. “Of the 30 OECD countries, …the only other… country in which private expenditures exceed public expenditures in health care is Mexico,” Tamagno noted.

United States. The US Medicare program is financed through several sources. About half of the funding comes from a payroll tax levied on active workers. The remaining half—covering physician care and other expenditures—is financed through the federal government’s general revenues and through premiums paid by beneficiaries.

Most beneficiaries also purchase “Medigap” insurance to cover expenses Medicare does not cover. Others may have retiree health care coverage from their pre-retirement employer, though
the prevalence of such coverage is declining. Nevertheless, “… beneficiaries are now paying about a quarter of their income in their own contributions to Medicare or costs that it doesn’t cover,” noted Feder.

**Cost comparisons and trends.** One of the problems facing most developed countries is that health care spending is growing at a faster rate than inflation.

**Canada.** Canada’s experience has been similar to that of most OECD countries, including the US. Over the last 25 years, Canadian health care costs generally increased faster than the Consumer Price Index (CPI). For Canada, the only exception to this trend was a period in the mid-1990s when the federal government was trying to reduce deficits, cut transfer payments, and reduce the rate of growth of transfers to the provinces.

In total per capita expenditures, Canada is in the high end of OECD countries, including Germany, France, and the Netherlands. According to the OECD, per capita health expenditures in Canada were $3,003 (in US dollars adjusted for purchasing power parities, or the dollar’s buying power in each country). But per capita spending in the US in the same year was $5,635. “When compared to United States, we realize we can go a lot higher,” noted Canada’s Tamagno.

Another measure of a country’s health care spending is the ratio of total health care expenditures to GDP. As in the case of per capita expenditures, Canada is at the higher end of a cross-section of OECD countries, spending 9.9 percent of GDP on health. This share is close to those of the Netherlands (9.8 percent), France (10.1 percent), and Germany (11.1 percent). “Of course,” added Tamagno, “the US [at 15.0 percent] is way above it all.”

**United States.** While one will hear arguments that the US Medicare program is inefficient, the evidence tells a different story, according to Feder. “In many years,” she pointed out, “Medicare has been more successful… than private insurers in containing costs.” At the same time, however, the Medicare program cannot be fully insulated from cost increases elsewhere in the US health care system. Medicare and private insurers are buying in the same market, so their costs tend to rise together.

In the US, the new Medicare prescription drug coverage promises to fill an important gap in the program’s overall coverage. Older adults will still face out-of-pocket costs, however, and the program’s effect on the federal government’s budget is expected to be substantial.

The cost problems that US Medicare and Medicaid face are problems that the whole health care system faces, noted Feder. However, the current policy and political debates are not focusing on controlling the nation’s health care costs or on the distribution of these costs between beneficiaries and taxpayers. Rather, “… it is the … [Medicaid] program that is in the budget crosshairs at the moment,” she said. But the challenge is greater with Medicare not only because there are larger numbers of older people but also because the program’s cost per person is rising steadily.

**France.** Health care costs in France are driven in part by demographic issues. The system depends on payroll taxes levied on employers and employees. The aging of the Baby Boom Generation will increase financial demands on the system. At the same time, the payroll tax base is shrinking due to demographic imbalances and high unemployment. Declining payroll tax
revenues must thus finance care for an ever-increasing number of patients, with more chronic and costly diseases, and for a longer period of time due to increased longevity. The cost of prescription drugs is also a major issue for the French system. “[This is] the single issue…” according to Le Guen.

Policy options going forward. Policy and reform debates in all three countries focus on containing the growth of health care costs.

United States. It has been proposed that the Medicare program reduce costs by shifting from public insurance to subsidies or vouchers for private insurance. “Arguments are made that [privatization] will lead to competition and greater efficiency in the health care system,” stated Feder, “but there is no evidence to support that claim, except for a very modest one-time reduction.”

There are only three options with respect to Medicare financing, she believes: raising payroll taxes, cutting benefits, or controlling health care costs. Politically, however, taxes are not under discussion, and health care costs have not been amenable to control. “What gives [in response to cost pressures] is access to health insurance for our citizens,” said Feder. Moreover, while retirees have been significantly protected from inequities in access due to cost pressures, that could change as the government backs away from areas where it has been most active.

The growth of biomedical technology also serves to increase health care costs. The US has more access to new technologies, in part because Americans are willing to pay for access to such technologies. There are both government and private-sector efforts aimed at joining the worldwide effort to assess value for the dollar as a guide to what the system will pay for and what it will not. As technology is able to do more and more, it does provide value, but the question is whether costs have to be as high as they are.

“The major difference between the US and other nations, albeit with some differences in access to technology, is that we pay much higher prices for our services than do people in other countries,” Feder concluded. But with respect to rising health care costs, she considers it important to remember the admonition of economist Herb Stein. Stein was often quoted as saying of health care costs, “That’s unsustainable, and if it’s unsustainable, the trend will stop.”

France. France’s health care system faces a difficult policy environment due to constraints on the growth of the payroll tax base that finances health care. Policymakers find it difficult to increase payroll taxes because these taxes are already high. High payroll taxes increase the cost of labor, depressing employment growth. Another disadvantage of tax increases is that they would raise the share of the system’s cost paid by employees, and the public already considers this share to be high. But both the government and individuals may need to pay more to maintain the system’s quality.
One problem in the French health care system has been that care is often uncoordinated. Self-employed physicians treating the same patient may not always communicate with each other, ambulatory and hospital care may be uncoordinated, and health care and social care for the older adults and people with disabilities may proceed on separate tracks.

Le Guen also suggested that France might need to give greater consideration to what is known in the US as managed care. To reduce costs and improve coordination, France has experimented with a health care delivery system that resembles US health maintenance organizations. Since 1998, every general practitioner can become a referring, or gatekeeper, doctor for a patient enrolled in the referral system. The physician agrees to observe certain system rules aimed at cost control and coordination of care. The physician receives a payment for each patient enrolled in the practice, as well as a fee for each visit and service provided.

The enrollee agrees to consult the designated general practitioner for all specialist referrals other than to pediatricians, psychiatrists, obstetrician/gynecologists, and ophthalmologists. Patient copayments are lower in the referral system than in the regular system. Despite generous financial incentives, however, enrollment in the system by both physicians and patients has been low to date.

While controlling the costs of health care in general and prescription drugs in particular are important policy priorities in France, public health issues also affect the financial stability of the system. Tobacco and alcohol abuse, as well as occupational health and safety, are more serious in France than among its European neighbors, Le Guen noted. These hazards can directly induce such serious diseases as cancer, and affect people who could otherwise still be active in the workforce.

**Canada.** Canada’s health care system is under financial pressure and will remain so, as in most other industrialized countries. “The chances of [the system’s] recovery are almost guaranteed,” according to Tamagno, “given Canadians’ strong support.”

However, the system will require continued incremental changes to deliver on its promise. “There will have to be a greater willingness to experiment with private systems,” he said. Such experiments could face obstacles. For example, many provincial governments are ideologically opposed to private clinics. But countries like France, with substantial private health sectors, have similar health outcomes to Canada. Accordingly, policy makers may have to examine whether prohibitions against such private participation actually help the Canadian system.

Canada’s provincial governments pay for a large share of total spending on prescription drugs, and thus are concerned that drug prices have been rising a good deal faster than either overall health care costs or the consumer price index. However, in Canada, as in the US and France, available policy options may be limited by the budget constraints facing governments at all levels.
CLOSING REMARKS
LADAN MANTEGHI, DIRECTOR, AARP GLOBAL AGING PROGRAM

I am hesitant to refer to this moment as the closing of the conference. It is my hope that this conference has served as a catalyst for deeper conversation and cooperation; that the end is in effect a beginning. This is the true aim of the Reinventing Retirement series—it’s a process, not an event. Retirement itself is being reinvented with or without us, yet we have much to contribute and can help shape the process so that retirement happens—but with dignity and purpose and meaning.

As our most recent global survey revealed, the most troubling finding was the severe lack of confidence among the general public about government’s ability to provide adequate retirement security amid demographic pressures.

This finding is all the more alarming when juxtaposed with the findings of our earlier poll released last November at AARP’s first Reinventing Retirement conference in London. That previous survey found that opinion leaders in G7 countries expect their governments to “muddle through” policy making for their aging populations rather than create and sustain a dialogue that involves all of its social partners and seek a strategy to navigate change and create opportunities for their aging societies.

These twin findings—the lack of a comprehensive policy agenda for an aging population and the related lack of confidence among the general public toward government’s ability to address these issues—require urgent action. Based on our deliberations over the course of this conference, a certain consensus emerged. The four points in particular strike home as critical action steps that I challenge all of you to take back to your home countries. They are as follows:

- Involve all stakeholders and social partners to increase employment opportunities to benefit older workers and economies. The coming labor crunch will need these older workers, who in turn can reduce pressures on public pension and health systems. If people want to or must work in their so-called retirement years, there should be no barriers.
- Better educate the public on what is needed to prepare for secure retirements. The lack of not just financial literacy, but retirement literacy, which includes planning for health and long-term care, dramatically reduces the options available to future retirees.
- Engage citizens in a transparent public debate to find agreeable solutions for solvent retirement systems. These programs represent contracts between government and the public and both must be at the table along with other social partners for solutions to be found and be implemented.
- Urge government to assume responsibility needed to build confidence within their constituencies that they will meet current and future commitments as they relate to retirement security.
Do you accept this challenge?

The idea that retirement is a process and not an event must drive our approach to problem solving. We must think broadly about aging and not in piecemeal fashion, or worse, by muddling through. We know it will be better to take steps now in the context of a long-term strategy, rather than take painful actions when it is too late and our choices are limited.

By coming to this conference and by being part of this broader conversation, you have all demonstrated that willingness to meet challenges and offer solutions. I look forward to the continued conversation, and better, to taking the real steps necessary to build security and confidence for our retirees.
LADAN MANTEGHI, DIRECTOR, AARP GLOBAL AGING PROGRAM PRESENTS CLOSING REMARKS.

REPORT CREDITS
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THE OVERALL CHALLENGE FOR ALL GOVERNMENTS WILL BE TO MAKE A GENUINE EFFORT TO PROMOTE GREATER UNDERSTANDING OF RETIREMENT SECURITY ISSUES, OPEN A REAL DEBATE, ENGAGE THEIR CITIZENS IN FINDING AND AGREEING TO SOLUTIONS, AND TO CLOSE THE GAPS BETWEEN THE CURRENT SITUATION, THE FUTURE OUTLOOK, AND THE PREFERENCES AND EXPECTATIONS OF THEIR POPULATIONS.

WILLIAM D. NOVELLI,
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REINVENTING RETIREMENT
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CONFERENCE PROCEEDINGS

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