

ADDRESS TO ACTUARIAL SOCIETY OF SOUTH AFRICA

JOHANNESBURG, 7 AUGUST 2007

KENNETH G. BUFFIN PhD, FIA, FSA

GOOD MORNING, LADIES AND GENTLEMEN.

IT IS TRULY AN HONOUR AND A PRIVILEGE TO BE INVITED TO ADDRESS YOU THIS MORNING.

YOUR PRESIDENT, ADRIAN BASKIR, AND I ARE BOTH ACTIVELY INVOLVED WITH THE INTERNATIONAL ACTUARIAL ASSOCIATION WHERE WE SERVE AS MEMBERS OF THE SOCIAL SECURITY COMMITTEE.

AND IT IS AS A RESULT OF OUR WORKING RELATIONSHIP AT THE INTERNATIONAL ACTUARIAL ASSOCIATION THAT ADRIAN HAS INVITED ME TO COME TO JOHANNESBURG TO ADDRESS YOU THIS MORNING.

WE LIVE IN A WORLD OF CONTINUING CHANGE AND PROGRESS, PARTICULARLY WITH RESPECT TO ECONOMIC, SOCIAL AND POLITICAL CONDITIONS. SUCH CHANGES PRESENT MANY CHALLENGES AND OPPORTUNITIES FOR THE ACTUARIAL AND RELATED PROFESSIONS.

SOUTH AFRICA IS CURRENTLY EXPERIENCING THE CHALLENGE AND EXCITEMENT OF ADDRESSING THE PROVISION OF INCOME SUPPORT AND SECURITY IN OLD AGE FOR ALL SOUTH AFRICANS.

THE CURRENT PROPOSALS REQUIRE DISCUSSION AND DEBATE, RESEARCH AND ANALYSIS, ASSESSMENT, AND ACHIEVING A CONVERGENCE OF VIEWS, ON THE PATH TO ACCEPTANCE AND IMPLEMENTATION.

ONE ASPECT OF THE DISCUSSION AND EVALUATION OF THE CURRENT PROPOSALS IS TO REVIEW THEM FROM AN OVERSEAS OR INTERNATIONAL PERSPECTIVE.

ALTHOUGH SOUTH AFRICA, AND INDEED EVERY NATION, WILL SEEK TO ACHIEVE ITS OBJECTIVES FOR RETIREMENT INCOME SUPPORT AND SECURITY IN TERMS OF ITS OWN PARTICULAR SOCIAL, ECONOMIC, AND POLITICAL CONDITIONS, AS WELL AS THE CULTURE AND HISTORY OF THE NATION, IT IS, NEVERTHELESS, INFORMATIVE TO REVIEW THE INTERNATIONAL LANDSCAPE TO DISCERN WHAT MIGHT BE USEFUL OR APPLICABLE FROM THE EXPERIENCES OF OTHER NATIONS WITH SIMILAR OBJECTIVES REGARDING THE PROVISION OF OLD-AGE INCOME SUPPORT AND SECURITY.

THERE ARE 192 MEMBER NATIONS OF THE UNITED NATIONS AND THERE IS A CORRESPONDINGLY LARGE AMOUNT OF INFORMATION AVAILABLE ON THE SOCIAL SECURITY AND RETIREMENT INCOME ARRANGEMENTS AND PRACTICES FROM NATIONS AROUND THE WORLD.

MY PURPOSE THIS MORNING IS TO PROVIDE YOU WITH SOME COMMENTARY ON THE CUSTOMARY PRACTICES AND MORE SIGNIFICANT FEATURES OF TYPICAL STRUCTURES FOR SOCIAL SECURITY SYSTEMS AND RETIREMENT INCOME ARRANGEMENTS AROUND THE WORLD.

I WOULD LIKE TO MENTION TWO IMPORTANT RESEARCH REFERENCE SOURCES WHERE YOU CAN FIND THE RELEVANT INFORMATION FOR MOST COUNTRIES.

THE FIRST IS THE INTERNATIONAL SOCIAL SECURITY ASSOCIATION AT WWW.ISSA.INT

THE SECOND IS THE LINK TO SOCIAL SECURITY AROUND THE WORLD FROM THE WEBSITE OF THE UNITED STATES SOCIAL SECURITY ADMINISTRATION AT WWW.SSA.GOV

THE QUESTIONS THAT WE MIGHT TYPICALLY ASK AS WE LOOK INTO THE INTERNATIONAL SOCIAL SECURITY AND RETIREMENT INCOME ARENA ARE:

- WHAT IS TYPICAL FOR DEVELOPED NATIONS?
- WHAT IS TYPICAL FOR DEVELOPING NATIONS OR NATIONS IN A PROCESS OF ECONOMIC, SOCIAL OR POLITICAL CHANGE?
- WHERE CAN THE LEADERSHIP AND INTELLECTUAL KNOWLEDGE ON INTERNATIONAL SOCIAL SECURITY AND RETIREMENT INCOME BE FOUND?
- WHAT ARE THE UNDERLYING PRINCIPLES GUIDING THE DESIGN AND DEVELOPMENT OF SOCIAL SECURITY SYSTEMS?
- WHAT ARE THE COMPONENTS OF A FRAMEWORK UPON WHICH TO CONSTRUCT A SOUND AND RELIABLE SYSTEM TO ACHIEVE SOCIAL AND ECONOMIC POLICY OBJECTIVES FOR OLD-AGE INCOME SUPPORT?

THESE ARE THE PRIMARY QUESTIONS THAT I WILL REVIEW WITH YOU THIS MORNING.

THERE ARE ALSO A NUMBER OF SECONDARY OR MORE DETAILED QUESTIONS THAT ARE TYPICALLY ENCOUNTERED IN A DISCUSSION OF INTERNATIONAL PRACTICES:

- WHAT IS THE ROLE AND INFLUENCE OF THE WORLD BANK?
- WHAT IS THE ROLE AND INFLUENCE OF THE INTERNATIONAL LABOUR ORGANISATION?
- WHAT IS MEANT BY THE CHILEAN MODEL?
- WHAT IS MEANT BY THE SWEDISH MODEL?
- WHAT ARE THE RELATIVE MERITS OF PAY-AS-YOU-GO FINANCING AND FUNDED ARRANGEMENTS?
- WHAT IS MEANT BY A NOTIONAL DEFINED CONTRIBUTION (NDC) SYSTEM?
- WHAT ARE AUTOMATIC BALANCING MECHANISMS?
- HOW ARE THE CHALLENGES OF CHANGING DEMOGRAPHICS BEING RESPONDED TO, SUCH AS IMPROVING MORTALITY TRENDS AND INCREASING LIFE EXPECTANCY, DECLINING FERTILITY RATES, AND CHANGES IN THE RATIO OF THE RETIRED POPULATION TO THE WORKING POPULATION?

- HOW ARE THE FINANCIAL CHALLENGES OF SUSTAINABILITY BEING ADDRESSED?

I WANT TO GIVE YOU A QUICK OVERVIEW OF THESE QUESTIONS AND ISSUES WITH REFERENCE TO SOME SPECIFIC COUNTRIES AS AN INTRODUCTION TO THE INTERNATIONAL LANDSCAPE AND THEN I WILL ADDRESS THE SPECIFIC PROPOSALS FOR SOUTH AFRICA FROM THIS INTERNATIONAL PERSPECTIVE. I RECOGNIZE THAT I AM AN INVITED GUEST AND VISITOR TO THIS GREAT NATION OF SOUTH AFRICA, BUT I HOPE THAT MY REMARKS WILL PROVE RELEVANT TO YOUR DEBATE AS YOU ADDRESS THE ISSUES POSED BY THE VARIOUS PROPOSALS FOR SOCIAL SECURITY AND PENSION REFORM.

LET ME NOW CIRCLE BACK TO IDENTIFY AND COMMENT ON SOME OF THE MAJOR SOURCES OF RESEARCH AND INFLUENCE IN THE AREA OF OLD-AGE INCOME SECURITY.

THERE ARE FOUR SPECIFIC RECOGNIZED AUTHORITIES THAT ARE REGULARLY CONSULTED OR THAT PROVIDE USEFUL AND PRACTICAL INFORMATION. THESE ARE:

- THE WORLD BANK, BASED IN WASHINGTON, USA
- THE INTERNATIONAL LABOUR ORGANISATION, BASED IN GENEVA, SWITZERLAND
- THE INTERNATIONAL ACTUARIAL ASSOCIATION, COMPRISING THE PROFESSIONAL ACTUARIAL ASSOCIATIONS FROM AROUND THE WORLD
- THE ACTUARIAL, RESEARCH AND CONSULTING COMMUNITY, COMPRISING UNIVERSITIES, THINK-TANKS, AND INTERNATIONAL CONSULTING ACTUARIAL FIRMS AND RELATED PROFESSIONALS

THE WORLD BANK GROUP HAS, AS ITS MAIN COMPONENT, THE INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT, ESTABLISHED AS AN OUTCOME OF THE BRETTON WOODS AGREEMENT IN 1944. ITS ORIGINAL FUNCTION WAS PRIMARILY TO AID IN RECONSTRUCTION FOLLOWING THE 1939-45 WORLD WAR.

IN RECENT YEARS ITS FOCUS HAS BEEN ALMOST EXCLUSIVELY ON DEVELOPMENT.

THE BANK PROVIDES LOANS OR GRANTS TO MEMBER COUNTRIES FOR SPECIFIC PROJECTS LINKED TO IMPLEMENTING POLICY CHANGES IN THE COUNTRY'S ECONOMY.

THE BANK'S PROGRAMMES ARE MAINLY TARGETED IN THE AREAS OF INFRASTRUCTURE DEVELOPMENT, ENVIRONMENTAL PROTECTION, RURAL AND AGRICULTURAL DEVELOPMENT, AND IMPORTANTLY FOR OUR TOPIC TODAY, HUMAN DEVELOPMENT AND PROTECTION.

THE BANK'S EXPERT STAFF ARE ASSIGNED TO SPECIFIC DEPARTMENTS OR SECTORS, SUCH AS THE HUMAN DEVELOPMENT SECTOR,

AND THE FINANCIAL SECTOR WITH ITS OPERATIONS AND POLICY DEPARTMENT.

EACH OF THESE GROUPS IS ACTIVE IN PROMOTING THE BANK'S POLICIES AND INITIATIVES IN THE AREA OF SOCIAL SECURITY AND OLD-AGE INCOME SUPPORT.

IN 2005 THE WORLD BANK PUBLISHED A SIGNIFICANT AND INFLUENTIAL REPORT WITH THE TITLE "OLD-AGE INCOME SUPPORT IN THE TWENTY-FIRST CENTURY" WITH A SUBTITLE "AN INTERNATIONAL PERSPECTIVE ON PENSION SYSTEMS AND REFORM"

AT THE HEART OF THIS REPORT WAS A RECOMMENDED MULTI-PILLAR APPROACH FOR THE STRUCTURE OF PENSION SYSTEMS COMPOSED OF A "FLEXIBLE AND DISCRETIONARY" COMBINATION FROM AMONG FIVE BASIC ELEMENTS:

- A NON-CONTRIBUTORY DEMOGRANT OR SOCIAL PENSION THAT PROVIDES A MINIMAL LEVEL OF PROTECTION
- A CONTRIBUTORY SYSTEM LINKED TO EARNINGS TO REPLACE SOME PORTION OF INCOME
- A MANDATORY SYSTEM OF INDIVIDUAL SAVINGS ACCOUNTS
- A VOLUNTARY SYSTEM THAT IS FLEXIBLE AND DISCRETIONARY THAT MAY TAKE MANY POTENTIAL FORMS, DEFINED BENEFIT OR DEFINED CONTRIBUTION, EMPLOYER-SPONSORED OR INDIVIDUAL
- INFORMAL FINANCIAL AND NON-FINANCIAL SUPPORT FROM INTRA-FAMILY OR INTER-GENERATIONAL SOURCES TO THE ELDERLY INCLUDING ACCESS TO HOUSING AND HEALTH CARE

TOGETHER THESE FIVE ELEMENTS HAVE BECOME THE WORLD BANK'S GLOBAL STANDARD OR FRAMEWORK FOR COMPARATIVE ASSESSMENT AND REFORM PURPOSES IN ADVISING ON OLD-AGE INCOME SECURITY IN COUNTRIES WHERE ITS INFLUENCE IS SOUGHT.

THE WORLD BANK ALSO PRESENTED FOUR PRINCIPLES TO BE CONSIDERED IN SETTING THE PRIMARY GOALS OF A SOCIAL SECURITY SYSTEM:

- ADEQUACY
- AFFORDABILITY
- SUSTAINABILITY
- ROBUSTNESS

AN ADEQUATE SYSTEM PROVIDES BENEFITS TO THE WHOLE POPULATION THAT ARE SUFFICIENT TO PREVENT OLD-AGE POVERTY IN ADDITION TO PROVIDING A MEANS TO SMOOTH LIFETIME CONSUMPTION FOR THE POPULATION.

AN AFFORDABLE SYSTEM IS WITHIN THE CAPACITY OF SOCIETY AND INDIVIDUALS AND DOES NOT DISPLACE OTHER SOCIAL OR ECONOMIC IMPERATIVES OR HAVE UNTENABLE FISCAL CONSEQUENCES.

A SUSTAINABLE SYSTEM IS FINANCIALLY SOUND AND CAN BE MAINTAINED OVER A FORESEEABLE HORIZON UNDER A BROAD SET OF REASONABLE ASSUMPTIONS.

A ROBUST SYSTEM HAS THE CAPACITY TO WITHSTAND MAJOR SHOCKS INCLUDING THOSE ATTRIBUTABLE TO ECONOMIC, DEMOGRAPHIC AND POLITICAL CHANGES OR TRENDS.

OVER THE LAST 20 YEARS, THE WORLD BANK HAS MADE MORE THAN 200 LOANS, INVOLVING MORE THAN 60 COUNTRIES, THAT WERE RELATED TO PENSION REFORM AND DEVELOPMENT.

THE BANK HAS SUPPORTED A DIVERSE RANGE OF PENSION REFORMS WITHIN THE BANK'S MULTI-PILLAR FRAMEWORK.

THE BANK HAS BEEN INFLUENTIAL IN MAKING SEVERAL DIFFERENT TYPES OF PENSION SYSTEM AND SOCIAL SECURITY REFORMS, INCLUDING:

- PARAMETRIC REFORMS THAT RETAIN THE BASIC STRUCTURE OF BENEFITS, PUBLIC ADMINISTRATION, AND THE UNFUNDED NATURE OF THE SYSTEM, BUT WHERE KEY ELEMENTS OF THE PARAMETERS THAT DEFINE BENEFITS, CONTRIBUTIONS AND ELIGIBILITY CONDITIONS ARE MODIFIED.
- REFORMS THAT CHANGE THE STRUCTURE OF BENEFITS THAT RETAIN PUBLIC ADMINISTRATION AND THE UNFUNDED NATURE OF THE SYSTEM, BUT INTRODUCE CONCEPTS SUCH AS THE NON-FINANCIAL OR NOTIONAL DEFINED CONTRIBUTION ARRANGEMENTS INTO THE SYSTEM.
- MARKET-BASED REFORMS THAT PROVIDE FULLY-FUNDED BENEFITS OF EITHER A DEFINED BENEFIT OR DEFINED CONTRIBUTION NATURE UNDER PRIVATE MANAGEMENT ARRANGEMENTS
- REFORMS THAT COMBINE PUBLIC PRE-FUNDING AND PUBLIC ADMINISTRATION, AGAIN BASED ON EITHER DEFINED BENEFIT OR DEFINED CONTRIBUTION CONCEPTS.
- MULTI-PILLAR REFORMS THAT DIVERSIFY THE STRUCTURE OF BENEFITS, FUNDING AND ADMINISTRATION OF THE SYSTEM.

IT IS THE STATED POLICY OF THE WORLD BANK TO INCLUDE IN ITS REFORM PROPOSALS THE NEEDS OF THE MAIN TARGET POPULATION GROUPS IN CLIENT COUNTRIES, INCLUDING: FORMAL SECTOR WORKERS; INFORMAL SECTOR WORKERS; AND THE LIFETIME POOR.

SOME OBSERVERS HAVE SUGGESTED THAT THE WORLD BANK HAS USED ITS ROLE AS LENDER TO IMPOSE ITS VIEWS AND OPINIONS RELATING TO PENSION REFORM AND SYSTEM STRUCTURE, ON CLIENT

COUNTRIES AS A CONDITION OF MAKING FUNDS AVAILABLE FOR SOCIAL AND ECONOMIC DEVELOPMENT PROJECTS.

THE WORLD BANK IS SOMETIMES CRITICIZED FOR ITS SOMEWHAT DOCTRINAIRE APPROACH TO ECONOMIC AND SOCIAL POLICY DEVELOPMENT AND IN PARTICULAR WITH ITS VIEWS IN FAVOURING FUNDING AND INDIVIDUAL ACCOUNT ARRANGEMENTS.

A PARTICULAR AREA OF CONTENTION RELATES TO THE WORLD BANK'S FAVOURING OF THE NOTIONAL DEFINED CONTRIBUTION CONCEPT. I WILL COME BACK TO THIS TOPIC AT A LATER POINT.

THE WORLD BANK'S GOALS OF IMPLEMENTING ADEQUATE, AFFORDABLE, SUSTAINABLE AND ROBUST SYSTEMS FOR PROVIDING RETIREMENT INCOME, OR OLD-AGE INCOME SUPPORT, IN THE TERMINOLOGY OF THE BANK, CONSTITUTE THE BANK'S PRIMARY OBJECTIVES.

THE BANK ALSO HAS SECONDARY DEVELOPMENT GOALS THAT ARE IMPORTANT INFLUENCES ON THE BANK'S POLICIES.

THESE SECONDARY DEVELOPMENT GOALS ARE INTENDED TO CREATE POSITIVE DEVELOPMENTAL OUTCOMES BY MINIMIZING THE POTENTIAL NEGATIVE IMPACTS ON LABOUR MARKETS AND MACROECONOMIC STABILITY, WHILE EMPHASIZING POSITIVE IMPACTS THROUGH INCREASED NATIONAL SAVING AND FINANCIAL MARKETS DEVELOPMENT.

LET ME NOW TURN TO THE SECOND INSTITUTION THAT I REFERRED TO EARLIER IN MY LIST OF FOUR IMPORTANT SOURCES OF RESEARCH AND INFLUENCE, NAMELY THE INTERNATIONAL LABOUR ORGANISATION (ILO). THE ILO IS AN AGENCY OF THE UNITED NATIONS, AS IS THE WORLD BANK.

THE ILO HAS A WELL-DOCUMENTED SET OF PRINCIPLES AND STANDARDS THAT ADDRESS THE FOLLOWING FIVE KEY OBJECTIVES FOR SOCIAL SECURITY:

- THE EXTENSION OF COVERAGE TO ALL MEMBERS OF THE POPULATION
- PROTECTION AGAINST POVERTY IN OLD-AGE, DURING DISABILITY, OR ON DEATH OF THE WAGE EARNER, FOR ALL MEMBERS OF THE POPULATION.
- PROVISION OF AN INCOME, IN REPLACEMENT FOR EARNINGS LOST AS A RESULT OF VOLUNTARY OR INVOLUNTARY RETIREMENT, FOR ALL THOSE WHO HAVE CONTRIBUTED
- ADJUSTMENT OF THIS INCOME TO TAKE ACCOUNT OF INFLATION, AND AT LEAST TO SOME EXTENT, OF THE GENERAL RISE IN LIVING STANDARDS.
- CREATION OF AN ENVIRONMENT FOR THE DEVELOPMENT OF ADDITIONAL VOLUNTARY PROVISIONS FOR RETIREMENT INCOME.

THE ILO TRANSLATES THESE PHILOSOPHICAL PRINCIPLES INTO FORMAL INTERNATIONAL LABOUR STANDARDS.

AS AN EXAMPLE, THE ILO ADVOCATES A TARGET MINIMUM LEVEL OF BENEFITS TO PROVIDE INCOME REPLACEMENT IN RETIREMENT AT 40 PERCENT OF EARNINGS.

THE FOCUS OF THE ILO IS VERY MUCH ON THE PRIMARY SOCIAL OBJECTIVE OF PROVIDING ADEQUATE RETIREMENT INCOME.

WHEREAS, BY CONTRAST. THE WORLD BANK'S APPROACH IS ALSO MOTIVATED AND INFLUENCED BY ECONOMIC POLICY OBJECTIVES AND BROAD DEVELOPMENT GOALS.

IN GENERAL, FOR BASIC SOCIAL SECURITY SYSTEMS, THE ILO FAVOURS DEFINED BENEFIT STRUCTURES AND UNFUNDED PAY-AS-YOU-GO FINANCING ARRANGEMENTS.

THE THIRD INSTITUTION THAT I REFERRED TO EARLIER IS THE INTERNATIONAL ACTUARIAL ASSOCIATION (IAA).

THE ACTUARIAL SOCIETY OF SOUTH AFRICA IS A MEMBER ASSOCIATION OF THE IAA

AND A NUMBER OF YOUR INDIVIDUAL MEMBERS ARE ACTIVELY INVOLVED IN THE WORK OF THE IAA THROUGH COUNCIL OR ITS VARIOUS STANDING COMMITTEES AND OCCASIONAL TASK FORCES.

THE IAA COMMITTEES ARE MADE UP FROM VOLUNTEER MEMBERS AROUND THE WORLD WHO BRING LOCAL COUNTRY EXPERTISE, AND VERY OFTEN, GLOBAL EXPERTISE, TO BEAR ON THE ACTIVITIES OF THE VARIOUS COMMITTEES.

THE IAA SOCIAL SECURITY COMMITTEE IS POPULATED WITH SOCIAL SECURITY EXPERTS FROM ALL REGIONS OF THE WORLD, INCLUDING ACTUARIES FROM GOVERNMENT ADMINISTRATIONS, AS WELL AS FROM THE ACADEMIC, RESEARCH AND CONSULTING COMMUNITY.

THE IAA PROVIDES THESE SOCIAL SECURITY EXPERTS WITH AN IMPORTANT FORUM TO MEET, EXCHANGE INFORMATION AND OPINIONS, AND UNDERTAKE PROJECTS AND TASKS OF A GLOBAL NATURE COVERING SOCIAL SECURITY ISSUES.

ONE IMPORTANT PROJECT THAT THE IAA SOCIAL SECURITY COMMITTEE MEMBERS UNDERTOOK IN 2006, WAS TO PREPARE A FORMAL REPORT AS A RESPONSE TO THE WORLD BANK'S PUBLICATION OF "OLD-AGE INCOME SUPPORT IN THE TWENTY-FIRST CENTURY"

THIS RESPONSE REPORT IS AVAILABLE ON THE IAA WEBSITE AND I WILL COME BACK TO THIS LATER ON TO REFER TO SOME OF THE COMMENTS IN THE RESPONSE REPORT BY THE IAA TASK FORCE OF SOCIAL SECURITY ACTUARIES.

THE FOURTH GROUP THAT I REFERRED TO EARLIER COMPRISES THE ACADEMIC, RESEARCH AND CONSULTING COMMUNITY THAT INCLUDES THE UNIVERSITIES, THINK-TANKS, AND INTERNATIONAL FIRMS OF ACTUARIES AND RELATED PROFESSIONALS.

IT IS THIS GROUP THAT OFTEN PRODUCES CREATIVE IDEAS OR NOVEL INSIGHTS OR SOLUTIONS FOR SOCIAL AND ECONOMIC POLICY CHALLENGES. THIS GROUP PROVIDES INDEPENDENT ADVICE TO POLICYMAKERS IN GOVERNMENT INSTITUTIONS, EMBRACING ECONOMIC, SOCIAL, FINANCIAL AND ACTUARIAL CONSIDERATIONS.

LET ME NOW TURN TO THE SPECIFIC PROPOSALS FOR THE FUTURE OF SOCIAL SECURITY AND RETIREMENT REFORM IN SOUTH AFRICA WITH SPECIFIC REFERENCE TO THE REPORTS FROM NATIONAL TREASURY AND THE SOCIAL DEVELOPMENT DEPARTMENT.

WE CAN CONSIDER THE PROPOSALS IN TERMS OF A THREE-TIERED STRUCTURE COMPRISING:

- BASIC SOCIAL ASSISTANCE GRANTS FUNDED FROM GENERAL GOVERNMENT REVENUE
- A MANDATORY NATIONAL SOCIAL SECURITY SYSTEM UP TO A SPECIFIC EARNINGS THRESHOLD LIMIT PROVIDING RETIREMENT, UNEMPLOYMENT, DEATH AND DISABILITY BENEFITS
- ADDITIONAL MANDATORY PARTICIPATION IN PRIVATE OCCUPATIONAL OR INDIVIDUAL RETIREMENT FUNDS FOR INDIVIDUALS ABOVE THE EARNINGS THRESHOLD OF THE SOCIAL SECURITY SYSTEM

IN ADDITION, THERE WOULD BE OPPORTUNITIES FOR SUPPLEMENTARY VOLUNTARY SAVINGS.

LET ME START BY QUOTING DIRECTLY FROM THE REPORT OF NATIONAL TREASURY WITH RESPECT TO A NUMBER OF INTERNATIONAL REFERENCES:

PARAGRAPH 5: ALTHOUGH CERTAIN FEATURES OF THE SOUTH AFRICAN SOCIAL SECURITY AND FUNDING SYSTEM COMPARE WELL WITH BOTH DEVELOPED AND DEVELOPING COUNTRIES, OTHER FEATURES ARE UNSATISFACTORY.

PARAGRAPH 7: THE REGULATORY FRAMEWORK WITHIN WHICH PRIVATE PENSIONS OPERATE IS BROADLY CONSISTENT WITH INTERNATIONAL STANDARDS.

PARAGRAPH 20: THE RATIO OF PENSION FUND ASSETS TO GROSS DOMESTIC PRODUCT (GDP) IN SOUTH AFRICA IS ABOUT 63 PERCENT, WHICH COMPARES FAVOURABLY WITH COUNTRIES SUCH AS AUSTRALIA, CHILE, MALAYSIA, SINGAPORE AND THE UNITED KINGDOM.

PARAGRAPH 25: MANY COUNTRIES THAT HAVE RELIED PREDOMINANTLY ON MANDATORY STATE-RUN FUNDING AND ADMINISTRATION IN THE PAST HAVE SOUGHT TO ENCOURAGE PARALLEL OR SUPPLEMENTARY SAVING AND INSURANCE MARKETS. THE EFFECTS OF AGEING POPULATIONS AND RISING

COSTS OF HEALTH CARE HAVE LED TO CONCERNS ABOUT SUSTAINABILITY AND AFFORDABILITY PARTICULARLY IN DEVELOPED COUNTRIES.

REFORM IN THESE COUNTRIES IS ABOUT BRINGING GREATER DIVERSITY AND PRIVATE SECTOR PARTICIPATION INTO SYSTEMS DOMINATED BY A MANDATORY EARNINGS-RELATED PILLAR.

ON THE OTHER HAND, MOST OF THE WORLD'S POOR HAVE NO ACCESS TO SOCIAL SECURITY AND CURRENT REFORM EFFORTS IN MANY DEVELOPING COUNTRIES ARE FOCUSED ON BASIC SOCIAL ASSISTANCE TO ALLEVIATE SURVIVAL-THREATENING POVERTY AND VULNERABILITY.

PARAGRAPH 26: WHILE INTERNATIONAL EXPERIENCE CARRIES IMPORTANT LESSONS, SOUTH AFRICA'S SOCIAL SECURITY REFORM CHALLENGE IS UNUSUAL IN SEVERAL RESPECTS. A REDISTRIBUTIVE SOCIAL ASSISTANCE PROGRAMME IS IN PLACE AND THERE ARE WELL-ESTABLISHED OCCUPATIONAL AND INDIVIDUAL RETIREMENT FUNDING SCHEMES, BUT SOUTH AFRICA LACKS A BASIC, POOLED, MANDATORY CONTRIBUTORY SYSTEM.

PARAGRAPH 32: INTERNATIONAL PRACTICE SUGGESTS THAT THERE ARE FOUR BROAD-BASED CRITERIA AGAINST WHICH A SOCIAL SECURITY AND RETIREMENT SYSTEM SHOULD BE ADDRESSED.

THESE ARE THE FOUR WORLD BANK CRITERIA THAT I DESCRIBED PREVIOUSLY: ADEQUACY, AFFORDABILITY, SUSTAINABILITY, AND ROBUSTNESS.

PARAGRAPH 36: THE MAIN IMPLICATIONS OF BEHAVIOURAL FACTORS IN RETIREMENT PROVISION ARE HIGHLIGHTED IN A 2004 REPORT OF THE UNITED KINGDOM PENSIONS COMMISSION:

- INDIVIDUAL DECISIONS ARE HEAVILY INFLUENCED BY DEFAULT OPTIONS;
- AN ACTION THAT REQUIRES LITTLE OR NO ONGOING DECISION-MAKING CAN BE MORE EFFECTIVE THAN INFORMATION CAMPAIGNS AND ADVICE.

PARAGRAPH 38: MANDATORY EARNINGS-RELATED CONTRIBUTIONS TO PUBLIC OR PRIVATE SCHEMES ARE A COMMON FEATURE OF PENSION SYSTEMS IN MANY COUNTRIES. THESE SYSTEMS TYPICALLY INCLUDE BOTH GUARANTEED MINIMUM BENEFITS (REDISTRIBUTIVE ELEMENTS) AND ENTITLEMENTS REPRESENTING LONG-TERM INSURANCE BENEFITS, EITHER OF A DEFINED BENEFIT OR DEFINED CONTRIBUTION KIND. ALMOST ALL MEMBERS OF THE ORGANISATION FOR ECONOMIC COOPERATION AND DEVELOPMENT (OECD) WHICH IS COMPOSED OF DEVELOPED AND MIDDLE INCOME COUNTRIES, HAVE SOME FORM OF MANDATORY EARNINGS-RELATED PROVISION, ALTHOUGH THE ARRANGEMENTS VARY CONSIDERABLY. AMONGST OECD COUNTRIES, ONLY IRELAND AND NEW ZEALAND DO NOT HAVE EITHER A PUBLIC OR PRIVATE MANDATORY SCHEME BASED ON EARNINGS-RELATED CONTRIBUTIONS.

THE MOST COMMON MANDATORY ARRANGEMENT IS A PUBLIC DEFINED BENEFITS SCHEME IN WHICH RETIREMENT BENEFITS ARE TYPICALLY CALCULATED BY REFERENCE TO YEARS OF CONTRIBUTION AND SOME MEASURE OF EARNINGS UP TO AN AGREED CAP.

MOST BUT NOT ALL PRIVATE COMPULSORY SAVINGS ARRANGEMENTS ARE DEFINED CONTRIBUTION SCHEMES IN WHICH FINAL BENEFITS RELY ON THE INVESTMENT RETURN ON ACCUMULATED CONTRIBUTIONS.

PARAGRAPH 39: THE PROPOSED INTRODUCTION OF MANDATORY RETIREMENT SAVINGS IN SOUTH AFRICA IS IN LINE WITH INTERNATIONAL PRACTICE IN THE DEVELOPMENT OF BROAD-BASED PENSION SYSTEMS.

HOWEVER, SEVERAL ALTERNATIVE FORMS OF MANDATORY PROVISION EXIST.

MOST DEVELOPED COUNTRIES HAVE MANDATORY SOCIAL SECURITY SCHEMES ESTABLISHED IN LAW AND COLLECTIVELY ADMINISTERED.

MORE RECENTLY, SEVERAL GOVERNMENTS HAVE SOUGHT TO SUPPLEMENT OR SUBSTITUTE SUCH PUBLIC PROVISION WITH MANDATORY CONTRIBUTIONS TO INDIVIDUAL ACCOUNTS IN PRIVATELY MANAGED SCHEMES.

SOME COUNTRIES HAVE ADDRESSED A SYSTEM OF AUTO-ENROLMENT, WHEREBY INDIVIDUALS ARE AUTOMATICALLY ENROLLED IN A RETIREMENT PLAN, BUT CAN STILL PRACTICE INDIVIDUAL CHOICE TO “OPT OUT”.

A VARIATION ON THIS IS TO ALLOW PEOPLE TO OPT OUT OF A PUBLIC SCHEME, PROVIDED THE INDIVIDUAL OR EMPLOYER PARTICIPATES IN A PRIVATE PENSION PLAN THAT MEETS APPROVED STANDARDS.

PARAGRAPH 53: WAGE SUBSIDIES OF ONE FORM OR ANOTHER ARE PROMINENT FEATURES OF THE EMPLOYMENT AND SOCIAL PROTECTION POLICIES OF MANY COUNTRIES TODAY.

EXAMPLES INCLUDE:

- THE EARNED INCOME TAX CREDIT IN THE UNITED STATES.
- THE TAX CREDIT FOR NEW JOB CREATION IN MEXICO
- THE SUBSIDY FOR SOCIAL SECURITY CONTRIBUTIONS OF LOW-WAGE EARNERS IN THE NETHERLANDS

SO HERE WE CLEARLY HAVE SEVERAL WELL-RESEARCHED REFERENCES TO THE BROAD SPECTRUM OF INTERNATIONAL PRACTICES.

AND NOW, FROM THIS INTERNATIONAL OVERVIEW BACKGROUND, I WOULD LIKE TO MOVE ON IN THE REMAINING AVAILABLE TIME THIS MORNING TO EXPANDING THE COMMENTARY ON THE FIRST TWO TIERS,

NAMELY THE BASIC SOCIAL ASSISTANCE GRANTS AND THE NEW CONCEPT OF A MANDATORY NATIONAL SOCIAL SECURITY SYSTEM.

TOMORROW I WILL THEN BE BACK TO TALK ABOUT THE ISSUES SURROUNDING THE PROPOSALS FOR REFORM TO THE THIRD TIER FOR ADDITIONAL MANDATORY PARTICIPATION IN PRIVATE OCCUPATIONAL OR INDIVIDUAL RETIREMENT FUNDS FOR INDIVIDUALS WITH EARNINGS ABOVE THE EARNINGS THRESHOLD FOR THE SOCIAL SECURITY SYSTEM.

AT THIS POINT IT MAY BE HELPFUL TO REVIEW THE STRUCTURES OF SOCIAL SECURITY SYSTEMS IN A FEW ILLUSTRATIVE COUNTRIES: THE UNITED STATES, CHILE, SWEDEN, NEW ZEALAND AND THE UNITED KINGDOM.

I WILL START WITH THE UNITED STATES OF AMERICA.

THE SOCIAL SECURITY BENEFIT FORMULA STARTS WITH THE EARNINGS ON WHICH THE WORKER AND EMPLOYER HAVE MADE CONTRIBUTIONS.

THIS LINK BETWEEN EARNINGS THAT HAVE BEEN TAXED UNDER THE FEDERAL INSURANCE CONTRIBUTIONS ACT, IN THE FORM OF AN EARMARKED SOCIAL SECURITY PAYROLL TAX, DURING A WORKER'S CAREER, AND THE BENEFITS THE WORKER RECEIVES AFTER RETIREMENT, ESTABLISHES AN "EARNED RIGHT" WHICH IS PART OF THE FOUNDATION OF THE PROGRAMME'S POPULAR SUPPORT.

THE US SOCIAL SECURITY SYSTEM WAS DESIGNED TO CONTAIN ELEMENTS OF BOTH INDIVIDUAL EQUITY AND SOCIAL ADEQUACY.

SOCIAL SECURITY RETIREMENT BENEFITS ARE HIGHER FOR WORKERS WITH A HISTORY OF HIGHER PRE-RETIREMENT EARNINGS BUT THE FORMULA IS TILTED SO AS TO PROVIDE A PROPORTIONATELY GREATER BENEFIT FOR LOWER-INCOME WORKERS TO HELP ACHIEVE THE AIM OF SOCIAL ADEQUACY.

THE PRIMARY SOURCE OF SOCIAL SECURITY FINANCING IS A PAYROLL TAX ON THE EARNINGS OF COVERED WORKERS UP TO A MAXIMUM ANNUAL AMOUNT, CURRENTLY \$97,500.

THE PAYROLL TAX RATE IS A FLAT 12.4 PERCENT, WITH EQUAL AMOUNTS OF 6.2 PERCENT PAID BY BOTH WORKERS AND EMPLOYERS.

THE PAY-AS-YOU-GO FINANCING ARRANGEMENT IS ESSENTIALLY AN INTERGENERATIONAL TRANSFER AND CREATES AN IMPLICIT INTERGENERATIONAL CONTRACT.

THE AMOUNT OF BASIC RETIREMENT PENSION IS COMPUTED ON THE BASIS OF A FORMULA APPLIED TO A WORKER'S RE-VALUED CAREER COVERED EARNINGS.

COVERED EARNINGS PRIOR TO AGE 60 ARE RE-VALUED ACCORDING TO AN INDEX OF NATIONAL AVERAGE WAGE LEVEL.

AVERAGE INDEXED EARNINGS ARE THEN COMPUTED OVER THE HIGHEST 35 YEARS TO PROVIDE THE AVERAGE INDEXED MONTHLY EARNINGS UPON WHICH THE BENEFIT CALCULATION IS BASED.

THE MONTHLY BENEFIT IS COMPUTED IN THREE SEGMENTS:

- 90 PERCENT OF EARNINGS UP TO \$680
- PLUS 32 PERCENT OF EARNINGS FROM \$680 TO \$4100
- PLUS 15 PERCENT OF EARNINGS ABOVE \$4100

THE BREAK-POINTS IN THIS FORMULA AT \$680 AND \$4100 ARE ADJUSTED EACH YEAR TO REFLECT CHANGES IN THE NATIONAL AVERAGE WAGE LEVEL.

AFTER BENEFITS COMMENCE PAYMENT, THEY ARE ADJUSTED EACH YEAR TO REFLECT CHANGES IN THE NATIONAL CONSUMER PRICE INDEX.

THE UNITED STATES SOCIAL SECURITY SYSTEM IS A DEFINED BENEFIT SYSTEM.

IT IS ESSENTIALLY A PAY-AS-YOU-GO SYSTEM FINANCED BY PAYROLL TAXES.

THE SYSTEM IS PROJECTED TO BE IN ACTUARIAL BALANCE WITH SUFFICIENT ASSETS AND INCOME TO MEET BENEFIT OUTGO UNTIL 2041.

ADJUSTMENTS TO TAXES OR BENEFITS WILL BE REQUIRED BEYOND 2041 TO MAINTAIN THE ACTUARIAL SOLVENCY UNLESS PARAMETRIC CHANGES ARE MADE TO BENEFITS OR CONTRIBUTIONS IN THE INTERIM. THE SYSTEM MAINTAINS A RESERVE OR "BUFFER" FUND TO ASSIST WITH STABILISING THE LEVEL OF THE PAYROLL TAX RATE.

THIS FUND IS INVESTED IN SPECIAL-ISSUE GOVERNMENT BONDS THAT PAY MARKET RATES OF INTEREST COMPARABLE TO OTHER TREASURY BONDS.

THE ADEQUACY OF THE SYSTEM MAY BE MEASURED BY THE EXTENT TO WHICH BENEFITS REPLACE PRE-RETIREMENT EARNINGS AT VARIOUS WAGE LEVELS.

THESE REPLACEMENT RATIOS ARE CURRENTLY:

- AT 56 PERCENT FOR LOW WAGE EARNERS WITH CAREER EARNINGS AT 45 PERCENT OF THE NATIONAL AVERAGE WAGE
- AT 41 PERCENT FOR MEDIUM WAGE EARNERS WITH CAREER EARNINGS AT 100 PERCENT OF THE NATIONAL AVERAGE WAGE
- AND AT 35 PERCENT FOR HIGH WAGE EARNERS WITH CAREER EARNINGS AT 160 PERCENT OF THE NATIONAL AVERAGE WAGE

- FOR WAGE EARNERS AT THE MAXIMUM COVERED EARNINGS LEVEL THE REPLACEMENT RATE IS 29 PERCENT

THE KEY POINT TO NOTE ABOUT THE BENEFIT AND CONTRIBUTION STRUCTURE IS THAT THE BENEFIT FORMULA IS TILTED SO AS TO EFFECTIVELY PROVIDE AN ELEMENT OF CROSS-SUBSIDY FROM THE HIGHER WAGE EARNERS TO THE LOWER WAGE EARNERS, BUT THAT THE FINANCING IS BY MEANS OF A LEVEL TAX RATE AT ALL COVERED EARNINGS LEVELS.

ANOTHER MUCH-QUOTED SOCIAL SECURITY SYSTEM FOR ITS DESIGN FEATURES IS THE CHILEAN SYSTEM. IN FACT THE CHILEAN SYSTEM, ADOPTED BACK IN 1981, BECAME THE ROLE MODEL FOR MANY OF THE REFORMS DEVELOPED BY THE WORLD BANK IN LATIN AMERICA AND CENTRAL EUROPE.

THERE IS TO BE A FULL-SCALE PRESENTATION AND DESCRIPTION OF THE CHILEAN SYSTEM ON THE SEMINAR PROGRAMME FOR TOMORROW MORNING, SO I WILL MAKE ONLY BRIEF REFERENCES TO ITS MOST SIGNIFICANT FEATURES.

BUT I WOULD EMPHASIZE THAT MANY EXPERTS HAVE ADOPTED STRONG ADVOCACY POSITIONS IN FAVOR OF THE CHILEAN SYSTEM WHILE MANY OTHER EXPERTS HAVE POINTED OUT THE SHORTCOMINGS, PITFALLS AND DISADVANTAGES OF THE SYSTEM.

I WILL REGARD MY ROLE TODAY AS SIMPLY TO PROVIDE A BRIEF OUTLINE OF THE CHILEAN SYSTEM'S MAIN FEATURES.

IN 1981 CHILE REFORMED ITS SOCIAL SECURITY SYSTEM IN A WAY THAT REVOLUTIONIZED THINKING ABOUT SOCIAL SECURITY. IT BECAME THE FIRST COUNTRY TO REPLACE ITS PUBLICLY MANAGED PAY-AS-YOU-GO DEFINED BENEFIT SYSTEM WITH PRIVATELY MANAGED INDIVIDUAL ACCOUNTS.

IN THE NEW SYSTEM, PRIVATE CORPORATIONS, KNOWN AS ADMINISTRADORAS DE FONDOS DE PENSIONES (AFPS) MANAGE THE INVESTMENT OF THE FUNDS.

WORKERS ARE REQUIRED TO CONTRIBUTE 10 PERCENT OF THEIR PRE-TAX EARNINGS UP TO A CEILING, TO A PRIVATE FUND OF THEIR OWN CHOOSING. THE CEILING IS INDEXED, ADJUSTED MONTHLY AT THE RATE OF INFLATION.

WORKERS CAN ALSO MAKE ADDITIONAL VOLUNTARY CONTRIBUTIONS.

AN ADDITIONAL AMOUNT IN A RANGE AVERAGING 3 PERCENT IS LEVIED TO FINANCE DISABILITY BENEFITS AND PRE-RETIREMENT SURVIVOR BENEFITS.

CONTRIBUTIONS ARE TAX DEDUCTIBLE.

EMPLOYERS DO NOT CONTRIBUTE.

EACH AFP OFFERS A CHOICE OF FIVE FUNDS RANGING IN RISK LEVEL. FOR PARTICIPANTS NOT CHOOSING AN INVESTMENT FUND, THERE IS A DEFAULT ARRANGEMENT WHERE AN APPROPRIATE FUND IS ALLOCATED BY RISK LEVEL ACCORDING TO THE PARTICIPANT'S AGE.

FOR WORKERS CONTRIBUTING FOR AT LEAST 20 YEARS, THE SYSTEM PROVIDES A GUARANTEED MINIMUM BENEFIT PROVIDED BY THE GOVERNMENT.

THE CHILEAN SYSTEM IS ESSENTIALLY A SAVINGS AND INVESTMENT PROGRAM.

AT RETIREMENT, ACCOUNT BALANCES MAY BE USED TO PURCHASE AN ANNUITY FROM A LIFE INSURANCE COMPANY THAT IS INFLATION-INDEXED,

OR THE PARTICIPANT MAY ELECT A PROGRAM OF SYSTEMATIC WITHDRAWALS FROM THE ACCOUNT THAT REMAINS INVESTED WITH THE AFP.

WE HAVE LOOKED BRIEFLY AT A DEFINED BENEFIT SOCIAL SECURITY SYSTEM AND AT A DEFINED CONTRIBUTION SYSTEM. THE US MODEL AND THE CHILEAN MODEL PROVIDE US WITH A FRAMEWORK FOR THE SPECTRUM OF DIFFERENT SYSTEMS THAT MAY BE USED AS COMPARATIVE BENCHMARKS.

I MIGHT ADD THAT IN THE EARLY YEARS AFTER THE CHILEAN REFORMS WERE INTRODUCED, THE WORLD BANK HAD ACTIVELY PROMOTED THE CHILEAN MODEL AS THE BLUEPRINT FOR SOCIAL SECURITY REFORMS OR THE INTRODUCTION OF NEW SOCIAL SECURITY SYSTEMS. IN MORE RECENT YEARS, THE WORLD BANK HAS BECOME MORE FLEXIBLE IN ADVOCATING ITS MULTI-PILLAR APPROACH THAT IT NOW REFERS TO AS "A BENCHMARK NOT A BLUEPRINT"

NEXT I WANT TO TALK ABOUT SWEDEN AND THE SWEDISH MODEL, AND IN PARTICULAR TO DESCRIBE THE CONCEPT OF NOTIONAL DEFINED CONTRIBUTIONS (NDCS) OR AS THE WORLD BANK NOW DESCRIBES THEM "NON-FINANCIAL DEFINED CONTRIBUTIONS"

PRIOR TO REFORM, SWEDEN HAD A NATIONAL SOCIAL SECURITY SYSTEM BASED ON DEFINED BENEFITS THAT PROVIDED RETIREES AT AGE 65 HAVING AT LEAST 30 YEARS OF ELIGIBLE WORK EXPERIENCE WITH INDEXED PENSIONS AVERAGING AROUND 60 TO 65 PERCENT OF PRE-RETIREMENT EARNINGS.

THE SYSTEM WAS FINANCED ON A PAY-AS-YOU-GO BASIS WITH TAX REVENUES FROM CURRENT WORKERS CONTRIBUTING TO THE PENSIONS OF THE RETIRED.

SUBSTANTIAL BUFFER FUNDS, INVESTED PRIMARILY IN SWEDISH GOVERNMENT BONDS, MINIMIZED THE EFFECTS OF VARIATIONS IN CONTRIBUTIONS, INVESTMENT RETURNS, AND BENEFITS.

BEGINNING IN 2001, SIGNIFICANT REFORMS WERE MADE TO THE SWEDISH SYSTEM. THE NEW SYSTEM IS BASED ON DEFINED CONTRIBUTIONS AND IS FINANCED BY A LEVY OF 18.5 PERCENT ON WAGES.

16 PERCENT IS ALLOCATED TO A NEW NDC SYSTEM THAT HAS AN AUTOMATIC BALANCING MECHANISM AND 2.5 PERCENT IS PLACED IN PRIVATE ACCOUNTS THAT INDIVIDUALS INVEST IN A CHOICE OF INVESTMENT FUNDS.

THE 16 PERCENT IS CREDITED INTO A NOTIONAL DEFINED CONTRIBUTION ACCOUNT, TO WHICH IS ADDED NOTIONAL INTEREST, AND THE PURPOSE OF WHICH IS TO DETERMINE THE CORRESPONDING BENEFIT PAYABLE AT RETIREMENT AND TO PROVIDE A LINK BETWEEN CONTRIBUTIONS AND BENEFITS.

THE SYSTEM REMAINS PAY-AS-YOU-GO.

THE NOTIONAL ACCOUNTS ARE NOT BACKED BY SEPARATE INDIVIDUAL ASSETS.

THE SYSTEM HAS SIMILARITIES TO AN INDEXED CAREER-AVERAGE EARNINGS DEFINED BENEFIT SYSTEM.

IT IS IMPORTANT TO NOTE THAT IN THIS TYPE OF SYSTEM, IT IS THE CONTRIBUTIONS THEMSELVES THAT CREATE BENEFIT RIGHTS AND THERE ARE NO CROSS-SUBSIDIES FROM HIGH EARNERS TO LOW EARNERS.

IN ORDER TO KEEP THE SYSTEM STABLE IN TERMS OF THE RELATIONSHIP BETWEEN CONTRIBUTIONS AND BENEFITS WITHOUT ADJUSTING THE CONTRIBUTION RATE, IT IS NECESSARY TO INTRODUCE AN AUTOMATIC BALANCING SYSTEM THAT, IN EFFECT, OPERATES BY ADJUSTMENTS TO THE BENEFIT INDEXING SYSTEM.

AND, ACCORDING TO SOME CRITICS WILL LIKELY REDUCE THE REAL VALUE OF FUTURE RETIREMENT INCOMES IN RELATION TO PRE-RETIREMENT INCOME WHEN EXPRESSED AS A PERCENTAGE REPLACEMENT RATE.

IT FOLLOWS THAT NDC PROGRAMMES FUNCTION AS EFFICIENT DEFINED BENEFIT SYSTEMS ONLY TO THE EXTENT THAT THE ADJUSTED INDEXATION PROVIDES ADEQUATE PENSION LEVELS.

THE NOTIONAL DEFINED CONTRIBUTION MODEL, OR SWEDISH MODEL, HAS BECOME THE NEW MANTRA OF SEVERAL INFLUENTIAL EXPERTS AT THE WORLD BANK, INSTEAD OF THE MANDATORY FUNDED INDIVIDUAL ACCOUNT MODEL, OR CHILEAN MODEL.

IT SHOULD ALSO BE POINTED OUT IN RELATION TO SWEDEN, THAT ONLY 2.5 PERCENT OF THE 18.5 PERCENT CONTRIBUTION RATE IS ACTUALLY DESIGNATED FOR INVESTMENT IN INDIVIDUAL ACCOUNTS.

IN COMMENTING ON NDCS IN RESPONSE TO THE WORLD BANK'S 2005 REPORT, THE INTERNATIONAL ACTUARIAL ASSOCIATION STATED; "PAY-AS-YOU-GO SYSTEMS CAN QUICKLY BE INTRODUCED INTO DEVELOPING COUNTRIES SINCE IN THIS WAY PENSIONERS CAN PARTAKE IN ECONOMIC ADVANCE, BUT THE SWEDISH MODEL IS NOT SUITABLE FOR LESS DEVELOPED ECONOMIES.

THE IAA REPORT ALSO STATES: "NDC SHOULD NOT BE USED AS A PALLIATIVE TO GIVE A PERCEPTION OF FUNDING WHEN REAL FUNDING IS NOT DEEMED APPROPRIATE"

WE HAVE LOOKED AT THE UNITED STATES, CHILE AND SWEDEN AS MAJOR REFERENCE POINTS IN THE GLOBAL SOCIAL SECURITY LANDSCAPE.

I WOULD LIKE NOW TO TURN TO NEW ZEALAND AS ANOTHER IMPORTANT REFERENCE COUNTRY AND THEN BRIEFLY REFER TO THE UNITED KINGDOM REFORMS.

NEW ZEALAND HAS ATTRACTED A LOT OF ATTENTION DUE TO THE INTRODUCTION OF THE KIWI SAVER FEATURE AS A GOVERNMENT INITIATIVE TO INCREASE INDIVIDUAL SAVINGS AND SUPPORT NEW ZEALANDERS IN RETIREMENT.

NEW ZEALAND HAS A BASIC SUPERANNUATION SYSTEM THAT PROVIDES A BASIC PUBLIC PENSION IN THE FORM OF A UNIVERSAL BENEFIT PAID TO ALL RESIDENTS OVER THE AGE OF 65 AND THAT IS INDEXED ANNUALLY, NOT SUBJECT TO AN INCOME TEST OR A MEANS TEST, NOT RELATED TO PAST EARNINGS HISTORY AND IS NOT A CONTRIBUTORY SCHEME.

A MARRIED COUPLE EACH RECEIVE A PENSION OF 32.5 PERCENT OF THE NATIONAL AVERAGE WAGE, OR 65 PERCENT TOGETHER.

SINGLE PERSONS RECEIVE A PENSION OF APPROXIMATELY 40 PER CENT OF THE NATIONAL AVERAGE WAGE.

KIWI SAVER IS A VOLUNTARY WORK-BASED SAVINGS PROGRAM.

IT APPLIES TO ALL NEW ZEALAND CITIZENS AND PERMANENT RESIDENTS BELOW AGE 65.

THE CONTRIBUTION RATE OF 4 PERCENT IS THE DEFAULT RATE, WITH AN OPTION TO CHOOSE 8 PERCENT. CONTRIBUTIONS ARE MADE BY PAYROLL DEDUCTION AND INVESTED WITH PRIVATE SECTOR PROVIDERS. NEW EMPLOYEES ARE ENROLLED AUTOMATICALLY BUT PARTICIPATION IS VOLUNTARY WITH AN "OPT OUT" PROVISION.

CONTRIBUTIONS ARE LOCKED IN UNTIL AGE 65 BUT MAY BE ACCESSED FOR THE PURPOSE OF A FIRST HOME PURCHASE.

CONTRIBUTION HOLIDAYS TO SUSPEND CONTRIBUTIONS ARE PERMITTED.

THE KIWI SAVER IS REPORTED TO HAVE BEEN AN INSPIRATION FOR A PART OF PROPOSED PENSION REFORM IN THE UNITED KINGDOM.

OFFICIAL UK REPORTS ON PENSION REFORM STATE THAT THE FIRST PRIORITY OF THE UK REFORMS IS TO FACILITATE PERSONAL SAVING FOR RETIREMENT.

A NEW UK SYSTEM OF PERSONAL ACCOUNTS WILL BE INTRODUCED IN 2012.

THERE WILL BE AUTOMATIC ENROLLMENT FOR ALL EMPLOYEES INTO EITHER A NATIONAL PERSONAL ACCOUNTS SYSTEM OR THEIR EMPLOYER'S OCCUPATIONAL SYSTEM.

EMPLOYEES WILL CONTRIBUTE 4 PERCENT OF COVERED EARNINGS AND EMPLOYERS WILL MAKE CONTRIBUTIONS OF 3 PERCENT ON THE SAME EARNINGS.

AN ADDITIONAL ONE PERCENT OF EARNINGS WILL BE CONTRIBUTED INTO THE PERSONAL ACCOUNTS REPRESENTING THE VALUE OF TAX RELIEF FOR THE EMPLOYEE'S CONTRIBUTIONS.

ALTHOUGH ENROLLMENT IS AUTOMATIC, EMPLOYEES WILL BE ABLE TO OPT OUT OF THE SYSTEM AND WILL THEN FORFEIT THE EMPLOYER CONTRIBUTIONS THAT WOULD OTHERWISE BE PAYABLE.

WELL, WE HAVE NOW TAKEN A LOOK AT THE UNITED STATES, CHILE, SWEDEN, NEW ZEALAND AND THE UNITED KINGDOM AS WELL AS DISCUSSING THE ROLES OF THE WORLD BANK AND THE INTERNATIONAL LABOUR ORGANISATION.

IN THE REMAINING MINUTES, I WILL FOCUS ON CERTAIN ASPECTS OF THE PROPOSED SOCIAL SECURITY REFORMS FOR SOUTH AFRICA.

THE KEY RECOMMENDATIONS CONTAINED IN CHAPTER 3 OF THE DEPARTMENT OF SOCIAL DEVELOPMENT'S RECENT DISCUSSION DOCUMENT ON REFORM OF RETIREMENT PROVISIONS ARE:

- THE STATE OLD AGE PENSION TO BE CHANGED FROM A MEANS-TESTED SOCIAL ASSISTANCE PROGRAMME TO A UNIVERSAL NON-CONTRIBUTORY BENEFIT AVAILABLE TO ALL CITIZENS AND QUALIFYING RESIDENTS.
- A MANDATORY CONTRIBUTORY SYSTEM TO BE INTRODUCED WITH CONTRIBUTIONS MANDATED FROM AGE 25 FOR ALL INCOME EARNERS. CONTRIBUTIONS TO BE SET AT 15 PERCENT OF PRE-TAX INCOME.
- ACCREDITED RETIREMENT FUNDS WOULD NEED TO MEET SPECIFIED STANDARDS.
- A GOVERNMENT SPONSORED RETIREMENT FUND TO BE INTRODUCED AS THE DEFAULT RETIREMENT PROVIDER
- TWO TIERS OF MANDATORY CONTRIBUTION TO APPLY. THE FIRST TIER, WITH 50 PERCENT OF THE CONTRIBUTION, SHOULD APPLY TO A PAY-AS-YOU-GO DEFINED BENEFIT SYSTEM OFFERED VIA THE GOVERNMENT SPONSORED RETIREMENT FUND.
- THIS PAY-AS-YOU-GO TIER SHOULD BE FORMULA BASED WITH AUTOMATIC ADJUSTMENTS IN BENEFITS IF THE RATIO OF CONTRIBUTIONS TO BENEFICIARIES CHANGES.
- DEATH AND DISABILITY ALSO TO BE COVERED.
- THE SECOND TIER OF MANDATORY CONTRIBUTION WOULD APPLY TO A DEFINED CONTRIBUTION BENEFIT FULLY FUNDED THROUGH THE GOVERNMENT SPONSORED RETIREMENT FUND OR AN ACCREDITED FUND.

- IN COMBINATION THE TWO COMPONENTS OF THE FULL MANDATORY TIER ARE TO TARGET A REPLACEMENT RATE OF 40 PERCENT OF EARNINGS, INCLUDING THE STATE OLD AGE PENSION.
- FUNDING FOR POST-RETIREMENT MEDICAL SCHEME CONTRIBUTIONS TO BE INCORPORATED INTO THE PAY-AS-YOU-GO PORTION OF THE MANDATORY CONTRIBUTION.

WHEN COMPARING THESE KEY RECOMMENDATIONS WITH THE BROAD SPECTRUM OF RELEVANT INTERNATIONAL PRACTICES, IT WOULD APPEAR APPROPRIATE TO CONSIDER THE FOLLOWING POINTS:

- ALTHOUGH IT IS PRECISELY CONSISTENT WITH THE ILO STANDARD, THE TARGET REPLACEMENT RATE OF 40 PERCENT INCLUDING THE STATE OLD AGE PENSION MIGHT BE MODIFIED TO A SLIDING OR TILTED SCALE TO GIVE A HIGHER PERCENTAGE REPLACEMENT RATE FOR LOW-INCOME EARNERS AND A LOWER PERCENTAGE REPLACEMENT RATE FOR HIGH-INCOME EARNERS. THE EXAMPLE THAT I QUOTED EARLIER FROM THE UNITED STATES SOCIAL SECURITY SYSTEM INVOLVED A PRIMARY BENEFIT FORMULA THAT COMPUTED THE BENEFIT AS 90 PERCENT ON THE FIRST TRANCHE OF EARNINGS, PLUS 32 PERCENT ON THE SECOND TRANCHE OF EARNINGS, AND PLUS 15 PERCENT ON THE THIRD TRANCHE OF EARNINGS. THIS FORMULA PROVIDES REPLACEMENT RATIOS OF 56 PERCENT FOR LOW-WAGE EARNERS, 41 PERCENT FOR AVERAGE WAGE EARNERS, AND 35 PERCENT FOR HIGH WAGE EARNERS, SO AS TO EFFECTIVELY DELIVER A CROSS-SUBSIDY FROM HIGH EARNERS TO LOW EARNERS.
- THE MANDATORY CONTRIBUTION RATE OF 15 PERCENT TO COVER BOTH A PAY-AS-YOU-GO DEFINED BENEFIT ARRANGEMENT AND AN ADDITIONAL DEFINED CONTRIBUTION ARRANGEMENT APPEARS TO FALL WITHIN A REASONABLE RANGE WHEN COMPARED TO INTERNATIONAL PRACTICE. I PREVIOUSLY QUOTED A RATE OF 12.4 PERCENT FOR THE UNITED STATES DEFINED BENEFIT SOCIAL SECURITY SYSTEM, AND WITH RESPECT TO CHILE I QUOTED A RATE OF 10 PERCENT FOR THE INDIVIDUAL SAVINGS PORTION PLUS APPROXIMATELY 3 PERCENT FOR DISABILITY AND DEATH BENEFITS. I THEN QUOTED 18.5 PERCENT FOR SWEDEN. THE RATES I QUOTED FOR NEW ZEALAND AND THE UNITED KINGDOM RELATE ONLY TO THE SUPPLEMENTAL DEFINED CONTRIBUTION TIER. IN THE UNITED STATES SYSTEM, THE CONTRIBUTION IS PAID EQUALLY BY EMPLOYEE AND EMPLOYER. IN CHILE ONLY THE EMPLOYEE PAYS CONTRIBUTIONS. IN THE UNITED KINGDOM, THE PROPOSED NEW MANDATORY SAVINGS ARRANGEMENT IS DESIGNED TO ENCOURAGE BOTH EMPLOYEE AND EMPLOYER PARTICIPATION WITH 4 PERCENT AND 3 PERCENT RATES RESPECTIVELY PLUS AN ADDITIONAL ONE PERCENT FROM TAX CREDITS.

- THE QUESTION OF WHETHER THE RECOMMENDED 15 PERCENT CONTRIBUTION IN SOUTH AFRICA IS TO BE SHARED BETWEEN EMPLOYER AND EMPLOYEE RAISES MANY STRATEGIC POLICY QUESTIONS WITH IMPORTANT ECONOMIC CONSEQUENCES TO BE ADDRESSED. WHILE THE ISSUE OF PROVIDING DIRECT WAGE SUBSIDIES HAS ALSO BEEN PROPOSED, THE ECONOMIC CONSEQUENCES OF DIVERTING THE 15 PERCENT PROPOSED CONTRIBUTION INTO A 50 PERCENT PARTIAL INTERGENERATIONAL TRANSFER AND A 50 PERCENT PARTIAL SAVINGS FOR DEFERRED CONSUMPTION WILL HAVE MANY ECONOMIC RAMIFICATIONS.
- ON THE ONE HAND, THERE IS A VIEW THAT A 15 PERCENT MANDATORY CONTRIBUTION FALLS ON THE EMPLOYER AS A PART OF THE COST OF EMPLOYED LABOUR AND THAT THE INTRODUCTION OF A MANDATORY CONTRIBUTORY SOCIAL SECURITY SYSTEM MERELY RE-ALLOCATES THE FLOW OF CASH RESOURCES TO EMPLOYEES OVER THEIR LIFETIMES TO EFFECT A SMOOTHING OF CONSUMPTION AND ALLEVIATION OF POVERTY IN OLD AGE.
- ON THE OTHER HAND, THERE IS LIKELY TO BE CONCERN EXPRESSED, PARTICULARLY BY TRADE UNIONS, REGARDING THE EFFECTS OF REDUCED NET TAKE-HOME PAY AND THE EXTENT OF REMAINING AVAILABLE DISCRETIONARY INCOME FOR CURRENT SPENDING.
- THESE ARGUMENTS MAY WELL LEAD TO A DEBATE OVER REQUIRING EMPLOYER CONTRIBUTIONS AS A PART OF THE MANDATORY CONTRIBUTION STRUCTURE, COMBINED WITH FEATURES TO ENABLE “OPTING OUT” WHERE THE EMPLOYER IS PROVIDING A SCHEME OF BENEFITS OR CONTRIBUTIONS OF EQUIVALENT VALUE.
- THE INCLUSION OF DEATH AND DISABILITY BENEFITS IS CONSISTENT WITH THE PRINCIPLES AND OBJECTIVES OF THE INTERNATIONAL LABOUR ORGANISATION.
- THE RECOMMENDATION THAT THE PAY-AS-YOU-GO TIER SHOULD BE FORMULA BASED WITH AUTOMATIC ADJUSTMENTS IN BENEFITS IF THE RATIO OF CONTRIBUTORS TO BENEFICIARIES CHANGES WILL DOUBTLESS BE REFINED AND DEVELOPED MORE FULLY IN THE PERIOD LEADING UP TO IMPLEMENTATION. THERE WILL BE MANY ISSUES TO BE RESEARCHED AND RESOLVED WHERE INTERNATIONAL EXPERIENCE MAY BE HELPFUL. A NUMBER OF KEY QUESTIONS WILL PROBABLY ARISE:
 - WHAT IS THE INITIAL FORMULA FOR DETERMINING PROJECTED BENEFITS?
 - WHAT MEANS OF INDEXING WILL BE APPLIED TO EARNINGS FOR THE PURPOSE OF DETERMINING BENEFITS AND WHAT MEANS OF INDEXING WILL BE APPLIED TO ADJUST BENEFITS IN PAYMENT FROM TIME TO TIME?

- WILL THE SYSTEM BE EXPECTED TO BE MAINTAINED IN CLOSE ACTUARIAL BALANCE? IF SO, OVER WHAT PERIOD OF PROJECTION, AND WHAT TRIGGER MECHANISM WILL BE USED TO ADJUST BENEFITS IF AND WHEN THE SYSTEM BECOMES OUT OF CLOSE ACTUARIAL BALANCE DUE TO CHANGES IN THE RATIO OF CONTRIBUTORS TO BENEFICIARIES OR FOR OTHER REASONS? IN THIS REGARD SWEDEN HAS THE MOST REFINED AND ELABORATE AUTOMATIC BALANCING MECHANISM. IN OTHER COUNTRIES, FORMAL CHANGES TO THE PARAMETERS OF THE SYSTEM ARE MADE BY STATUTE FROM TIME TO TIME FOLLOWING SPECIAL REVIEWS AND LEGISLATIVE ACTION TO APPROVE THE CHANGES.
- WITH RESPECT TO THE PROPOSAL FOR THE SECOND TIER OF THE MANDATORY CONTRIBUTION TO BE APPLIED TO ACCUMULATE A DEFINED CONTRIBUTION BENEFIT FULLY FUNDED THROUGH THE GOVERNMENT SPONSORED RETIREMENT FUND OR AN ACCREDITED FUND, INTERNATIONAL EXPERIENCE SHOWS THAT MANY INDIVIDUALS WILL SIMPLY ELECT THE DEFAULT FUND, PARTICULARLY IF FACED WITH A WIDE RANGE OF CHOICES. IN CHILE THE NUMBER OF CHOICES IS LIMITED AND THE AVAILABLE FUNDS ARE IDENTIFIED BY RISK LEVEL AS BEING APPROPRIATE AT VARIOUS AGES. IN SWEDEN SOME 600 FUNDS ARE MADE AVAILABLE AND AS A RESULT, MOST INDIVIDUALS ELECT THE DEFAULT FUND.

THAT ABOUT BRINGS US TO THE END OF OUR AVAILABLE TIME THIS MORNING.

I WILL BE BACK HERE AGAIN TOMORROW MORNING TO EXPLORE VARIOUS RETIREMENT MATTERS MORE SPECIFICALLY RELATED TO THE PROVISION OF BENEFITS ABOVE THE LEVEL PROVIDED BY THE PROPOSED NEW 15 PERCENT MANDATORY CONTRIBUTION SYSTEM. THANK YOU.