

ICELAND

Iceland: pension system in 2006
The public pension has three components: a basic and two income-tested schemes. There are also mandatory occupational pensions with a hybrid (albeit mainly defined-benefit) formula.

Key indicators		Iceland	OECD
Average earnings	ISK(million)	3.48	2.50
	USD	49 800	35 800
Public pension spending	% of GDP	2.0	7.2
Life expectancy	at birth	81.2	78.9
	at age 65	84.5	83.4
Population over age 65	% of working-age population	19.5	23.8

Qualifying conditions

The normal pension age is 67. A full basic pension is earned with 40 years' residency. The pension is proportionally reduced for shorter periods of residency, with a minimum of three years required. The pension age is also 67 for members of private-sector occupational plans but is 60 for seamen who have been working in this occupation for at least 25 years.

Benefit calculation

Basic

The full basic pension value is ISK 24 131 per month, equivalent to around 8% of average earnings. This benefit is income-tested: withdrawal begins once income (from sources other than the supplementary pension) exceeds ISK 1 998 438, equivalent to 57% of average earnings, and lapses at ISK 2 963 678. This income test applies only to non-pension income, such as earnings from work or social assistance as well as 50% of capital income.

Targeted

A second element is the pension supplement. The maximum value of this benefit is ISK 44 838 per month for a single person, some 15% of average earnings. This benefit is withdrawn against income above ISK 607 850 per year (around 17% of average earnings). The basic pension, however, does not affect the value of the pension supplement. The withdrawal rate for the income test in the pension supplement is 45%.

Finally, there is an additional pension supplement with a maximum entitlement of ISK 22 109 per month, just under 8% of average earnings. This is withdrawn against all other income at a rate of 45% and lapses at a level of 589 573.

The benefit levels are adjusted annually in accordance with the current State Budget. Adjustments are to take account of public-sector pay (which is assumed here to be equal to the standard assumption of economy-wide earnings growth) and the price level pursuant to the cost-of-living index.

Mandatory occupational

Employer schemes are mandatory. The law requires schemes to target a replacement rate of 56% with 40 years' contributions, giving an accrual rate of 1.4% for each year of service. Coverage is mandatory for people aged 16 to 70. The earnings base in this calculation is average lifetime salary for each year of membership. There is no ceiling to pensionable earnings. Past earnings are valorised in line with price inflation plus 3.5% interest rate.

Occupational pensions in payment must by law be increased in line with consumer price inflation.

In practice, many schemes pay more than the legal minimum outlined above, typically introducing a hybrid defined-contribution/defined-benefit element into the system. There is a minimum contribution to occupational schemes of 12% of earnings. The employee pays 4% and the employer 8%. Contributions above the level needed to finance the statutory benefits described above can be used either to increase defined-benefit entitlements or diverted to individual accounts thus delivering a defined-contribution pension. However, the modelling covers only the mandatory component and not these extra-statutory benefits as they are not guaranteed.

Variant careers

Early retirement

Under the mandatory occupational scheme, early retirement rules vary between funds, depending on the structure of fund membership. In the private sector, the normal retirement age is 67 and the pension can be claimed from 62. In general, pensions are reduced by 7% for each year that pension is claimed early.

It is not possible to claim the basic or targeted pensions before the normal pension age.

Late retirement

Under the mandatory occupational scheme, workers can postpone retirement until the age of 70 with a pension increase of 9% for each year of deferral. Workers who defer their pension continue to contribute and earn extra pension entitlements. In some cases, the total contribution period is limited to 32 years.

It is not possible to defer the basic or targeted pension after normal pension age. The basic pension is subject to an earnings test (see above), while the targeted schemes are tested against all income, including earnings.

Childcare

The residency-tested basic pension and the targeted schemes automatically protect women who leave paid work to care for children. There are no specific credits for childcare absences. The occupational pension funds themselves make no provisions for women who must leave work to care for children. The government social assistance scheme contains benefits for parents (men or women) who must take care of children with long-term illnesses or disabilities. Such benefits are also provided in cases where people must take care of close relatives (*e.g.* adult son or daughter taking care of aged parent).

Unemployment

The contribution base, on which the minimum 10% contribution is levied, includes unemployment insurance benefits as well as earnings but excludes all other benefits.

Personal income tax and social security contributions

Taxation of pensioners

Pensioners are taxed in the same way as people of working age; there are no additional allowances.

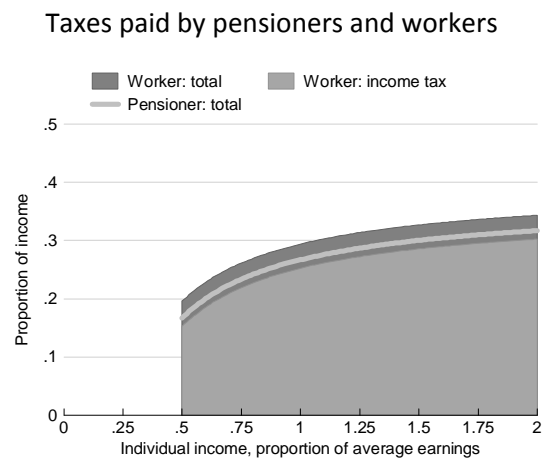
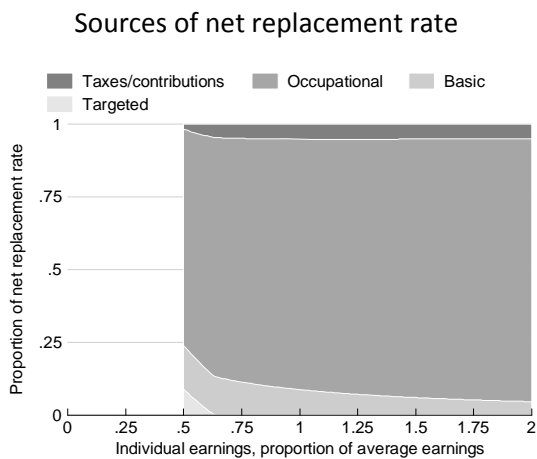
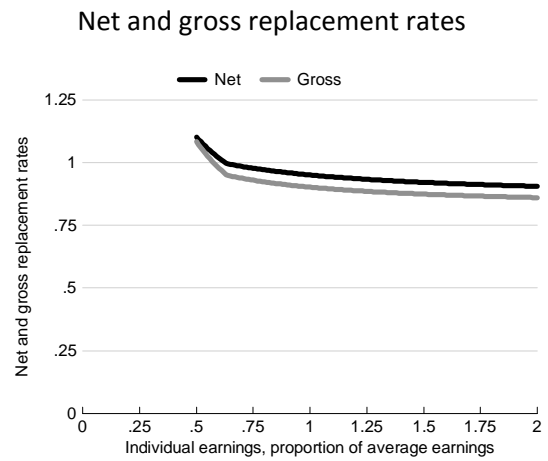
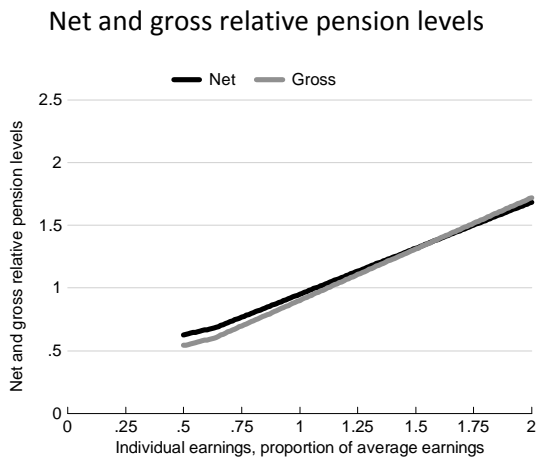
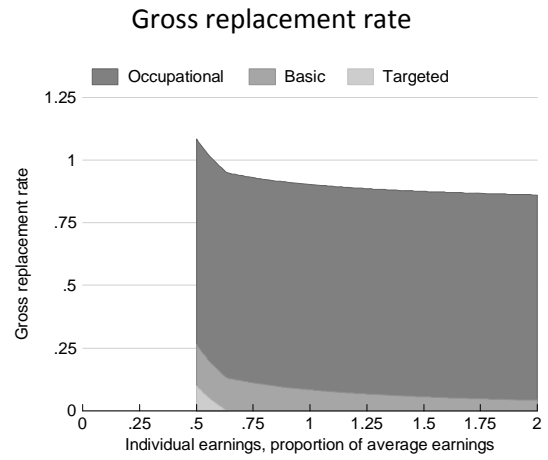
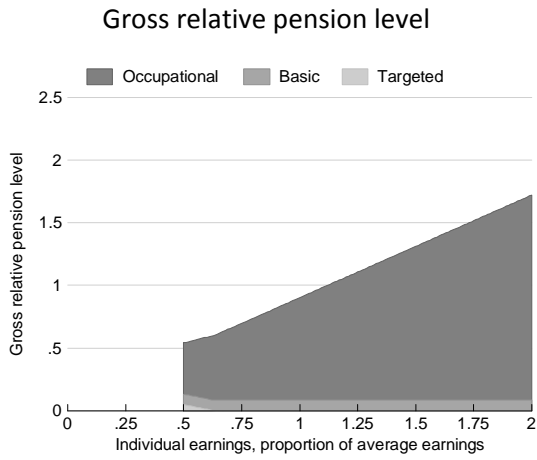
Taxation of pension income

There is no specific relief for pension income.

Social security paid by pensioners

Pensioners as well as wage earners do not pay social security contributions.

Pension modelling results: Iceland



Men Women (where different)	Median earner	Individual earnings, multiple of average				
		0.5	0.75	1	1.5	2
Gross relative pension level (% average gross earnings)	77.9	54.2	69.8	90.2	131.2	172.1
Net relative pension level (% net average earnings)	84.1	62.7	76.7	95.1	131.8	168.5
Gross replacement rate (% individual gross earnings)	91.7	108.3	93.0	90.2	87.5	86.1
Net replacement rate (% individual net earnings)	96.5	110.1	97.7	95.1	92.1	90.6
Gross pension wealth (multiple of average gross earnings)	14.0 15.7	17.0 19.1	14.2 15.9	13.7 15.4	13.2 14.8	12.9 14.5
Net pension wealth (multiple of average net earnings)	10.6 11.9	13.9 15.6	11.0 12.4	10.2 11.4	9.3 10.5	8.9 10.0