# DENMARK

**Denmark: pension system in 2006**

There is a public basic scheme (public old age pension, "folkepension") which consists of a basis amount and an income-tested pension supplement. A means-tested supplementary pension benefit is paid to the financially most disadvantaged pensioners. There are also two schemes based on individuals' contribution records, the ATP (the Danish labour market supplementary pension) and the SP (the special pension savings scheme). In addition, compulsory occupational schemes negotiated as part of collective agreements cover about 90 % of the full-time employed workforce.

**Key indicators**

| | | Denmark | OECD |
|---|---|---|---|
| Average earnings | DKK | 330 900 | 212 700 |
| | USD | 55 700 | 35 800 |
| Public pension spending | % of GDP | 5.4 | 7.2 |
| Life expectancy | at birth | 78.4 | 78.9 |
| | at age 65 | 82.7 | 83.4 |
| Population over age 65 | % of working-age population | 25.3 | 23.8 |

## Qualifying conditions

The normal pension age is currently 65 but will be increased gradually to age 67 in the period 2024-27. A full public old-age pension requires 40 years' residence. Shorter periods qualify for a pro-rated benefit.

A full entitlement under the labour-market supplementary pension (ATP) and the special saving scheme (SP) requires a full career of contributions. The ATP scheme was established in 1964. The ATP scheme is a collective insurance-based DC scheme. The SP scheme was established in 1999. SP is a statutory, purely savings-based scheme, where contributions are paid to individuals accounts.

## Benefit calculation

### *Basic*

The full basic pension amount is DKK 4 836 per month or DKK 58 032 per year, equivalent to 17.5% of average earnings. There is an individual earnings test which means that the basic pension will be reduced if work income exceeds DKK 246 500 (approximately three-quarters of general earnings per year for an average production worker). The benefit is reduced at a rate of 30% against earned income above this level.

### *Targeted*

The full pension supplement is DKK 4 868 per month or DKK 58 416 per year for single persons and DKK 27 276 per year for couples. The actual amounts are tested against all sources of personal income (including ATP, SP and occupational pensions) apart from public pension. If personal income exceeds DKK 54 400, the targeted pension supplement is reduced by 30% of the excess income for single persons. For couples this income test is calculated of income beyond DKK 109 200 at a rate of 15%.

Connected with the public old-age pension, a new supplementary pension benefit of DKK 6 300 (2006) was introduced in 2004. The supplementary pension benefit is taxable and paid once a year. The benefit is means-tested and targeted to the poorest pensioners without significant cash savings (max cash savings DKK 56 800).

The public old-age pension (the basic and targeted amounts plus the pension supplement) and the supplementary pension benefit are adjusted annually in line with average earnings. The adjustment is based on an index of wage increases during the two preceding years. If nominal earnings growth exceeds 2%, a maximum of 0.3 percentage points of the excess increase is allocated to a social spending reserve. Thus, indexation of pensions and other social benefits is based upon wage increases less any allocation to the reserve.

***Occupational***

These schemes are fully funded defined-contribution schemes agreed between the social partners. Coverage of these schemes is almost universal. Contributions are typically between 9% and 17% of earnings. In 2006, the percentage for the majority of Danish workers has been raised to 10.8% and this contribution rate is used for the modelling. Benefits are usually withdrawn as an annuity. The assumed interest rate is 1.5% for recent contributions or new schemes. However, the schemes operate on a "with-profit" basis, with pension increases depending on the return on assets and mortality experience of the fund. Many schemes also allow lump sum withdrawals. Since 2000, the annuity calculation must use unisex mortality tables.

***Defined contribution***

ATP is a statutory, fully funded, collective insurance based, defined-contribution scheme. ATP provides a lifelong pension from the age of 65 and a survivors' lump sum benefit for dependents in the case of the death of the individual member. ATP covers all wage earners and almost all recipients of social security benefits. ATP membership is voluntary for the self-employed. ATP covers almost the entire population and comes close to absolute universality.

Technically, the old age pension of ATP is a guaranteed deferred annuity. The contribution is a fixed amount – as opposed to a percentage of income – varied only against the number of hours worked. A full-time employee paid DKK 2 924 in 2006. Contributions are split with two-thirds paid by the employer and one-third by the worker. The contribution schedule (the sum of employer and employee contribution) against hours worked is shown in the following table (for monthly paid workers):

| Monthly hours | <39 | 39-77 | 78-116 | >116 |
|---|---|---|---|---|
| Contribution, DKK/month up until 2009 | 0 | 81.3 | 162.6 | 243.9 |
| Contribution, DKK/month as from 2009 | 0 | 90 | 180 | 270 |

The contribution is adjusted if and when the social partners decide to do so as part of collective agreements. Over the past 20 years the contribution has been increased in steps more or less in line with average earnings. The modelling assumes that the contribution will increase in line with average earnings. An increase of approximately 10% has been agreed for 2009.

Until 2002, each DKK 396 of contributions earned DKK 100 of pension benefits paid from 65 regardless of the age at which they were made. This implied an average (across all accruing cohorts) interest rate of around 4.5%. From 2002, a nominal interest rate of 1.5% has been assumed. In the model, it is assumed that the ATP earns the same interest rate as assumed for funded defined-contribution schemes in other OECD countries.

The ATP scheme increases pensions in payment and pension rights alike if its financial condition allows. This is done in the form of bonus allowances. Increases are guaranteed as are earned rights.

The modelling assumes full indexation to price inflation.

An entirely new ATP pension accrual system has been introduced as from 2008. The model is based on swap interest rates as opposed to a fixed nominal interest rate of *e.g.* 1.5 %.

***Defined contribution (Special pension, SP)***

Employees, self-employed and recipients of unemployment and sickness benefits contribute 1% of earnings to this mandatory individual retirement savings scheme. Investments are currently managed centrally. As from 2005, members have been able to choose their manager and portfolio. There is no ceiling to earnings covered by this scheme. Benefits are paid at normal pension age. If the account balance is less than DKK 15 000, it is paid as a lump sum and taxed at 40%. If it is between DKK 15 000 and DKK 120 000, the balance is paid out over a period of ten years. If the balance is more than DKK 120 000 at normal pension age, the balance is paid out periodic monthly over ten years Periodic payments are taxed as personal income.

As part of agreements, contributions to the SP scheme have been suspended since 2004. The model takes a long-term perspective and so assumes that SP contributions resume.

## Variant careers

***Early retirement***

There is a partial early retirement pension for workers aged between 60 and 65 who continue to work for 12 to 30 hours a week. The scheme is being phased out. It now applies only for workers born before 1 January 1959. The beneficiary must reduce weekly hours worked by at least seven hours a week or at least one quarter of total hours worked in an average week. The partial pension is calculated as a fixed amount for every hour that is reduced. The amount is approximately DDK 76 an hour for 2007. Since 1999 beneficiaries are subject to a pension deduction.

There is also a voluntary early retirement programme linked with unemployment insurance, which pays benefits between ages 60 (gradually increased to age 62 in the period 2019-22) and until the normal pension age. To qualify, individuals must have been members of the unemployment insurance fund for at least 25 years within the last 30 years and have paid voluntary early-retirement contributions during this period. They must also satisfy the conditions for entitlement to unemployment benefits in the event of unemployment at the time of transition to the voluntary early-retirement scheme. The benefit amount corresponds to the rate of unemployment benefits, subject to a limit of 91% of the maximum rate of unemployment benefit, equivalent to DKK 3 110 per week for full-time workers and DKK 2 075 or part-time workers (2006 figures). It is not possible to combine receipt of voluntary early-retirement benefits with the social pension.

People who defer the take up of voluntary early-retirement benefits for at least two years after they have become entitled to the benefit and are still working receive a higher rate of voluntary early-retirement benefit that is equivalent to the maximum rate of unemployment benefit (or DKK 3 415 per week in 2006). For three years' full-time work when an individual qualifies for voluntary early retirement or the equivalent, a one-off lump-sum is paid up to a maximum of DKK 124 860 in 2006.

People covered by either early-retirement programme revert to the standard old-age pension once they reach the normal retirement age of 65 (due to their age they will not be affected by the legislated rise in the retirement age in the period 2024-27).

***Late retirement***

It is possible to defer the public old age pension for up to ten years. The increment for deferring pension for a year is the ratio of the period of deferral to average life expectancy at the time the pension is drawn. For example, the World Bank/UN population projections show life expectancy for a

68-year old to be 17.1 years. Thus, the increment for deferring for a year from age 67 would be 1/17.1 = 5.8%.

***Childcare***

For periods on maternity/paternity/parental benefits, the double amount of contributions is paid for ATP. The beneficiary will pay one-third of the contribution, two-thirds is paid by the government/municipality. Maternity/paternity/parental benefits can be paid for up to 52 weeks in total. Four weeks prior to the birth and the first 14 weeks after the birth are reserved for the mother. The father is entitled to two weeks of leave during the first 14 weeks after the birth (paternity leave). The last 32 weeks can be divided or shared between the father and the mother (parental leave). Those out of the labour market caring for children beyond the maternity period typically switch to another scheme which also carries an ATP contribution. Young parents usually resume work when the leave period ends unless the child is *e.g.* ill or disabled in which cases there normally will be possibilities for drawing on some sort of public benefit with contribution to ATP. Parents on maternity/paternity/parental benefits have contributed to SP and will do so again when the SP contributions resume. There are no credits or contributions for occupational pension schemes for periods out of paid work caring for children.

***Unemployment***

During unemployment, the unemployment insurance (or municipality if not insured) take over the payment obligation of employer and ATP contributions are paid at the double rate when receiving benefit from the unemployment insurance (normal rate if social assistance benefit). The government pays two-thirds of the payment when unemployment insurance is exhausted and the individual is on unemployment/social assistance. There are no credits or contributions for occupational pension schemes for periods of unemployment.

## Personal income taxes and social security contributions

***Taxation of pensioners***

There are no special tax allowances or credits for pensioners. Pensioners can receive a tax credit for the property value tax.

***Taxation of pension income***

Periodic pension payments are subject to personal income tax. There are no special reliefs for pension income.

The ATP, the SP, occupational pensions and other private pension savings are subject to an ETT tax regime.

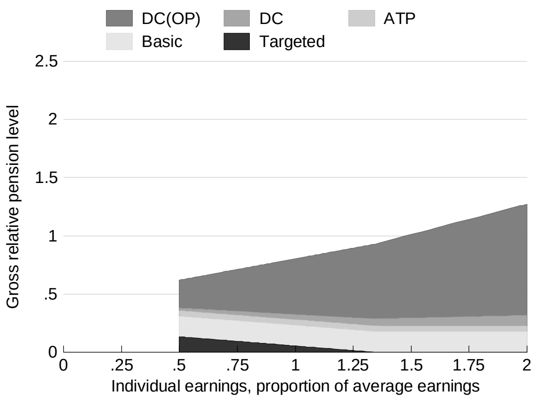
The payment under a funded pension scheme is subject to a flat tax at 40% on lump-sum withdrawals. Since 1984, the return on assets in pension schemes has been subject to a special tax. From 1984 to mid-1998, returns on bonds were taxed at a variable rate. The rate depended on the interest rate and inflation (*i.e.*, real-interest tax). The rate ranged between 40 and 50% for most of the period. From mid-1998, the return on equities was taxed at 5%. In 2000, the tax was changed to a fixed rate of 26% on bond returns and 5% on equities. Since 2001, all returns from the pension savings are taxed at 15%.

***Social security contributions paid by pensioners***

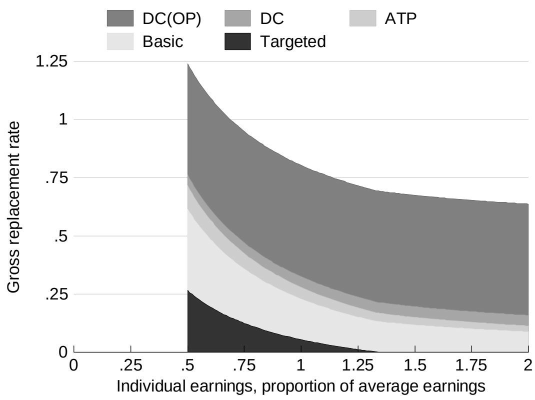
Pensioners do not pay social security contributions.

**Pension modelling results: Denmark**

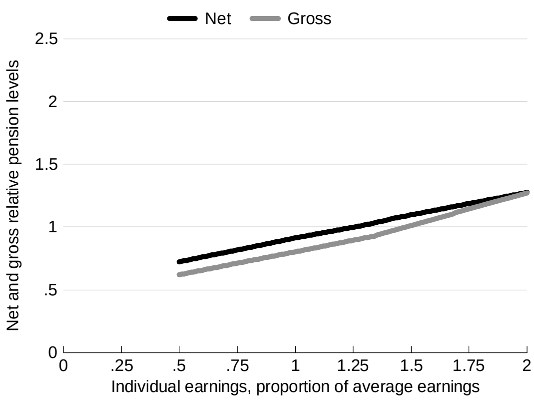
Gross relative pension level



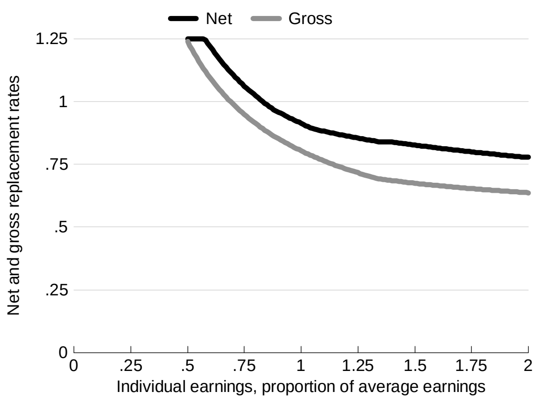

Gross replacement rate



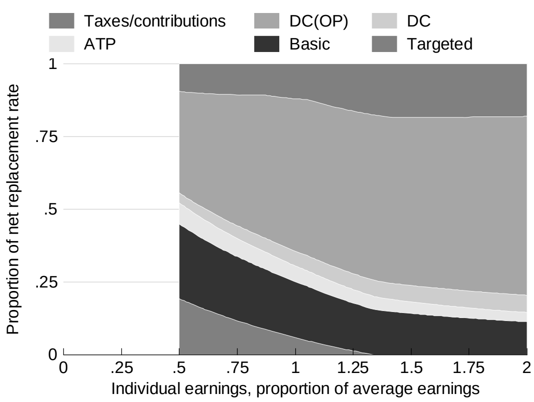

Net and gross relative pension levels



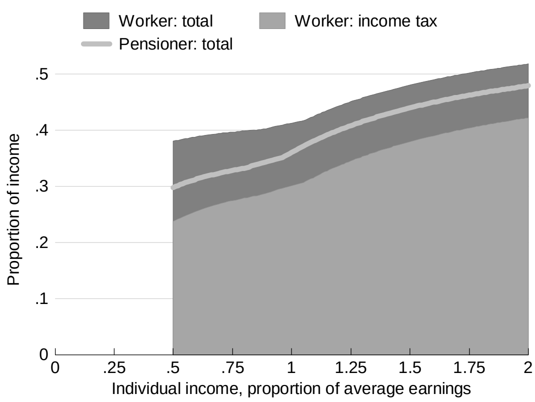

Net and gross replacement rates




Sources of net replacement rate




Taxes paid by pensioners and workers



| Men<br>*Women* (where different) | *Median earner* | *Individual earnings, multiple of average* | | | | |
|---|---|---|---|---|---|---|
| | | *0.5* | *0.75* | *1* | *1.5* | *2* |
| Gross relative pension level<br>(% average gross earnings) | 74.8 | 62.0 | 71.2 | 80.3 | 101.2 | 127.4 |
| Net relative pension level<br>(% net average earnings) | 85.6 | 72.2 | 81.8 | 91.3 | 109.7 | 127.6 |
| Gross replacement rate<br>(% individual gross earnings) | 88.0 | 124.0 | 94.9 | 80.3 | 67.5 | 63.7 |
| Net replacement rate<br>(% individual net earnings) | 98.7 | 137.0 | 106.2 | 91.3 | 82.7 | 77.7 |
| Gross pension wealth | 12.8 | 18.5 | 13.9 | 11.6 | 9.6 | 9.0 |
| (multiple of average gross earnings) | *14.7* | *21.3* | *16.0* | *13.3* | *11.0* | *10.3* |
| Net pension wealth | 8.6 | 12.7 | 9.4 | 7.8 | 6.1 | 5.3 |
| (multiple of average net earnings) | *9.9* | *14.6* | *10.8* | *8.9* | *7.0* | *6.1* |