

## SWEDEN

<p><b>Sweden: pension system in 2006</b></p> <p>The new pension system, introduced in 1999, applies to people born in 1954 and after. The old and the new systems will cover older workers proportionally: people born 1938-53 will receive pensions under a mix of the old and new rules. The earnings-related part is based on notional accounts and there is a small mandatory contribution to individual, defined-contribution funded pensions. There is also a pension-income-tested top-up. Occupational pension plans – with defined-benefit and defined-contribution elements – have broad coverage.</p> <p>For the occupational plan, in 2006 the new ITP scheme was passed. The scheme has long transitional rules but came into effect fully for those born in 1979 and after.</p>
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		<b>Key indicators</b>	
		Sweden	OECD
Average earnings	SEK	324 600	263 800
	USD	44 000	35 800
Public pension spending	% of GDP	7.7	7.2
Life expectancy	at birth	80.8	78.9
	at age 65	84.2	83.4
Population over age 65	% of working-age population	29.4	23.8

### Qualifying conditions

The pension from the income and premium pension can be received from the age of 61.

Eligibility for the guarantee pension will be earned with three years' residency. It is possible to get a guarantee pension from age 65.

Maximum guarantee pension is earned with 40 years' residency and is reduced proportionally for shorter periods. The pension can be claimed from age 65.

### Benefit calculation

Contributions of 18.5% of pensionable pay are credited and then up-rated in line with a three-year moving average of economy-wide average earnings. Pensionable pay is defined as earnings less the employee contribution to the pension system (*i.e.* to both the notional accounts system and the premium pension system) of 7% of gross earnings, giving an effective contribution rate on gross earnings of 17.21%, 14.88% to the notional-accounts system and 2.33% to the defined-contribution funded pensions. Contributions are only levied when annual earnings exceed a small floor of SEK 16 800 in 2006, just over 5.2% of average earnings, although they are due on the whole of earnings for all people earning above the floor. There is a ceiling to benefits calculated in terms of pensionable earnings of SEK 333 750 in 2006. However, this again relates to pensionable earnings, giving an effective ceiling relative to gross earnings of SEK 359 100 in 2006 (around 111% of average earnings). Employer contributions are also paid only to the ceiling, but there is an additional tax on earnings above the ceiling. This tax has the same percentage as the pension contribution but goes directly to the central government budget. It does not accrue any pension rights.

## *Earnings-related*

The new earnings-related scheme uses notional accounts. The notional accounts are increased every year by the distribution of the pension balances of deceased persons of the same age as the survivors (inheritance gains). The inheritance gains from people who die before the earliest possible retirement age (61 years) are relevant. After this age the inheritance gains factor is estimated on the basis of the mortality observed for an earlier period (computed from five year unisex mortality tables).

At retirement, the accumulated notional capital will be converted into an annuity. This calculation will use a coefficient depending on individual retirement age and contemporaneous life expectancy (based on the previous five year unisex mortality tables). A real discount rate of 1.6% a year will be assumed in this calculation. Illustrative values for the annuity coefficient at age 65 are 15.4 for 2000 rising to 16.8 by 2020 and 17.4 by 2040. The annuity coefficient is currently 18.0 for retirement at 61 and 12.8 at age 70 for people born in 1940.

After retirement, pensions are uprated with the increase in nominal average earnings less the imputed interest rate in the annuity divisor of 1.6%.

There is also a “balance mechanism”: if assets (the buffer fund plus the estimated value of assets in the form of contribution revenues) fall below liabilities (accrued notional pension capital and capital value of outgoing pensions), then indexation of pensions in payment and returns credited to notional accounts are reduced by the ratio of assets to liabilities. The balancing ratio reached a low point of 1.0014 in 2004 and remained just over one until 2007 (1.0097 in 2003, 1.0014 in 2004, 1.0044 in 2005 and 1.0149 in 2006). In 2008, however, this has fallen to 0.9672. The balancing ratio for year  $t$  is used to calculate the balance number or the need for activating the balancing mechanism in year  $t+2$ . An activated balancing mechanism would mean lower replacement rates from the national system but could also produce higher results when the pension system recovers and the balance figure increases (the balance index can exceed the income index during the recovery period).

For modelling purposes, the annuity coefficients are calculated using the above rules and the relevant mortality data from the UN/World Bank population database. It is assumed that the balance mechanism does not affect the uprating of benefits.

## *Minimum*

The “guarantee pension” is an income-tested top-up for people with low levels of benefit from notional accounts. For a single person, the full guaranteed benefit in 2006 was SEK 84 561 for a single pensioner born after 1938 or 26% of gross average earnings.

The guarantee pension is withdrawn at 100% against the first SEK 50 022 (2006) of income, for a single person, from the earnings-related pension, thereafter at 48%. This threshold is equivalent to 15% of average earnings. Only when earnings-related pension exceeds SEK 121 879 – nearly 38% of average earnings – is entitlement to the guarantee exhausted.

The guarantee level is price indexed under current legislation. However, the baseline assumption in the modelling for all countries is that the value of safety-net retirement benefits will tend, over time, to track average earnings rather than decline relative to general living standards.

There is also a housing benefit that covers 93% of housing costs up to a maximum of SEK 5 000 per month for a single pensioner. The benefit is an important part of the minimum living standard for Swedish pensioners. This means-tested benefit is not included in the modelled calculations.

### ***Defined contribution***

A further 2.5% of pensionable income (giving an effective contribution rate against gross earnings of 2.325%) will be paid into personal pension accounts: the premium pension. People have a broad choice of where these funds are invested.

At retirement, people have a choice over the way benefits are withdrawn. First, people can convert the pension into an annuity to avoid investment risk. Alternatively, people will be able to choose a variable annuity, where their funds continue to be invested by their chosen fund manager. These annuities do not have a guaranteed value. The principle of the pension calculation in this case is that the value of the account is divided by an annuity divisor (based on estimated average life expectancy) and the pension benefit is credited with an estimated future interest rate of 3% minus administrative costs. If returns exceed 3%, then either an additional payment is made or the balance of the account is higher and so, therefore, is the base for calculating the annual pension.

### ***Quasi-mandatory occupational***

The occupational schemes together are estimated to cover almost 90% of employees. There are only four major occupational schemes. The modelling has used the ITP scheme for white-collar workers, which mixes defined-benefit and defined-contribution elements. This plan has now been renegotiated. The old plan is current for those born 1978 or earlier with some minor changes and the new plan covers those born 1979 or later.

### ***ITP1***

From 1 January 2007, salaried employees born in or after 1979 begin to accrue a retirement pension under the new ITP1 plan from the age of 25. The plan is a complete defined-contribution plan. The contribution is 4.5% of salary portions up to 7.5 income base amounts (SEK 333 750 for 2006). For salary portions in excess of 7.5 income base amounts (divided by 12 for one month) the contribution is 30%. The pensionable salary becomes the gross salary paid out in cash, excluding reimbursement of expenses. Premiums are paid from the first SEK of salary.

The employee can choose the form of the savings and the fund manager. However, at least half the contribution is invested in traditional pension insurance. The employee can also choose repayment cover and family cover of one, two, three or four price base amounts per year over five, ten, 15 or 20 years. The contributions of those who do not specify a choice are invested in traditional pension insurance with no repayment cover or family cover. This default choice is the one that is modelled.

Employees whose yearly salary exceeds ten income base amounts (SEK 445 000 in 2006) may choose to be covered under the new plan upon agreement with their employer. This applies regardless of whether the employee has a traditional ITP2 plan or has taken out an alternative ITP.

## **Variant careers**

### ***Early retirement***

Retirement is possible from age 61 in the public pension scheme (both the income pension and the premium pension). There is no fixed retirement age. The notional-accounts and annuity calculations provide an automatic actuarial reduction depending on the age of retirement.

The income-tested guarantee pension cannot be claimed before 65. If the notional-accounts pension is withdrawn before or after age 65, the guarantee pension is still calculated as if the pension had been withdrawn at age 65.

In the new ITP1 plan, pensions are normally paid from the age of 65, but may be taken out from the age of 55. Pensions are life-long but can be paid in full or in part for a limited period of at least five years. The annuity is modelled as one that gives lifelong payments. The size of the pension is determined by the amount of premiums paid, the return, fees and taxes, and for how long the pension is to be disbursed.

### ***Late retirement***

It is possible to defer the notional accounts and premium pension with no upper age limit, again with automatic actuarial adjustments. It is also possible to combine work and pension receipt. Finally, pensions can be withdrawn partially (at 25, 50 or 75% of the full pension). The guarantee pension is adjusted against other pensions from the Swedish old-age pension system and from comparable foreign national pensions, but is not reduced by wage income, capital income, occupational pension or private pension insurance. Thus, it is also possible to combine work with receipt of the guarantee pension.

It is possible to defer the ITP1 occupational pension after age 65. No additional pension rights can be accrued after age 65.

### ***Childcare***

Years are credited under the public pension scheme for any period spent caring for children aged four or under. In a household with two parents the credits go to the parent with the lowest income if an active choice is not made. Individuals receive the best of three different ways of calculating the credit. First, if income is zero or lower than previous earnings, then the credits are based on the earnings the year before the child was born. Secondly, for low-income workers or people who were not working before childcare responsibilities started, the credits are based on 75% of economy-wide average earnings. Thirdly, if income actually rises or does not decrease to a great extent as childcare responsibilities begin, then the credit is set at one income base amount. In all three cases, the government makes the total contributions to the pension system (covering both the income pension and the premium pension). This is, however, up to the earnings ceiling in the pension system. Furthermore, parental benefits paid to people on parental leave from work are also considered pensionable income. The beneficiary pays the employee pension contribution of 7% on benefit income. The government makes all the “employer contributions” of 10.21% for incomes from social security including parental benefits.

The parental benefit is payable for a period of 480 days as follows:

- 390 days at 80 % of the parent’s annual income up to a ceiling of ten price base amounts (SEK 39 000 in 2006);
- 90 days at a universally applicable flat rate of SEK 180/day.

The parental benefit is computed daily. Parents on low income or no income at all receive a minimum guaranteed benefit of SEK 180/day. The 480 cash benefit days are divided equally between the parents (*i.e.* 240 days to each parent). A parent may also transfer up to 180 of her or his days to the other parent.

Under the ITP occupational plan, there is a recommendation that the employer contributes to an employee’s pension during periods of up to 11 months for parental leave (and most do so).

## ***Unemployment***

Unemployment benefits and training allowances paid to unemployed people taking up labour market programmes are pensionable income, with the government making the “employer” contribution. Income-related unemployment benefits are 80% of previous earnings for the first 200 days. From day 201 up to day 300 the benefit is 70% of previous earnings. Thereafter the benefit is 65% of previous earnings unless one is the parent of a child below the age of 18 for whom the benefit remains at a level of 70% of previous earnings. The unemployment benefits are disbursed up to a ceiling of SEK 680 per day and subject to a minimum payment of SEK 320 per day. Unemployment benefits can be paid for up to 600 days subject to certain conditions.

After the receipt of unemployment benefits for a prolonged maximum period of 600 days, the beneficiary is entitled to an activity guarantee that implied the receipt of a training allowance where the compensation is at the same level as the unemployment benefit and accrues pension rights. The activity guarantee and the subsequent training benefit are obtainable for an unlimited period until the age of 65. An individual who is unemployed would seldom opt to take out their old age pension instead of receiving a training allowance, as this would mean a lower pension.

## **Personal income tax and social security contributions**

### ***Taxation of pensioners***

There are no special concessions for older people.

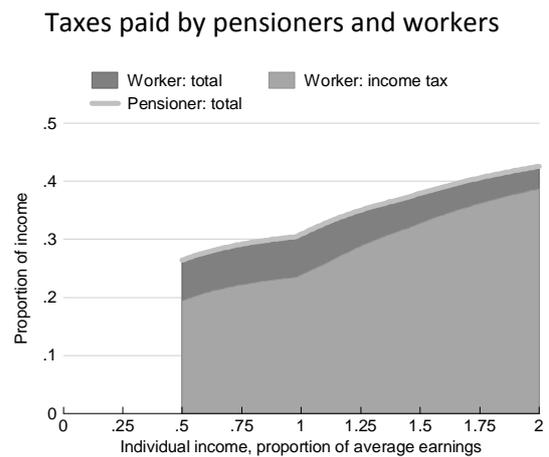
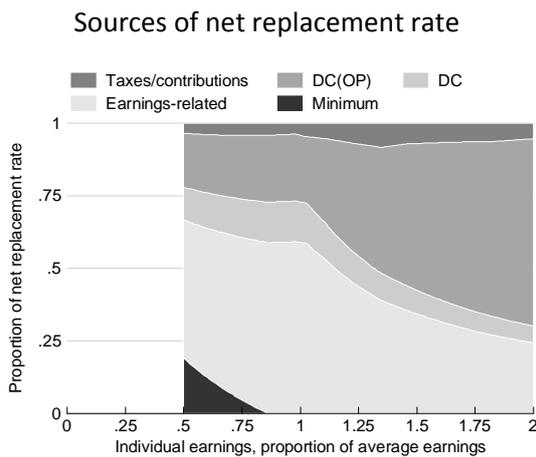
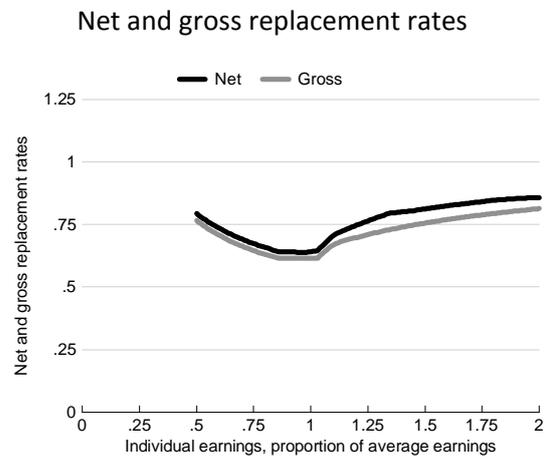
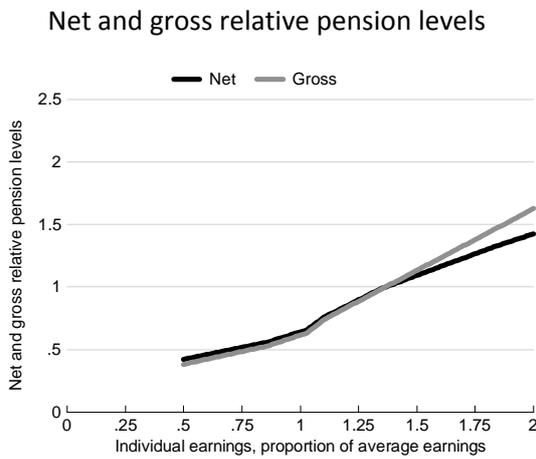
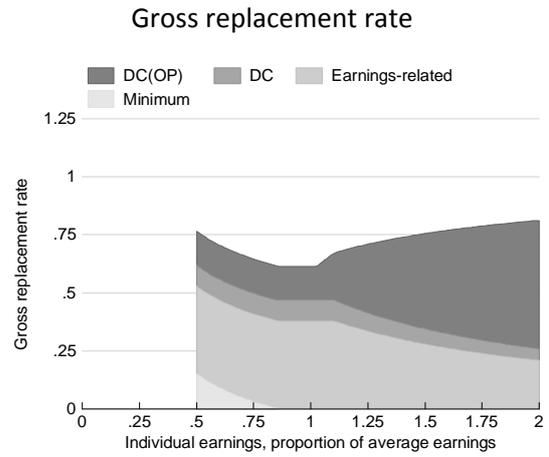
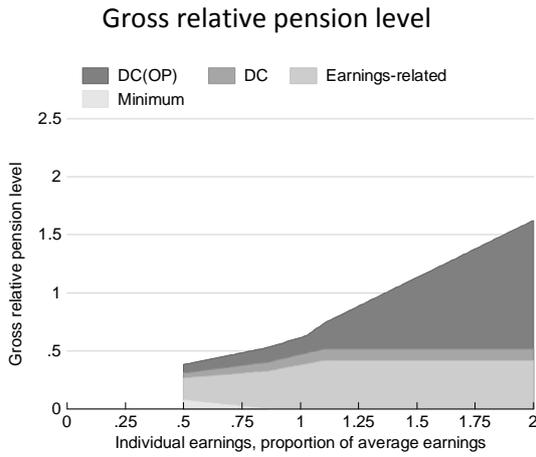
### ***Taxation of pension income***

There is no special relief for pension income.

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

Social security contributions are not levied on pension income.

## Pension modelling results: Sweden



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)	54.1	38.3	48.4	61.5	113.3	162.6
Net relative pension level (% net average earnings)	57.2	42.2	51.8	64.1	109.4	142.6
Gross replacement rate (% individual gross earnings)	61.5	76.6	64.6	61.5	75.6	81.3
Net replacement rate (% individual net earnings)	64.1	79.3	67.4	64.1	81.2	85.9
Gross pension wealth (multiple of average gross earnings)	9.9 11.3	12.2 14.0	10.3 11.8	9.9 11.3	12.0 13.7	12.9 14.7
Net pension wealth (multiple of average net earnings)	7.2 8.2	9.3 10.6	7.6 8.7	7.1 8.1	8.0 9.1	7.8 8.9