Denmark

Denmark: Pension system in 2020

There is a public pension scheme which consists of a basic pension and a means-tested pension supplement that is paid to the financially most disadvantaged pensioners. There is also a mandatory occupation pension scheme based on lump-sum contributions (ATP). In addition, compulsory occupational pension schemes negotiated as part of collective agreements or similar cover about 90% of the employed work force.

Key indicators: Denmark

		Denmark	OECD
Average worker earnings (AW)	DKK	437 094	256 310
	USD	66 812	39 178
Public pension spending	% of GDP	8.0	7.7
Life expectancy	at birth	80.7	80.6
	at age 65	19.2	19.7
Population over age 65	% of working- age population	34.9	30.4

Qualifying conditions

The public pension scheme is universal and covers the entire Danish population. Entitlement to pension is acquired on the basis of residence in Denmark and is thus not conditional on payment of contributions. The public retirement age is currently 66 years but will be increased gradually to 67 years in the period 2021-22 and to 68 in 2030. After this increases are directly linked to increases in life expectancy. A full public old-age pension requires 40 years of residence until 1 July 2025. Thereafter a full public old age pension requires 9/10 years of residence from the age of 15 to the public retirement age. Shorter periods qualify for a pro-rated benefit.

Benefit calculation

Public pension

The public pension scheme consists of a basic amount and a pension supplement. Pensioners whose financial situation is particularly difficult may also receive a supplementary pension benefit, a personal allowance and a health allowance.

Basic

The basic amount is DKK 6 419 per month or DKK 77 028 per year, equivalent to around 18% of average earnings. There is an individual earnings test which means that the basic pension will be reduced if income from work (net of the 8% labour market contribution exceeds DKK 336 900 (approximately 80% of average earnings). The benefit is reduced at a rate of 30% against earned income above this level.

Targeted

The full pension supplement is DKK 7 122 per month or DKK 85 464 per year for single pensioners and DKK 3 576 per month or DKK 42 912 per year for married or cohabiting pensioners. The actual amounts are tested against all sources of personal income (including ATP and occupational pensions) apart from public pensions. The pension supplement is reduced by 30.9% of personal income exceeding DKK 88 700 for single pensioners. For pensioners cohabiting with a spouse/partner, who also receives social pension, the pension supplement is reduced by 16% of their total personal income exceeding DKK 177 700. If the spouse/partner does not receive a public pension the pension supplement is reduced by 32% of the couples total personal income exceeding DKK 177 700.

Pensioners whose financial situation is particularly difficult may also receive a supplementary pension benefit of DKK 18 000. The supplementary pension benefit is taxable and paid once a year. The benefit is means-tested and targeted to the poorest pensioners without significant liquid assets (the liquid assets may not exceed DKK 89 800).

The public old-age pension scheme is adjusted annually in line with average earnings. The adjustment is based on an index of wage increases during the two preceding years. Thus, indexation of the public old-age pension is based upon wage increases.

Income from work up to DKK 122 004 annually is not taken into consideration when calculating (income-testing) the pension supplement and the supplementary pension benefit.

ATP - statutory savings based supplementary pension

ATP (the Danish Labour Market Supplementary Pension) is a statutory, fully funded, collective insurance based, defined-contribution scheme. ATP provides a lifelong pension from the normal pension age and a survivors' lump sum benefit for dependents in the case of the early death of an individual member. ATP covers almost 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.

Pension rights with ATP and occupational pension schemes are accrued on a what-you-pay-is-what-you-get basis. The longer the working career, the higher the employment rate, the longer contribution record and the higher the contribution level, the greater the pension benefits.

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 will pay DKK 3 408 per year in 2020. 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 table below (for monthly paid workers). In order to compensate recipients of unemployment insurance benefits, sickness insurance benefits and maternity/paternity/parental benefits, for the loss of occupational pension contributions suffered during their absence from the labour market, extra contributions are paid into the ATP pension scheme:

Monthly hours	<39	39-77	78-116	>116
Contribution, DKK/month as from 2009	0	94.65	189.34	284

The contribution is adjusted if and when the social partners decide to do so as part of collective agreements.

Pension rights with ATP are accrued on a what-you-pay-is-what-you-get basis. In principle each generation finance their own rights and ATP is devoid of intergenerational transfers. Pension rights are guaranteed nominal life-long rights paid from the statutory age of retirement. 80% of the contribution paid is used to purchase new individual pension rights with ATP based on a discount rate matching the long term interest hedgeable in the market place at the time of inception. Hence, the discount rate applied to new accruals will vary from year to year. The remaining 20% of the contribution is transferred to ATP's free reserves serving as an investment buffer and financing source for longevity increases.

The ATP scheme increases pensions in payment and pension rights if the board finds it to be financially sound. This is done in the form of bonus allowances which are increased in line with earned rights.

The modelling assumes full annuitisation and indexation to price inflation.

Occupational pensions

The occupational pension schemes are fully funded defined-contribution schemes agreed between the social partners through collective agreements. Some 90% of the employed work force is covered by such schemes. The coverage ratio has increased from insignificance in the mid-1980s to the current level of around 85% due to the formation of new schemes covering blue collar workers. All public sector workers are enrolled in a collectively agreed fully funded defined contribution scheme, whereas for private sector workers it's a little less. Self-employed workers are not covered by such schemes, but can choose to establish a similar scheme. Contribution rates are set by the collective agreement and will be similar for all workers under the agreement. Contribution rates range from around 10% to 18%. The modelling assumes a contribution rate of 12%.

Typically, occupational pension schemes will cover a variety of social risks and provide a range of benefits – disability, survivors' benefits, old-age benefits and critical illness benefits. While old-age benefits are fully funded insurance benefits, other benefits are insurance benefits financed from the current contribution. For occupational pension schemes pension rights are accrued on a what-you-pay-is-what-you-get basis. In principle each generation finances its' own rights and schemes are devoid of any intra- or intergenerational transfers other than those attributed to the insurance coverage.

Benefits are usually withdrawn as a life-long annuity. Schemes may allow some choice for members to design their pay-out phase e.g. in order to front load the benefit payments. Some schemes offer the option of allocating some of the contribution into a lump sum savings policy.

There are no vesting or portability issues related to Danish occupational pensions.

Variant careers

Periods of unemployment, maternity, periods with part time employment and other elements of variant careers will affect the accrual of private pensions and therefore the aggregate pension. However, the composition of the overall pension system moderates such effects as the state pension is substantial for most workers. Therefore changes in employment or employment status will only affect part of the overall pension.

Early retirement

From January 2022, those who have been insured for at least 42 years before the age of 61 will be able to receive a benefit equal to the basic pension amount up to three years before the normal retirement age of 67. More precisely, retiring one, two or three years earlier will be allowed after 42, 43 or 44 years of work between ages 16 and 61, respectively. The benefit is equal to the amount of the full basic pension received at the normal retirement age and is subject to means-, earnings- and asset-testing.

Late retirement

Those who has reached the public retirement age (66 in 2020), and who are entitled to public old age pension may choose to defer the pension and participate actively on the labour market in return for a higher pension at a later stage. It is a condition that the person who has deferred his public pension has income from personal work for at least 750 hours each calendar year. The pension can be deferred up to two times and for up to 10 years in total.

Benefits from occupational pensions and ATP will increase for those retiring late, because the "pay-out" period is reduced (and the pay-in period is increased). Public pensions are also increased (if these criteria are met) proportionate to the shortening of the (expected) pay-out period. The exact percentages are defined in legislation.

Childcare

For periods on maternity/paternity/parental benefits, double the amount of contributions is paid for ATP. The beneficiary will pay one-third of the contribution, with two-thirds being paid by the government/municipality. The government expense is covered by contributions paid by private employers. Maternity/paternity/parental benefits can be paid for up to 52 weeks in total. The 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. It is common for young parents to resume work when the leave period ends unless the child is, for example, ill or disabled in which cases there will normally be possibilities for drawing on some sort of public benefit with contribution to ATP. 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 the employer, and ATP contributions are paid at the double rate when receiving benefit from the unemployment insurance. The government or private employers and unemployment insurance funds pays two-thirds of the ATP contribution.

When unemployment insurance is exhausted and the individual is on unemployment/social assistance the ATP contribution decreases to the normal rate. The government pays two-thirds of the ATP contribution. There are no credits or contributions for occupational pension schemes for periods of unemployment.

There is also a voluntary early retirement programme linked with unemployment insurance, which pays benefits between ages 62 (gradually increasing to age 64 in 2023 and further to age 65 in 2028) and until the normal pension age. To qualify, individuals must have been members of the unemployment insurance fund for at least 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 17 366 per month for full-time workers and DKK 11 577 for part-time workers in 2020. It is not possible to combine receipt of voluntary early-retirement benefits with the social pension.

In 2022, another new option to retire early will be introduced: it allows individuals who have at least 20 to 25 years (depending on occupations) of full-time employment and are unable to work more than 15 hours a week (18 hours from 2024) in their most recent jobs to receive a pension up to six years before the normal retirement age.

People who defer the take up of voluntary early-retirement benefits until three years before normal pension age, and are still working, receive a higher rate of voluntary early-retirement benefit equivalent to the maximum rate of unemployment benefit (or DKK 19 083 per month for full-time workers and DKK 12 722 for part time workers in 2020). For three years' full-time work when an individual qualifies for voluntary early-retirement, a one-off tax-free lump-sum is paid up to a maximum of 72% of the yearly amount of maximum unemployment benefit.

Self-employed

None of the earnings-related schemes for employees, including ATP, is mandatory for the self-employed, thus, unless saving voluntarily, they would receive only the basic pension and targeted benefits. The self-employed have different ceilings to tax-deductible contributions to private schemes because their income fluctuates more. Around 60% of the self-employed contribute on average 7% of their income to voluntarily private pension schemes.

Personal income taxes and social security contributions

Tax treatment of pension contributions and pension savings

Private pension contributions to lifelong pensions and annuity pensions are deductible. From 2018, an additional tax deduction for such pension savings – the Pension Contribution Tax Credit – has been imposed on contributions until a ceiling of DKK 73 100.

Pension contributions to lump sum pension schemes are not deductible. Payments of non-deductible lump sum pension schemes are tax exempt.

Taxation of pensioners

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

Taxation of pension income

Periodic pension payments from lifelong pensions and annuity pensions are subject to personal income tax. There are no special reliefs for pension income. If the value of an individual pension scheme at the time of withdrawal is relatively low, total savings are paid out as a lump sum amount, which is not included in taxable income (and does not affect means testing). Instead, it is subject to a separate 40 % flat tax.

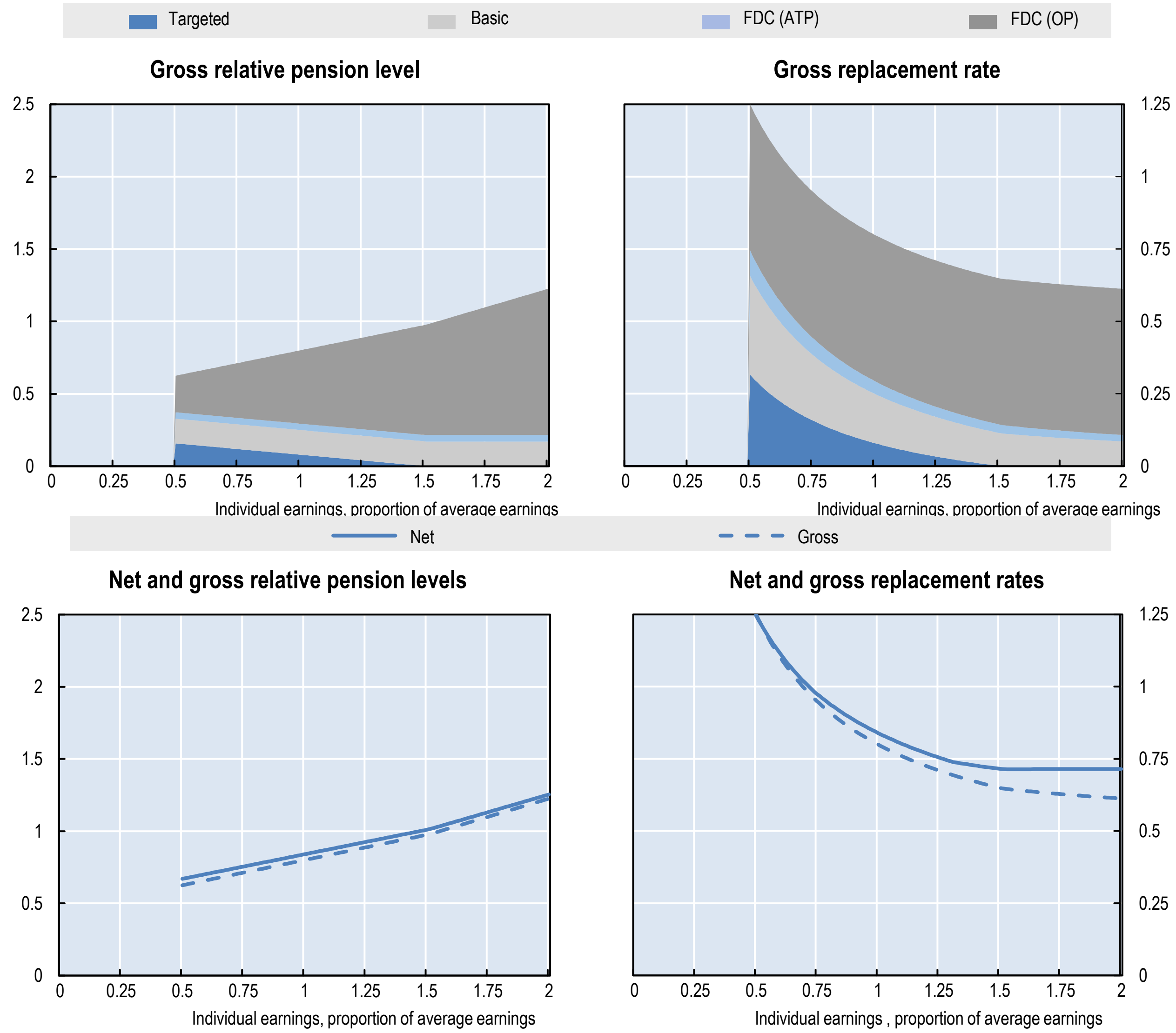
The ATP, occupational pensions and other private pension savings, besides lump sum pensions, are subject to an ETT tax regime. Lump sum pensions are subject to a TTE regime.

All returns from the pension savings are taxed, currently at a rate of 15.3%.

Social security contributions paid by pensioners

No social security contributions are paid in Denmark, as the social security is funded by the normal tax payments. Therefore, pensioners do not pay social security contributions.

Pension modelling results: Denmark in 2072 retirement at age 74



Men	Individual earnings, multiple of average					
Women (where different)	0.5	0.75	1	1.5	2	3
Gross relative pension level	62.5	71.3	80.0	97.5	122.5	173.1
(% average gross earnings)						
Net relative pension level	67.0	75.5	84.0	101.0	125.4	164.9
(% net average earnings)						
Gross replacement rate	125.1	95.0	80.0	65.0	61.3	57.7
(% individual gross earnings)						
Net replacement rate	124.7	97.5	84.0	71.5	71.4	67.4
(% individual net earnings)						
Gross pension wealth	17.3	13.0	10.9	8.8	8.2	7.7
(multiple of individual gross earnings)	*19.0*	*14.3*	*12.0*	*9.6*	*9.0*	*8.5*
Net pension wealth	17.3	13.4	11.4	9.6	9.6	9.0
(multiple of individual net earnings)	*19.0*	*14.7*	*12.5*	*10.6*	*10.5*	*9.9*

Assumptions: Real rate of return 3%, real earnings growth 1.25%, inflation 2%, and real discount rate 2%. All systems are modelled and indexed according to what is legislated. Transitional rules apply where relevant. DC conversion rate equal 90%. Labour market entry occurs at age 22 in 2020. Tax system latest available: 2020.