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Finland's national

Pension Strategy Report 2005

MINISTRY OF SOCIAL AFFAIRS AND HEALTH

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Finland's National Pension Strategy Report 2005

Summary
The Laeken European Council agreed on the content and procedures in the application of the open method of co-ordination in the field of pensions. The introduction of the open method of co-ordination involved endorsing the eleven common pension policy objectives at the Community level, their inclusion in the national pension strategies, and regular monitoring of the attainment of the objectives at EU level. The common objectives are based on the three principles for pension policy that were adopted at the Gothenburg European Council in June 2001, comprising adequacy of pensions, financial sustainability of the pension systems, and adjustment of the pension systems in response to the changing needs of the economy, society and individuals.

Finland submitted its first national Pension Strategy Report to the EU in September 2002, evaluating the implementation of the common objectives in the national pension system. The joint report of the Commission and the Council on adequate and sustainable pensions that was drawn up based on the national reports was endorsed in the Employment, Social Policy, Health and Consumer Affairs Council and in Ecofin in March 2003.

A broad-based Working Group appointed by the Ministry of Social Affairs and Health has prepared the second national Pension Strategy Report. The report deals with the Finnish pension system and the pension policy decisions made in Finland, as well as the grounds for them and their social, employment and economic motives from the point of view of each pension policy objective adopted at the Laeken European Council. Furthermore, the report looks at the progress made in the reforms dealt with in the previous report and updates the information furnished in it.

Finland’s national pension policy decisions are, in broad outline, in harmony with the EU’s common objectives. The challenges of the Finnish pension system are mainly due to the change in the age structure and the accelerated growth of the pension expenditures resulting from that. Achievement of longer work careers and a higher employment rate are issues that are crucial to ensuring both the adequacy and sustainable financing of pensions.

Key words
ageing, employment, EU, financing, pensions, social protection

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<table>
<tr><td colspan="2">Julkaisija
Sosiaali- ja terveysministeriö</td><td colspan="2">Julkaisun päivämäärä
15.7.2005</td></tr>
<tr><td colspan="2" rowspan="3">Tekijät (toimielimestä: toimielimen nimi, puheenjohtaja, sihteeri)
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Pirjo Moilanen, STM
Mika Vidlund, ETK</td><td colspan="2">Julkaisun laji
Työryhmämuistio</td></tr>
<tr><td colspan="2">Toimeksiantaja
Sosiaali- ja terveysministeriö</td></tr>
<tr><td colspan="2">HARE-numero ja toimielimen asettamispäivä
STM087:00/2004
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<tr><td colspan="4">Tiivistelmä

Laekenin Eurooppa-neuvostossa sovittiin niin kutsutun avoimen koordinaation menetelmän soveltamisen sisällöstä ja menettelytavoista eläkkeiden alalla. Avoimen koordinaation menetelmän käyttöönotto merkitsi 11 yhteisen eläkepoliittisen tavoitteen hyväksymistä yhteisötasolla, niiden sisällyttämistä kansallisiin eläkestrategioihin sekä tavoitteiden toteutumisen säännöllistä seurantaa EU-tasolla. Yhteiset tavoitteet perustuvat Göteborgin Eurooppa-neuvostossa kesäkuussa 2001 hyväksytylle kolmelle yhteiselle eläkepoliittiselle periaatteelle, jotka ovat eläkkeiden riittävyys, eläkejärjestelmien rahoituksellinen kestävyys ja eläkejärjestelmien sopeuttaminen vastaamaan talouden, yhteiskunnan ja yksilöiden muuttuviin tarpeisiin.

Suomi toimitti EU:lle syyskuussa 2002 ensimmäisen kansallisen eläkestrategiaraporttinsa, joissa arvioitiin yhteisten tavoitteiden toteutumista Suomen kansallisessa eläkejärjestelmässä. Kansallisten raporttien pohjalta laadittu komission ja neuvoston yhteinen selvitys riittävästä ja kestävästä eläketurvasta hyväksyttiin työllisyys- sosiaalipolitiikka, terveys ja kuluttaja-asiat sekä Ecofin-neuvostossa maaliskuussa 2003.

Tämän järjestyksessään toisen kansallisen eläkestrategiaraportin on laatinut STM:n asettama laajapohjainen työryhmä. Raportissa tarkastellaan Suomen eläkejärjestelmää ja Suomessa tehtyjä eläkepoliittisia ratkaisuja sekä niiden perusteluja ja sosiaali-, työllisyys- ja talouspoliittisia vaikuttimia kunkin Laekenin Eurooppa-neuvostossa hyväksytyn yhteisen eläkepoliittisen tavoitteen kannalta. Lisäksi raportissa tarkastellaan edellisessä raportissa todettujen uudistusten edistymistä sekä päivitetään siinä esitettyjä tietoja.

Suomen kansalliset eläkepoliittiset ratkaisut ovat pääpiirteissään sopusoinnussa EU:n yhteisten tavoitteiden kanssa. Suomen eläkejärjestelmän haasteet johtuvat pääosin ikärakenteen muutoksesta ja siitä seuraavasta eläkemenojen kasvun kiihtymisestä. Niin eläkkeiden riittävyyden kuin rahoituksen kestävyyden kannalta ratkaisevassa asemassa ovat työurien pidentäminen ja työllisyysasteen nostaminen.</td></tr>
<tr><td colspan="4">Asiasanat:
eläkkeet, EU, ikääntyminen, rahoitus, sosiaaliturva, työllisyys</td></tr>
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</table>

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<table>
<tr><td colspan="2">Utgivare
Social- och hälsovårdsministeriet</td><td colspan="2">Utgivningsdatum
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<tr><td colspan="2" rowspan="3">Författare (Uppgifter om organet: namn, ordförande, sekreterare)
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Vid Europeiska rådet i Laeken avtalades om innehåll och förfaringssätt vid tillämpning av den s.k. öppna samordningsmetoden på pensionsområdet. Att ta i bruk den öppna samordningsmetoden innebar att man godkänner elva gemensamma pensionspolitiska mål på unionsnivå, inkluderar dessa i de nationella pensionsstrategierna och regelbundet följer upp genomförandet av målen på EU-nivå. De gemensamma målen baserar sig på tre gemensamma pensionspolitiska principer som godkändes vid Europeiska rådet i Göteborg i juni 2001 enligt vilka pensionerna skall vara tillräckliga, pensionssystemen ekonomiskt hållbara och pensionssystemen anpassas utgående från de föränderliga behoven i ekonomin, samhället eller hos individerna.

Finland inlämnade sin första nationella pensionsstrategirapport till EU i september 2002 där man utvärderade hur de gemensamma målen genomförs inom ramen för det nationella pensionssystemet. Kommissionens och rådets gemensamma redogörelse om ett tillräckligt och hållbart pensionsskydd som utarbetats på basis av de nationella rapporterna godkändes vid rådet för sysselsättning, socialpolitik, hälso- och konsumentfrågor och vid Ecofinrådet i mars 2003.

Denna nationella pensionsstrategirapport som är den andra i ordningen har utarbetats av en bred arbetsgrupp tillsatt av SHM. I rapporten granskas pensionssystemet i Finland och pensionspolitiska beslut som fattats i landet och motiveringar till dessa samt social-, sysselsättnings- och ekonomiskpolitiska incitament utifrån varje gemensamt pensionspolitiskt mål som godkänts vid Europarådet i Laeken. Dessutom granskar man i rapporten hur reformerna som behandlades i den förra rapporten framskridit samt uppdaterar uppgifter som presenterats i denna.

De nationella pensionspolitiska besluten i Finland stämmer i stora drag överens med EU:s gemensamma mål. Utmaningarna för pensionssystemet i Finland består i huvudsak av förändrad åldersstruktur och en accelererande ökning av pensionsutgifterna till följd av detta. Både när det gäller tillräckliga pensioner och ekonomisk hållbarhet har en förlängning av tiden i arbetslivet och ökad sysselsättningsgrad en avgörande roll.</td></tr>
<tr><td colspan="4">Nyckelord
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To the Ministry of Social Affairs and Health

The Ministry of Social Affairs and Health appointed on 24 January 2005 a working group (decision of appointment STM087:00/2004) to prepare Finland's second National Pension Strategy Report as agreed at the Laeken European Council.

When preparing the National Pension Strategy the Working Group should take into account the common pension policy objectives endorsed within the framework of EU co-operation, present the corresponding national objectives, assess the current situation of the Finnish pension system in relation to the common objectives and present the measures – including the implemented or decided measures – that are necessary to attain those objectives. Furthermore, it should report on the implementation of the national strategies dealt with in the report of 2002 and update those strategies. The report should use indicators measuring the common objectives.

The Working Group should take into account any studies, surveys and working group reports that are available on the theme. If necessary, the Working Group should commission further studies on the issue.

The chairman of the Working Group was Director-General Tarmo Pukkila of the Ministry of Social Affairs and Health. As the members of the Working Group were appointed Kari Välimäki, Director-General; Tuulikki Haikarainen, Deputy Director-General; Heikki Palm, Ministerial Adviser; Leena Väänänen, Senior Actuary; and Tiina Palotie-Heino, Senior Financial Officer, all of the Ministry of Social Affairs and Health. As the members of the Working Group were invited Jorma Tuukkanen, Ministerial Adviser, Ministry of Finance; Matti Sihto, Labour Market Counsellor, Ministry of Labour; Jarkko Soikkeli, Chief Economist, Federation of Finnish Enterprises; Maija-Liisa Kotiranta, Senior Adviser, Insurance Supervisory Authority; Timo Silvola, Senior Manager, Life Insurance, Federation of Finnish Pension Institutions; Kaarina Knuuti, Director, Central Union of Agricultural Producers and Forest Owners MTK; Kallinen Kaija, Social Policy Adviser, Central Organisation of Finnish Trade Unions SAK; Jarmo Pätäri, Lawyer, Confederation of Unions for Academic Professions AKAVA; Seija Ilmakunnas, Head of Department, Finnish Centre for Pensions; Jari Sokka, Director, Local Government Pension Institution; Matti Leppälä, Director, Finnish Pension Alliance TELA; Anne Neimala, Director of Department, Social Insurance Institution; Jorma Skippari, Negotiations Manager, Finnish Confederation of Salaried Employees STTK, Director Helli Salminen, Association of Pension Foundations; and Vesa Rantahalvari, Adviser, Confederation of Finnish Industries EK.

The secretaries of the Working Group have been Tiina Granlund, Senior Officer, and Pirjo Moilanen, Actuary, from the Ministry of Social Affairs and Health, as well as Mika Vidlund, Researcher, from the Finnish Centre for Pensions.

When Timo Silvola was prevented from taking part in the work of the Working Group his place was taken by Tero Salonen, Special Advisor, Life Insurance. When Anne Neimala was prevented her place was taken by Heikki Niemelä, Leading Researcher.

The Working Group held seven meetings during the period from 31 March to 27 June 2005. It will continue its work up to 31 December 2005 in order to take part in the discussion regarding the National Pension Strategy Report in the EU.

The Working Group hereby respectfully submits its report to the Ministry of Social Affairs and Health.

Helsinki, 15 July 2005.

Tarmo Pukkila

Tuulikki Haikarainen	Heikki Palm
Leena Väänänen	Kari Välimäki
Tiina Palotie-Heino	Jorma Tuukkanen
Matti Sihto	Jarkko Soikkeli
Maija-Liisa Kotiranta	Timo Silvola
Kaarina Knuuti	Kaija Kallinen
Jarmo Pätäri	Seija Ilmakunnas
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Anne Neimala	Jorma Skippari
Helli Salminen	Vesa Rantahalvari
	Pirjo Moilanen
	Mika Vidlund
	Tiina Granlund

TABLE OF CONTENTS

Foreword

The Laeken European Council agreed on the content and procedures in the application of the open method of co-ordination in the field of pensions. The introduction of the open method of co-ordination involved agreement on the eleven common pension policy objectives at the Community level, their inclusion in national pension strategies, and regular monitoring of the attainment of the objectives at the EU level. The common objectives were based on the three principles concerning pension policy that were adopted at the Gothenburg European Council in June 2001: adequacy of pensions, financial sustainability of pension systems, and modernization of pension systems in response to the changing needs of the economy, society and individuals.

In September 2002, the EU was presented with Finland's first report on the National Pension Strategy assessing the attainment of the common objectives in the national pension system. On the basis of the Members States' national reports, the Commission and the Council drafted a joint report on adequate and sustainable pensions, which was approved by the Employment, Social Policy, and Health and Consumer Affairs Council and the Ecofin Council on March 6 and 7, 2003.

The first round of national reports has increased Finland's interest in the other Members States' pension systems and the related reforms. While the reports have been subject to a great deal of discussion among experts, this has not as yet had any major effect on Finnish national pension policy. On the other hand, the problems that Finland has long sought to solve are the same as in the other Member States, and Finnish pension policy addresses common objectives.

This second national pension strategy report reviews the Finnish pension system and the pension policy decisions made in Finland, as well as the grounds for them and the social, employment and economic policy related motives for them with regard to the eleven common pension policy objectives agreed at the Laeken European Council. In general the common objectives are in harmony with Finland's pension policy decisions. The report also describes the progress in the reforms described in the previous report and provides updates on the related data. The report contains statistics and graphical charts linked to each objective (Appendixes 1 and 2).

The report has been drawn up by a working group set up by the Ministry of Social Affairs and Health. The members of the working group represent the Ministry of Social Affairs and Health, the Ministry of Labour, the Ministry of Finance, the Insurance Supervisory Authority, the Confederation of Unions for Academic Professionals AKAVA, the Central Union of Agricultural Producers and Forest Owners MTK, the Central Organization of Finnish Trade Unions SAK, the Finnish Confederation of Salaried Employees STTK, the Confederation of Finnish Industries, the Social Insurance Institution, the Local Government Pensions Institution, the Finnish Centre for Pensions, the Finnish Pension Alliance TELA, the Association of Pension Foundations, the Federation of Finnish Insurance Companies, and the Federation of Finnish Enterprises. The composition of the working group is in line with the procedural recommendations issued by the EU for the preparation of national reports. Earnings-related pension provision in Finland has also traditionally been developed on a tripartite principle, i.e. in cooperation between the Government and the labour market organizations. This report has also been submitted to the Advisory Board for Ageing and Pensioners' Affairs and to the National Advisory Board for Pensioners' Associations. Moreover, the report has been presented to the Finnish Parliament.

1 Introduction

The main objective of the Finnish pension system is to ensure that the population is covered against the economic risks caused by ageing, disability and death of a family provider. The statutory pension provision for all residents in Finland consists of an earnings-related pension scheme and a national pension scheme. The earnings-related pension scheme provides earnings-adjusted, insurance-based pensions, which ensure to a reasonable degree that all wage and salary earners and self-employed persons retain their level of consumption after retirement, and the national pension scheme provides the whole population with a residence-based minimum pension which complements the earnings-related pension. These two pensions together form the total statutory pension for a pensioner. The statutory pension provision can be supplemented with supplementary pension arrangements.

The future challenges for the Finnish pension system mostly arise from the change in the age structure of the population (see Tables 1.1 and 1.2) and the subsequent increasingly rapid rise in pension expenditure. While the fertility rate in Finland is among the highest in Europe (1.80 in 2004), it is still lagging behind the regeneration rate. The size of the working-age population will begin to decrease in 2010, while those age groups with traditionally low employment rates will begin to grow. The economic dependency ratio (the ratio of non-employed people to employed people) is expected to rise after 2015 from the present level of almost 120 per cent to 140 per cent by 2030. (See Figure 1.1). The old-age dependency ratio (the ratio of over-65s to the working-age population) is expected to double from today’s level by 2030 and remain high thereafter.

This rise in the economic dependency ratio will also affect the population’s need for social and health care services. Aged people need more care than younger age groups. However, people retiring from work today are on average clearly in better health than older age groups and will be able to remain independent well into fairly old age. (See Table 1.3 and Figure 1.3 and Appendix 2). The Finnish Government’s primary target for old-age care is to support living at home for older people. Accordingly, the starting-point for developing the service system for the elderly is to promote their functional capacity and independence.

In Finland, a number of steps have been taken to prepare for the change in the age structure of the population. One of these steps is the pension reform which took effect at the beginning of 2005 with the specific aims of postponing the average effective retirement age and adjusting the pension system to the increase in average life expectancy. It promotes intergenerational income distribution by strengthening the linkage between contributions and benefits and by aiming at an optimally stable development of pension contributions over time. The reform will curb the rise in pension expenditure and increase pension funds. In the long term, the reform will lighten the growing burden of pension contributions on the younger generations. An important tool adopted for achieving sustainable financing for the pension reform is the life expectancy coefficient: the costs arising from increased life expectancy can be avoided by reducing the new pensions correspondingly.

In 2004, a total of EUR 17.3 billion was paid out in pensions in Finland, which was 11.4% of GDP and 42.6% of social expenditure. These figures have remained about the same over the past few years. During the recession at the beginning of the 1990s, the percentage of GDP represented by pension expenditure went up while the percentage of social expenditure went down. Today, their percentage of social expenditure is about the same as in 1990, before the recession. The percentage of GDP represented by pension expenditure, however, is still somewhat higher than before the recession. (See Figure 1.3.)

Trends in the employment situation are of key importance in achieving goals in comprehensive social security and reasonable economic growth. The main targets set out by Prime Minister Matti Vanhanen's Government for employment are reducing the unemployment rate, deferring the withdrawal from the labour market by 2—3 years in the long term and raising the employment rate. In 2004, the employment rate in Finland was 67.2 per cent and the average unemployment rate was 8.8 per cent.

By international standards, the current state of the Finnish general government is good. In the next couple of decades, however, there will be heavy financial pressure on the management and balance of the general government, particularly as the ageing of the population will increase expenditure on pensions and care services. The estimated increase in health care and social expenditure places a further strain on the balance of the general government. Further financial pressures will be imposed among others by international tax competition, which will weaken the general government's potential for financing social benefits. The general government surplus has decreased every year since 2000. In 2004, the financing surplus of the general government dropped to about 2per cent of total production. General government debt was 45.1 per cent and the central government debt was 42.6 per cent of the total production at the end of 2004. In 2004, the interest expenditure of central government debt was EUR 2.4 billion (1.6 per cent of GDP). In terms of national accounts, the central government finances were more or less in balance, with a surplus of about 0.1 per cent of GDP. GDP per capita in 2004 was about EUR 25,500[1].

Economic growth in Finland remained quite rapid up to the end of last year. GDP increased by 3.7 per cent in 2004. Total production is estimated to grow by 3.3 per cent in 2005 and 2.7 per cent in 2006.

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The Finnish pension system

The Finnish public pension system (the first pillar) is made up of two statutory pension schemes: one is the national pension scheme guaranteeing a minimum pension to all residents whereas the other is an employment-based, earnings-related pension scheme.

Voluntary pension schemes (the second and third pillars) have played a minor role in Finland due to the relatively high net replacement rate of public pensions, the lack of pension ceilings and full coverage of the system.

[1] EU15: EUR 25,690; EU25: EUR 23,160 in 2004

The statutory schemes are closely linked together, with the amount of the national pension depending on the size of the earnings-related pension benefits. Increases in the earnings-related pension reduce the national pension by 50 per cent. If the earnings-related pension is above a defined level, the national pension is not paid at all. Payments in statutory pensions amounted to 11.4 per cent of GDP in 2004, of which the employment-based earnings-related pensions accounted for 84 per cent and the basic national pensions for the rest. In the future, the role of the national pensions in the total pension coverage will diminish, as the level of earnings-related pensions will rise. (See figure 2.1.)

Pension-tested *national pensions* are administered by the Social Insurance Institution supervised by Parliament. These pensions are financed based on a pay-as-you-go system by contributions paid by employers (49 per cent) and by a state share (51 per cent). The purchasing power of national pensions is kept intact by indexation to the consumer price index.

The *earnings-related pension system* is based on a tripartite arrangement, consisting of employees, employers and the government. There are several different Acts, the Employees Pensions Act (TEL) forming a kind of framework Act, which functions as the basis for other Acts. The self-employed are also covered. There are about 60 authorized pension providers of very different sizes. The Finnish Centre for Pensions is the statutory central body for private sector pension schemes. The Ministry of Social Affairs and Health is in charge of the general supervision of the earnings-related schemes. Employees in central and local government as well as employees of the Finnish Evangelical-Lutheran Church have their own earnings-related schemes. The schemes for central government employees are managed by the State Treasury under the general supervision of the Ministry of Finance, whereas the Local Government Pensions Institute administers the scheme for local government employees.

The financing of earnings-related pensions is a combination of a pay-as-you-go (PAYG) system and a funded system based on pension contributions from both employers and employees. The PAYG system covers approximately ¾ of the earnings-related pension outlays, and the funded scheme covers the rest. Despite the partially funded pension system, Finland's earnings-related pension scheme is entirely of defined-benefit type. The funding is collective in the sense that it has no effect on the size of the pension. The main purpose of the funding is to cut the peak of pension contributions in the coming years.

The retirement age is flexible (62-68) and pensions accrue from the age of 18 to 52 at the rate of 1.5 per cent of wages a year, from 53 to 62 at 1.9 per cent and from 63 to 68 at 4.5 per cent a year without any cap. There are two indices in the earnings-related pension system. The first index adjusts past earnings to the present level when calculating the pension at the time of retirement. This wage coefficient puts a weighting of 80 per cent on changes in wages and 20 per cent on changes in prices. The other index, i.e. earnings-related pension index aims at keeping the purchasing power of earnings-related pensions ahead of inflation. This index has a weighting of 80 per cent on changes in prices and 20 per cent on changes in wages. The life expectancy coefficient adjusts the pensions to be paid to the changes in longevity as of 2009.

The financial position in the earnings-related pension schemes is fairly good as the system is running on surpluses. The annual surplus is some 2.5 per cent in relation to GDP. The market value of the pension fund’s assets was 58.7 per cent of GDP in 2004.

Statutory pensions are taxed as earnings-based income (progressive tax rate) with special deductions applying for smaller pensions. The contributions to pension schemes and investment incomes of the pension providers are exempt from taxation. The taxation arrangement of earnings-related pensions is of the EET type.

Tax treatment of supplementary pensions arranged by the employer is the same as that of statutory pensions, except for certain restrictions related to the retirement age.

Self-acquired voluntary pensions are taxed in the capital income taxation regime at a flat tax rate, and pension contributions can also be deducted to a certain amount in the taxation within the capital income taxation regime.

2 Adequacy of pensions – implementation of social objectives

Target 1: Ensure that older people are not placed at risk of poverty and can enjoy a decent standard of living; that they share in the economic well-being of their country and can accordingly participate actively in public, social and cultural life.

Target 2: Provide access for all individuals to appropriate pension arrangements, public and/or private, which allow them to earn pension entitlements enabling them to maintain, to a reasonable degree, their living standard after retirement.

Target 3: Promote solidarity within and between generations.

2.1 Policy objectives

All persons residing in Finland are guaranteed certain economic, social and cultural rights under the Constitution of Finland. According to the Constitution, all persons residing in Finland have a statutory right to social security and equal treatment irrespective of their occupation, status or place of residence. The purpose of the social security system is to ensure that people have a healthy work and living environment, good health and functional capacity and sufficient income, and access to services and social protection at the various stages of their lives. The statutory social insurance forms the core of the Finnish income security system. Its purpose is to provide insurance cover for all citizens against loss of income or high costs arising from major social risks such as illness, disability, unemployment, accidents, old age, spouse's death or childbirth. The basic principles of the Finnish social security system are founded on the Nordic welfare model.

The objective of Finnish pension policy is to guarantee a reasonable level of consumption for pensioners, to maintain a stable income ratio between the retired and the working population and to keep the risk of poverty for pensioners low.

In Finland, the mandatory statutory pension provision is formed by the earnings-related and national pension schemes. The purpose of the statutory earnings-related pension is to guarantee that the level of consumption acquired during active working life is maintained to a reasonable degree after retirement. The statutory earnings-related pension covers all wage and salary earners and self-employed persons. The earnings-related pension is supplemented by the residence-based national pension, which is intended to guarantee a minimum income for all pensioners. The national pension is proportional to the earnings-related pension. People who receive no earnings-related pension at all or a very small earnings-related pension receive the full amount of national pension. (See Figure 2.1). The pension scheme is supplemented by pensioners' housing allowance, pensioners' care allowance for supporting living at home and independent coping, special tax treatment of pensions, and public social and health care services.

Statutory pension provision can be supplemented by supplementary pension provision arranged by the employer or acquired by individuals themselves according to their individual needs. Together, the statutory pension and the supplementary pension form a total pension provision which ensures an adequate income during retirement.

2.2 The current situation

The statutory earnings-related pension provision is comprehensive, and it is mandatory for employers and self-employed persons to arrange it. In practice, pension accrues from all work and self-employment. There is no upper limit, i.e. ceiling, for the earnings-related pension. The national pension scheme covers all people resident in Finland.

In 1995, earnings-related pension recipients accounted for 90 per cent of all pensioners; national pension recipients accounted for 92 per cent of all pensioners. In 2003, 92 per cent of all pensioners received an earnings-related pension, while 53 per cent received a national pension. (See Figures 2.2 and 2.3 and Table 2.1.) The percentage of those receiving a national pension has been declining increasingly rapidly since 1996 when the basic amount of the national pension, which was paid to all pensioners, was abolished and the national pension became entirely proportional to the earnings-related pension. No national pension is paid if the amount of earnings-related pension exceeds a certain income limit.

The statutory pension provision can be supplemented by supplementary pension provision arranged by the employer or by self-acquired insurance. As the statutory pension provision itself is comprehensive, the proportion of supplementary pension arrangements has been fairly modest (see tables 2.1.a and 2.2.b) compared with the proportion in other countries. Supplementary pension assets (i.e. the 2nd and 3rd pillars) were about 11 per cent of GDP in 2003.

2.2.1 Level of pension provision

At the end of 2003, the average pension based on an old-age pensioner’s own career (statutory earnings-related and national pension), which did not include a survivor’s pension payable after the death of a spouse, was about EUR 1,040 per month (gross), or about 45 per cent of the average earnings of wage-earners in 2003. The average total pension for old-age pensioners (including survivors’ pensions) was approximately EUR 1,137 per month, or about 49 per cent of the average earnings for wage-earners.

The average statutory pension (earnings-related and national pensions) for persons who retired on a pension based on their own career (i.e. new retiree) was about EUR 1,377 per month (gross) in 2003, or about 60 per cent of the average earnings of wage-earners in the same year.

As a rule, all earnings-related pension rights accrue on the basis of all earned income. It is increasingly common today for the earnings-related pension to constitute a basic pension, which is supplemented by a national pension at a low wage levels. After the pension reform earnings-related pension also accrues during certain unpaid periods. The target level in the earnings-related pension scheme has been 60 per cent of the previous earnings after a 40-year career; this also used to be the maximum level for the total amount of pensions accrued from the various contracts of employment. This 60 per cent ceiling was removed by the 2005 pension reform, which, together with the accelerated accrual rates towards the end of the career, provides people with an opportunity to earn higher amounts of pension than before. (See 2.2.5. The reform of the earnings-related pensions)

People who receive no earnings-related pension at all or only a small earnings-related pension receive the full amount of national pension; for a single person, the monthly amount is approximately EUR 505 or EUR 485 (about 21 per cent of average wage-earners' income), depending on their place of residence. For spouses, these amounts are approximately EUR 445 and EUR 428 respectively. As a rule, the amount of the national pension decreases as the person's other pension income increases. If the amount of other pensions exceeds a certain limit no national pension is paid.

A pension recipient can also be paid housing allowance, pensioners' care allowance and child increases. Low-income pensioners may receive pensioners' housing allowance, the amount of which depends on the costs of housing, the pensioners' family conditions, their annual income and their assets. On average, housing allowance in 2004 was EUR 138 a month. Pensioners' care allowance is paid to compensate for sick or disabled pensioners living at home and the care which is provided at home. The amount of the care allowance granted to a pensioner depends solely on the pensioner's functional capacity and its amount varied between EUR 52 and EUR 256, approximately. Pensioners' care allowance is not affected by the pensioners' or their families' other income or assets. In 2004, the average amount of the pensioners' care allowance was approximately EUR 117 a month. Those who served in the war or under war-like circumstances are in addition entitled to a front-veterans' supplement and an additional front-veterans' supplement. (Table 2.3.) Risks of exclusion are addressed not only through social income transfers but through public social welfare and health care services for all population groups. Pensioners' participation in public, social and cultural life is also supported through reduced fees for public transportation and cultural events, for instance.

In addition to a normal index adjustment, the level of the national pension was increased by about EUR 7 on March 1, 2005. A similar increase was previously made in 2001. At that time, the increase was about EUR 12 per month. The size of the overall increase was not affected by the pension recipient's municipality of residence or family conditions or the amount of the earnings-related pension. The overall increase in the national pension also increased the amount of pension income deduction in municipal taxation and provided extra income for low- or medium-income recipients of an earnings-related pension who are not entitled to a national pension. The overall increase in the national pension benefits about 670,000 recipients of a national pension. As a joint result of the overall increase in the national pension and the subsequent rise in pension income deductions in municipal taxation, the income of more than 900,000 pensioners is estimated to rise in 2005. The same overall and index increases were made in the survivors' pensions as well.

2.2.2 Adequacy of pension provision

The level of income for pensioners has remained stable at about 80 per cent of the income of the entire population. (See Figure 2.4.)

According to theoretical replacement rate calculations, total statutory pension (earnings-related pension + national pension) for a wage-earner with average income who retires in 2005 would be about 57 per cent of the wage level preceding retirement (gross replacement rate). The net replacement rate, where income tax was taken into account, was about 63 per cent for wage-earners with average income. The EU calculations are based on a 40-year career and a retirement age of 65 years. (See Table 2.4.)

The full amount of a national pension supplemented with other related statutory benefits could be considered as the minimum level of income for pensioners. Social assistance can be considered as the general minimum income level, the basic amount of which is a maximum of EUR 378 per month. The basic amount may be supplemented with a supplementary benefit for housing expenses and health care expenses in addition to the basic amount. The amount of the supplementary benefit varies case by case. Housing allowance for working-age families was paid to 159,000 households. The average amount of housing allowance in 2004 was EUR 213. In recent years the proportion of people aged 65 and over receiving social assistance has been less than 4 per cent (see Table 2.5).

The percentage of pensioners receiving a full national pension has declined continuously. In 2004, 52 per cent of all pensioners received a national pension and a full national pension was paid to 8 per cent. Pensioners' housing allowance supplementing small pensions was paid to about 22 per cent of all pensioners in 2004. About 24 per cent of all pensioners received pensioners' care allowance, the amount of which depended on their functional capacity but not on their income. The percentage of recipients of other benefits was lower.

According to the European Community Household Panel (ECHP) survey, the income of 23 per cent of over-65s remained under 60 per cent of the median income in 2001. The relative risk of poverty for under-65s was 9 per cent. If poor households are defined as households whose disposable income is less than half of the median disposable income for all households calculated per consuming unit, the risk of poverty for over-65s was 9 per cent, while the risk of poverty for under-65s was 5 per cent. The risk of poverty is higher for women, especially women over 75, than for men. For 31 per cent of women over 65 and for 37 per cent of women over 75, the income was less than 60 per cent of the median income; for men, the respective figures were 12 per cent and 10 per cent. (See Appendix 2). In recent years, the relative risk of poverty for the elderly has been very close to that for the entire population, with the at-risk-of-poverty threshold set at 50 or 40 per cent of the median income. If the poverty threshold is set at 60 per cent, however, the risk of poverty for the elderly clearly increases. Thus, a relatively large percentage of the elderly has an income between the 50 and 60 per cent brackets.

All poverty indicators are far from straightforward, however, which is something that should be taken into account when the results are examined. Several important factors should be considered when the results are being interpreted. For instance, the data from ECHP surveys do not cover benefits in kind, owner-occupied housing (imputed rent), property or other important factors related to the standard of living of the elderly. This affects the risk of poverty of the elderly in particular.

According to national statistics[2], the income of 10.5 per cent of over-65s, with imputed housing income taken into account, remained below 60 per cent of the median income in 2001, while the risk of poverty for under-65s was 10.8 per cent. Among 13.1 per cent of women over 65, the income was less than 60 per cent of the median income; among men over 65, the percentage was 6.6. (See Table 2.6.) The income of pensioners can be considered reasonable compared with the situation of other population groups (Figure 2.4).

In recent years, the relative at-risk-of-poverty threshold has risen considerably as earnings have increased. The difference between the median income for those living below the at-risk-of-poverty threshold has remained stable, which means that the income level for those with low income has also risen. For men, the distance from the at-risk-of-poverty threshold has been slightly greater than for women; in other words, low-income men have been poorer than low-income women. (See Table 2.7.)

In addition to the relative risk of poverty, a fixed at-risk-of-poverty threshold can be applied to the examination of low income; in this case, the real income limit (the threshold) remains the same year after year (although adjusted with the cost-of-living index to reflect changes in price level), regardless of any changes in the income level in society. With a fixed 60 per cent indicator (for the 1995 level), it may be noted that the risk of poverty for the over-65s has declined steadily from 1990 (12.7 per cent) to 2003 (2.4 per cent). The risk of poverty for the elderly remains lower than that for the population as a whole. (See Table 2.8.)

Maintaining a reasonable and stable income for the pensioners also in the future compared with the working population, requires that the costs arising from the ageing of the population remain reasonable and are divided evenly between the different generations. Pension funding alleviates the pressures to increase pension contributions as the population ages and equalises income distribution between the generations. Finland has been preparing for the retirement of the post-war baby-boom generation as a partial funding system has been in place in the statutory earnings-related pension scheme since it was introduced. The development of the level of contributions is examined in the context of Chapter 3.

2.2.3 Taxation

Finland has traditionally been a country of even income distribution. Throughout the 1990s, income distribution among the elderly population was more even than that among the population as a whole. Income distribution among the over-65s in Finland (S80/S20, i.e. the median income among the one fifth with the highest income divided by the median income among the one fifth with the lowest income) is among the most even in the EU (see Appendix 2). The comprehensive statutory pension provision in conjunction with taxation and other social income transfers have resulted in reasonable income disparities among pensioners compared with the entire population.

National pensions and earnings-related pensions are taxable income. Because of the pension income deduction granted in income taxation, however, no tax is collected for

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[2] Statistics Finland, Income Distribution Statistics. (The figures also correspond more closely with the new EU Survey on Income and Living Conditions, or EU-SILC, which has replaced the EHCP surveys and where imputed housing income are included in the income concept.)

pension income to the amount of the full national pension. The pension income deduction lightens the taxation of pensioners on small incomes. All taxable earned income and pensions reduce the amount of the pension income deduction. The deduction is granted until the income exceeds a certain limit. (See Table 2.9.)

If the pension income is about EUR 8,000 – 16,000 a year, the pensioner's marginal tax rate will be higher than the marginal tax rate for a person who earns the same amount of income in wages due to the smaller pension income deduction. Average pensions fall within this range of high marginal tax rate.

As a rule, tax treatment of the supplementary pension provision in the 2nd pillar is equal to that of the statutory pension provision. It is based on the EET model: contributions are deductible, the return on funds is not taxed during the period of saving, and pensions are taxable income. Taxation of earned income in Finland is progressive, while capital income is subject to a flat tax rate (28 per cent in 2005). A set of amendments to income tax provisions concerning voluntary pension insurance (3rd pillar) came into effect at the beginning of 2005. The main structural changes introduced relate to a transfer to capital income taxation in the taxation of voluntary pension insurance savings and a reform of the deduction system. Taxation of voluntary individual pension insurance taken out by taxpayers for themselves or their spouses falls under capital income taxation and the premiums are deducted from capital income. Pension paid under the insurance will be subject to capital income taxation. The minimum retirement age for tax deductibility of premiums was raised by two years from 60 to 62; it is hoped that this will help reduce incentives for early retirement.

2.2.4 Indexation

The value of statutory pensions is maintained through indexation. In the case of earnings-related pensions, a wage coefficient is applied to earnings made during a person's career, with the weight of the earnings index at 80 per cent and the weight of the consumer price index at 20 per cent. In the case of all earnings-related pensions under payment, an index is used where the weight of the earnings index is 20 per cent and the weight of the consumer price index 80 per cent.

National pensions are adjusted yearly by a national pension index that follows changes in consumer prices. For national pension recipients, therefore, the level of the pension provision has risen at a slower pace than that for the recipients of earnings-related pensions (see Figures 2.5 and 2.6), which has been compensated for with separate increases in the level of the pension. On the other hand, fewer and fewer new pensioners retire on full national pension, and earnings-related pension has increasingly become a basic pension supplemented by national pension.

As the calculations in Figure 2.7. illustrate, pensioners' purchasing power increased steadily throughout the 1990s. The calculations outline the development of the purchasing power of a person retiring in 1991 from a variety of income levels, with taxation and price level changes taken into account. During the recession, pensioners' purchasing power was reduced by heavier taxation, but it began to rise again in 1995 as a result of lighter taxation. In the case of small pensions, purchasing power has remained about the same: because of the pension income deduction, changes in taxation have less impact on the amount of pension than on higher income levels.

2.2.5 The reform of the earnings-related pensions

The reform of the Finnish earnings-related pensions entered into force at the beginning of 2005. While the reform will strengthen the sustainability of the earnings-related pension scheme for the changes in working life and the new conditions arising from population ageing, this pension scheme will be made more equitable than it is today as far as determination of pension provision is concerned. The reform of the earnings-related pensions will improve equality between careers as pensions will no longer be calculated on the basis of individual periods of employment but on earnings from the entire career. The amount of the pensions will thus not depend on what types of employment people have had during their careers. People with equal earnings during their careers will have an equal amount of earnings-related pension. The earlier calculation method was more advantageous for people who had long-term permanent employments. In addition, the new rule for determining the amount of the pension increases equality between employees as all pensions are calculated similarly irrespective of the employees' positions or lines of work.

An old-age pension now starts to accrue from the age of 18 instead of the previous 23. It accrues at the rate of 1.5 per cent per year of employment until the age of 53, at the rate of 1,9 per cent between ages 53 and 62, and at the rate of 4.5 between ages 63 and 67. As far as the national pension is concerned, the retirement age for the old age pension is retained at 65. Earnings-related pension accrued from work after the age of 63 will not reduce the amount of the national pension. Before the reform, the accrual was 1.5 per cent per year until the age of 60 and 2.5 per cent per year between ages 60 and 65.

A person may retire on an early retirement pension at the age of 62; in such a case, there will be a 0.6 per cent reduction for early retirement per month until the age of 63.

According to the 2005 legislation, earnings-related pensions granted to a person will not be integrated (= confinement of the pensions to a target level) and the 60 per cent ceiling (for pensionable earnings) will be removed. This amendment is in line with the key objectives of the earnings-related pension reform on deferring the age of retirement and increasing incentives for work.

The new calculation rules will only apply to pension accrued from the beginning of 2005. Pensions accrued from employment before 2005 are calculated according to the old rules. The reform will not affect pensions already under payment. The principles applied to private-sector earnings-related pensions are also applied to local government and State sector earnings-related pensions.

The reform has also improved the earnings-related pension provision during unpaid periods and brought equality for people in different labour market positions where pension provision accrued during unpaid periods. Before the reform, unpaid periods would have different effects on pensions governed by different pension Acts.

During unpaid periods, pension now accrues by 1.5 per cent per year, irrespective of the person's age. From the beginning of 2005, pension will also accrue during periods when a wage-earner is paid earnings-related allowance. Earnings-related pension will not accrue from minimum-level benefits, except parental allowance. Pension accrues from earnings used as the basis of calculating the benefits paid or from a specific percentage of the earnings, depending on the type of benefit. Pension accrues from the following social benefits:

– unemployment allowance, parental allowance, training allowance, sickness allowance and rehabilitation allowance;
– compensation for loss of earnings under motor insurance or accident insurance;
– job alternation compensation and adult education subsidy.

In addition, according to a separate Act enacted in conjunction with the earnings-related pension reform, pension also accrues during 3—5 years of studies for a degree or diploma and from child home care allowance paid for the first three years to a parent looking after his or her child. The amount of pension accrued from these periods is based on calculated earnings of about EUR 538 (in 2005). These benefits will not reduce the amount of national pension.

The pension reform helps adjust the pension system to the continuous increase in average life expectancy. In order to prepare for the increase in average life expectancy, a life expectancy coefficient will be used in the calculations. This coefficient is determined separately for each age group at the age of 62. The same life expectancy coefficient is used for both men and women. The life expectancy coefficient will be determined for the first time in 2009 for those born in 1947, with the value of 1. The first age group whose old-age pensions may be affected by the life expectancy coefficient are those born in 1948. (See Figure 2.8.) In the future, the amount of the starting pension will thus depend on the development of life expectancy. Reductions in pension caused by the coefficient can be compensated for through longer careers. (See Chapter 3.)

The reform promotes intergenerational income distribution by improving the linkage between contributions and benefits and by aiming at an optimally even development of pension contributions over time. The reform will curb the increase in pension expenditure and increase pension funds. In the long term, the reform will reduce the growing pressure from pension contributions on the younger generations. (See Chapter 3)

2.2.6 The role of supplementary pension provision

The percentage of supplementary pension provision arranged by the employer (2nd pillar) has recently decreased to a significant degree. However, the percentage of independently acquired pension provision has increased over the past few years, a trend which is likely to continue. (See Figure 2.9.) Alterations in the level of the statutory pension provision also contribute to this trend. The 2005 pension reform contains factors that raise the pension level as well as those that lower it. Aspects that raise the pension level include expansion of accrual periods, rises made in accrual rates at the end of careers, the wage coefficient and accrual of pension during so-called unpaid periods. Aspects that lower the pension level are the life expectancy coefficient and the career average principle. Future working careers will also have an essential impact on the level of pension provision. Longer careers compensate for the impact of factors that reduce the pension provision.

Individual pension insurance policies are defined contribution-type arrangements. In 2004, slightly more than one half of the total contribution income was related to pension insurance policies based on a technical rate of interest. Most of the contributions to new insurance policies are related to investment-linked insurance policies, where the risk for the return from the insurance is borne by the policyholder. Investment-linked allocation is most common at the early stages of the policy. The contributions under individual pension insurance policies are paid for an average of 23 years.

2.3 Challenges

The challenges for the future are the same as during the previous round of reporting. The most important challenge for the financing of pensions and the solidarity between generations in the coming decades is to slow down the rise in the economic dependency ratio. The economic dependency ratio is increased by the ageing of the post-war baby-boom generation, low fertility rate, early retirement and unemployment. The pensioners' percentage of the population is increasing at a rapid pace, and in 2030 one in four Finns will be over 65.

Low income levels and the risk of poverty faced by pensioners are connected with the structure of the pension system and the minimum level of pension. The number of low-income pensioners largely depends on their employment history. In the case of a short employment history, the total pension consists mostly of national pension. If a low-income worker's employment history is shorter than the customary, continuing to work will increase the total pension only partially, as the earnings-related pension reduces the amount of national pension. Employment after the age of 65 will not reduce the amount of national pension.

The current persistent long-term unemployment, the exclusion of untrained young people from the labour market and their social exclusion will show as an increase in the number of low-income pensioners in the future, unless their unemployment and exclusion can be prevented. For aged unemployed people, a permanent return to the labour market is often hampered by poor education, poor health or other reasons. Young people aged 18-24 at risk of exclusion and without post-basic education account for about 10 per cent of the age group (Figure 2.10.). Helping excluded people back to the labour market is not only a challenge in terms of pension policy but a major challenge for adult education, labour policy and rehabilitation, as well.

The pension levels of those receiving only national pension may lag behind the living standards of other sections of the population particularly in cases of a lengthy retirement period. National pensions are tied to a cost-of-living index, which ensures the purchasing power of the pensions. However, the real growth of the national pension lags behind the level of wages and earnings-related pensions, and improving the real level of national pensions will require separate policy decisions. The backwardness in the pension level affects especially young people on a disability pension under the national pension and aged women on old-age pension, many of whom have accrued no earnings-related pension at all and are facing a lengthy retirement period. Nevertheless, the number of people living solely on national pension is declining continuously.

2.4 Future prospects

Securing the income of pensioners and the development of public social and health care services are essential objectives for the Government.

The development of the level of the national pension is monitored and care is taken to ensure that its recipients get their share of the increased welfare in society. This can be achieved by separate increases in the level of pension and index increases, for instance.

For a growing number of pensioners, income is mainly based on earnings-related pension. Social exclusion and poverty are best prevented through achievement of employment targets. The pension reform will improve the incentives for staying longer on the labour market and the opportunity for adequate pension provision. A higher 'incentive accrual' of pension after the age of 63 aims at both lengthening people's careers and improving their opportunities to acquire adequate pension provision. However, the incentive accrual will not benefit those excluded from the labour market such as people with disabilities or the long-term unemployed. Furthermore, accrual of pension from unpaid periods (e.g. child care leave) will protect the recipient from loss of accrual during career interruptions and improve reconciliation of work and child care in particular. Accrual of pension provision during unpaid periods will therefore improve the pension level for women in particular.

In accordance with the Government Programme, adequate income security must be guaranteed to prevent poverty and social exclusion. Falling outside income security may reduce a person's income considerably. Programmes on developing working life will be continued and expanded with a greater emphasis on reconciliation of work and family life, protection of employees' mental health, well-being at work and capabilities to cope with the work. Intensification of rehabilitation also aims at these targets. Vocational rehabilitation became a statutory benefit at the beginning of 2004. Thus, an employee or a self-employed person has the right to apply for rehabilitation and is entitled to an appealable decision. Rehabilitation aims at preventing a person from being forced to retire on a disability pension or at helping them back to the labour market.

3 Financial sustainability of pension systems - sound financial basis

Target 4: Achieve a high level of employment through, where necessary, comprehensive labour market reforms, as provided by the European Employment Strategy and in a way consistent with the Broad Economic Policy Guidelines (BEPG).

Target 5: Ensure that, alongside labour market and economic policies, all relevant branches of social protection, in particular pension systems, offer effective incentives for the participation of older workers; that workers are not encouraged to take up early retirement and are not penalised for staying in the labour market beyond the standard retirement age; and that pension systems facilitate the option of gradual retirement.

Target 6: Reform pension systems in appropriate ways taking into account the overall objective of maintaining the sustainability of public finances. At the same time sustainability of pension systems needs to be accompanied by sound fiscal policies, including, where necessary, a reduction of debt. Strategies adopted to meet this objective may also include setting up dedicated pension reserve funds.

Target 7: Ensure that pension provisions and reforms maintain a fair balance between the active and the retired by not overburdening the former and by maintaining adequate pensions for the latter.

Target 8: Ensure, through appropriate regulatory frameworks and through sound management, that private and public funded pension schemes can provide pensions with the required efficiency, affordability, portability and security.

3.1 Policy objectives

To ensure sustainable financing for pensions, the objective is to raise the effective retirement age by about three years in the long run. While the pension reform launched in 2005 will adjust pension expenditure to the increase in average life expectancy in the future, pressure to raise pension expenditure and pension contributions will remain considerable. The rate of return for pension fund investments should be raised to curb any pressure to raise pension contributions. Because the Finnish system is based on benefits and partial funding, the return from the investments will affect the level of pension contributions. The funding level of the pension system will rise in the future, increasing savings in the national economy.

The main target in ensuring the financing basis for pensions is to raise the employment rate and reduce unemployment. The Government aims at increasing employment by at least 100,000 people by 2007 and to raise the employment rate to 75 per cent by 2011. The Government aims to reduce structural unemployment and prevent social exclusion. It also aims to ensure the availability of skilled labour and prepare for a shortage of labour force arising from the changes in the age structure of the population. The

Government also aims to promote the training of young people and their placement in the labour market and to reduce youth unemployment, and to prevent and reduce long-term unemployment. Government programmes and measures related to labour market policy and education policy should also address the needs of employees and employers better than they do currently. In addition to the economic incentives included in the pension reform, staying longer on the labour market should be made an attractive option, which requires improving the quality of working life as well. To increase employment and the purchasing power of wage-earners, the general incomes policy settlement for 2005–2007 includes lighter taxation of work. Reducing central government debt is also an important objective.

3.2 Current situation

3.2.1 Pension expenditure

After a long decline, the ratio of Finnish social expenditure to GDP turned slightly upwards at the beginning of this decade. Social expenditure is of the average EU level, about 27 per cent of GDP for 2003. Public pension expenditure under social expenditure in 2003 was 11.7 per cent of GDP. National pensions accounted for 16.5 per cent of the pension expenditure, earnings-related pensions for 77.2 per cent and other pensions for the remaining 6.3 per cent (see Figure 3.1).

Because the Finnish statutory pension system (1st pillar) is comprehensive and provides reasonably good benefits, the 2nd and 3rd pillars are much less significant for pensioners' overall income security. In 2003, these so-called supplementary pensions were paid for a total of EUR 0.6 billion (0.4 per cent of GDP), of which individual pension insurance (3rd pillar) accounted for about one third.

3.2.2 Financing of pensions

Private-sector earnings-related pensions are financed through pension contributions from the insured persons and the employers and through return from pension funds. The pensions of seafarers, self-employed persons and farmers are co-financed by the State. National pensions are financed through employer contributions and through taxes. In 2004, transfers from the State budget to pension costs amounted to EUR 4.6 billion, which was approximately 3 per cent of GDP.

The earnings-related pension expenditure for each person over 68 in 2005 is about EUR 10,500; the national pension expenditure for each person over 65 is about EUR 3,300.

Because of the decentralization of the pension system, pension contributions vary between sectors. The private sector accounts for more than 60 per cent of the premium income. In 2005, the average earnings-related pension contribution in the private sector is 21.6 per cent of the employee's pay. In the local government sector, the contribution is 28.3 per cent of the wage and salary sum; in the State sector, 23.4 per cent. A majority of these contributions are paid by the employers. In 2005, employee contributions, which are the same in all systems and are included in the percentages mentioned above, are 4.6 per cent of the pay of employees under the age of 53 and 5.8 per cent of the pay of employees aged 53 or older. The rest of the contribution is paid by the employer. National pension contributions paid by employers are 1.4 – 4.5 per cent of the wage and salary sum, depending on the degree of capital-intensiveness of their operations.

Total operating costs of statutory pension insurance, deducted by investment management costs, in relation to contribution income were 2.8 per cent in 2003; this included the statutory earnings-related pension and national pension.

Employers' contributions to the pension provision under the 2nd pillar have remained at about 2 per cent of the wage and salary sum. The employee can also contribute to the payment of pension contributions, except in cases where the insurance policy has been provided by a company pension fund. Employees' contributions have been less than 0.5 per cent of the wage and salary sum. Contributions for individual pension arrangements under the 3rd pillar have been about 3 per cent of the wage and salary sum.

For supplementary pension provision, total operating costs minus investment management costs, in relation to contribution income were 8.1 per cent in 2003.

3.2.3 Funding of pensions

Financing of the statutory earnings-related pensions is for the most part based on the PAYG system. Partial funding for private-sector pensions has existed since the system was launched in 1962. The public-sector pension systems were originally based purely on a PAYG system. To curb the increase in pension contributions, buffer funds were later founded for the public sector: the Local Government Pension Institution began funding for pensions in 1988 and the State Pension Fund in 1990.

The funding rate in regard to statutory earnings-related pensions in the private sector was more than a quarter (27 per cent) of the value of the accrued pension entitlements in 2004. The statutory pension funds amounted to about 59 per cent of GDP in 2004, and are projected to rise to almost 80 per cent of GDP by 2020. (Figure 3.2). Private-sector pension funds stood at EUR 64.1 billion at the end of 2004, which was about 1.6 times the private-sector wage and salary sum; public-sector funds amounted to EUR 23.8 billion, which was about 1.4 times the public-sector wage and salary sum.

The breakdown of total investments under the pension funds at the end of 2004 is presented in Figure 3.3. The market-value return from pension funds in 2004 was 8.1 per cent. The average return on the pension fund assets in 1998-2004 was in nominal terms 6.0 per cent and in real terms 4.4 per cent per year. In future projections, the expected real long-term return for pension fund assets is 3.5 per cent.

The partial funding of private-sector earnings-related pensions will reduce pressure to increase contributions as half of the projected rise in the pension expenditure percentage will be covered by increasing the contributions, while the rest can be financed through the return from the funds. So far, private-sector pension contributions have exceeded pension expenditure. Around 2014, however, pension expenditure will exceed the sum of pension contributions and the difference will be covered by return from the pension funds (Figure 3.4). It has been agreed that the funding of private-sector pensions will be increased by 7.5 per cent of the private-sector wage and salary sum in 2003–2013. This decision reflects the need to prepare for the retirement of the baby-boom generation and maintain a steady rise in contributions.

The objective of the local government pension fund is to keep the pension contributions below 30 per cent of the wage and salary sum through the returns from the fund. The purpose of the State Pension Fund is to gather funds that will help to reduce the pension cost burden when the baby boom generation retires, which will mark the peak years for pension expenditure.

Supplementary pensions are fully funded. At the end of 2003, the size of 2nd pillar pension funds was about 6 per cent of GDP and the size of 3rd pillar pension funds was about 4 per cent of GDP. The rate of return for company pension funds in 2003 was 7.9 per cent and for industry-wide pension funds 7.5 per cent. For 3rd pillar pension funds using a technical rate of interest, the rate of return was 5–7 per cent. The average return from company pension funds in 1998-2003 was 7.3 per cent and from industry-wide pension funds 7.0 per cent.

3.2.4 Employment and unemployment

After the slowdown of the first years of the current decade, the outlook for the Finnish economy is now brighter as the global economy has picked up. In 2004 the average employment rate (the number of employed people in relation to the working-age population) was 67.2 per cent (see Figure 3.5). The average employment rate among men was 68.9 per cent and women 65.5 per cent. (See Figures 3.6 and 3.7.) In Finland women have traditionally been actively involved in working life, and the infrastructures of the Finnish welfare state have, since the beginning, been developed in a way that supports women's gainful employment, through comprehensive child care services and individual social security rights for the entire population. The improvement in the employment rate among ageing people has been among the best in the EU in this decade, something that is partly based on the restrictions made on early retirement pensions.

The unemployment rate has varied between 8 and 9 per cent in recent years; the long-term unemployed account for about one quarter of the unemployed. At present, unemployment affects mostly the oldest age groups and regionally the so-called development regions of Northern and Eastern Finland. A large number of older workers permanently lost their jobs as a result of the depression in the 1990s. A particular risk in the employment development of young people is the permanent exclusion of school drop-outs and unskilled young people from the labour market. A major reason for regional unemployment is the concentration of economic growth in population centres. The scale of the grey economy in Finland is very low, combated by broad cooperation between the authorities.

The main target of Prime Minister Matti Vanhanen's Government is to improve employment. This is to be achieved through reduction of unemployment and deferment of retirement from working life. Attaining the employment targets has become an even greater challenge because of the globalisation of the economy, for instance.

In order to raise the overall employment rate, measures have also been taken to lower the threshold for self-employment and legal provisions on social and pension security have been reviewed to facilitate the transition from wage-earner to self-employed person, for instance, in such a way that the former wage earner's social security remains intact. Self-employed persons' pension contributions have been made more flexible to allow for temporary changes in their business operations. The aim of this amendment is to raise the level of self-employed persons' pensions and to take their solvency into better consideration. During good years, self-employed persons can improve their pension provision by paying higher pension contributions without a permanent rise in their confirmed income. When times are harder, the premiums can be lowered. In this way, the pension will accrue more in good years and less in poorer years.

3.2.5 Transferability of pensions

From the employees' point of view, the significant aspect of statutory pension provision is that each period of employment, even a short one, will add to the earnings-related pension and that the pension provision already earned will not be lost when an employment ends. The values of pension entitlements accrued cannot be transferred, however. An exception to this is the possibility of transferring pension entitlements between the Finnish earnings-related pension system and the pension systems of the European Communities.

Earnings-related pension accrued in Finland is paid from Finland to any foreign country irrespective of the payee's nationality. Exceptions to this are unemployment pension and part-time pension. Under Council Regulation No. 1408/71, unemployment pension is only paid to EU and EEA countries[3]. Part-time pension is paid only for part-time work performed in an EU or EEA country or a country with which Finland has a social security agreement. Part-time pension is therefore paid only to these countries. Under Finnish legislation, national pension is only paid to people residing in Finland. Restrictions on paying national pension to foreign countries do not apply to pension recipients moving to another EU or EEA country who, during their careers as an employee or self-employed person, were governed by Council Regulation No. 1408/71.

A right to transfer supplementary pension entitlements or funds from one supplementary pension scheme to another has not been considered expedient in Finland, as supplementary pensions have no significant bearing on the overall pension provision nor do they constitute a hindrance to the mobility of the workforce. Supplementary pensions are considered as part of corporate personnel policies rather than essential elements of pension provision. Particularly because of their small amounts, supplementary benefits are comparable to staff benefits which cannot be transferred from one job to the next. According to the Employment Contracts Act, an employee's right to supplementary pension provision will remain in the case of a transfer of business, however. Furthermore, about one half of those provided with supplementary pension are entitled to retain accrued pension rights as a vested period. Accrued supplementary pension provision is not transferred from one pension institution to another.

3.3 Challenges

3.3.1 Employment

Longer working lives and staying longer on the labour market are still major challenges for the Finnish pension system. In 2004, 83 per cent of Finns retiring on a pension were

[3] Council Regulation (EEC) No. 1408/71 on the application of social security schemes to employed persons, to self-employed persons and to members of their families moving within the Community

under 65 years old. This is a slight improvement on the situation during the previous reporting round, when the percentage was 86. Two out of three persons aged 60-64 are currently pensioners. The most common reason for this is reduced work ability. The employment rate among 55-64-year-old men, the raising of which was named as a particular challenge in the previous report, has risen from 42 per cent to 51 per cent. The 2005 pension reform has significantly reduced pathways to early retirement.

The age at which people withdraw from the labour market should be raised since the projected change in the population's age structure is likely to cause a shortage of labour. The number of working-age people will begin to decline in 2010 and the size of the labour force around 2006, which will weaken the conditions for economic growth. However, pension policies offer only a limited expedient to defer people's retirement. Therefore, it is essential to develop working life in order to promote ageing people's staying on the labour market. Particular challenges are related to maintaining work ability, favourable attitudes among employees and work communities, and employees' occupational skills. For women in particular, reconciling work and family life without restricting their involvement in the labour market is a challenge.

One of the challenges related to longer working lives for younger age groups is providing earlier entry into the labour market and making workers' skills meet the needs of working life more precisely than before. With regard to entry into working life in Finland, 80 per cent of those aged 26 are in the labour market. A special challenge is to hasten the transfer from upper secondary education to post-secondary education, which currently takes two to three years on average, and to reduce the duration of post-secondary education. With regard to safeguarding the proper functioning of the labour market, Finland's goal is to ensure as high a level of education among its citizens as possible.

In the Finnish statutory pension system, disability pensions, early old-age pension and part-time pension are pension benefits payable before the statutory retirement age. Disability is the most common reason for retiring on early retirement pension (see Figures 3.8 and 3.9). As a rule, such a pension is granted for medical reasons related to the individual's health or work ability. Thus the incentives for early retirement are mainly linked to the two pension types mentioned last. Vocational rehabilitation supports a person's staying in the labour market. The purpose of vocational rehabilitation is to improve or maintain a person's work capacity and earning potential. Vocational rehabilitation includes career guidance, assessment of rehabilitation need, trial work and training, labour market training, vocational and other training, vocational guidance and work placement, financial assistance to help with self-employment, technical aids for work and study and subsidy for arrangement of working conditions. Vocational rehabilitation became a statutory earnings-related pension benefit at the beginning of 2004. The options for rehabilitation are always established before a decision is made on granting disability pension. Causes for disability pension are presented in Table 3.1. Mental health problems have become the most common reason for retirement on disability pension.

The average age of retirement in Finland is 59 years. Future projections concerning the retirement age are based on the expected effective retirement age (i.e. expectancy), an indicator introduced in 2003. This indicator describes trends in retirement ages quite accurately as it is not affected by the population's age structure. According to recent calculations, the average age of retirement in Finland in 2004 was 59.1 years; the year before, the average age of retirement was 58.9. These figures include both private-sector and public-sector earnings-related pensions. (See Figure 3.10.) Wage and salary earners' expected effective retirement age is expected to rise by two years by 2025 and by three years by 2050.

In the case of dismissals of ageing employees, employers can transfer them to a so-called unemployment path to retirement, which means that the employees can retire on unemployment pension after receiving daily unemployment allowance for a specific period. This option is sometimes also taken by older workers themselves as a way of withdrawal from the labour market. These are considerable problem since over-55s are unlikely to find new employment and will therefore retire on unemployment pension at the age of 60. Since unemployment pension is now being removed from the pension system, people born in 1950 or later will not be entitled to unemployment pension. However, they may, under certain conditions, receive unemployment allowance until the age of 65 or retire on old-age pension at 62. The reform of earnings-related pensions raises the minimum age for the unemployment path to retirement by two years to the age of 57. Now that the income security of ageing long-term unemployed people is managed through the unemployment security system, providing opportunities for them to find work has become a special challenge.

The fact that major employers bear the costs of their own corporate unemployment pensions has been considered a serious obstacle to employment of older workers, who are facing a higher risk of unemployment. On the other hand, additional employer contributions have been considered to encourage employers to look after ageing employees' health, as healthy employees mean lower disability costs. High additional employer contributions have been presumed to encourage employers to prevent employees' illnesses and disabilities. With regard to private-sector company pension funds and industry-wide pension funds, employers are responsible for their own corporate pension costs irrespective of the size of the company.

In 2006 and 2007, employers' responsibility for disability pension costs will change in ways that will reduce annual fluctuations in disability pension contributions. First of all, disability costs will be divided between pension institutions in proportion to the person's earnings from the two years preceding disability. The reform will level out any disability pension costs incurred during the first years by the employer from hiring an older worker, for instance. In addition, there will be changes in the basic amount of the employer contributions and in employer contributions for deductibles payable by large employers. The basic contribution based on the insured person's age will continue to increase with that person's age to some extent, but cease to depend on age from 2007 onwards. Depending on the size of a large employer, part of the basic contribution is currently replaced by an employer contribution for deductibles. As of 2006, employer contributions for deductible will be changed into a risk based contribution, with large employers placed in different payment categories on the basis of actual disability costs. The risk based contribution will be determined for each age on the basis of disability risk. The change will reduce fluctuations in disability pension costs incurred by large employers: the various categories are based on data from a number of years, disability pension costs will in general not be affected by isolated disability pension cases, and the costs within each category will be shared by the employers.

Aiming simultaneously at both a high employment rate and high productivity is quite a challenge as achieving the former may require cutting back on the latter. In the light of recent trends in the global economy, it is also important to keep jobs in Finland, as the financing of the Finnish pension system is mainly based on a pay-as-you-go principle.

3.3.2 Trends in pension expenditures, pension funds and pension contributions

According to forecasts, social expenditure will increase from today's 27 per cent to 30.6 per cent of GDP by the year 2030 and remain at that level until 2050. The fastest growing expense item in social spending is pension expenditure. According to current estimates, population ageing will raise pensions expenditure by more than 3 percentage points from 11.7 per cent to more than 15 per cent of GDP by the 2030s. From then on, pension expenditure as a percentage of GDP will decline and then settle at above 14 per cent. The expenditure on earnings-related pensions will increase by 5 percentage points and the expenditure on national pensions will decrease by about one percentage point in ratio to total production. (See Figure 3.11.)

According to recent calculations[4], private-sector earnings-related pension contributions will rise by about 6 percentage points from today's 21.6 per cent by the 2030s; after that, there will not be any major change (see Figure 3.12.). The pension reform will significantly reduce pressure to raise pension contributions in the private sector. Pension contributions in the public sector (local and central government) are calculated to stay at the current level in the long term. By 2050, the average amount of employers' national pension contribution is calculated to go down steadily by less than one percentage point from today's more than 2 per cent.

More than a quarter of all statutory pensions are financed out of the State budget. In 2004, statutory pension expenditure was a total of 11.4 per cent in relation to total production; pensions financed out of the State budget amounted to 3.1 per cent of total production. Most of the pensions financed by the State, or two-thirds, are State employees' earnings-related pensions; the remaining one third are national pensions and earnings-related pensions of farmers, self-employed persons and seafarers, which are covered by the State where pension contributions are not sufficient.

In the future, the State's share in financing of statutory pensions will mostly decline as national pensions account for less and less of the overall pension provision and the level of earnings-related pensions increases. The State's share in financing for pensions will probably go down from today's 3 per cent of total production to 2.5 per cent by the year 2050. As total pension expenditure rises to about 15 per cent of total production, the current 27 per cent State financing of total pension expenditure will drop to about 17 per cent by 2050.

With regard to the financing of pension expenditure, the proportional shares of the various factors will change in the future as the return from pension funds and the percentage of employees' contributions will rise and the percentage of employers' pension contributions will decline.

According to calculations, statutory private-sector pension funds can be increased on the basis of decisions already made so that the funding rate for statutory pension funds will

[4] Finnish Centre for Pensions: Pension expenditure, pension contributions and pension funds up to 2075

rise 4 percentage points to 31 per cent by the year 2029. At that point, pension funds would amount to about EUR 133 billion (at 2004 prices) or 59 per cent of GDP.

Private-sector funds will be used for payment of old-age pensions and disability pensions. The funds will accrue as people's future old-age pensions are funded during their careers and disability pensions are funded with a lump sum at the inception of a pension. According to calculations, these will have the combined effect of increasing until 2075 as old-age pension liabilities increase.

It is calculated that the local government pension fund will grow until the year 2030 and then decline to the 2025 level of more than EUR 37 billion (at 2004 prices, about 18 per cent of GDP). The target for State funding rate is of the same level as for private-sector funding. It is calculated, that the State Pension Fund will grow to about EUR 18 million (at 2004 prices, about 9 per cent of GDP) by the year 2020.

The annual combined surplus of the authorized pension providers is about 2.5 per cent of GDP.

As the private and public-sector earnings-related pension reform is being gradually implemented from the beginning of 2005, increases in both the earnings-related pension expenditure and pension contributions are expected to remain far below what they would have been under the former legislation. In particular, the introduction of the life expectancy coefficient and replacement of the final earnings principle with a career average principle will curb rising of costs in the future. It is calculated that the 2005 pension reform will reduce the increase in the 2050 pension expenditure by one percentage point of GDP. A major challenge is, however, to raise the effective age of retirement by 2—3 years, as envisaged in the pension reform, and also to make younger age groups enter the labour market earlier than their predecessors have.

While the main emphasis of the Finnish pension policy is on statutory pension provision, supplementary pension provision may be required if the earnings level or employment career do not guaratee an adequate pension. The percentage of supplementary pension provision expenditure of GDP is expected to remain the same as today.

3.3.3 Sensitivity analysis of trends in pension expenditure and pension contributions

The following is a presentation of the calculated effects of employment rates, investment return, earnings level, life expectancy and fertility rates on trends in pension expenditure and pension contributions.

Employment rate

Improving employment rates attend to reduce pension expenditure and pension contributions. If the employment rate reached a targeted 70 per cent by 2010 and further nearly 75 per cent by 2050, pension expenditure could be reduced by up to one percentage point from the baseline scenario. (See Table 3.2 and Figure 3.13.) Corresponding changes in pension contributions would be about one third smaller than changes in pension expenditure. In the long term, however, the effects on pension expenditure and pension contributions will level off as the future pension expenditure will accrue from work.

Investment returns

In the baseline scenario for private-sector earnings-related pension contributions, real return from investments is expected to be 3.5 per cent. Raising real return to 4.5 per cent would have no immediate impact on the level of contributions; in fifteen years, however, the level of contributions would decline by one percentage point, and the impact would grow significantly over time (Figure 3.14).

Earnings level

The growth rate for the earnings level has a significant effect on the percentage of pension expenditure of the wage and salary sum, but a less significant effect on the level of contributions. The stability of contributions depends on two factors. Firstly, funding itself reduces the impact of changes in the pension expenditure percentage on the level of contributions. In addition, as the growth rate for the earnings level picks up, the difference between the growth rate for the wage and salary sum and real return from investments grows narrower and funding reduces the level of contributions less than before. Correspondingly, a slower rise in the earnings level will increase the difference between the growth rate of the wage and salary sum and real return from investments, thus emphasizing the effect of diminishing contribution levels.

Life expectancy

While the development of the mortality rate has a high impact on the old-age dependency ratio (65+/20-64), the life expectancy coefficient minimizes its effect on pension expenditure.

Fertility rate

Within the next few decades, the fertility rate is not expected to have any significant effect on the percentages of pension expenditure or pension contributions. In the long term, however, a higher fertility rate (2.1) than applied to the baseline scenario (fertility rate: 1.8) would reduce pension expenditure by more than 4 percentage points with regard to wages and salaries and reduce pension contributions by less than 3 percentage points. A low fertility rate (1.5), on the other hand, would increase pension expenditure by nearly 6 percentage points and pension contributions by nearly 4 percentage points.

3.3.4 Financing gap

The public sector in Finland includes the State, the local government, and social security funds such as pension institutions. The ageing of the population has a particular impact on the pension expenditure and on the social and health care services provided by the local authorities.

In recent years, the overall tax rate in Finland has declined. By international standards, however, the tax rate (44.0 per cent in 2004) seems quite high. Comparisons of overall tax rates in different countries are not unambiguous. There are considerable variations between countries with regard to whether social benefits are considered taxable income, for instance, or whether special deductions are granted to taxes or social security contributions on social grounds. In Finland, most of the income transfer benefits are taxable and deductions which used to be applied to determination of a person's tax-paying ability have been abolished almost entirely.

Central government finances were in balance in 2004 and at the end of the year the central government debt amounted to EUR 63.8 billion, which was about 42.6 per cent of GDP. Because of funding for earnings-related pensions, the general government on the whole showed a 2 per cent surplus in relation to GDP. At the end of 2004, consolidated debt for the entire general government was 45.1 per cent in relation to GDP.

Finland has prepared for the growing pressures on general government financing and expenditure caused by population ageing by adopting a strict policy on expenditure, reducing general government debt, funding for future pensions and strengthening the general conditions for economic growth, for instance. Despite the rapid ageing of the Finnish population, economic competitiveness is considered to be based on a highly trained workforce, a stable economic environment and an efficient public sector.

Central government's structural surpluses and debt reductions help to ensure that a rising expenditure and a diminishing income base due to the population ageing will not begin to increase central government debt and/or the tax rate again. The recent pension reforms and the funding for earnings-related pensions are also significant in reducing pressure to increase pension contributions in the future. To improve employment, Finland has reformed taxation and social security systems in a way that promotes employment and initiative. Investments in skills and expertise and support for enterprise and innovation aim at stronger economic growth, as do improved efficiency and quality of public services.

According to the baseline scenario for calculations under Finland's latest economic stability programme (2004), the general government (State and local government and social security funds) will retain a surplus until 2020; after that, the surplus will turn into a deficit, with general government debt exceeding 60 per cent in relation to total production within a little over 20 years. In the calculations, the overall tax rate was kept constant at the current level throughout the period under review: pension contributions were let to rise, while other taxation was reduced. The annual surplus of the authorized pension providers was about 2.5 per cent in relation to total production. On the basis of the above baseline scenario, the overall general government would not be on a sustainable basis without adjustment measures or tax increases. If these adjustments were made immediately, tax rates would have to be increased by about one percentage point of GDP. If the adjustment were done to keep pace with demand for supplementary financing, the tax rate would have to be increased by two percentage points.

Finland should therefore maintain the current strategy for at least the next ten years and continue to further reduce the general government debt and accrue pension funds. This will help to create a sufficient buffer against significant cuts in welfare expenditure (income transfers, public services) that may arise once population ageing begins to increase the expenditure. In addition to a stronger general government, favourable conditions must be ensured for economic growth. It is also essential to improve the productivity of public welfare services, which is pursued through promoting new production systems and advanced technology and product development. It is also necessary to raise the rate of return of pension fund investments to curb pressure to increase pension contributions.

The financing of the local government pension scheme is, like the private-sector earnings-related pension scheme, highly dependent on actual economic growth. The size of the local government workforce depends largely on the obligations imposed by society on local government and the response of local government to these obligations. If the current model, which is largely based on local government authorities producing services within their own organizations, is widely replaced by outsourcing, the local government wage and salary sum which constitutes the local government pension contributions may decline significantly. Covering the pension expenditure would require large increases in pension contributions. The increase of the costs of work within local government would probably make outsourcing even more popular with local government, which would weaken the financing of the pension system even further. On the other hand, this would reduce the pressure for financing earnings-related pensions in the private sector. This would not have any major effect on the overall pension expenditure financing needs. If necessary, the financing of the local government earnings-related pension scheme should be reviewed in such a way that the financing of the pension provision will support expedient production of local government services.

3.3.5 Risk management

Regulation of Finnish insurance institutions and preparation of the related legislative reforms are carried out by the Ministry of Social Affairs and Health. The responsibility for the operational supervision of insurance institutions lies with the Insurance Supervisory Authority, which began its work in 1999. While the Insurance Supervisory Authority is an institution subordinate to the Ministry of Social Affairs and Health, it has independent decision-making powers. One of the main responsibilities of the Insurance Supervisory Authority is to protect the interests of the insured, which emphasizes the importance of solvency supervision.

The statutory earnings-related pension scheme for the private sector is decentralized into private pension providers. Employers, who are under the obligation to arrange the statutory earnings-related pension provision for their employees, may opt for its arrangement in a pension insurance company, a company pension fund or an industry-wide pension fund.

To avoid losses for the insured in the event of a private-sector pension institution going bankrupt, the pension institutions' joint liability for bankruptcy has been in place ever since the statutory earnings-related pension scheme for the private sector was launched in the 1960s. Similar guarantee systems were created for industrial injuries insurance, motor third party liability insurance and patient insurance schemes. Thus, all Finnish statutory insurance schemes have statutory guarantee systems; these have not been applied to voluntary insurance schemes, however.

Legislative amendments implemented at the beginning of 1997 introduced a new mechanism for the supervision of solvency. The higher the risks related to the investments of a pension institution, the higher the solvency required from it. The lower the solvency of a pension institution falls, the stronger the measures that the Insurance

Supervisory Authority will have to remedy the problems related to the solvency of the institution under supervision.

Regulations concerning the investment plans of the pension funds under private-sector pension institutions are provided by the law. The Investment plan is drawn up by the boards of directors of the institutions and submitted to the Insurance Supervisory Authority. In addition to the solvency requirements, the investment activities of a pension institution are subject to Decrees on the coverage of the pension liability of pension funds and related regulations issued by the Ministry of Social Affairs and Health and the Insurance Supervisory Authority.

By international standards, the system applied in Finland for the supervision of private pension providers is highly advanced.

3.4 Future prospects

To improve the sustainability of the pension system, Finland has carried out a pension reform which will reduce pressure to increase pension contributions. The pressure will begin to decline around the year 2030, when the level of the pension contribution would settle at about 27 per cent.

The inclusion of a life expectancy coefficient is significant for the sustainability of the financing of the pension system, as costs arising from longer life expectancy can be compensated for by reducing the amount of pension. However, employees may compensate this reduction by working for a slightly longer time.

To ensure as equable a trend in pension contributions as possible, improving the real return on investments in the long term is pursued. Increasing return on investment will help to reduce pressure to increase pension contributions and thus improve sustainability of the pension system. Development of new provisions on investments and the pension liability and solvency of pension institutions is currently underway.

A favourable trend in employment is the main requirement for a sustainable pension system. Essential objectives for sustainable financing are deferring the effective retirement age and improving the quality of working life, which are promoted through adjusting work assignments and routines and working hours to better suit the needs of ageing workers, through age management and through development of working conditions within occupational health care, for instance.

The effects of the pension reform will be monitored actively. For instance, deferment of the retirement age is monitored annually with the help of an annually published expected effective retirement age (see 3.3.1.).

3.4.1 Reform of the earnings-related pensions

Finland has carried out a major reform of the earnings-related pensions, which entered into force at the beginning of 2005. The reform is described in more detail in Chapter 2. The following is a list of elements introduced in the pension reform which will reduce (-) or increase (+) pension level and expenditure:

- In the calculation of pensionable earnings, shift from the rule of the last 10 years' earnings to accrual based on annual earnings (-)
- Wage coefficient (+)
- Application of earnings-related pension indexes to all new pensions (previously applied only to over-65-year-olds) (-)
- Changes in the accrual rate (+)
- Expansion of accrual time (+)
- Unpaid periods (+)
- Life expectancy coefficient (-)
- Reduction in the early retirement pensions and increased staying on the labour market (pension level +, pension level -)

The pension reform will increase intergenerational equity in the long run. It will curb the rising pressure on contributions payable by future generations while ensuring reasonable level of consumption for pensioners. The life expectancy coefficient will reduce pressure to raise pension contributions as it decreases the impact of longer life expectancy by reducing the amount of new old-age pension. The employee may compensate this reduction by working for a longer time.

In order to level out the increase in earnings-related pension contributions in the private sector caused by the baby-boom generation, funding for old-age pension has been increased since 2003 with an optimally stable trend in earnings-related pension contributions as a target. The target is to dimension the additional funding in such a way that it would be 7.5 per cent of the insured wage and salary sum in 2013. Under the current rules, according to recent calculations, private-sector employee pension funds will increase from the current figure of 27 percent to 31 per cent of the value of earnings-related pension entitlements by 2029. It is calculated that the percentage of State pension funds of the value of earnings-related pension entitlements will increase to 35 per cent from the current 13 per cent by 2020. Local government pension funds currently cover about a quarter of the value of pension entitlements; by 2020, they will cover more than one third of the value.

The reform also promotes the prolongation of ageing employees' participation in working life, as it is generally a more favourable option in view of the pension level than retiring before the standard retirement age.

Because of the pension reform, increases in both the earnings-related pension expenditure and pension contributions are expected to remain far below those expected under the former legislation. Nevertheless, the increase of the pension contributions is calculated to be 6 percentage points by the 2030s. Without the pensions reform the growth of the contributions would have almost doubled (see Figure 3.12.b.). The sustainable financing of the pension systems depends essentially on economic growth, employment increase, the relationship between the lengths of working lives and retirement, and returns on investment of the earnings-related pension assets. The reform is expected to increase the employment rate particularly in older age groups, as their retirement ages rise. Reducing early retirement pension schemes and providing more economic incentives for longer working lives aim at deferring retirement. Transitional periods, however, allow early retirement for those born in the 1940s. Achievement of the goals set for the pension reform and the effectiveness of these goals are monitored; and a set of specific indicators have been established for that purpose.

3.4.2 Improving employment

Measures for improving employment

The Finnish Government is carrying out a cross-administrative employment policy programme which will create favourable preconditions for significant improvement of the employment rate. The main goals of the programme are to reduce structural unemployment and prevent social exclusion, ensure the availability of a skilled workforce, prepare for a shortage in the workforce due to the projected demographic change, lengthen working careers, increase the productivity of work, and improve the organization of work and make it more meaningful.

Ways of reducing structural unemployment and raising the employment rate include for instance dissociation of employment service and services for people with low employment potential by centralizing the latter services and related resources in forty labour service centres, which will be established in 2004–2006.

Active labour policy programmes are being developed for prevention and reduction of long-term unemployment. The aim is to ensure that labour and education policy programmes and measures will meet the needs of both employers and jobseekers better than they do now. Individual activation programmes should be drawn up for all long-term unemployed persons, who will also be offered long-term service processes, and all young persons will be offered training, work practice or workshop activities after three months of unemployment. The use of labour market subsidy as an active form of support for improving job seeking competences can be increased by making labour market subsidy more of a consideration for the recipient’s actual input and obliging the recipient of labour market subsidy to participate in active labour market measures after a specific period of unemployment.

The Government is committed to the result of the negotiations for general incomes policy settlement for 2005—2007 in such a way that employment, purchasing power and competitiveness are promoted through lower taxation, transport investments and support for innovation. In accordance with the incomes policy settlement, new legislative amendments aiming at improving re-employment opportunities in conjunction with dismissals will come into effect during 2005. Such change security includes measures helping people find new employment in the face of dismissal; these measures include preparation of individual employment programmes, paid leave for finding a new employment, improved unemployment security, and training a mobile group of special experts for employment offices who could be transferred to locations where dismissals of the workforce are taking place.

In conjunction with deciding on the central government framework for 2006—2009, the Government considers that extending the impact of economic growth on employment increasingly to people in weak labour market positions will require special measures to strengthen the demand for labour for low-wage full-time work. This is pursued through reductions in employer contributions.

Promotion of employment will also be supported through taxation policy. The aim of the reform of corporate and capital income taxation which was implemented at the beginning of 2005 was to make taxation of Finnish companies competitive in terms of both the level and the extent of the tax base. For employment reasons, the lighter taxation of earnings has largely focused on taxation of the earnings of those on low or medium incomes.

Incentives for work provided by the pension system

The Finnish pension system contains a number of elements aimed as incentives for longer working lives and making retirement as flexible as possible. Older age groups are encouraged to stay longer in the labour market as this will mean a higher accrual of pension. The life expectancy coefficient, on the other hand, reduces the amount of pension and is thus another incentive for people to stay on the labour market to ensure a sufficiently high pension. Also, the reduction of early retirement pension options serves as an incentive to stay on the labour market. Accordingly, the pension reform has changed early retirement pension schemes significantly for the purpose of achieving the goals mentioned above. Incentives for staying longer on the labour market include the following:

- A more flexible retirement on old-age pension: a person has the right to continue at work until the end of his or her 68th year instead of the previous 65th but also the right to retire on old-age pension earned by the age of 63. In other words, people can choose whether they wish to continue to work and thus accrue the future pension or retire on the pension they have already earned. Pension accrues at the rate of 1.5 per cent of the earnings per year at the age of 18-52, at the rate of 1.9 per cent at the age of 53-62 and at the rate of 4.5 per cent at the age of 63-67.
- Integration of pensions (i.e. the previous 60 per cent ceiling) is abolished, making work always increase the amount of pension.
- The individual early retirement pension is no longer available for people born in 1944 or later. From now on, the occupational character of the disability will be taken into consideration when assessing the right of an employee over 60 to disability pension.
- A person may retire on early old-age pension at 62; in that case, a 0.6 per cent abate for early retirement will be made in the pension for each month before the age of 63 years.
- Unemployment pension will be abolished and the minimum age for continued unemployment allowance will rise by two years to 59 years.
- The 2005 pension reform also brought changes in part-time pension used for gradual retirement. The minimum age for part-time pension rose to 58 years as of the beginning of 2005, applying to employees born in 1947 or later. Accrual of pension from the reduced earnings during part-time pension retirement will drop from 1.5 per cent to 0.75 per cent.
- The life expectancy coefficient will reduce the payable amount of new pensions as of 2010.

The pension reform has strengthened the linkage between contributions and benefits. At the moment, benefits accrue from the age of 18 up to the age of 68 at most, with pension contributions paid during the same period. On the other hand, the pension reform has extended the accrual of pension to periods which are not subject to payment of pension contributions by employees or their employers.

Programmes on development of working life

Reducing the options for early retirement pension and creating positive incentives do not alone suffice to defer the age of retirement: retirement is essentially linked both with employers' ability and willingness to keep on or employ ageing employees and with employees' attitudes, health and work ability, as well as overall development of the social protection system.

To achieve the goals set by the Government – extending careers by 2—3 years – several Ministries, the State, local government authorities and other institutions have launched a number of projects and programmes on development of working life. The national Programme for Promoting the Attractiveness of Working Life (the "Veto" Programme, or "Pull"-Programme in Finnish language) comprises measures on well-being at work and extending working lives. The main message of the programme is that looking after employees' safety, health and welfare creates opportunities for job satisfaction throughout their entire careers. The programme is the latest in a series of projects contributing to the development of working life in Finland, such as the National Programme for Ageing Workers (1998—2002) and the National Well-being at Work Programme (2000—2003). The programme will continue until 2007. The measures taken under the programme and their results are assessed regularly on the basis of given indicators, for instance.

Other similar programmes include the National Working Life Development Programme (2004—2009), which supports development of work organizations based on cooperation between management and personnel and at the same time aims at improving productivity and welfare at work; the "Kesto" action programme (2004—2007) for development of measures based on research data to promote employees' work ability and functional capacity, to promote the attractiveness of working life and to prevent social exclusion; and the "Noste" programme (2003-2007) on raising the educational level of adult workers to improve their staying in the labour market and to improve the employment rate.

3.4.3 Supplementary pensions (2nd and 3rd pillars)

Changes in the legislation on company pension funds and industry-wide funds are currently being prepared in line with the IORP Directive. The projected amendments are designed to allow establishment of new pension funds for voluntary supplementary pension provision and to allow life insurance companies to provide supplementary pension provision.

The Insurance Contracts Act is currently being reformed, which will improve consumer protection with regard to pension provision under the 3rd pillar, for instance.

4 Modernization of pension systems in response to changing needs of the economy, society and individuals

Target 9: Ensure that pensions systems are compatible with the requirements of flexibility and security in the labour market; that, without prejudice to the coherence of Member States' tax systems, labour market mobility within Member States and across borders and non-standard employment forms do not penalise people's pension entitlements and that self-employment is not discouraged by pension systems.
Target 10: Review pension provisions with a view to ensuring the principle of equal treatment of women and men, taking into account obligations under EU law.
Target 11: Make pension systems more transparent and adaptable to changing circumstances, so that citizens can continue to have confidence in them. Develop reliable and easy-to-understand information on the long-term perspectives of pension systems, notably with regard to the likely evolution of benefit levels and contribution rates. Promote the broadest possible consensus regarding pension policies and reforms. Improve the methodological basis for efficient monitoring of pension reforms and policies.

4.1 Compatibility of pension systems with flexibility in the labour market (Target 9)

4.1.1 Current situation

Under the statutory earnings-related pension scheme, pension accrues, as a rule, from all wages and salaries and from all earnings from self-employment. Pension also accrues from certain unpaid periods that are comparable with working life (e.g. child care). As a rule, geographical or sectoral movement will not cause loss of a person's entitlement to pension. Employers must arrange statutory earnings-related pension provision for all their employees irrespective of the length of the employment. Short-term and other atypical employment contracts are also covered by pension provision.

Since the entry into force of the pension reform at the beginning of 2005, pension will now accrue on the basis of annual earnings. Before the reform, pensions were determined separately for each employment on the basis of the wages and salaries of the last ten years: people who had had long careers with an ascending wage trend received better pensions than those who had received equal wages and salaries but had had less consistent working careers. As of 2005, the duration of employments will no longer affect pension benefits, whereas annual earnings will.

For self-employed persons, pension provision is governed by separate legislation. Self-employed persons shall insure their gainful activity in accordance with the Self-Employed Persons' Pensions Act, while the pensions of farmers, fishermen and people engaged in reindeer husbandry are governed by the Farmers' Pensions Act. Self-employed persons' pensions accrue on the basis of annual pension insurance contributions, which are based on their confirmed income. Failure to pay contributions and expiry of the statute of limitations will reduce pension in proportion to the outstanding contributions. To improve self-employed persons' pension provision, the financing of the pension provision has been made more flexible from the beginning of 2005. Self-employed persons now have the option of flexible contributions. Self-employed persons may improve their pension provision by paying higher contributions in good years without an increase in their confirmed income; when times are harder, contributions can be reduced, accordingly. Similar flexibility of contributions is not available to farmers.

As of the beginning of 2005, the eligibility for residence-based social security benefits, such as the national pension, of persons coming from EU or EEA countries or Switzerland to Finland, will be determined on the basis of the duration of their employment or self-employment. The eligibility for residence-based social security begins as of the commencement of the employment or self-employment in Finland, if these last at least four months. When the person falls within the scope of coverage, pension will accrue from the entire duration of the employment or self-employment. Before the pension reform, such a requirement did not exist.

In accordance with the Regulation on the coordination of social security for migrant workers, the pensions of persons moving into the European Economic Area accrue in accordance with the legislation of the country of employment. Today, pensions accrued in Finland can be paid to any country. Supplementary pensions are also paid to countries within the European Economic Area. Supplementary benefits can be paid to countries outside the European Economic Area unless prohibited by the rules of the paying institution.

4.1.2 Challenges

The preservation of pension rights is ensured in Finland in an appropriate manner, and thus this does not present any specific challenges for the development of the system. The pension provision for self-employed persons is not facing any challenges in Finland, either. The main challenge is to develop the pension system in such a way that it will continue to adapt to changes in the labour market and to the increasing diversity of working life.

Development of the pension provision for recipients of art or research grants is currently being investigated as these are not, as a rule, covered by any statutory earnings-related pension scheme.

4.2 Equality between men and women (Target 10)

4.2.1 Current situation

Finland's comprehensive statutory pension system ensures equal treatment for men and women. The benefits, contributions and entitlements under the earnings-related pension scheme are individual and do not depend on the gender of the recipient. The national pension scheme has a key position in the provision of personal, independent minimum pension for those who have remained outside working life. As the national pension is affected by the earnings-related pension, it equalizes the differences in pension incomes between women and men.

In 2003, the average pension based on an old-age pensioner's own career (statutory earnings-related and national pensions), which did not include a survivor's pension payable after the death of spouse, was approximately EUR 1,338 per month for men and EUR 840 for women. The average overall pension for old-age pensioners (including survivors' pensions) was about EUR 1,348 per month for men and EUR 997 for women. The average statutory pension (earnings-related and national pensions) for those who retired on an old-age pension based on their own career (i.e. new retiree) was about EUR 1,652 per month for men and EUR 1,070 for women in 2003.

There are still considerable differences in the pensions between men and women, both in terms of pension accrued from their own careers and the overall pension. The difference between the old-age pension of men and women can be attributed to women's lower wage and salary levels and men's longer working careers, for instance. On average, the duration of women's working career is 1—2 years shorter than men's. Women's wages and salaries constitute approximately 80 per cent of men's wages and salaries. As a rule, women's lower wage and salary level is due to the fact that women are doing work that is lees paid than that of men. Women's wage-earning careers are interrupted more often than men's because of child care, for instance. Furthermore, discontinuous employment and agency work are more common among women than among men; in the public sector, women have more temporary employments than men.

The new provisions included in employee pensions legislation concerning unpaid periods will promote equality between workers. As of 2005, pension will accrue from unpaid periods under the same terms for both permanent employment and temporary employment. As women are more often employed for temporary employments than men, this reform will improve equality between men and women in pension provision. Women working in different sectors will also be on an equal footing with regard to pension entitlements accrued during maternity leave. Men are also eligible for child care leave and thus entitled to pension accrued during that time.

Persons in conscript service or non-military service are covered by the national pension scheme. The aforementioned service periods do not accrue earnings-related pension.

The Government is committed to gender impact assessment in the preparation of legislative and budget proposals. This commitment promotes equality between men and women in the society as a whole, as equality is considered a starting-point in the preparation of legislative proposals and other measures, the impact of which on equality is taken into account. With regard to pension legislation, the first gender impact assessment took place in the context of the legislative proposal relating to the reform of the private-sector earnings-related pension legislation. According to the assessment, the reform would ensure a functional system from the point of view of its impact on equality. Studies and calculations produced for the preparation of the legislation showed that the projected career average model would not create inequality between men and women, nor did it contain any individual features that would be problematic from the point of view of equality between men and women. When the reforms related to accrual of pension during unpaid periods and the impact of the National Pensions Act on the pension provision are taken into account, the reform will narrow the difference between the pensions of men and women in the long run.

Aged women face a clearly higher risk of poverty than men. This is because national pension accounts for most of the overall pension provision for more retired women than retired men. Some women have never been in any gainful employment that would have accrued earnings-related pension. The number of women living on a full national pension declines with each younger generation, however.

Under the Finnish pension system, pension entitlements are not shared between spouses in divorce cases.

4.2.2 Challenges

The Finnish pension system promotes equality. Maintaining the high employment rate among women, narrowing the differences in wages and ensuring adequate levels of pension are nevertheless important challenges. Promoting a more equal distribution of family leave between men and women is also a challenge.

Aged women who have not accrued any earnings-related pension face a particular risk of poverty as divorce or the death of the family provider will leave them with only the full national pension. The employment rate among Finnish women, however, is quite high by international standards and more and more of the younger age groups accrue earnings-related pension, which will reduce the risk of poverty for women.

4.2.3 Future prospects

Promotion of equality between men and women will continue. The Government has launched a national action programme on gender equality, which is mostly being carried out in 2004—2007. The effectiveness of the programme will be assessed at the end of the Government's term of office. Under this extensive programme, a total of 98 measures will be launched and summed up to promote gender equality and improve the position of both men and women. The aims of the programme include removing unfounded differences in wages between men and women, something which is addressed by the wage equality programme, which will be prepared in cooperation with the social partners.

In May 2005, the tripartite working group set up by the Ministry of Social Affairs and Health presented the Government with its proposal for a programme on narrowing the wage differences between men and women. In the working group's view, equal wages and salaries are a key requirement for equality, quality and productivity in working life. The proposals submitted by the working group aim at narrowing the wage difference between men and women by at least five percentage points from today's 20 per cent by 2015.

As part of the equality programme, a significant amendment to the Act on Equality between Women and Men became effective on June 1, 2005. One of the main changes introduced by the amendment was the more detailed provisions on equality planning.

From now on, all workplaces with at least 30 employees should establish an equality plan which comprises descriptions of the equality situation at the workplace, the placement of men and women in the various jobs, and the wages and salaries of men and women, and includes plans on how to address any drawbacks brought up in the equality plan.

4.3 Transparency and adaptability of pension systems and the action policy on pension reforms (Target 11)

Because earnings-related pension provision in Finland is based on work and wages, issues related to earnings-related pensions are prepared in cooperation with the key labour market organizations. From the very beginning, decisions on the earnings-related pension scheme for the private sector have been made at negotiations between the labour market organisations and the Government. Parliament approves the pension legislation proposed by the Government. Studies have shown that the agreements on pensions have achieved a broad consensus in society. Decisions made on the development of the private-sector pension scheme in recent years have been implemented in the public sector as well, where applicable. Tripartite agreements between labour market organisations and the Government on pension policy reforms bring stability and predictability to the system.

The Finnish pension system has been adjusted to changing circumstances. Rapid and broad responses have been provided to each long-term challenge, also to the acute demands following the recession in the 1990s. The changes have related to both the national pension scheme and the earnings-related pension scheme, and pensioners both today and in the future. One of the aims of the 2005 pension reform was to improve the adaptability and sustainability of the pension system for future changes in the operating environment, such as extension of life expectancy. The sustainability of the pension system and the adequacy of pensions is monitored both regularly and under special projects. In accordance with the Government programme, a set of specific indicators has been established for the monitoring of the implementation and effectiveness of the goals of the pension reform.

Transparency of the insurance data for insured persons

Services for the insured have been developed recently. The insured can now have access to employee pension services on the Internet. In December 2002, a joint Internet site for the entire earnings-related pension sector was launched to provide a service for everyone insured under the pension scheme. The site contains pages that can be accessed by anyone and pages that require personal identification. The former provide information on the grounds and benefits related to the earnings-related pension scheme and up-to-date information on pensions, and include a pension application form and a pension calculator, for instance. Pages that require personal identification provide a list of the customer’s employments and periods of self-employment and include forms for ordering pension estimates or filing pension applications.

In accordance with a legislative amendment which became effective at the beginning of 2004, a pension decision issued to a customer covers all earnings-related pensions accrued from both public and private-sector employment. Before 2004, public and private-sector pensions were granted and paid separately. The reform simplifies the processing of pension applications submitted by applicants whose working careers have been covered by several pension schemes. The ‘last institution principle’ was also extended to pensions accrued from work for local government, the State, the church or the Social Insurance Institution; before the reform, this principle was restricted to private-sector employees and self-employed persons.

The system of filing only one pension application was already in place before the reform. In practice, a pension applicant now needs to contact only one pension institution. The pension will be paid by the institution where the applicant was insured last. The pension institutions will share the pension costs. If the amount of the earnings-related pension is small, the person will also receive national pension, which is paid by the Social Insurance Institution. Decisions on national pension are issued separately.

As before the reform, people also have the right to obtain information on the current accruals of their earnings-related pension. Employees (except for State employees) receive information from their pension accrual records free of charge, which consists of a list of past and current employments and an estimate of the accrued pension. Those currently or earlier employed in the private sector receive a pension record sent to their home address about a year after the termination of each employment. Those currently or earlier employed in the local government sector receive a pension record at least once during their employment. In addition, pension institutions send records to the insured about every five years after the insured person turns 35. The record can also be ordered by telephone or over the Internet. Local and regional theme days and presentations of the pension schemes at a number of trade fairs are also organised. The insured are also served by Social Insurance Institution offices and pension companies. Due to the 2005 pension reform, the dissemination of information has increased considerably.

Insured persons have access to a comprehensive range of information on accrual of pensions from private-sector employment. Because of the pension reform and accrual of pensions from annual earnings, the insured will receive (from 2008 on) annual pension data records containing information on the accrued pension provision and an estimate of the pension amount. This will increase their awareness of the level of their pension provision. The pension reform has brought more emphasis on the pension recipients' obligation to check the correctness of the data on their wages.

The Directive on supplementary pensions stresses the importance of information on pension arrangements given to persons covered by them and contains a number of related provisions. Implementation of the Directive on supplementary pension funds will thus improve access to information for persons covered by voluntary arrangements.

It should also be noted that despite the large amount of information provided for the public, increasing the insured persons' knowledge of the operation of the pension system remains a challenge.

Public confidence in the pension system

Public opinion on and confidence in the pension systems are established with the help of questionnaire surveys every three years, for instance. The latest survey on public attitudes towards earnings-related pensions was carried out in October 2004. The results were slightly different from those in 2001. According to the results, more and more people wish to stay on the labour market longer than today. The age considered the best for retirement has risen from 61 years to 62 years. As the average effective retirement age today is 59, Finnish views on earnings-related pension are falling in line with the objectives of the 2005 pension reform which encourage staying longer on the labour market.

Half (49 per cent) of the population believe that there will be enough money for the payment of pensions even if pension benefits remain unchanged. This view was slightly more common in 2001 (57 per cent). The percentage of those who believe that the current pension benefits will be sufficient in the future was about the same as in 2001 (55 per cent). Nearly 70 per cent of the respondents believed their level of income would remain good during retirement; this percentage has remained more or less the same in the past ten years.

An increasing number of people believe that pension benefits will decline, but this view is still in a clearer minority than between 1992 and 1998. (See Table 4.1.) A majority (56 per cent) believes that there will be another pension reform within the next ten years.

People's wishes concerning the amount of their pension reflect a need for supplementary pension provision. According to surveys carried out by the Finnish Pension Alliance TELA and the Federation of Finnish Insurance Companies in 2004, people would like their pensions to be 67—72 per cent of their wages in their last year of employment. In general, pensions fall below that level. Anticipation of career interruptions and diversity of working careers may also increase the need for voluntary pension provision. On the other hand, the maximum limit for pensions (60 per cent of the pensionable earnings) has been removed from the statutory pension scheme, which means that working longer will increase the amount of pension and reduce the need for supplementary pension provision.

4.4 Other planned reforms

Streamlining the pension system requires merger of the different Acts on earnings-related schemes and simplification of the legislation. Earnings-related pension provision is based on several Acts, and each amendment based on changes in the operating environment has made the legislation even more complex.

At the beginning of 2007, the various Acts on the pensions of private-sector employees will be merged into a single Employees' Pension Act. Once the Act is in force, employers can arrange common pension provision for their employees. The Self-Employed Persons' Pensions Act, the Farmers' Pensions Act and the Seamen's Pensions Act will be excluded from the new Act, but steps will be taken to streamline these Acts as well in the future. Instead of introducing new changes in pension policy, these reforms aim at clearer and simpler legislation.

5 Conclusions

Adequacy of pensions

People retiring on earnings-related pension are not facing a particular risk of poverty. The risk of poverty is higher for those who live on full national pension, particularly aged women, than for other pensioners. The outline of pensioners' income is particularly sensitive to the at-risk-of-poverty threshold applied. Using a relative income indicator alone will give an incomplete picture of the risk of poverty, as it excludes other elements of social security provided for pensioners, such as social and health care services. On the whole, the income of the older people does not appear to differ from that of the rest of the population.

Achieving the employment objectives set by the Government is important for both the adequacy of pensions and the sustainability of their financing. The 2005 pension reform will also help people to acquire adequate pension provision by staying on the labour market longer than before and accruing more pension between the ages of 63 and 68.

Sustainability of financing

Population ageing will be a major challenge, as the demographic change will be more rapid in Finland than anywhere else in the EU during the following 20 years. In the statutory earnings-related pension scheme, preparations have been made for population ageing through partial funding from the start. The challenges posed by population ageing have been addressed with the recent pension reform. The use of a life expectancy coefficient introduced by the reform will automatically adjust pensions to longer life expectancy and transfer the risk related to change in life expectancy from contributions to benefits. The use of the life expectancy coefficient will begin to affect pensions from 2010, whereas the other positive incentives and the positive effects on the sustainability of the pension system will emerge sooner.

Longer careers and higher employment rates are crucial for the sustainability of the financing of pension systems. Improvements in employment rates bring immediate reductions in pension expenditure and pension contributions. The pension reform has also increased incentives for reducing early retirement. Extensive measures are increasingly being taken to improve people's work ability. While improvement of the employment rate among ageing people in Finland has been among the highest in the EU in this decade, higher employment rates and achieving employment objectives has become an even greater challenge (due to globalisation, for instance).

The pension reform has curbed pressures to increase the level of pension contributions. In the private sector, the necessary increase is estimated at 6 percentage points. According to calculations, the pressure to increase the pension contributions would equalize around the year 2030 at the level of about 27 per cent.

The Finnish pension system is based on partial funding. The rate of funding is expected to increase in the future. This will maintain saving in the national economy and economic growth as the population grows older.

The investment income from pension funds can reduce pressure to increase the level of pension contributions and thus support the sustainability of the pension system. The regulation of investment activities is currently being reviewed. This includes examining whether pension providers could invest more of their funds in equities and whether earnings-related pension funds could be used to support Finnish ownership and employment.

Reform of pension systems

The Finnish pension system is well prepared to meet the challenge of pension provision for a mobile workforce and people in atypical employment (part-time and temporary employees and self-employed persons).

As a rule, the Finnish pension system ensures equality between women and men. Nevertheless, the promotion of equality will continue through measures focusing on working life.

The pension reform includes implementation of new indicators for assessing the achievement of the objectives of the reform.

ANNEX 1 (Statistics and Tables)

1. Introduction

Table 1.1. Finnish population by age and gender in 2004 and a projection until 2050 (Source: Statistics Finland)

	2004			2010			2020		
	Males	**Females**	**Total**	**Males**	**Females**	**Total**	**Males**	**Females**	**Total**
0-14	466695	447537	914232	445374	426153	871527	447699	428623	876322
15-24	332846	318160	651006	333203	319772	652975	302523	289367	591890
25-44	700123	673402	1373525	676321	648995	1325316	681095	652697	1333792
45-59	598595	594147	1192742	567919	565565	1133484	511520	505129	1016649
60-64	132864	140382	273246	198080	204440	402520	175734	180934	356668
65-74	203992	246665	450657	236166	270545	506711	342044	375889	717933
75+	126089	252088	378177	149697	267426	417123	205016	313296	518312
Total	2561204	2672381	5233585	2606760	2702896	5309656	2665631	2745935	5411566

	2030			2040			2050		
	Males	**Females**	**Total**	**Males**	**Females**	**Total**	**Males**	**Females**	**Total**
0-14	436796	417994	854790	417212	399180	816392	410870	393118	803988
15-24	304340	291197	595537	301017	287863	588880	285916	273317	559233
25-44	649257	621441	1270698	623302	595105	1218407	621803	592792	1214595
45-59	491681	479615	971296	504748	490278	995026	479662	463775	943437
60-64	164029	166096	330125	160829	159560	320389	161392	157891	319283
65-74	324593	347658	672251	294855	306589	601444	310940	315397	626337
75+	311661	436483	748144	348643	477708	826351	345942	456470	802412
Total	2682357	2760484	5442841	2650606	2716283	5366889	2616525	2652760	5269285

Table 1.2. *Life expectancy at birth and at ages 60 and 65, by gender (current and projected for 2010, 2030, 2050)* (Source: Statistics Finland)

Year	0-year-olds		60-year-olds		65-year-olds	
	Males	Females	Males	Females	Males	Females
2004	75,31	81,91	19,84	24,27	16,01	19,89
2005	75,54	82,06	20,00	24,40	16,14	20,01
2010	76,64	82,78	20,78	25,02	16,81	20,58
2020	78,68	84,09	22,23	26,16	18,05	21,63
2030	80,49	85,26	23,52	27,17	19,17	22,58
2040	82,09	86,30	24,67	28,07	20,18	23,41
2050	83,49	87,22	25,69	28,87	21,08	24,15

Figure 1.1. Development of the economic dependency ratio in 1950 – 2003 and a projection until 2050 (Source: Ministry of Social Affairs and Health)

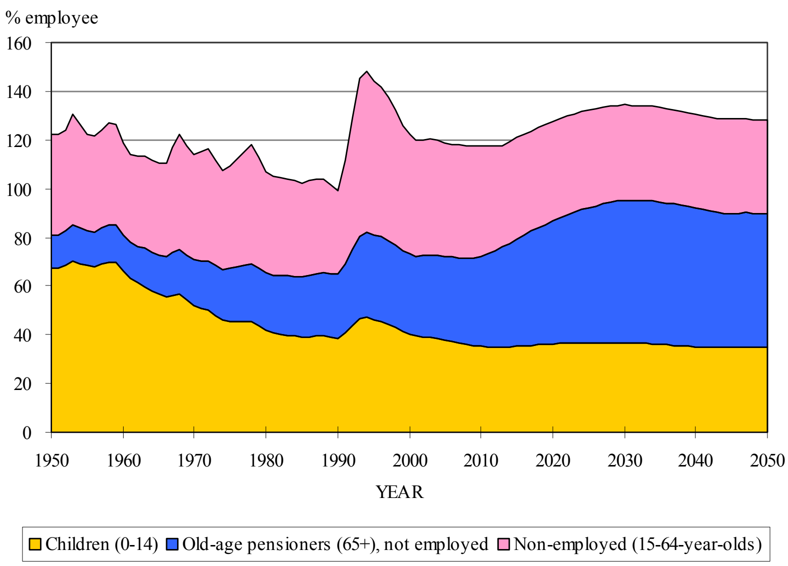


Table 1.3. Coverage in services for older people by age and gender in 2003 (% of the age cohort 65 +) (Source: National Research and Development Centre for Welfare and Health STAKES)

	Service housing with 24-hour assistance	***Residential homes for old people***	***Health centres, long- term inpatients***	Total
Men	0,9	1,5	0,9	3,3
Women	1,9	3,0	1,7	6,6
Total	1,5	2,4	1,4	**5,3**

As long-term clients are counted all those with a decision on long-term care or who have been in inpatient care for more than 90 days.

Figure 1.2. (Sources: STAKES, Ministry of Social Affairs and Health)

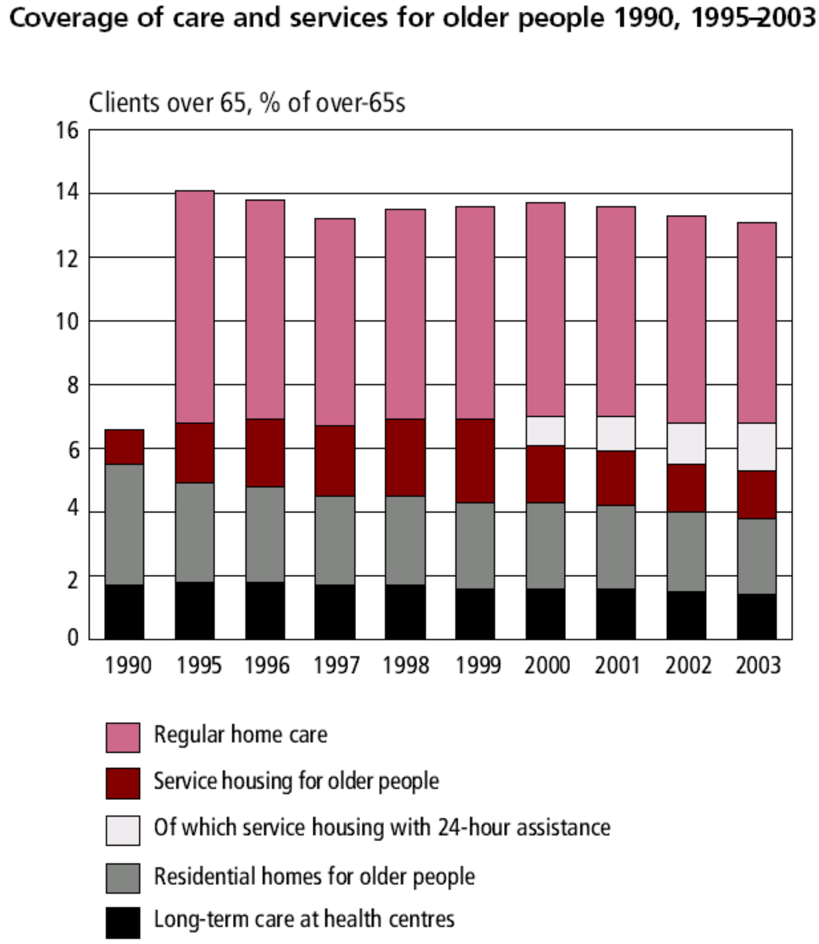
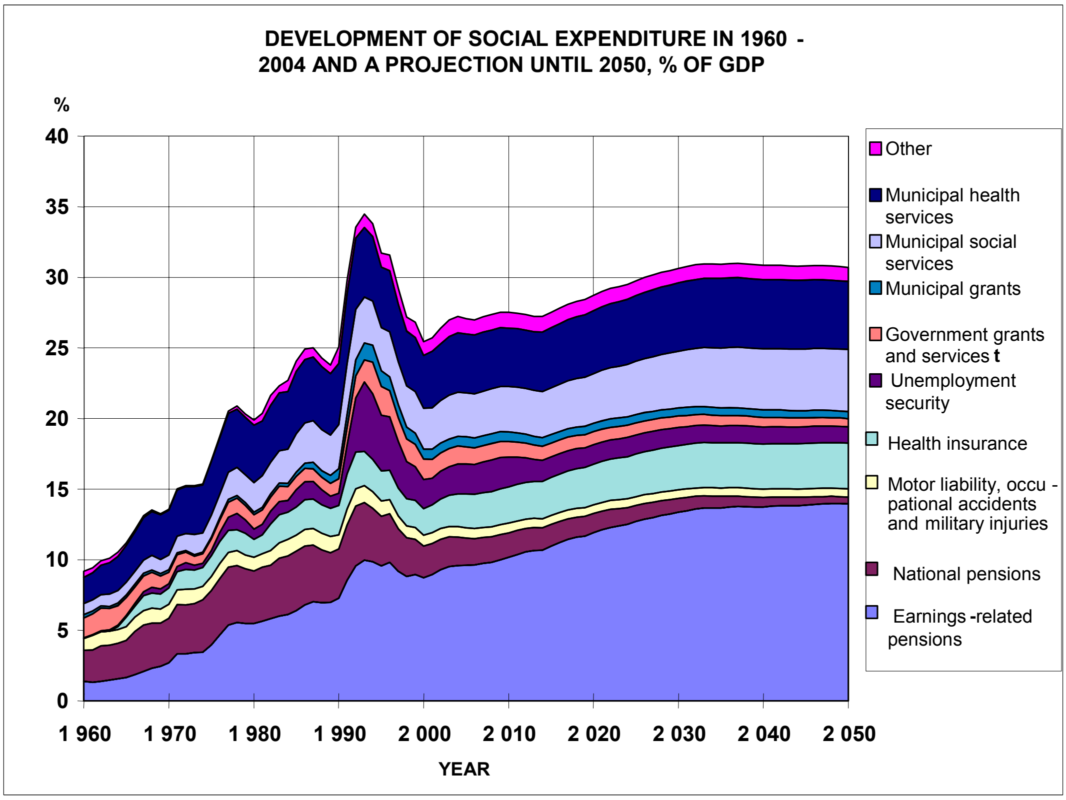
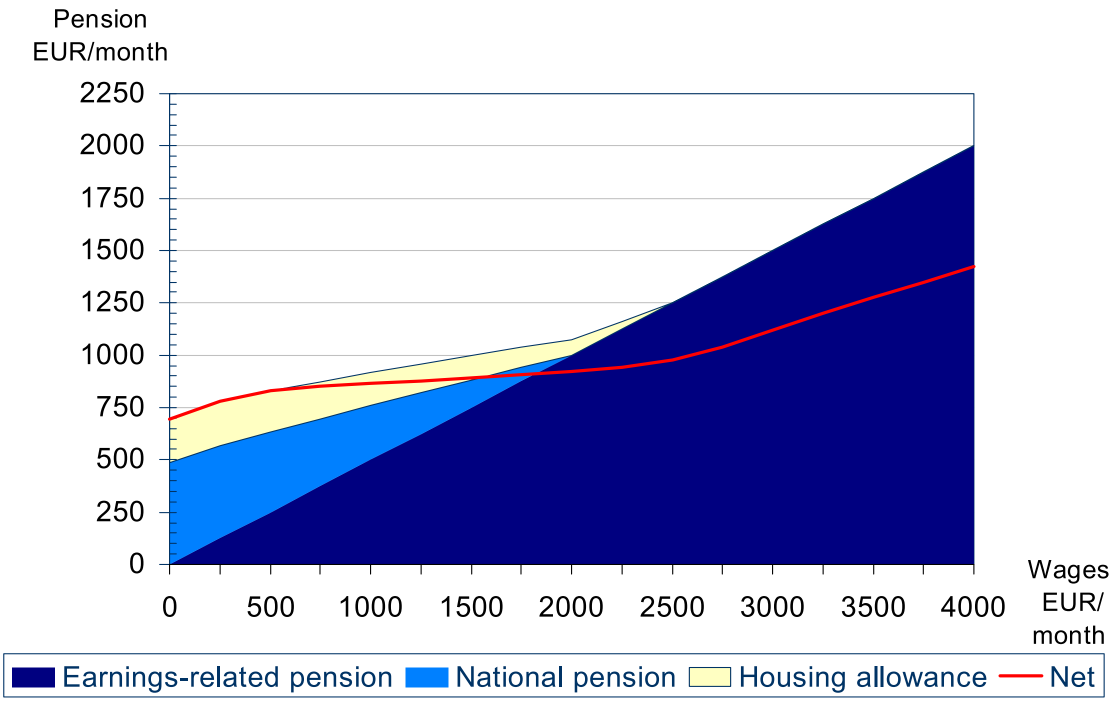


Figure 1.3. (Source: Ministry of Social Affairs and Health)



2. Sufficiency of pensions – achievement of social goals

Figure 2.1. Total pension on 1 Jan. 2005 (Source: Finnish Centre for Pensions ETK)



In the figure earnings-related pension is 50 per cent of pay. Single pensioner, municipality category 2. National pension includes the increase in the rate of pension. Housing costs EUR 288 /month (average in 2003). Possible earnings-related pension accrual of 4.5 per cent after the age 63 / from 2005 on is not taken into account in the figure.

Figure 2.2. Number of all pensioners by pension structure at year-end 1988 - 2004 (Source: Finnish Centre for Pensions, Social Insurance Institution KELA)

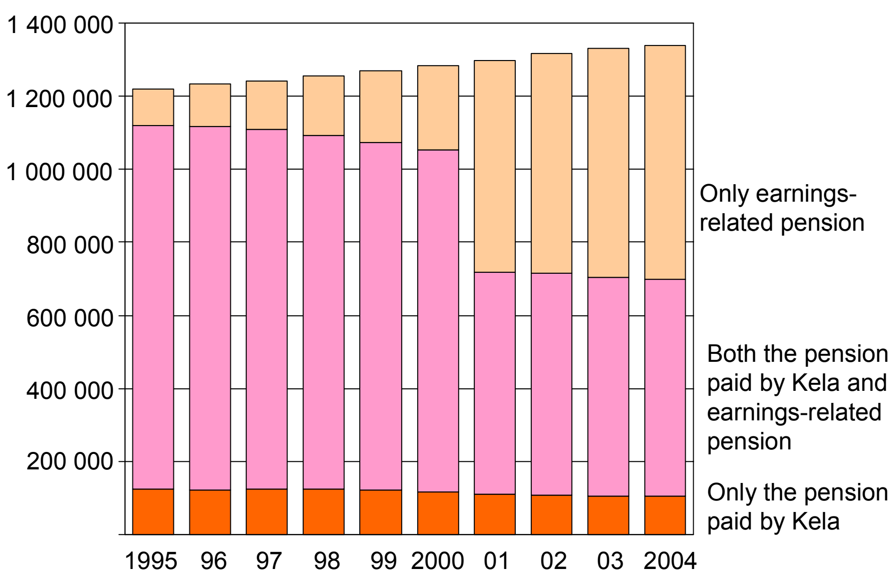
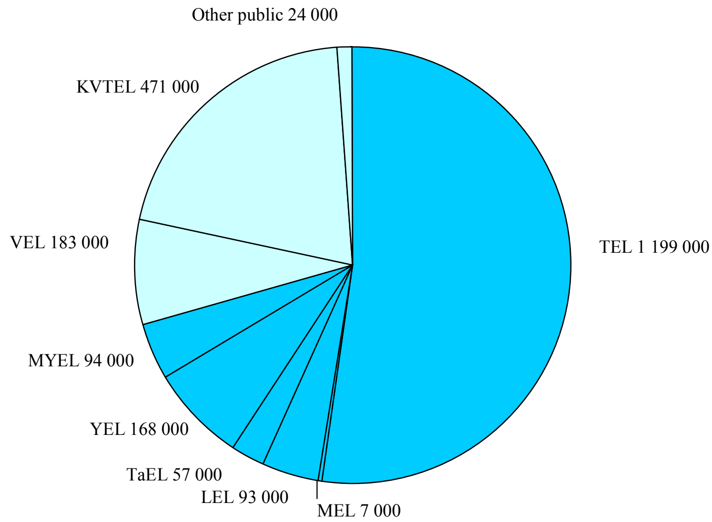


Figure 2.3. Numbers of people who have earned their pensions under different employees pensions acts, 31 Dec. 2003 (Source: Finnish Centre for Pensions)



KVTEL Local Government Employees Pensions Act
VEL State Employees Pensions Act
MYEL Farmers Pensions Act
YEL Self-Employed Persons Pensions Act
TaEL Freelance Employees Pensions Act
LEL Temporary Employees Pensions Act
MEL Seamen's Pensions Act
TEL Employees Pensions Act

Table 2.1. All recipients of earning-related pension by pension sector and age, 31 Dec. 2004 (Source: Finnish Centre for Pensions)

Age at the end of statistical year	Number of pensioners			Average total earnings-related pension EUR month		
	Males	Females	All	Males	Females	All
	Recipients of pension from the private sector					
-4	263	236	499	231	247	239
5 - 9	1 194	1 128	2 322	237	226	232
10 - 14	3 254	3 155	6 409	251	249	250
15 - 19	3 477	3 363	6 840	290	284	287
20 - 24	205	153	358	455	402	432
25 - 29	512	341	853	587	476	542
30 - 34	1 150	877	2 027	578	469	531
35 - 39	2 993	2 312	5 305	580	489	540
40 - 44	5 660	4 803	10 463	620	525	577
45 - 49	10 337	9 070	19 407	696	575	639
50 - 54	19 939	18 948	38 887	799	611	707
54 - 59	44 115	43 730	87 845	915	685	800
60 - 64	79 516	80 202	159 718	1 186	857	1 021
65 - 69	106 194	110 239	216 433	1 266	872	1 065
70 - 74	82 000	97 060	179 060	1 117	773	930
75 - 70	60 869	89 999	150 868	963	671	789
80 -	50 315	119 558	169 873	856	573	657
All	471 993	585 174	1 057 167	1 047	721	866
	Recipients of pension from the public sector					
-4	82	89	171	238	262	251
5 - 9	447	448	895	258	253	256
10 - 14	1 338	1 331	2 669	283	273	278
15 - 19	1 488	1 402	2 890	333	319	326
20 - 24	25	27	52	263	225	243
25 - 29	70	134	204	467	535	512
30 - 34	319	527	846	538	529	532
35 - 39	1 074	1 601	2 675	516	534	527
40 - 44	2 179	3 449	5 628	640	583	605
45 - 49	4 261	6 322	10 583	818	668	728
50 - 54	8 648	11 535	20 183	1 052	723	864
54 - 59	18 764	26 924	45 688	1 196	807	967
60 - 64	36 516	59 577	96 093	1 484	1 077	1 232
65 - 69	42 296	67 975	110 271	1 634	1 130	1 324
70 - 74	30 390	52 771	83 161	1 563	1 096	1 267
75 - 70	21 540	42 077	63 617	1 474	1 057	1 198
80 -	18 069	49 746	67 815	1 453	1 028	1 141
All	187 506	325 935	513 441	1 424	1 021	1 168
	Recipients of pension from both the private and public sector simultaneously*)					
-4	59	57	116	242	273	257
5 - 9	282	302	584	259	251	255
10 - 14	881	870	1 751	279	279	279
15 - 19	1 010	936	1 946	332	315	324
20 - 24	3	2	5	361 ..		275
25 - 29	25	46	71	461	545	516
30 - 34	131	211	342	623	507	551
35 - 39	592	732	1 324	563	515	537
40 - 44	1 541	2 022	3 563	616	555	581
45 - 49	3 089	4 032	7 121	724	616	663
50 - 54	5 865	8 177	14 042	872	667	753
54 - 59	11 205	16 127	27 332	1 063	798	907
60 - 64	23 324	34 561	57 885	1 357	962	1 121
65 - 69	32 349	48 214	80 563	1 522	1 031	1 228
70 - 74	21 037	36 139	57 176	1 404	990	1 142
75 - 70	13 603	28 128	41 731	1 269	948	1 053
80 -	10 654	32 109	42 763	1 198	901	975
All	125 650	212 665	338 315	1 287	928	1 062

*) Total pension includes the euro the amount of
both the pension in one's own rigth and survivor's pension

Table 2.2. a Pension contributions, pension funds and pension benefits paid in Finland according to the EU pension pillars, in ratio to GNP in 2003 (Sources: Insurance Supervisory Authority, Social Insurance Institution, Federation of Finnish Insurance Companies)

	1st pillar: statutory schemes	*2nd pillar: voluntary collective schemes*	*3rd pillar: voluntary individual schemes*	*Total*
Contributions, % of GDP	*11,1*	*0,2*	*0,4*	*11,7*
Funds at end-year, % of GDP*	*56,4*	*6,3*	*4,4*	*67,1*
Benefits paid, % of GDP	*11*	*0,3*	*0,1*	*11,4*

**) 2nd and 3rd pillar: provision for unearned premiums + provision for outstanding claims*

Table 2.2. b Proportions of revenues, funds and pension benefits in Finland according to the EU pension pillars in 2003 (Sources: Insurance Supervisory Authority, Social Insurance Institution, Federation of Finnish Insurance Companies)

	1st pillar: statutory schemes	*2nd pillar: voluntary collective schemes*	*3rd pillar: voluntary individual schemes*	*Total*
Contributions	*94 %*	*2 %*	*4 %*	*100 %*
Funds at end-year	*84 %*	*9 %*	*7 %*	*100 %*
Benefits paid	*96 %*	*3 %*	*1 %*	*100 %*

Table 2.3. Amounts of parts of/supplements to pension, 1 March 2005, €/month (Source: Social Insurance Institution)

Fixed-amount benefits		**Housing allowance** (full allowance for singles)	
Front-veteran's supplement	41,38	Greater Helsinki Area	351,75
Care allowance for pensioners		Other Finland	318,95/281,76
- Care allowance	51,98		
- Higher-rate	129,40	**Others** (full amount for singles, municipality category 1)	
- Special-rate	258,79	National pension	505,24
- Compensation for diet expenses	21,00	Front-veteran's additional supplement	188,85
Child increase	18,47	Basic amount supplement to child's pension	67,15
Basic amount of child's pension	50,26		

Figure 2.4. Real income level of all households and pensioners' households in1987-2003. (Source: Statistics Finland, Income Distribution Statistics)

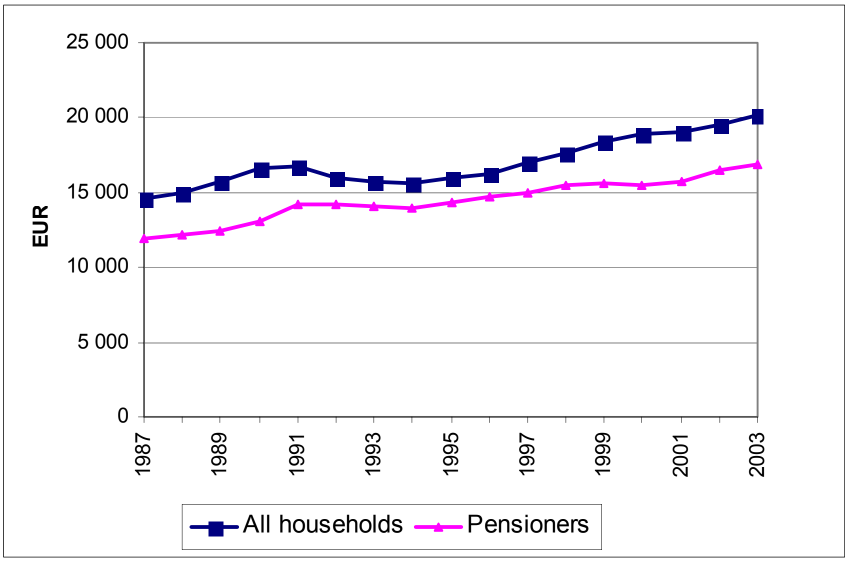


Table 2.4. Replacement rates summary table 2.6.2005 (Source: Finnish Centre for Pensions)

	Base case 100% of average earnings (and 10 years after retirement; relative to projected average earnings)					2/3 of average earnings		Concave earning profile		Rising earnings from 80% to 120% of average		Rising earnings from 100% to 200% of average		Broken career(30 years of seniority at retirement		*Working career 38 years between 25-63*		*Working career 42 years between 25-67*	
	2005	In 10 years	2010	2030	2050	2005	2050	2005	2050	2005	2050	2005	2050	2005	2050*	2005	2050	2005	2050
Gross replacement rate 1st pillar	56,6	48,7	60,3	57,3	53,9	64,8	53,9	56,6	51,8	54,5	46,1	53,4	42,3	45,8	42,3 (44,7)	51,2	46,8	64,2	60,8
Gross replacement rate 2nd pillar	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Total gross replacement rate	56,6	48,7	60,3	57,3	53,9	64,8	53,9	56,6	51,8	54,5	46,1	53,4	42,3	45,8	42,3 (44,7)	51,2	46,8	64,2	60,8
Total net replacement rate	62,6	55,1	66,2	65,7	63,6	74,1	67,0	63,5	60,7	60,7	56,1	61,5	53,2	54,6	54,3 (56,1)	58,5	56,2	66,5	69,5
Of which means-tested benefits in percentage points of total net replacement rate	-	-	-	-	-	4,9	-	-	-	-	-	-	-	0,6	-	-	-	-	-

Notes: 2005 refers to pension in 2005 with reference to work income in 2004 except in case a MS needs to refer to a different moment or a previous year.

* First calculated without any benefits for the missing 10 years. In brackets pension calculated with two children born 5 years between them. Childcare (when employment is interrupted) gives right to pension only according to the new rules.

Assumptions used for the calculation of replacement rates (Table 2.4.):

The pension has been calculated for a person insured under the most general pension scheme in Finland, TEL, which covers over 50 % of the insured (the rules are practically the same in each scheme). The career length is 40 years between 25 and 65. The retirement age is 65. In all the cases it is assumed for simplicity reasons that the person was employed by only one employer. The assumption of the amount of employers affects the amount of pension in the old system, but not in the new one, as the pension is no longer calculated by employment.

The average annual real wage growth has been assumed to be 1.9% between 2005 and 2050. As the Finnish pension scheme is a defined-benefit scheme, the contribution affects the pension level only by being subtracted from the earnings before the calculation of the pension.

The pension contribution is divided into the employer's and employee's parts. In 2005, the employer pension contribution is in average 17% and for the employee (under 53 years of age) 4.6%. In the reform, a higher contribution was introduced for those over 53 years of age. It is about 27% (19/15) higher than the contribution of the younger ones, being 5.8% in 2005. The total contribution in 2005 is 21.6%. When the older ones pay more, the employers pay less, meaning that the total contribution doesn't change according to age.

Real interest rate of 3% has been used to calculate the contributions in the future as has been done in the pension expenditure calculations for the Ageing Working Group of the Economic Policy Committee (AWG). The level of the interest rate doesn't affect the pension directly as it is a defined-benefit scheme. If an interest rate of 2.5% would be used it would mean a 0.3 percentage point decrease in the gross replacement rates (RR).

It has been assumed that the tax income brackets and all the other parameters in taxation follow the real wage growth, which means that the level of wage taxation remains the same as in the 2005 cases. The deductible employee pension contribution is assumed to change as predicted from 4.6% to 10.2% in 2050. To calculate the life expectancy coefficient, the Eurostat predictions that were used to calculate the pension expenditures to the AWG has been used.

As agreed, it is assumed that there will be no other increases in the national pension and housing allowances than what is stated in the legislation. That means that no additional increases have been taken into consideration except price changes even though the practice so far has been to increase these benefits occasionally by separate Parliament decisions.

The broken career is calculated without childcare and with childcare. In the old system, this doesn't change the results, because childcare, if employment is interrupted (interruption lasts over a year without pay) doesn't give any extra accrual. But in the new system it does. Childcare accrues pension during the first three years after the child is born. The first year of childcare accrues pension according to the wage to which the benefit is based (assumed to be the wage of the year before childcare) and the next two years according to a fixed wage of about 523 euros/month (in the 2004 level). After this there is no accrual until the next child is born. Because the person has not worked between the childbirths, the pension accrues according to the before mentioned 523 during all the three years for the care of the second child.

Table 2.5. Recipients of social assistance by age in 1996–2003 (Source: National Research and Development Centre for Welfare and Health, Statistical summary 31/2004)

% Ikä Alder *Age*	1996	1998	2000	2002	2003
-17	27,3	27,0	26,6	27,2	26,9
18-19	3,6	3,2	3,4	3,9	4,0
20-24	15,1	14,5	13,3	13,3	13,6
25-29	10,5	9,5	8,7	8,6	8,8
30-39	16,8	16,8	16,2	15,0	14,5
40-49	14,7	15,2	15,7	15,1	15,0
50-59	6,8	8,4	10,3	11,1	11,6
60-64	1,4	1,6	1,9	1,9	1,9
65-74	2,0	2,1	2,3	2,2	2,2
75-	1,3	1,3	1,5	1,5	1,5
Ei tietoa - Uppgift saknas - *No information*	0,5	0,4	0,2	0,1	0,0
Yhteensä - Totalt - *Total*	**100**	**100**	**100**	**100**	**100**

Table 2.6. (Source: Statistics Finland, Income Distribution Statistics)

Proportion of people on low incomes by age and gender

60 % of the median of equivalent income, adjusted OECD consumption unit scale

Gender and age	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
Total	7,9	7,8	7,1	6,3	6,5	7,3	8,3	8,2	9,7	9,8	10,4	10,8	11,0	11,2
65 +	18,7	13,7	10,9	6,6	7,4	7,2	6,9	6,3	9,5	9,2	9,9	10,5	9,6	11,0
Men	6,5	6,9	6,6	6,2	6,6	7,7	8,4	8,5	9,6	9,5	10,1	10,8	11,3	11,1
- 65 +	10,4	6,6	3,6	2,2	2,8	4,3	3,6	4,2	7,2	6,8	6,3	6,6	7,1	7,4
Women	9,3	8,6	7,4	6,3	6,5	7,0	8,1	8,1	9,8	10,0	10,7	10,9	10,7	11,2
- 65 +	23,5	17,6	15,0	9,3	10,1	8,9	8,9	7,6	11,0	10,7	12,2	13,1	11,2	13,3

50 % of the median of equivalent income, adjusted OECD consumption unit scale

Gender and age	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
Total	3,4	3,7	3,2	2,8	2,8	3,0	3,5	3,7	4,1	4,1	4,3	4,8	5,1	4,7
- 65 +	5,8	3,5	2,5	1,0	0,9	1,2	1,5	1,9	2,7	2,4	3,2	2,8	2,0	2,8
Men	2,9	3,3	3,3	3,0	3,2	3,2	3,9	4,0	4,2	4,0	4,4	5,3	5,5	5
- 65 +	2,6	0,9	0,7	0,3	1,0	0,9	0,6	1,2	1,8	1,1	1,7	1,9	1,6	1,5
Women	3,8	4,0	3,1	2,6	2,5	2,8	3,2	3,5	4,0	4,2	4,2	4,4	4,7	4,4
- 65 +	7,6	4,9	3,4	1,4	0,9	1,3	2,0	2,4	3,3	3,2	4,2	3,4	2,2	3,6

Table 2.7. (Source: Statistics Finland, Income Distribution Statistics)

Distance from the poverty threshold of the median income for population below the threshold for low income
60 % of the median of equivalent income, adjusted OECD consumption unit scale

Distance from poverty threshold	**1990**	**1991**	**1992**	**1993**	**1994**	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**	**2002**	**2003**
All	13,5	15,2	14,4	13,4	14,0	13,2	13,3	14,7	13,6	13,6	14,2	15,1	15,2	14,3
Men	14,0	15,3	16,4	15,5	15,9	13,3	14,5	14,9	13,9	14,0	14,8	16,4	16,1	14,7
Women	13,2	15,1	12,9	11,9	11,9	13,0	12,3	14,2	13,4	13,4	13,0	13,2	13,6	13,1
65 years and over	10,2	8,9	9,4	6,7	7,5	5,9	6,7	8,1	8,6	9,2	8,8	8,1	7,6	8,5

*Difference between the median income for population below poverty threshold and poverty threshold, as percentage of poverty threshold.

Table 2.8. **Low income rate with a fixed threshold for low income, base year 1995** (Source: Statistics Finland, Income Distribution Statistics)

60 % of the median of equivalent income, adjusted OECD consumption unit scale

Poverty threshold	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
The threshold for low income calculated from the median for each year = regular measurement	7,9	7,8	7,1	6,3	6,5	7,3	8,3	8,3	9,7	9,8	10,4	10,8	11,0	11,2
Inflation-adjusted* fixed threshold														
Total	5,9	5,6	6,4	6,9	7,3	7,3	7,2	6,5	6,5	5,8	5,9	5,7	5,2	4,3
Population + 65 years	12,7	7,6	9,2	7,6	8,3	7,2	5,8	4,5	5,1	4,3	4,2	3,5	2,1	2,4

Low income rate with a fixed threshold for low income, base year 1995
50 % of the median of equivalent income, adjusted OECD consumption unit scale

Poverty threshold	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
Inflation-adjusted* fixed threshold	2,5	2,8	2,9	3,0	3,1	3,0	3,2	3,0	3,0	2,4	2,4	2,6	2,28	1,92
65 years and over	3,8	2,3	2,0	1,1	1,1	1,2	1,3	1,8	1,7	1,2	1,2	0,9	0,48	0,51

*Deflated by cost-of-living index.

Table 2.9. Income limits for deduction from pension income, EUR, in 2005 (Source: Finnish Centre for Pensions)

	Full deduction	Pension from which tax is payable	Pension from which no deduction is made
Municipal taxation			
Single pensioner	6 810	7 681	16 538
Married pensioners	5 830	6 701	14 159
State taxation			
All pensioners	1 430	12 000	-

Figure 2.5. Development of pension indexes in Finland in 1962–2005, value for 1962 100 (Source: Social Insurance Institution)

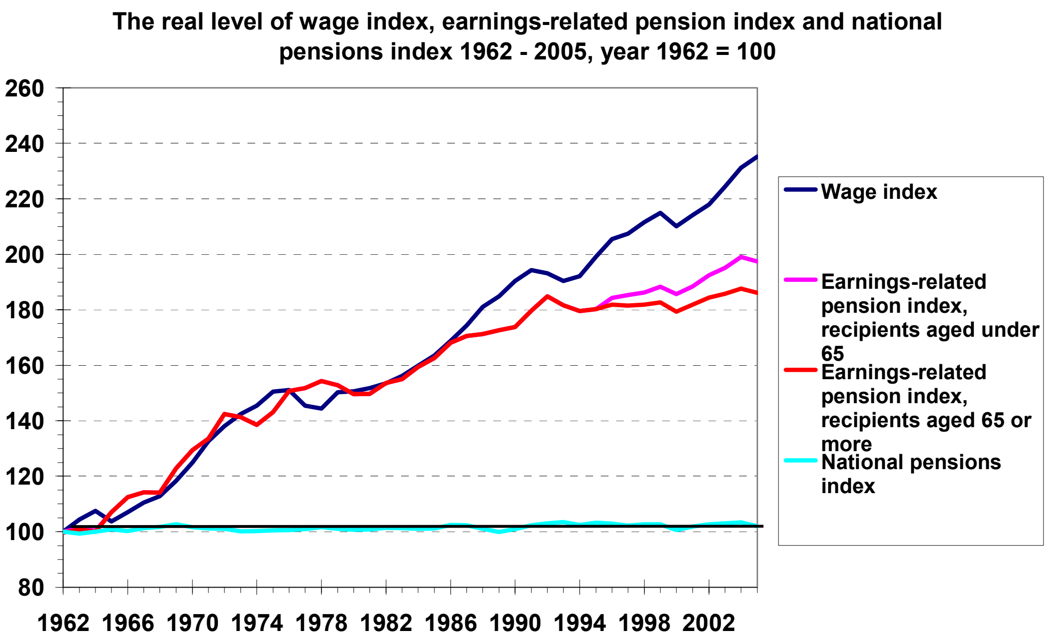


Figure 2.6. Real change in indexes and full national pension in 1962-2005, year 1984=100 (Source: Social Insurance Institution)

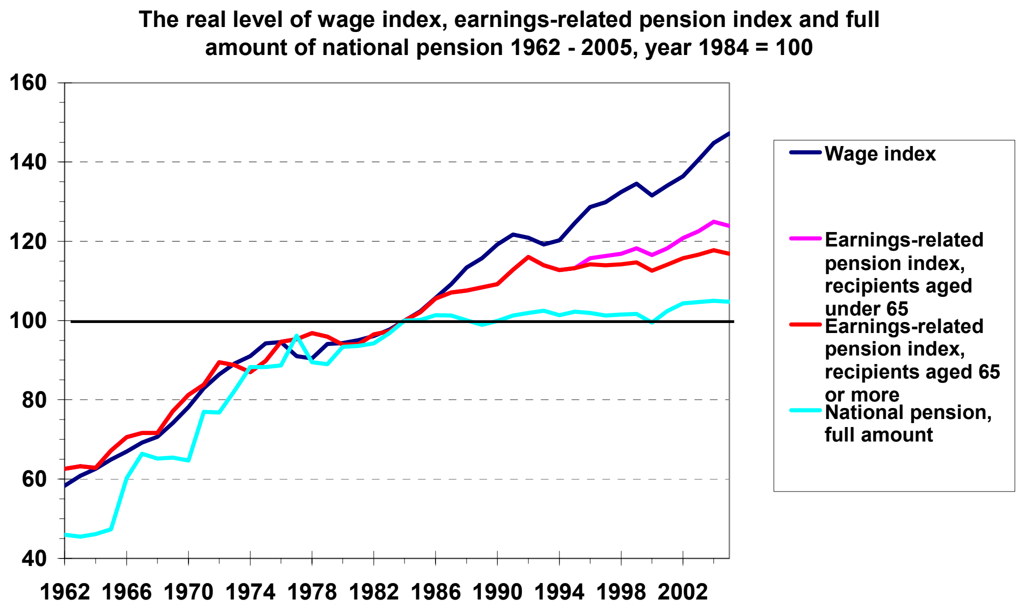


Figure 2.7. Purchasing power of persons retired on an old-age pension in 1991 in 1991 – 2004 (pension – direct taxes). Example calculation. (Source: Central Union of Taxpayers.)

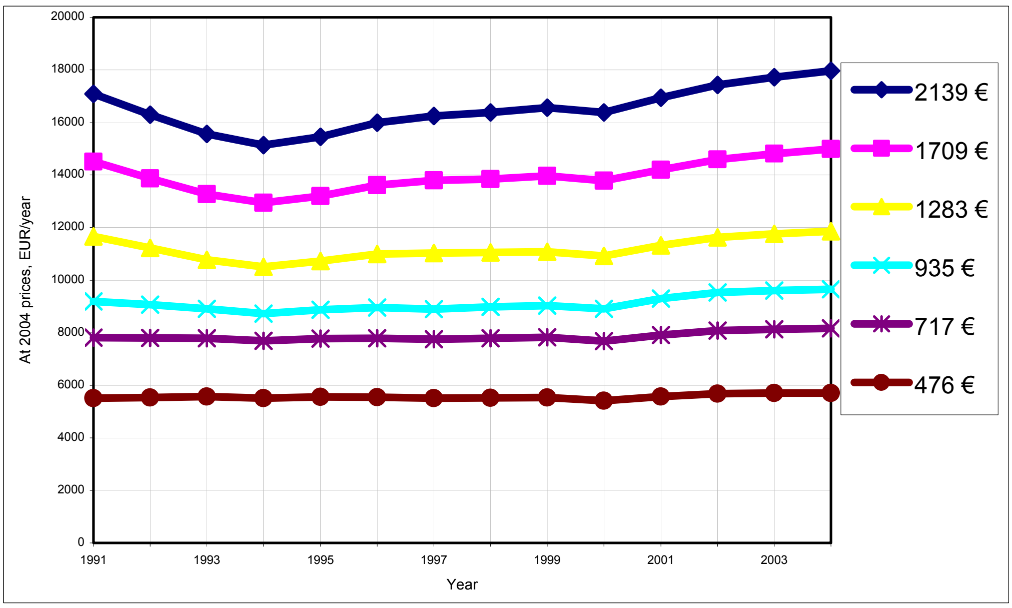


Figure 2.8. Lifetime coefficient; the first year of application of the coefficient and the year of birth of the cohort to which the coefficient is applied on the horizontal axis (Source: Finnish Centre for Pensions)

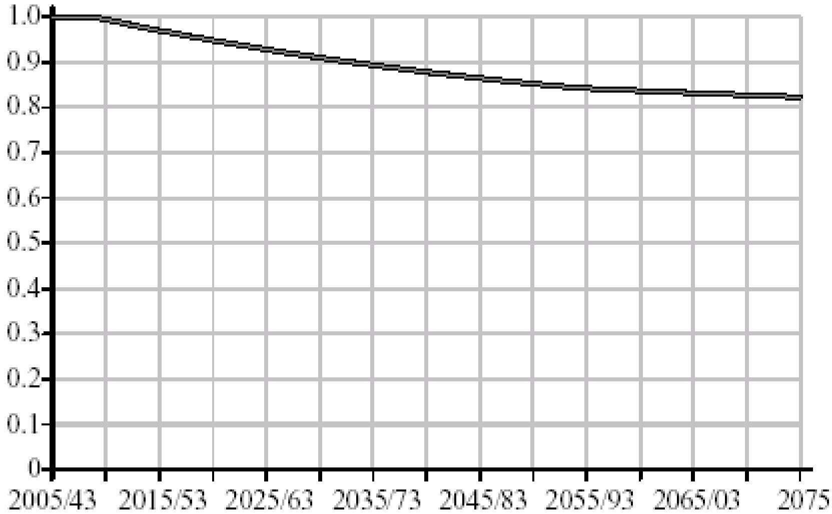


Figure 2.9. Premium income from voluntary supplementary pension insurance (Source: Insurance Supervisory Authority)

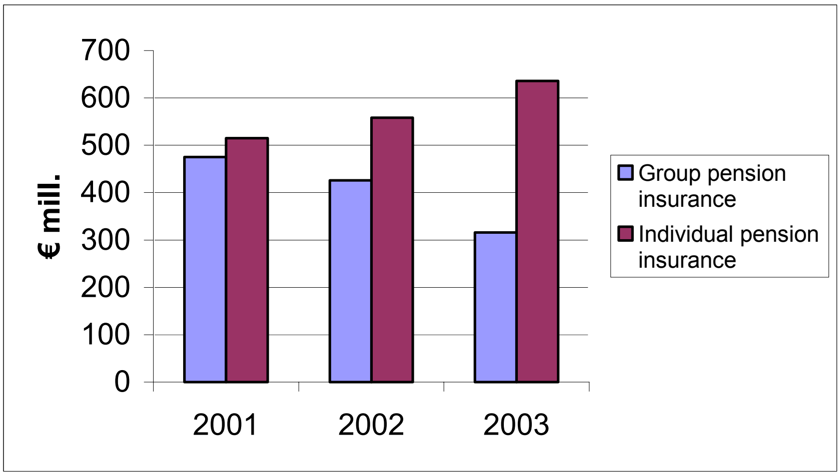
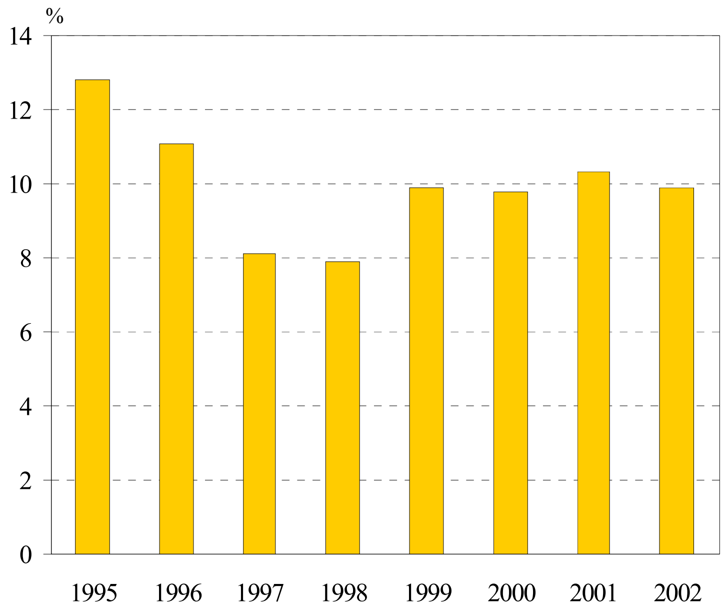


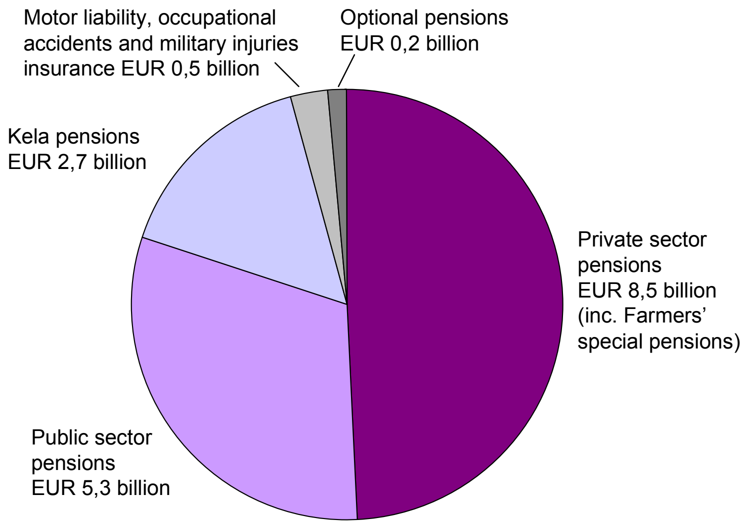
Figure 2.10. Young people* with low education, proportion of age cohort 18 -24 years in 1995-2002, % (Source: Ministry of Social Affairs and Health)



* 18-24-year-olds who are not participating in education and who only have completed basic education

3. Sustainability of the financing of pension schemes – sound financial basis

Figure 3.1. Total pension expenditure in 2004 (Source: Finnish Centre for Pensions)



Optional pensions inc. so called unregistered supplementary pensions paid by pension foundations and funds.

Figure 3.2. Development of statutory pension funds/ per cent of GDP (Source: Finnish Centre for Pensions)

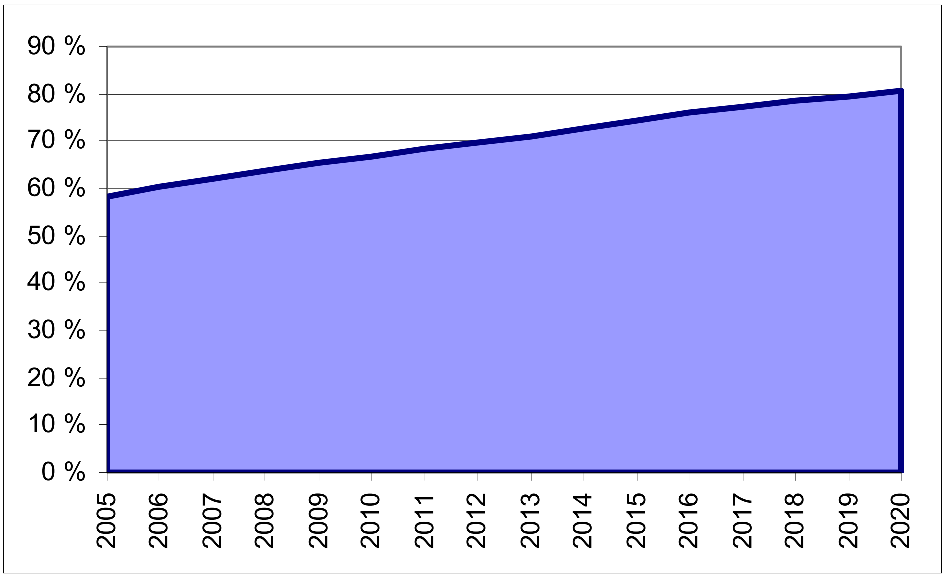
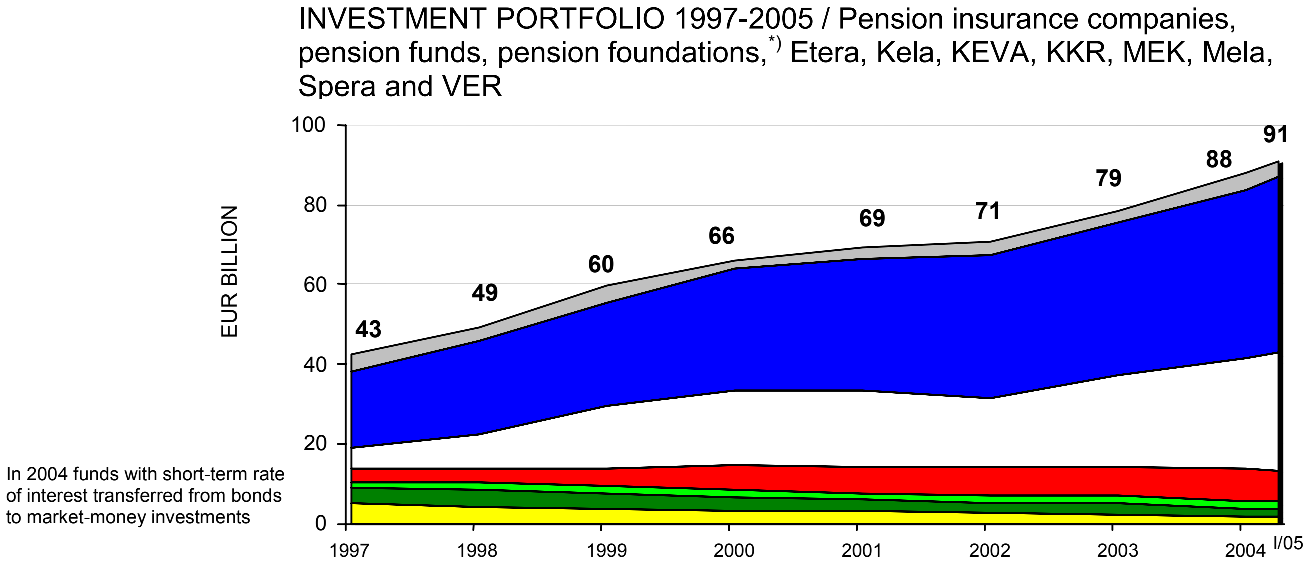


Figure 3.3. Investment portfolio 1997-2005 (Source: Finnish Pension Alliance TELA)



Since the begin of 1999 all at market value	31.12.97	31.12.98	31.12.99	31.12.00	31.12.01	31.12.02	31.12.03	31.12.04	31.3.05
Market money investments	4,6	3,2	4,1	1,7	2,8	3,3	3,1	4,3	3,8
Bonds and convertible bonds	18,9	23,8	25,9	30,9	32,9	36,0	38,3	42,2	44,2
Shares	5,0	8,5	15,5	18,7	19,4	17,1	22,7	27,7	29,5
Real estates and shares	3,4	3,5	4,6	6,1	6,5	7,2	7,5	8,0	7,9
Loans to own companies	1,7	1,7	1,9	1,7	1,7	1,9	2,0	1,8	1,9
Lending other than premium loans	3,9	4,2	3,9	3,5	2,8	2,5	2,5	1,8	1,8
Premium loans	5,0	4,4	3,7	3,3	3,1	2,8	2,5	2,0	1,9
	42,5	**49,3**	**59,6**	**66,00**	**69,2**	**70,9**	**78,6**	**87,9**	**91,0**

*) **Etera** Mutual Insurance Pension Company/ **Kela** - Social Insurance Institution/ **KEVA** – Local Government Pension Institution/ **KKR** - Central Fund of the Evangelical Lutheran Church of Finland/ **MEK** – Seamen's Pension Fund/ **Mela** – Farmers' Social Insurance Institution/ **Spera** – Bank of Finland Pension Fund / **VER** – State Pension Fund

Figure 3.4. Expenses and contributions under the new Employees Pensions Act, in percentage of total payroll (Source: Finnish Centre for Pensions)

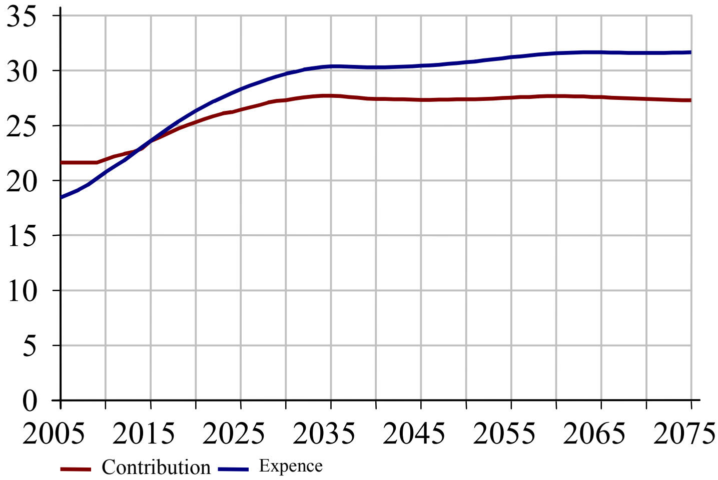


Figure 3.5. (Source: Ministry of Social Affairs and Health, VETO – Work attraction programme)

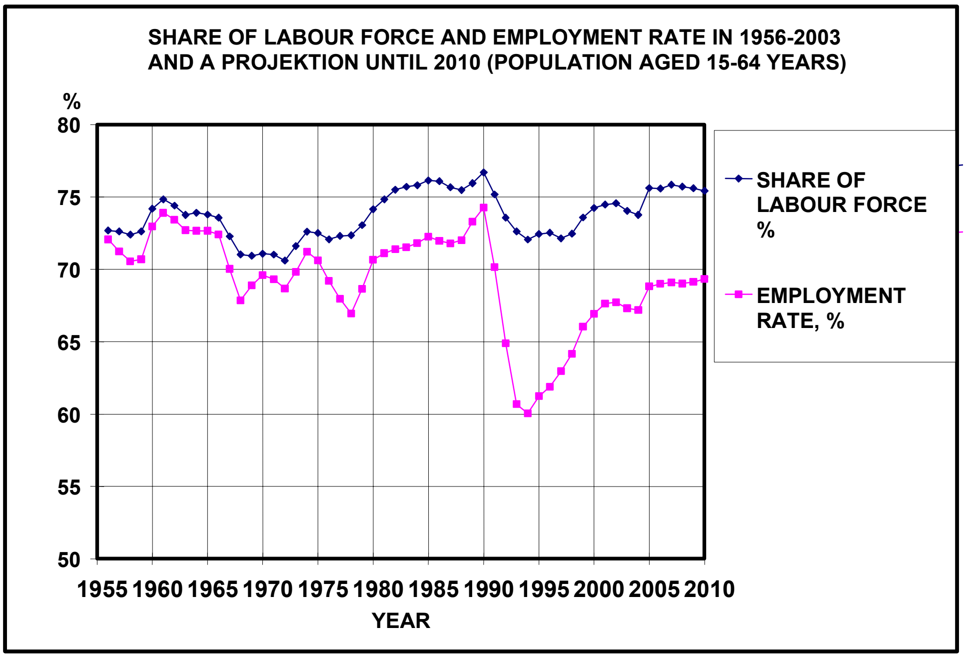


Figure 3.6. (Source: Ministry of Social Affairs and Health)

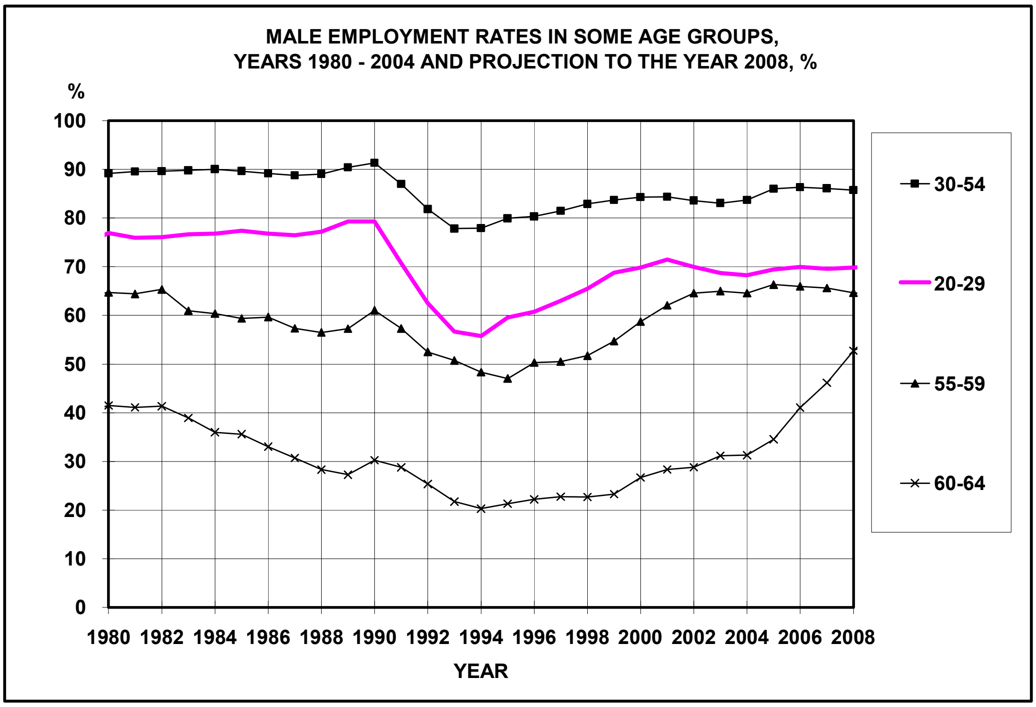


Figure 3.7. (Source: Ministry of Social Affairs and Health)

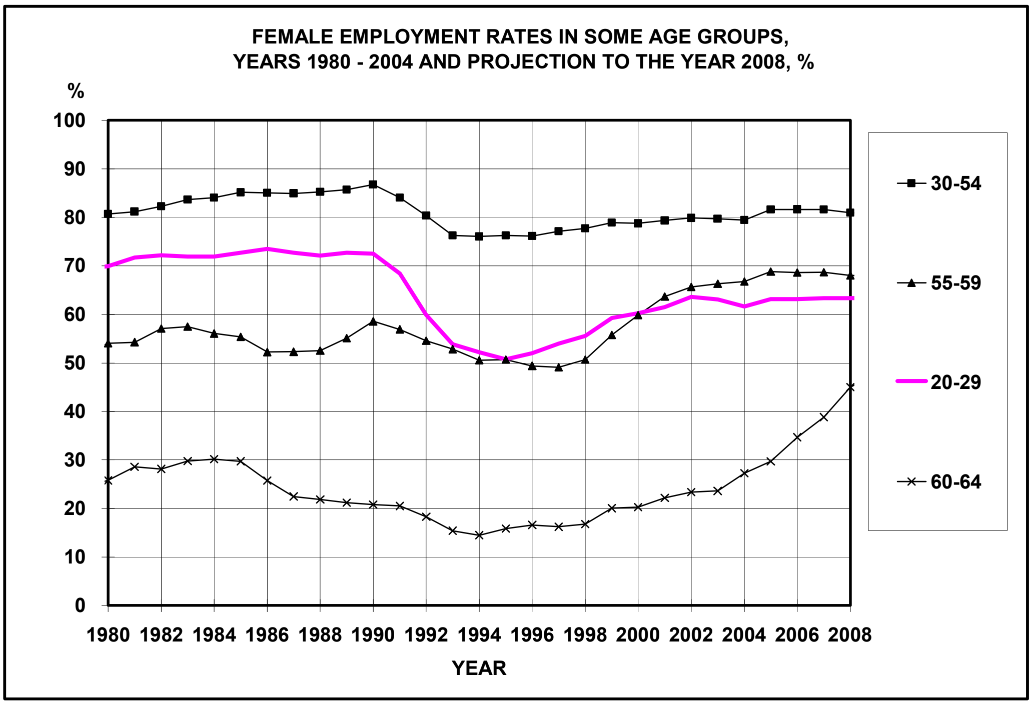


Figure 3.8.

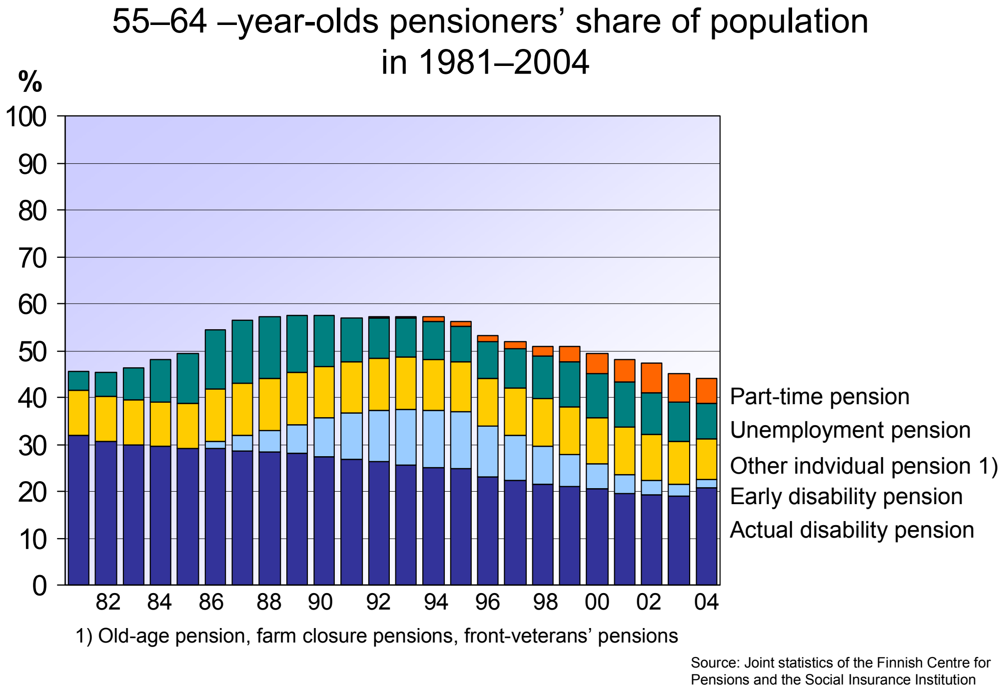
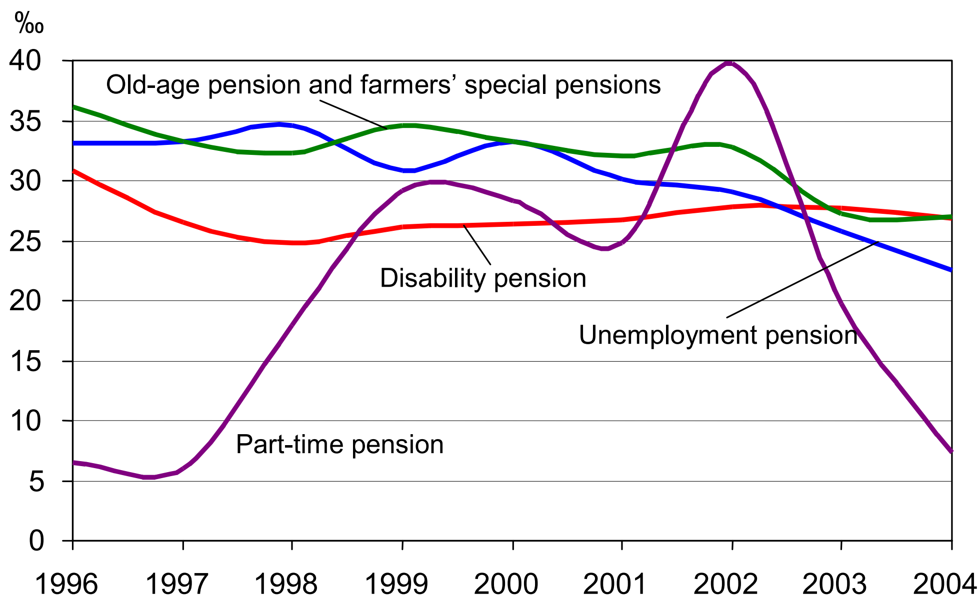


Figure 3.9. Numbers of new age-standardized earnings-related pensions for 55–64-year-olds in 1996–2004 (Source: Finnish Centre for Pensions)



Standard population = Non-retired population insured under the earnings-related pension scheme in 2004. The numbers of new pensions of all types calculated irrespective of age limit in relation to the whole population aged 55-64 years.

Table 3.1. Recipients of disability pensions resident in Finland by main diagnosis and age as at 31.12.2004.(Source: Finnish Centre for Pensions)

		Age All		16 - 44		45 - 54		55 - 64	
Disease category1)		Total	Males	Total	Males	Total	Males	Total	Males
	All	254 588	136 649	43 126	24 476	66 004	36 114	145 458	76 059
I	Communicable and parasitic diseases	1 207	659	87	55	331	179	789	425
	- Tuberculosis	235	132	2	1	27	12	206	119
II	Tumors	6 060	2 607	617	292	1 557	651	3 886	1 664
	- Malign tumors	4 921	2 137	469	226	1 246	511	3 206	1 400
IV	Endocrine, nutritional and metabolic diseases	4 401	2 658	609	325	1 119	679	2 673	1 654
	- Diabetes	3 068	2 036	372	211	824	547	1 872	1 278
V	Mental and behavioural disorders	109 427	55 954	28 931	16 449	33 805	17 744	46 691	21 761
	- Mental and behavioural disorders included by alcohol and drugs	5 186	4 090	459	351	2 007	1 560	2 720	2 179
	- Schizophrenia, delusional disorders, mood disorders, disorders of adult personality and behaviour, etc	84 376	40 688	19 671	10 981	26 039	12 947	38 666	16 760
	- Disorders of psychological development	1 656	983	761	494	547	323	348	166
	- Mental retardation	16 550	9 181	7 762	4 473	4 839	2 665	3 949	2 043
VI	Diseases of the nervous system	18 925	10 451	4 285	2 259	5 784	3 101	8 856	5 091
	- Multiple sclerosis	3 319	1 068	793	267	1 256	378	1 270	423
	- Epilepsy	2 625	1 447	746	385	842	459	1 037	603
VII	Diseases of the eye and adnexa	3 071	1 774	632	359	797	479	1 642	936
VIII	Diseases of the ear and mastoid process	1 351	704	88	51	231	111	1 032	542
IX	Diseases of the circulatory system	19 948	14 438	714	442	3 555	2 533	15 679	11 463
	- Hypertensive diseases	536	330	5	2	52	38	479	290
	- Ischaemic heart diseases	7 476	6 020	48	33	845	713	6 583	5 274
	- Cerebrovascular diseases	7 924	5 221	503	290	1 905	1 208	5 516	3 723
X	Diseases of the respiratory system	5 737	3 062	115	66	827	436	4 795	2 560
	- Asthma	3 233	1 393	68	41	488	225	2 677	1 127
	Other cronic lower respiratory infections	1 890	1 325	19	13	237	153	1 634	1 159
XI	Diseases of the digestive system	1 560	935	165	100	477	285	918	550
XII	Diseases of the skin and subcutaneous tissue	1 451	771	60	36	358	220	1 033	515
XIII	Diseases of the musculoskeletal system and connective tissue	61 917	30 008	2 284	1 157	12 043	6 212	47 590	22 639
	- Rheumatoid arthritis	6 379	1 798	435	107	1 531	446	4 413	1 245
	- Arthrosis	15 257	6 940	150	99	2 100	1 078	13 007	5 763
	- Dorsopathies:	29 340	16 196	1 160	694	6 135	3 642	22 045	11 860
	- Ankylosing spondylitis	1 623	1 122	132	86	486	350	1 005	686
	- Spondylosis	5 444	3 097	57	37	705	462	4 682	2 598
	- Other dorsopathies	22 273	11 977	971	571	4 944	2 830	16 358	8 576
XIV	Diseases of the genitourinary system	713	393	111	65	216	121	386	207
XVII	Congenital malformations, deformations and chromosomal abnormalities	4 919	2 493	2 472	1 299	1 187	598	1 260	596
	- Congenital malformations and deformations of the musculoskeletal system	1 214	550	189	76	313	142	712	332
XIX	Injuries, poisoning and certain other	11 989	8 685	1 773	1 411	3 352	2 547	6 864	4 727
	consequences of external causes	3 713	2 456	455	347	965	686	2 293	1 423
	Other diseases	1 912	1 057	183	110	365	218	1 364	729

Figure 3.10. The expected effective retirement age (i.e. expentancy) by gender in 1996-2004, all persons in receipt of an earnings-related pension (Source: Finnish Centre for Pensions)

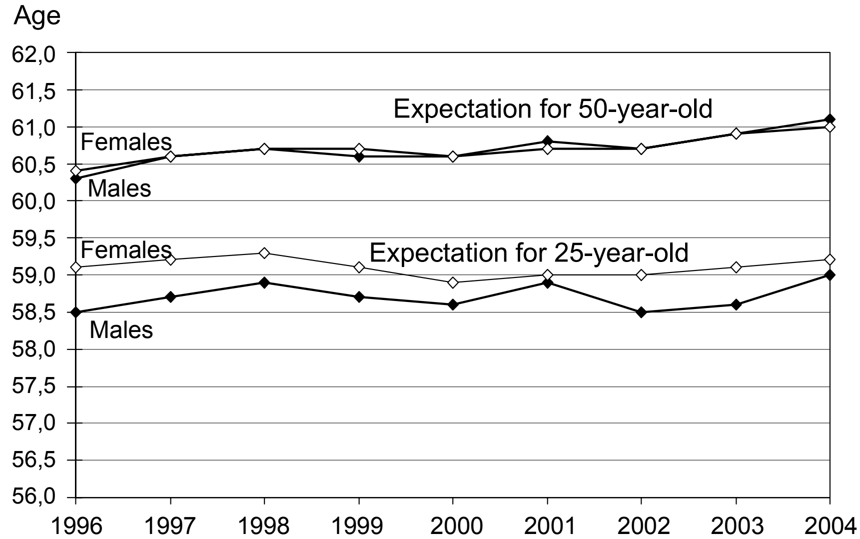


Figure 3.11. Total pension expenditure in percentage of GDP (Source: Finnish Centre for Pensions)

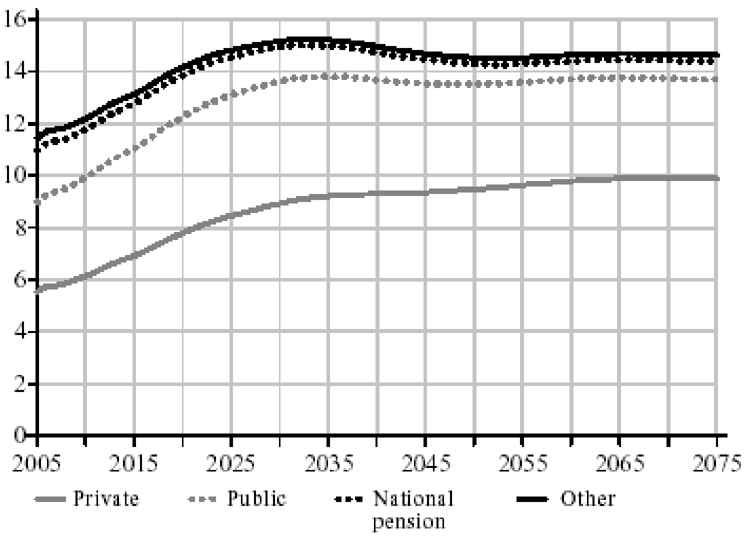


Figure 3.12. Contribution under the new Employees Pensions Act in percentage of wages and salaries and different components of the contribution (total contribution, employer, insured -53, insured +53)
(Source: Finnish Centre for Pensions)

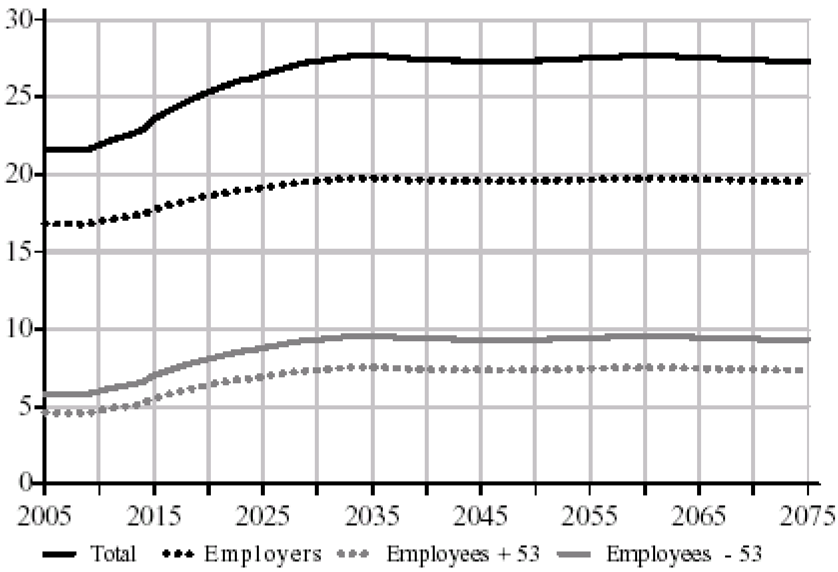
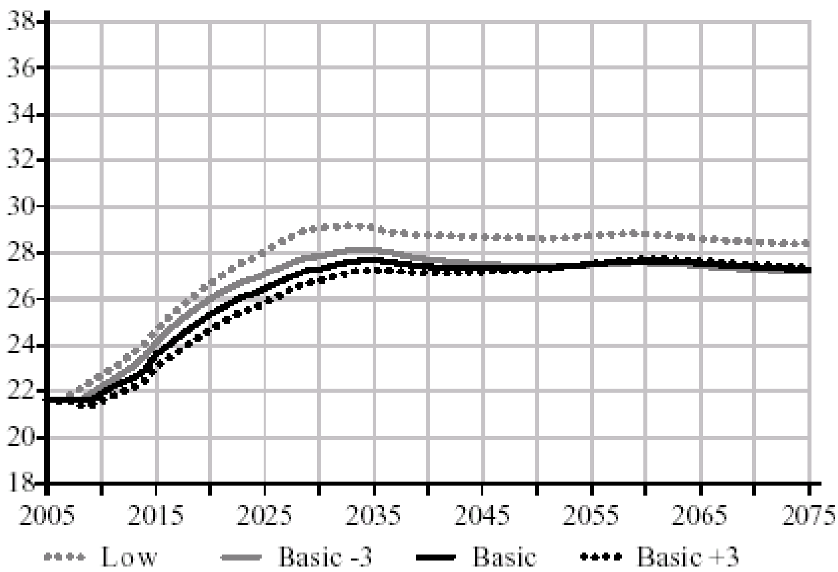


Figure 3.13. Contribution under the new Employees Pensions Act, %, in different employment options (Source: Finnish Centre for Pensions)



Tables 3.2.

a. Employment rate in the basic calculation and deviations in alternative calculations in relation to the basic calculation (Source: Finnish Centre for Pensions)

Year	2005	2010	2015	2025	2050	2075
Basic calculation	67,4	68,8	69,4	70,1	71,8	71,9
Basic +3	+ 0,2	+ 1,5	+ 2,7	+ 3,0	+ 3,0	+ 3,0
Basic -3	- 0,3	- 1,5	- 2,7	- 3,0	- 3,0	- 3,0
Low employment	- 0,6	- 3,8	- 3,9	- 4,5	- 6,0	- 6,2

b. Unemployment rate in the basic calculation and deviations in alternative calculations in relation to the basic calculation (Source: Finnish Centre for Pensions)

Year	2005	2010	2015	2025	2050	2075
Basic calculation	11,4	8,7	7,6	7,4	7,5	7,5
Basic +3	- 0,2	- 1,0	- 1,4	- 1,4	- 1,4	- 1,4
Basic -3	+ 0,2	+ 1,1	+ 1,7	+ 1,7	+ 1,7	+ 1,7
Low employment	+ 0,4	+ 2,4	+ 3,5	+ 3,6	+ 3,5	+ 3,5

Figure 3.14. Contribution under the new Employees Pensions Act by different assumed returns (Source: Finnish Centre for Pensions)

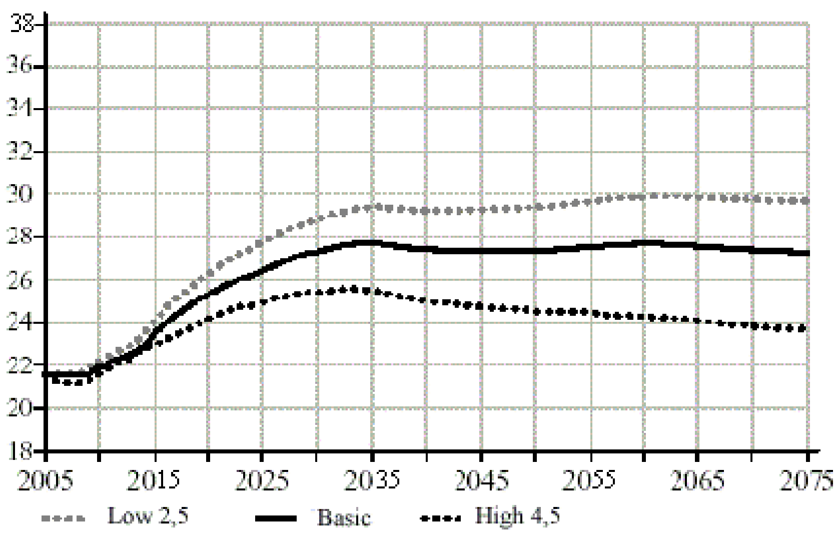
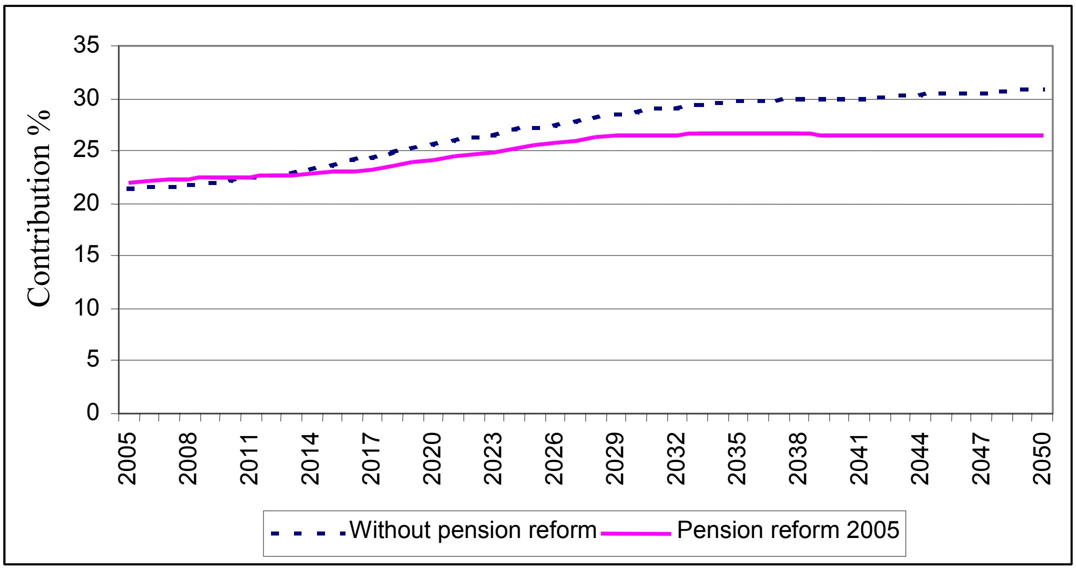


Figure 3.15. Impact of the pension reform on the development of the TEL (Employees Pensions Act) contribution (Source: Finnish Centre for Pensions)



4. Reform of the pension schemes in response to the changed needs of the economy, society and individuals

Table 4.1. Do people believe that their own pension benefits remain unchanged/change in the future (%) (Source: Finnish Pension Alliance TELA, attitudes to earnings-related pension 2004)

	1986	1987	1992	1995	1998	2001	2004
	%	%	%	%	%	%	%
Remain unchanged	32	31	26	23	30	39	35
Improve	39	34	4	5	7	12	11
Weaken	15	24	63	63	58	41	50
Don’t know	15	10	4	9	5	7	3

ANNEX 2. EU-data Tables

1 Demography

1,1 Population breakdown by age groups (2003)

2003						
0–14	**15–24**	**25–44**	**45–59**	**60–64**	**65–74**	**75+**
17,8	12,5	26,7	22,5	5,1	8,5	6,9

2003: Population at 1st January
Source: Eurostat
Date: 18.11.2004
EU-25 not available

1,2 Life expectancy at birth and at ages 60 and 65, by gender (2002)

	at birth		at age 65		at age 60	
	Men	Women	Men	Women	Men	Women
FIN	74,9	81,5	15,8	19,6	19,5	24,0
EU-25	74,8	81,1	16,0	19,6	19,6	23,8

Source: Eurostat
Date: 17.11.2004

1,3 Demographic old-age dependency ratio (2003): number of persons aged 65+ (60+) in relation to number of working age population (aged 15-64 and 15-59)

	65+/15-64	60+/15-59
FIN	22,9	33,2
EU-25	na	na

Number of persons aged 65+ (60+) in relation to number of persons aged 15-64 (15-59)
Source: Eurostat
Date: 17.11.2004

2 Household structures

2,1 Housing tenure status: percentage of people aged 65+ (75+. 60+) and for complementary age groups (below 65 and below 60 and 75) by the housing tenure status of the household they live in (owner-occupied with and without mortgage obligations on the property they live in, rent-free and rented accommodation) (total)

	75+					0-74					65+					0-64				
	owner occupied			rented	rent-free	owner occupied			rented	rent-free	owner occupied			rented	rent-free	owner occupied			rented	rent-free
	total	mortg.	no mortg.			total	mortg.	no mortg.			total	mortg.	no mortg.			total	mortg.	no mortg.		
FI	85	3	82	11	4	76	40	36	23	1	86	7	79	11	3	75	43	32	24	1

60+					0-59				
owner occupied			rented	rent-free	owner occupied			rented	rent-free
total	mortg.	no mortg.			total	mortg.	no mortg.		
85	9	76	12	2	75	43	32	24	1

EU-25 not available
mortg.: with mortgage obligations on the property lived in
Source: Eurostat (2004), ECHP UBD version December 2003

2,2 Household context of people aged 60+, 65+ (, 75+) in 2001 (% of the respective group)

	Persons living with their children		People aged 65+ living with another adult aged 65+	People aged 65+ living alone
	Lone parents aged 65+	All households		
FI	0,0	51,0	9,0	6,0
EU25	:	:	:	:

Source: Eurostat
Date: 13.12.04

3 General socio-economic data

3,1 GDP per capita and growth rates in 2002-04

	GDP per head in PPP (EU25=100)			GDP growth rates (%)		
	2002*	2003*	2004*	2002	2003	2004*
FI	111,2	109,8	109,4	2,3	1,9	3,0
EU25	100,0	100,0	100,0	1,1	0,9	2,4

* forecast
GDP growth rate: annual growth of real GDP from the preceding to the named year
Source: Eurostat, European Commission (ECFIN/50485/04, Information note for Ageing Working Group)
Date: 19.11.2004

3.2: Employment and unemployment rates by age in 2003 (%)

	Employment rates						Unemployment rate					
	25-54			55-64			25-54			55-64		
	Total	Men	Women	Total	Men	Women	Total	Men	Women	Total	Men	Women
FI	81,1	83,3	78,9	49,6	51,0	48,3	7,2	7,5	7,0	7,6	7,7	7,6
EU25	76,5	85,2	67,7	40,2	50,3	30,7	8,1	7,2	9,1	6,6	6,6	6,5

Source: Eurostat, Labour Force Survey - Annual averages (except DE, CY: spring results for all results except employment rate 55-64)
Date: 03.01.2005

3.3: Social protection expenditure and pension expenditure 1995-2000-2002 (ESSPROS, % of GDP)

	Social protection expenditure			Pension expenditure		
	1995	2000	2002	1995	2000	2002
FI	31,7	25,5	26,4	12,8	10,7	11.2.
EU25	:	27,0	:	:	12,6	:

Source: ESSPROS, Eurostat
Date: 3.02.2005
Social protection expenditure including social benefits, administrative and other expenditure covers the functions sickness/health care, disability, old age, survivors', Pension expenditure: old-age, early-retirement, survivors' and disability benefits from Eu25 data do not include CY data

3.4: Public debt and budget balance in 2002/2003

	Public debt (% of GDP)		Budget balance (% of GDP)	
	2002	2003	2002	2003
FI	42.6 (r)	45.6 (r)	4,3	2.3 (r)
EU2	61.6 (r)	63.3 (r)	-2.3 (r)	-2.8 (r)

r Revised value
Eurostat - EU excessive deficit procedure - ESA 95
Date: 6.12.2004

4 Adequacy of pensions

4.1a: Risk of poverty of people aged 60+, 65+, 75+ and <60, <65, <75 in 2001 (%)

	65+			0-64			75+			0-74			60+			0-59		
	Total	Men	Women	Total	Men	Women	Total	Men	Women	Total	Men	Women	Total	Men	Women	Total	Men	Women
FI	23,0	12,0	31,0	9,0	9,0	10,0	28,0	10,0	37,0	10,0	9,0	12,0	19,0	11,0	25,0	9,0	9,0	10,0
EU25	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:

At risk of poverty: people with equivalised income of less than 60% of overall median equivalised income
Source: Eurostat (2004), ECHP UBD version December 2003

4.1b: Risk of poverty of people aged 60+, 65+, 75+ and <60, <65, <75 by household type in 2001 (%)

	65+	0-64	
	living alone	living with adult 65+	living alone
FI	45,0	8,0	31,0
EU25	:	:	:

At risk of poverty: people with equivalised income of less than 60% of overall median equivalised income
Source: Eurostat
Date : 30.11.04

4.2: Risk of poverty of people aged 60+, 65+, 75+ and <60, <65, <75 by housing tenure status in 2001 (%)

	65+					0-64					75+					0-74		
	owner occupied			rented	rent-free	owner occupied			rented	rent-free	owner occupied			rented	rent-free	owner occupied		
	total	mortg.	no mortg.			total	mortg.	no mortg.			total	mortg.	no mortg.			total	mortg.	no mortg.
FI	23,0	9,0	25,0	28,0	9u	5,0	3,0	7,0	23,0	37,0	29,0	:	30,0	23u	:	6,0	3,0	10,0
EU25	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:	:

	0-74 (cont.)		60+					0-59				
	rented	rent-free	owner occupied			rented	rent-free	owner occupied			rented	rent-free
			total	mortg.	no mortg.			total	mortg.	no mortg.		
FI	23,0	27,0	19,0	7,0	20,0	21,0	15u	5,0	3,0	7,0	23,0	37,0
EU25	:	:	:	:	:	:	:	:	:	:	:	:

At risk of poverty: people with equivalised income of less than 60% of overall median equivalised income
mortg.: with mortgage obligations on the property lived in
Source: Eurostat (2004), ECHP UBD version December 2003

4.3: Risk of poverty at different income thresholds of people aged 60+, 65+, 75+ and <60, <65, <75 in 2001 (%)

	65+				0-64				75+				0-74				60+				0-59			
	40%	50%	**60%**	70%	40%	50%	**60%**	70%	40%	50%	**60%**	70%	40%	50%	**60%**	70%	40%	50%	**60%**	70%	40%	50%	**60%**	70%
FI	1,0	9,0	**23,0**	37,0	3,0	5,0	**9,0**	17,0	2,0	11,0	**28,0**	44,0	2,0	6,0	**10,0**	19,0	1,0	7,0	**19,0**	32,0	3,0	5,0	**9,0**	17,0
EU25	:	:	**:**	:	:	:	**:**	:	:	:	**:**	:	:	:	**:**	:	:	:	**:**	:	:	:	**:**	:

At risk of poverty: people with equivalised income of less than 40%, 50%, 60% or 70% of overall median equivalised income
Source: Eurostat (2004), ECHP UBD version December 2003

4.4: Relative risk of poverty in 2001

	65+ / 0-64			75+ / 0-74			60+ / 0-59		
	Total	Men	Women	Total	Men	Women	Total	Men	Women
FI	2,5	1,4	3,0	2,7	1,1	3,2	2,1	1,2	2,5
EU25	:	:	:	:	:	:	:	:	:

Risk of poverty (poverty line: 60% of overall median equivalised income) for age group 60+ (65+, 75+) relative to the risk of poverty for the complementary age group
Source: calculations based on 4.1

4.5: Risk of poverty for people whose main activity is 'retired' in 2001 (%)

	Retired people			Active people (16-64)		
	Total	Men	Women	Total	Men	Women
FI	20,0	11,0	26,0	6,0	5,0	6,0
EU25	:	:	:	:	:	:

At risk of poverty: people with equivalised income of less than 60% of overall median equivalised income
Source: Eurostat (2004), ECHP UBD version December 2003

4.6: Relative income of people aged 60+, 65+, 75+ (relative to the complementary age groups) in 2001 (%)

	Relative income 65+ / 0-64			Relative income 75+ / 0-74			Relative income 60+ / 0-59			Relative income 65+ / 45-54			Relative income 75+ / 45-54			Relative income 60+ / 45-54		
	Total	Men	Women	Total	Men	Women	Total	Men	Women	Total	Men	Women	Total	Men	Women	Total	Men	Women
FI	74,8	84,6	70,0	71,6	81,2	67,8	78,70	87,40	74,50	67,2	76,5	62,8	63,2	72,9	59,0	70,80	79,00	66,80
EU15	:	:	:	:	:	:	:	:	:	:	:	:	:	:				
EU25	:	:	:	:	:	:	:	:	:	:	:	:	:	:				

Relative income: ratio of median equivalised income of the complementary age groups
Source: Eurostat (2004), ECHP UBD version December 2003

4.7a: Composition of equivalised income by source in 2001 (%)

Age	65+				0-64				75+				0-74				60+				0-59			
Income source	Pensions	Other social benefits	Income from work	Other sources	Pensions	Other social benefits	Income from work	Other sources	Pensions	Other social benefits	Income from work	Other sources	Pensions	Other social benefits	Income from work	Other sources	Pensions	Other social benefits	Income from work	Other sources	Pensions	Other social benefits	Income from work	Other sources
FI	74	9	14	4	3	14	78	4	78	6	12	4	8	14	74	4								
EU15	72	4	17	7	8	8	80	4	75	5	13	7	14	8	74	4								
EU25																								

Source: Eurostat (2004), ECHP UBD version December 2003

4.7b: Composition of equivalised income by source by income quintile in 2001 (%)

Aged 65+

	Pensions						Other social benefits						Income from work						Other sources					
	Q1	Q2	Q3	Q4	Q5	All	Q1	Q2	Q3	Q4	Q5	All	Q1	Q2	Q3	Q4	Q5	All	Q1	Q2	Q3	Q4	Q5	All
FI	89	87	81	73	59	74	8	9	11	9	8	9	3	2	5	15	26	14	1	2	2	4	6	4
EU15	86	84	78	72	63	72	6	7	6	5	2	4	5	6	12	18	24	17	3	3	4	5	11	7
EU25																								

4.7b continued

Aged 0-64

	Pensions						Other social benefits						Income from work						Other sources					
	Q1	Q2	Q3	Q4	Q5	All	Q1	Q2	Q3	Q4	Q5	All	Q1	Q2	Q3	Q4	Q5	All	Q1	Q2	Q3	Q4	Q5	All
FI	6	3	3	3	2	3	40	26	14	8	5	14	52	70	81	86	84	78	2	1	1	2	9	4
EU15	10	9	8	8	7	8	29	13	8	5	3	8	58	75	80	83	84	80	3	2	3	3	6	4
EU25																								

Source: Eurostat (2004), ECHP UBD version December 2003

4.9: Inequality of income distribution (S80/S20) among people aged 65+, 75+ and <65, <75 in 2001 (%)

	65+			0-64			75+			0-74		
	Total	Men	Women	Total	Men	Women	Total	Men	Women	Total	Men	Women
FI	2,9	2.9u	2,9	3,4	3,5	3,4	2.8u	:	2.8u	3,4	3,5	3,4
EU25	:	:	:	:	:	:	:	:	:	:	:	:

Based on equivalised income; income share ratio 80th percentile/20th percentile
Source: Eurostat (2004), ECHP UBD version December 2003

4.10: Relative inequality of income distribution (S80/S20) in 2001

	65+ / 0-64			75+ / 0-74		
	Total	Men	Women	Total	Men	Women
FI	0,85	0.83u	0,85	0.82u	:	0.82u
EU25	:	:	:	:	:	:

Source: calculations based on 4.9
percentile for age groups 65+ and 75+ relative to the income share
ratio for complementary age groups

5 Financial sustainability of pension systems

5.1: Employment rates in 2003 and projected for 2010, 2030 and 2050 (% of the respective population)

	15-64				55-64			
	2003	2010	2030	2050	2003	2010	2030	2050
FI	67,7				49,6			
EU25	63,0				40,2			

Source: Eurostat
Date: 03.01.2005 (structural indicator - as data extracted for the spring report to the Council)

5.2: Effective economic old-age dependency ratio in 2003 and projected for 2010, 2030 and 2050 (%)

	2003	2010	2030	2050
FI	30,4			
EU25	33,6			

Inactive population 65+ in relation to employed population aged 15-64
Source: Eurostat, Labour Force Survey - Annual averages (except DE, CY: spring results)
Date: 03.01.2005

5.3: Employment rates of older workers in 2003 (% of the respective population)

	55-59			60-64			55-64			65-69		
	Total	Men	Women	Total	Men	Women	Total	Men	Women	Total	Men	Women
FI	65,6	64,9	66,3	27,3	31,1	23,7	49,6	51,0	48,3	5,8	9,0	3.2u
EU25	54,2	65,2	43,5	24,9	33,5	16,9	40,2	50,3	30,7	7,5	10,3	5,1

u: data lack reliability due to low sample size / : unreliable data
Source: Eurostat, Labour Force Survey - Annual averages (except DE, CY: spring results for the age classes 55-59, 60-64 and 65-69)
Date: 03.01.2005

5.4: Effective age of withdrawal from the labour market in 2001-2003 (years)

	2001			2002			2003		
	Total	Men	Women	Total	Men	Women	Total	Men	Women
FI	61,4	61,3	61,5	60,5	60,4	60,6	60,3	60,0	60,7
EU25	59.9e	59.4e	60.4e	60.4e	60.0e	60.8e	61.0p	60.5p	61.5p

e: estimated value, p: provisional value, b: break
Calculation based on estimated probabilities of labour-market exit for each age between 50 and 70 (see Joint Pension Report 2003, pp. 48/49)
Source: Eurostat, LFS
Date: 03.01.2005 (structural indicator - as data extracted for the spring report to the Council)

6 Modernisation of pension systems

6.1: Gender differences in the risk of poverty of people aged 60+, 65+, 75+ in 2001 (percentage points)

	65+	0-64	75+	0-74	60+	0-59
FI	19,0	1,0	27,0	3,0	14,0	1,0
EU25	:	:	:	:	:	:

Gender difference: risk of poverty rate women - risk of poverty rate men, in percentage points
Source: calculation based on 4.1

6.2: Gender difference in the relative income of people aged 60+, 65+, 75+ (relative to the complementary age group and to the age group 45-54) by household type of the elderly person in 2001 (percentage points)

	65+ / 0-64	75+ / 0-74	60+ / 0-59	65+ / 45-54	75+ / 45-54	60+ / 45-54
FI	-14,6	-13,4	-12,9	-13,7	-13,9	-12,2
EU25	:	:	:	:	:	:

Gender difference: relative income of women - relative income of men, in percentage points
Source: calculation based on 4.6

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