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Pan-European Pension System, Possibility or Fiction?

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Abstract

Today Europe has different pension systems. According to the history of forming, there are some based on the Bismarck model, like in central and southern Europe; and others on Beveridge's model, like in UK, Ireland, Netherlands and Cyprus; and those based on the Scandinavian model in the Scandinavian countries. In the past two decades there are pension reforms that are conducted in the eastern European countries based on the World Bank model. Most Western European countries did not reform their pension systems. In the past two decades they have made only adjustments but not reforms.

Some countries of the EU, like Greece, France, Spain and Portugal, have problems with the financing of their pension systems and also they have worker strikes over this issue. Conversely, Netherlands, UK, Sweden, Ireland and Denmark do not have those kinds of problems. The question is what is the difference in the pension models that makes the models of some countries to be more sustainable and others not. What are the differences in the models? On the one hand, some models can provide better solutions for the elderly population and, on the other hand, some models are not enough suitable for the future retirees. If we know that the EU is a market that is based on the freedom of movement of capital, goods and labor force, the question is, if EU countries do not have similar or connected pension systems, do we have a problem with freedom of movement of the labor force within the EU? In a time of crises, it is notable that in the USA, for example, the equality of the pension rights made it easier for the people to move from one region to another and to mitigate the effect of the crisis. Is it possible to have the same situation in the EU? Do we have to think of a Pan European Pensions System? What will be the features of that kind of system?

Pension Reform in EU as a Continuous Process

The pension reform issue is considered as top priority in EU member states. Reform of public pension systems commonly includes a limiting of public expenses increment, second and third pillar reforms which are necessary for the reform process to be successful and individuals to acquire an additional amount of pension for future pensioners.

Most EU member states in the past two decades have implemented a multi – pillar model which unites public and private pension schemes. Every pillar is important, although first pillar acquires pension for most pensioners. Current systems of mandatory insurance are not capable of providing a high social security rate, that's why the European social model, economic growth and EU stability is not possible without the significant reform processes.

Necessary measures commonly are not pleasant, so politicians usually want to bypass them. But reality forces them to start thinking about reforms. Often, certain individuals or groups of interest try to transfer the burden of reform to other generations. But, pension reform must be a process which should be adapted and implemented continuously. Gary Becker, Nobel Prize winner from Chicago University, is calling pension reform the “mother of all reforms”. Reform solves main long – term problems of pension financing, and moreover at the same time there are positive effects of capital price, employment increment and increment of GDP, which is the basis of economic development and a better life standard for citizens (Талески/Taleski, 2005, p.19).

Need of Pension Reform in EU and EU Member States Candidates

During the 1980s and 1990s, the population aging issue, forced almost all countries – EU member states from western Europe to change key elements of their pension systems, which were built on a PAYG (pay-as-you-go) solidarity basis in a period of rapid employment increment, young labor force and low rates of dependence between the old and young population.

Pension systems were founded in Europe at the end of 19th century, usually as part of larger systems for social security. Their progressive build in the first half of the 20th century enabled large expansion after World War Two, ranging over the entire working population. All systems had similar goals: to provide insurance against aging risks and initially range overall working population.

As a parallel, another part of the social security system provides security from unemployment risks, disability and so on. These systems were founded on welfare theory, based consequently on “imperfections of market economy” (Hubbard, Judd, 1987, p.631) and the elimination approach which eliminated certain imperfections of society.

Every pension system is the result of a delicate balance of economic, social and political power. Specific divisions which should describe characteristics of western European pensions and social systems that existed before the reform are:

Qualification - under certain criteria, all citizens are subject of pension insurance, usually based on equal amount of pension or in certain countries – pension based on earnings during individual’s career and specific professional (occupational) pension schemes which are based on participant’s status in it (profession);

Financing - financed from taxes and contributions. Solidarity systems (PAYG) were based on received benefits from current contributions, while other pension schemes with capital mechanism enjoyed benefits of the capitalization of assets;

System managing - centralized managed from public service or other systems are highly decentralized with certain types of semi – public institutions which are commonly functioning as autonomy agencies;

More of western European pension systems evolved into mixed systems with different elements based on defined benefits or defined contributions; with actuary or non – actuary components.

Europe in the next few decades will be faced with significant population aging, because of fertility decrement and prolonged life duration. Because of population aging, the rate of dependence of the elderly population from young population will increase. It is expected that this rate will double. Most Europeans have pessimistic views for the pension system future, due to PAYG base, which is not sustainable on a long term basis. The first response of this situation was increment of retirement age, in regards to the fact that European citizens spend around 20 years in retirement now, which in the 60’s of last century was on average 13 years. For the same reasons were raised contribution rates, but constant increment of the contributions in PAYG systems is a question that cannot be discussed on a long–term scale. The conclusion was to start a reform process of the pension system.

Regarding the problems, EU experts have changed the conceptual base of their opinions. The trend is crossing from “social welfare theory” to “contractual approach”. While “social welfare theory” is focusing on expenses, “contractual approach theory” searches institutional rights through particular procedures, ethical constellations, social security rights and fair play rules which lead individuals toward reaching the right for pension. Welfare approach permits greater liberty regarding the choice of contribution rate and levels of future benefits, retirement age (O’Dwer, 2006, p.17).

According to Vittas (2000), basic observation refers to goals that can be achieved with pension reform. It is important for pension reform to acquire higher efficiency and economic growth as well as development of financial markets, but these should not be primary goals of pension reform. The main goal of pension reform is acquiring adequate, decently evaluated and particular pension benefits. Besides that, there are additional effects which cause economy development and are not among the primary reasons for conducting the pension reform. The second main goal is establishing a strong relation between contributions and benefits with the purpose of minimizing certain unparticular distortions of labor market functioning and to be bypassed by unparticular redistribution. The third goal is forming of long – term savings which will stimulate capital market development. With it, the overall savings rate is increasing.

Pension reform may take three different forms: Parameter, NDC (notional defined contribution) and systematic form. Parameter reform means certain adjustments regarding retirement age, contribution rates, etc. NDC reform establishes a link between contributions and benefits and eliminates distortions of labor market. Neither parameter reform or NDC reform can stimulate long – term savings, which can bring direct effects for financial market development. Only systematic reforms that introduce fully funded pension insurance may have such effects (Vittas, 2000, p.2).

From the 1980s, many western European countries (Austria, Belgium, Denmark, Finland, France, Germany, Greece, Portugal and Spain) introduced their parameter pension reforms which changed the basic parameters in their systems, commonly: retirement age, contribution rates, and amounts of pension benefits and investment rules.

Italy and Sweden established their NDC systems, while Great Britain has made structural reform moving toward an almost totally “fully funded pension system” (O’Dwer, 2006, p.19).

Why Pension Systems are Reforming?

Pension systems should provide three main goals – saving, redistribution and insurance. While public pension plans acquire surpluses for a population that receives pension benefits, the situation is under control. But with time, these systems mature and the financing problem is actualizing and surpluses which were created and accumulated in the past were slightly spent. Most EU countries faced with these deficits and by the public pressure of the pension reform process was introduced in many EU countries. Surely not all reforms enable permanent solutions for problems.

According to Anita Schwarz and Asli Demirguc Kunt (1999, p.9) reform typology is based on solving several criteria: how benefits are calculated and how expenses are covered, how benefits are financed and who manages the pension system. According to the fact about what types of benefits exist and which are opportunities for their financing, governments approach various possibilities for pension reform conduct. Therefore the situation is totally different if in the country was functioning just on a solidarity system-PAYG, or beside solidarity system-PAYG were functioning also on fully funded pension schemes.

Minor Adjustments or Huge Reforms

After reviewing all of these questions, two reforming options may be posed; minor adjustments and huge reforms.

Minor adjustments are changes which can be implemented in the current pension schemes, primarily – to be postponed by fiscal problems, and sometimes to correct existing non – particularities. Government institutions may change criteria for acquiring pension benefits, may change contribution structure, structure of benefits and similar characteristics. Most of these processes cannot be enough to solve problems in public pension plans, but temporarily may solve fiscal crisis in pension insurance. As minor adjustments may be mentioned:

- Change of qualification criteria. All EU member states have made corrections of retirement age.
- Change of contributions structure: change of contribution rates or changing the replacement rate. Most EU countries in the last two decades increased the contribution rates.

- Change in benefit structure - change of pension amount calculation or change of pension indexing. Some EU countries, like Portugal, changed the pension calculation method.
- Under real reform are defined the situations in which a defined benefit system is replaced with a defined contribution system or vice versa or switching from PAYG system to a fully funded pension system or vice versa. Huge reforms which were accomplished in EU member states are:
- From mandatory PAYG defined benefit system to: Combination of mandatory PAYG defined benefit system or defined contribution – NDC system with mandatory fully funded pension system. These types of reform were conducted in countries which have accepted the World Bank model.
- From mandatory PAYG defined benefit system to: Combination of mandatory PAYG defined contribution system (NDC system) and additional fully funded pension system. This kind of reform was conducted in Sweden and Italy

Although many countries declared that they are changing the pension system, just about 25% of those reforms can be named “huge” reforms. In EU member states, real reforms were conducted in central and eastern European countries such as: Poland, Hungary, Czech Republic, Slovakia, Slovenia, Estonia, Lithuania and Latvia. In western European countries, real pension system reforms were conducted in Sweden and Italy. Remaining countries from EU have conducted reforms which have more elements of adjustment than real structural reforms (O’Dwer, 2006, p.21).

Successfulness of Reform Functioning

Crossing from a solidarity system-PAYG to a combination of solidarity-PAYG and fully funded pension system can be graded through answers to several questions.

May fully funded pension systems guarantee highest return rates? Reviewing the financial markets history in the last 30 years, it can be noticed that the average return rate is moving from 4% to 7%. If we make a simple comparison between return rates of solidarity-PAYG and fully funded pension system, it’s obvious that a fully funded pension system has an advantage. But, a fully funded pension system has advantage if we compare only “purely return rates" which brings two systems. But if we compare return rates with transition costs, inflation rate, possible economic and financial shocks, fully funded pension system does not have "huge advantages". Some authors think that fully funded pension system increases economic welfare, but other author's think that it does not, because of transition costs. Also, fully funded pension systems can better endure the aging population issue, but sooner or later, with decreased demand of stocks and bonds (because of decreased population), prices of financial instruments may fall.

Also, analyzing the goals which bring pension reform may be reviewed from several aspects:

- Acquiring long – term fiscal sustainability for the next 50 years.
- If it will be necessary in the future to take minor reforms, will the reform cause political difficulties and non – particularities?
- Acquiring gains and economic efficiency from basic reform (what kind of gains and ways of acquiring)

EU candidate members, such as Macedonia and Croatia have a need for a pension reform because of the aging population, as well as decreased economic activity in the country. Pension reforms which these two countries have conducted are according to the World Bank model – crossing from solidarity-PAYG pension insurance system to combination of solidarity-PAYG and fully funded pension insurance (mandatory and voluntary).

EU Pension System Strategies

In all EU countries, expenses for pension systems were getting higher and higher. Expenses for pension, as well as expenses for healthcare insurance, for social protection and unemployment could not continue without high contribution rates. Current pension systems were non – transparent, rigid and did not respect basic economic functioning principles. Reform was needed. An extreme solution would be the absolute replacement of the PAYG defined benefit model with a voluntary fully funded pension system with defined contributions. But extreme solutions sometimes pose questions for economic sustainability of transition costs towards establishing that sort of pension system and problems that will eventually arouse.

Main questions which were shown in national strategies of EU member states for pension system reforming are:

- Way of financing of pension schemes (solidarity-PAYG or fully funded)
- Way of managing (public or private pension schemes)

- Obligatory function (mandatory or voluntary membership into pension scheme)
- Benefits determining - schemes with previously determined benefits-DB or schemes with defined contributions-DC.

What opportunities did governments have in various countries? Choice of pension system of EU member states was not a decision in frames of EU, but every member state created its own pension system shape and conducted the pension reform in its own way. One thing can be concluded – a multi-pillar model is “mandatory” for all countries, but member states individually decide about combinations of founding it.

Membership Contour – Mandatory or Voluntary

A problem of voluntary pension systems is that voluntary membership does not acquire strictly defined contribution rates, which should be paid. In certain countries, because of complexity of question and lack of information, as well as short – sighted (myopia) employees, beside the mandatory solidarity-PAYG system were established also mandatory fully funded pension schemes. Mandatory fully funded pension schemes were established in Poland, Slovakia, Hungary, Lithuania, Latvia, Estonia as well as Finland and Denmark. For remaining member states, membership in fully funded workers unions and unions of employers. The state has an obligatory function because the individual has no initiative to take care of his retirement days, and individually to acquire pension amount. From another point of view, it is important that individual contributions into fully funded pension systems which will mean decrement of contribution evasion which was a common case in solidarity-PAYG system.The third characteristic which propagates mandatory fully funded pension insurance is risk diversification between mandatory solidarity and mandatory fully funded pension insurance is under the supposition that if one of the systems fails to acquire enough assets the other will.

Way of Financing – Solidarity or Fully Funded Pension System

Discussion about solidarity-PAYG or fully funded pension systems demands serious attention in economic and political public. Crossing to a privatized pension system in 1994 was proposed by World Bank and the International Labor Office. Investment schemes will be a solution for demography and financing problems, as well as future contribution rate decrement, and by competition increment the decrement of fiscal deficit in the state would be managed. Private pension schemes favoritism was conducted in Great Britain, Ireland, Netherlands and Denmark. Commonly pension schemes were functioning together with solidarity-PAYG systems, which enables minimum rights. Expectations from fully funded pension schemes were large. These pension schemes, although voluntary, are 90% financed by the working population who were included in these schemes. Also Scandinavian countries, Sweden and Finland dedicate great attention to fully funded pension systems for retirement.

Remaining member states have private pension schemes, but until recently, their growth was not stimulated by the state. Pension schemes are based on voluntary principles and include minor parts of a working population.

According to the experience of many countries that have experience with fully funded pension systems such as Netherlands, Sweden, and United Kingdom, it could be concluded that one safe way for individuals to acquire a satisfactory pension level is to make additional savings.

Schemes with Defined Benefits-DB or Schemes with Defined Contributions-DC

One basic principle of pension systems is the prediction of income after retirement. By schemes with defined contributions that principle is not fulfilled and the amount of pension income could not be predicted. Simulations show that the altitude of insured assets varies almost 30% compared to interest rates and salaries increment in the last 40 years. Most commonly PAYG systems in Europe are based on defined benefits except in Sweden, Italy, Poland and Estonia, where the PAYG system is with defined contributions (transformation to NDC system).

Fully funded pension systems in western European countries, usually were with defined benefits, but the tendency within the last 10 years is that, those systems have to be transformed into defined contribution systems. While fully funded pension systems in central and eastern Europe in their mandatory and voluntary schemes established defined contributions system.

In EU member states, PAYG systems are publicly managed, while fully funded pension schemes are managed privately. Only fully funded collective pension schemes of the public sector in western EU countries have elements of public managing.

In Great Britain, Ireland, Netherlands and Denmark every individual whether he was employed or not, has the right to a minimum pension. In Scandinavian countries there is guaranteed state pension of social amount whether an individual was employed or not. Within the rest of EU member states, state pension has a value depending on paid contribution and years of contributing.

Throughout the world there are solutions for public fully funded pension schemes, but in EU member states these types of solutions do not exist. There are only possible combinations of solidarity-PAYG with fully funded pension systems. Various options of functioning for the first and second pillar in frames of pension systems within the EU member states are provided in the table that follows.

Lisbon Strategy for Coordinated Pension System in Europe

The Lisbon strategy, known also as Lisbon Agenda was concluded by the European Council in Lisbon, Portugal in 2000. The European Union created strategic goals, until 2010 to become the most competitive and most dynamic economy in the world, founded on knowledge, capability of sustainable economic growth with a greater number and more quality labor need, as well as bigger social cohesion. It was an answer to global challenges, especially for USA development regarding the new economy of knowledge and domination of informational and communicational technology. For accomplishing that ambitious goal Europe needs preparation along with a qualified policy, market development and modernization of the European social model. (Boromisa, Samardžija, 2004, p.200)

According to Dekker, Ederveen, Jehoel, Gijsberg, de Mooij, Soede, Wildeboer, and Schut (2003), the Lisbon Agenda strategy is based on three main goals:

- Productivity increment in EU economies (dynamic knowledge);
- increment of employment (accomplishment of full employment with promoting labor market participation);
- increment of social cohesion (poverty decrement and decrement of social programs);

On December 2001, the European Council found out that significant results will be met with setting dialog and coordination of questions in relation to the pension system reform. It refers to goals of adequacy, financial sustainability, and adaptability of the working method based on coordination between pension systems and policies-Open Method of Coordination.

In 2005, a Commission suggested revision, and the Council approved revision of the Lisbon strategy for employment increment and revised "integrated guidelines". Open method of coordination in social protection field and social participation matches with the Lisbon strategy. The Commission also has the intention to improve the level of coordination in the social protection field with strengthening the "Open method communication" about pensions, social protection and healthcare insurance in 2006.

Reports of the Commission recommended to the EU member states to encourage older workers to stay longer on the labor market and to strengthen the link between contribution and benefits, and to promote public and private pension financing, in the context of long-term implications so that the individual's life duration increment may have postive influence on the living standard of the people. Until 2050, the European population will be insignificantly decreased, but older in average.

Beside the encouragement of older populations working and a better relationship between contributions and benefits as a means to reduce the poverty, some EU countries in their strategies put an objective to maintain levels of guaranteed minimal pensions. The Open method of pension coordination is based on 11 target groups, divided by adequacy, sustainability and modernization of pension systems. Detailed progress analysis toward these goals is presented in the Second Round of the National Strategy Report. In these reports it was pointed out that the efforts for maintaining pensions system sustainability with reduction of public debt.

The Joint Report for Adequate and Sustainable Pensions of the European Commission from 2003 has four high priority issues, mentioned below:

- Encouraging individuals to work in elder years.
- Life cycle development and strengthening the relationship between contributions and benefits.
- Pension systems modernization to enable pension systems to be adaptable to structural changes.
- The Guarantee of minimum pension income.
- Additionally, two questions are placed with recent reforms:

- Acquiring private pensions with the purpose of partial replacement of public pensions. Many EU member states establish private fully funded pension systems with the purpose of acquiring convenient pension income and maintaining a positive role regarding demographic risk diversification between public and private schemes.
- Strengthening pension systems regulation. Periodic ad-hock pension system revisions, as well as automatic and semi-automatic adjusted mechanisms need to be established in order to control pension systems.

Differences between Pension Systems and the Process of Their Overcome

With the purpose of overcoming the differences which exist in EU member states, and creating the mechanisms for coordination of the pension systems, EU institutions have brought acts and documents which regulate pension insurance issues. The EU council in 1993 declared resolution for a flexible principle of retiring which encourages the older population to be active in the labor force market. Flexible arranging of retirement policy is individually decided by each member state, but it is important for each country to respect the principle of subsidiary. In the book “echo of demographic changes: New solidarity between generations”, the EU Commission warned about the necessity of global debates on “social security systems” issues, surely with respect to different measures that can bring various government institutions and states. With these resolutions and recommendations, EU countries need to minimize the differences between pension systems of member states.

European institutions (Commission, Council and Parliament) and other independent EU institutions (agencies, committees and partnerships) are seriously analyzing the situation of pension systems. For that purpose specific institutions have issued numerous recommendations, announcements and other optional justice acts which warn about the importance of the pension issue, and to help another state towards solving current problems with its pension financing. The EU institutions, have limited influence on the EU members, regarding the pension issue, because every member state solves this problem individually. The question related to the free flow of labor force, services and capital are connected with the pension system question.

Mutual social policy, which is necessary for EU cohesion, is brought according to Lisbon Agenda. Numerous goals of pension policy, related to mutual market and monetary union demand policy adjustments. Numerous EU acts treat the economic and social cohesion, but they do not interfere with the pension model questions of individual member states. Member states shape their pension models in their own way. Their responsibility is to accomplish duties from certain EU bounding acts which refer to an agreed benefit level of the pension systems. Beside EU level obligatory acts, the EU brought various acts which refer to the income of pension systems. EU acts regarding the pension insurance system are as follows:

- Basic principles about free flow of labor force and transferring pension rights which refer to mandatory pension insurance can be found in an EU council agreement for social system security using employed individuals, self – employed individuals and their family members in EU frames (EC 1408/07).
- Directive referring to additional pension insurance rights for employed and self – employed individuals in EU frames (EC 98/49). The Directive arranges the question for the protection of an individual's rights which are moving inside the Union or resettled, or have worked abroad and acquire additional pension insurance rights. The Directive supposes that additional pension insurance benefits can be paid in other member states without additional tax or other transaction costs.
- Directives for activities and supervision of additional professional pension insurance. EU Parliament directive and EU Council for work and supervision of institutions (EC 2003/41) refers to this issue. In the Directive are also added basic principles of capital investments and activities at foreign capital markets, the possibility of contributions transfer in occupational insurance schemes, as well as the economic and social development that results. This Directive is brought in order to acquire larger competition regarding products at pension insurance market.
- Regarding Tax frames for professional (occupational) pension schemes, the EU Commission has issued an Announcement for a tax frame referring pension which includes professional pension schemes (COM/2001/0214final). In the life insurance field, the EU Council brought three Directives (79/267/EEC, 90/619/EEC, 92/96/EEC, 95/26/EC, 2000/64/EC, 2002/12/EC, 2002/83/EC).

One of the basic themes of the Commission is resolving the older population problem in the EU, three reports have been instigated in relation to: demographic increment, acquiring equity between generations at redistribution, financing of retirement pensions and health care expenses and new income division between older and younger population, in addition to income between active and non – active population (COM/2005/0094final).

In the frame of reforms for social security systems, Commissions have implemented optional law acts that stimulate cooperation between member states and provide support in configuring their strategy. Pension systems in EU countries must be compatible and be directed toward realizing targeted goals. The ultimate challenge of pension systems is its relation to capital market. Beside healthy macroeconomic policy and structural reforms that stimulate economic growth and employment, as well as public finances balance, the governments should work on the public expenses field, especially pension system expenses from the national budget.

States with independently owned development of the pension systems may find solutions by establishing mutual cooperation. Pension systems may reach a higher degree of social safety through mutual cooperation. A Commission in the report labels as a "Backup of national strategies for adequate and sustainable pension system" (COM 2001/0362final) suggesting cooperation between states based on OMC (Open Method of Coordination) in the pension reform field .By introducing the OMC system, member states cooperate and report about the strategies.

The question of the efficiency of the OMC method is whether it can be implemented in pension reform processes in various institutional structures and political environments of individual member states. Related questions about suggested cooperation between states are numerous: whether current development is moving in a direction of individual pension model development, whether the OMC method is a primary tool for directing the process on the "right way" through commitment of individual member states reporting; whether suggested models strengthen targeted goals of sustainability and pension adequacy, as well as the modernization of the pension system; whether suggestions are exact so member states can easily respect them and whether suggestions are flexible enough to be adjusted to a national environment?

David and Andros (2006) evaluate the OMC method through three views: normative, cognitive and processed. Member states in the last two decades face a series of challenges, which in different systems are set on a different priority scale.

The OMC method establishes the coordination of pension systems national processes and challenges are set in certain frames. Under a normative view, OMC determines economic and social goals of pension policy. From a cognitive view, it can be identified best through the implementation of theory practically, approach and measures. The processed view acquires transparency of pension reform over the entire process.

With EU member states pension reforms and through their coordination, adequacy of pension systems can be acquired after having fulfilled several goals:

- Protection from social distortions by implementing guaranteed minimum income level of the older population, as well as minimum guarantees for future income that will keep the older population out of poverty.
- Enabling people to keep living standards through acquiring pension arrangements, public and private that can enable solid living standard after retirement. A significant factor for achieving this goal is replacement rates.
- Promotion of solidarity between generations and inside a generation, through sharing risk, pension indexation and decrement of income inequality at older population.
- Financial sustainability can be acquired through:
- Increment of employment rates that will increment the possibility of pension system financing
- Extending the working duration and retirement date
- Establishing sustainable pension system in context of public finances
- Adjustment of contributions and benefits on a balanced way, maintaining fair balance between working and retired population
- Acquiring adequate and financially significant private pensions, through establishing a regulatory frame from this kind of pension scheme.
- According to Synthesis report (2006), of Directorate-General for Employment, Social Affair and Equal Opportunities of European Commission, modernization of pension systems is achieved through:
- Adaptation of more flexible employment that provides compatibility of pension systems with demand of flexibility and safety of labor market.
- Facing aspirations for equality between men and women.
- Demonstrating the possibility for facing the pension systems challenges.

Establishing a Pan– European Pension System – Potential Structure and Transitional Questions

The need of pension system reform is recognized in all EU member states. Demands for a mutual approach toward reforms do not enjoy mutual support. The European Commission, which on various fields sees the need of coordination and total harmonization has the role of issuing recommendations, not Directives related to internal rules that will maintain member states.

An idea for a common EU pension system is supported by the Pan – European approach, in order to achieve a unity of the pension field and to contribute to reaching set goals – bigger flow of products, services, labor force, capital and accomplishing Maastricht criteria. The pension system must stimulate mobility between occupations and sectors, as well as between various regions and states. Different occupational pension schemes discourage people to change their working place and have negatively influenced the labor market development. Also, transferability of rights acquired from public pension schemes, as well as transferability of rights from additional pension schemes is significantly limited. One common pension system will surely provide bigger mobility in capital market. Besides eliminating the differences between various pension systems, the differences between social policies and programs are eliminated also.

A Pan – European approach should lead toward a coordinated pension structure. Pension systems are treated as well as other social policy programs. By national agendas the EU member states show low indications that recognize opportunity for better harmonization and coordination. Introduction of a common currency is part of the European economic integration, which causes implications toward member states budget. The Euro has implications on other elements of national economies such as flexibility of labor market and fulfilling the gap of labor force in various countries with a higher proportion of elderly citizens. The Euro as a currency enabled bigger budget expansion in particular member states because there is no opportunity for independent monetary policy and that indirectly influenced fiscal policy; inability to influence interest rates causes asymmetrical shocks that hit particular member states. The main instrument that can regulate the shock of decreased fiscal policy efficiency in a mutual monetary zone because of transferring economic activity to other countries is the flexibility of labor market, as well as flexibility of salaries and migration.

Empirical studies from other countries, as USA for example, show that although salaries adjustment is important in solving regional crisis, the main adjustment mechanism is migration from regions with lower economic activity toward regions with higher economic activity. In the past in Europe, inter – regional mobility was very low because of rigid labor force market as well as because cultural and linguistic barriers. But with globalization and the introduction of common values, these mechanisms should be strengthening allowing adjustment and annulations of certain shocks of economic and social nature. One important mechanism which can help the common currency shock adjustment is the pension system. If it is coordinated, it can provide excellent mobility of labor force between sectors and occupations as well as between states. In many European countries, different rules about the public and private sector decrease mobility between sectors. Mobility between states exists also for public pension schemes as well as for fully funded pension funds. The EU doesn't have a coordinated or harmonized pension system, which is not characteristic for other economically integrated regions with common values as Australia, Canada, USA, and Switzerland. These confederations or federations have huge differences on the level of state or province (including taxes or short – term social benefits), but have one thing in common – public pension schemes which refer to all states or provinces.

The third major instrument for a more coordinated Pan–European pension system refers to integration of labor market and bigger flexibility. European market is free for trade of goods and services as well as free flow of capital. By declaration, free flow of labor force exists but serious integration of the European labor force market also demands equality of pension rights between the states.

The long–term value of the Euro against other currencies should be determined from European countries development. Current balances or misbalances of goods and services flow influence the relative prices of currency under the globalization effect. Aging of the European population may compensate partially with GDP increment effect of member states, as well as the increment of productivity which refers to mechanisms for worker's allocation toward sectors and regions of development. It means need of mutual pension systems which will enable that possibility (Holzmann, 2004, p.33).

A Pan–European approach suggests a pension system that will include mandatory NDC pension scheme and voluntary additional occupational or individual pension schemes in second and third pillar frames. Pensioners should receive guaranteed minimum pension which is not related to contributions into the system. A suggested model will fulfill basic goals of adequacy, financial sustainability and modernization of pension systems which will mean creating a Pan – European system: greater mobility of the labor market, solidarity and redistribution and a simple transfer system from one to another pension system. Establishing a NDC scheme is the simplest process in all member states because expenses incurred crossing to the new system, for most countries will be minimal. Fully funded pension schemes in second and third pillar frames are familiar for most countries and that is why this field needs small adjustment and coordination. Fully funded pension schemes bring additional income for a period after retirement. Regarding a Pan – European approach the economies should make a different combination of choices. One question is obligatory function of fully funded pension schemes and the way of determining rights, simplicity and transparency of schemes and regulative, supervision and taxing. According to Holzmann (2004), it's necessary to be introduced as voluntary, occupational and individual pension schemes based on defined contributions with a simple structure, standardized processes and transparent. Relating regulative and supervision, there are two possible approaches: a centralized approach or mutual rights recognition approach.

According to David Natalli (2006), the recent process of pension policies adjustment is called a "hybridization process". It represents reform that leads through mutual interference of individual pension systems, a model in which traditional instruments from one system type unite themselves with instruments of another system type and the overall pension system will become hybrid. Hybridization of pension systems is a process that is happening in EU member states. PAYG schemes interfere with fully funded schemes, and social protection is offered from both the public and private sector. Besides the existence of similar elements of pension system hybridization, we cannot talk about their "fraternization". It's more usual to talk about mutual revision of pension systems in individual states, but not about a "fraternization" process.

Conclusion

The process of establishing a pan-european pension system is very important for the existence of the European Union. The compatible pensions systems in the EU facilitate the free flow of people within the EU. In the USA, which consists of 50 states, the emigration of the population from one state to another is 1,6% of the total population of the USA. In Europe it is 0,3% of whole population within the EU, and mostly the migration is from Poland, Romania and Bulgaria to some West European countries within the EU. As it is proclaimed, the free flow of people is one of the principles of the EU. By the limitations that are created by language and cultural differences and also by limitations based on differences of pension and fiscal systems, people in the EU are practically faced by strong limitations in their intention to move in another member state. The most important thing in this kind of migration is that in some situations when some regions (states) face local crisis, people usually migrate to another country where they can find a job or better job. By this process, the risk of spreading the crisis to another member states is smaller.

The conclusion is that the unified structure of the pension system within the EU, will be of great importance in the process of stronger unification of the European economy and in the process of stronger unification of the fiscal systems in the member countries of the EU. That stronger unification will mean less risk in the spillover effect of a local crisis to another country and also to the whole European economy. It is very rare to hear that some EU countries like Netherlands and Sweden that have some problems in their pension systems. From the other side it is very often to hear information that for example Greece, France and Portugal have big problems with their pension systems. The point is how to avoid this kind of difference between pension systems, because that means that some countries in the EU practically enlarge their public debt by having unsustainable pension systems. There are very large differences in the pension systems of the member countries within the EU. Those differences are in the structure, retirement age, benefits and other characteristics. Another point is how to reduce the differences and also how to eliminate them in the long run.

The further steps within the EU will have to be to make circumstances for the creation of a process of gradual unification of the pension systems within the EU accompanied with the process of fiscal unification. This process will be very real within the EU after the debt crisis that some countries in the EU have faced recently.

Most of the European countries are in a debate over the pension reform characterized by fiscal issues at the national or EU level. There is no discussion about moving toward a more coordinated pension system within the EU and how such a system may be created.

There has to be a leader in a creation of that kind of system in the future. It could be the European Commission and the member states have to empower the Commission or this institution of the EU has to take such a lead in a process of upgrading the Open Method of Coordination in order to accelerate the reforms in the member countries.

Another approach could be adoption of a model by competitive approach across EU countries. In that case the advantages and the lacks of the systems have to be measured and documented in order to make imitations of these systems from one country to another (example adoption of NDC Swedish model in Austria and Germany. This could be a restricted and long lasting solution.)

The third possible situation is to make a follow of leading example as a created model that would have characteristics of most used pension systems in EU countries. The creation of that kind of universal model has to be presented by Economic Policy Committee of the EU which represents high-level officials from ministries of finance of the EU countries. This approach could overcome only the fiscal consequences and to be focused on broader stability of the pension system including mobility across the European Union.

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Table 1: Approaches toward pension reform

Status	*Type of reform*	*Measure of change*
Minor adjustment	Eligibility Criteria	Retirement age
		Service years
	Contribution Structure	Coverage
		Contribution rate
		Contribution base
		Source
		Taxation of contrinutors
	Benefit Structure	Benefit formula
		Pension base
		Indexation
		Minimum pension
		Payment form
		Taxation of benefits
	Administration	Ministerial authority
		Investment policy
Major reforms	PAYG to Defined Contribution fully funded	Public/Private mix
		Minimum pension
		Other guarantees
		Transition period
		Transition mechanism
	PAYG DB to PAYG NDC	Minimum pension
		Other guarantees
		Transition period
		Transition mechanism

Source: Schwarz, A., Demirguc-Kunt, A., "Taking Stock of Pension Reforms Around the World", The World Bank, Social Protection Unit, 1999, page 27.

Table 2. Types of pension reforms

Minor reforms		
Eligibility Criteria	Retirement Age	Czech Republic,Estonia, Hungary
		Lithuania, Greece, Ireland
		Italy, Portugal and
		Latvia
	Service Years	Greece, Italy
		Portugal, Latvia
Contribution Structure	Contribution Rate	Bulgaria, Czech Republic, Estonia
		Latvia, Lithuania, Poland
		Slovakia, Slovenia, Cyprus
		Malta, France, Germany
		Greece, Italy, Netherlands
		Portugal and Sweden
	Contribution Base	France
Benefit Structure	Pension Formula	Estonia, Hungary, Latvia
		Lithuania, Poland, Denmark
		Finland, France, Greece
		Italy, Portugal, Czech Republic
	Indexation	Malta, France, Germany
Major reforms		
PAYG to reformed PAYG and Defined Contribution fully funded		Hungary, Lithuania, Estonia
		Slovakia, Romania, Bulgaria
		Czech Republic and Slovenia
PAYG DB to PAYG NDC		Poland, Latvia
		Sweden and Italy

Source: Schwarz, A., Demirguc-Kunt, A., “Taking Stock of Pension Reforms Around the World”, The World Bank, Social Protection Unit, 1999, page 27

Table 3. Modalities of the functioning of the pension systems in EU countries

Countries	*first pillar*	*second pillar*	
	Conditions for retirement	PAYG-DB/NDC	additional pension insurance
Austria	retirement age / service years	PAYG-DB	Voluntary
Belgium	retirement age / service years	PAYG-DB	voluntary *
Cyprus	flat rate	PAYG-DB	Voluntary
Czech Republic	flat rate	PAYG-DB	Voluntary
Denmark	flat rate	PAYG-DB	Obligatory
Estonia	retirement age / service years	PAYG-DB /	Obligatory
Finland	flat rate	PAYG-DB /	Obligatory
France	retirement age / service years	PAYG-DB /	Voluntary
Greece	retirement age / service years	PAYG-DB	Voluntary
Ireland	flat rate	PAYG-DB	voluntary *
Italy	retirement age / service years	NDC	Voluntary
Latvia	retirement age / service years	NDC	Obligatory
Lithuania	retirement age / service years	PAYG-DB	Obligatory
Luxembourg	retirement age / service years	PAYG-DB	Voluntary
Hungary	retirement age / service years	PAYG-DB	Obligatory
Malta	retirement age / service years	PAYG-DB	does not exist
Germany	retirement age / service years	PAYG-DB	Voluntary
Netherlands	еднаков износ	PAYG-DB	voluntary *
Poland	retirement age / service years	NDC	Obligatory
Portugal	retirement age / service years	PAYG-DB	Voluntary
Slovakia	retirement age / service years	PAYG-DB	Obligatory
Slovenia	retirement age / service years	PAYG-DB	Voluntary
Spain	retirement age / service years	PAYG-DB	Voluntary
Sweden	flat rate	NDC	voluntary *
United Kingdom	flat rate	PAYG	voluntary *

* Obligatory by membership in work and trade unions.

Source: Škrlj, N., *Pomen sistema, osnovanega na fiktivnih individualnih racun (NDC) vo okviru pokojninskih reform*, Ekonomska fakulteta, Ljubljana.

Table 4. Characteristics of the models of pension insurance

	Traditional models	Liberal models
Population ageing	High	Low (rising tendention)
Maturity of the pension systems	High	Low (rising tendention)
Level of benefits	Lowering tendention	Stable
Unemployment	High	Low
Economic development and increment of salaries	High	Low
Flexibility in finding job	High	High
Integration of the financial market	High	High

Source: Škrlj, N., *Pomen sistema, osnovanega na fiktivnih individualnih racun (NDC) vo okviru pokojninskih rform*, Ekonomska fakulteta, Ljubljana.