UNIVERZA V LJUBLJANI
FAKULTETA ZA DRUŽBENE VEDE

Katja Rihar Bajuk

REFORMA POKOJNINSKIH SISTEMOV V IZBRANIH SREDNJE- IN VZHODNOEVROPSKIH DRŽAVAH

ŠTUDIJA PRIMEROV SLOVENIJE IN MADŽARSKE

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Povzetek

Ena pomembnih značilnosti zadnjega desetletja je hitro spreminjajoča se demografska situacija, ki je posledica višje pričakovane življenjske dobe in zmanjšane stopnje rodnosti. Omenjena demografska tranzicija se kaže v staranju prebivalstva in posledično predstavlja težko finančno breme za obstoječe pokojninske sisteme. V srednje- in vzhodnoevropskih državah so v devetdesetih letih dodaten izziv finančni stabilnosti predstavljale posledice prehoda s centralno-planskega na tržno gospodarstvo.

Pokojninska reforma, ki je predmet obravnave te naloge, predstavlja enega izmed neizogibnih odgovorov na zgoraj omenjene demografske in ekonomske trende. Različne države so se pri tem odločile za različne politike. Tako na nacionalnih kot tudi na globalni ravni sta se pojavili dve prevladujoči, med seboj nasprotujoči si, opciji. Prva zagovarja ohranitev javnih sistemov socialne varnosti korporativistično-konzervativne narave, ki sicer zahtevajo manjše prilagoditve, druga pa govori bolj v prid privatizaciji pokojninskih sistemov in vzpostavitvi troplastne strukture le-teh. Pri tem bi le minimalni prejemki izhajali iz javnih shem, preostali pa iz dodatnih skladov drugega in tretjega stebra. V sprejetih nacionalnih politikah je v večini primerov opaziti srednjo pot, ki vključuje elemente obeh pristopov, pri čemer je slovenski sistem precej bliže prvi opciji, madžarski sistem pa je šel z vzpostavitvijo obvezne udeležbe v zasebnih skladih drugega stebra bolj v smer privatizacije pokojninskih sistemov.

Cilj te naloge je najti razlago za ugotovljene razlike med reformiranima pokojninskima sistemoma na Madžarskem in v Sloveniji. V ta namen sta bili pokojninski reformi v omenjenih državah analizirani na dva načina;

- najprej s pomočjo primerjave izvedenih sprememb posameznih elementov pokojninske politike in
- nato s pomočjo analize procesa oblikovanja nove pokojninske politike v posamezni državi, s posebnih poudarkom na ideologiji in moči najbolj vplivnih političnih akterjev.

Še pred tem sem analizirala širši demografski in ekonomski kontekst procesa oblikovanja pokojninske politike v posamezni državi.

V prvem delu je izvedena analitična primerjava med posameznimi elementi pokojninskih sistemov, ki naj bi pripomogli k:

- ponovni vzpostavitvi primernega razmerja med delovno dobo in obdobjem upokojitve (npr.: zahtevnejši pogoji za pridobitev pravice do pokojnine, okrepljene spodbude za podaljšano udeležbo na trgu dela in spremembe v višini pokojnin)

- zagotovitvi primernih dohodkov upokojencem s porazdelitvijo tveganj med javnimi in privatnimi shemami ter s spodbujanjem udeležbe v privatnih pokojninskih shemah.

Glavna ugotovitev prvega dela naloge je, da so izvedene spremembe znotraj javnih shem v obeh državah usmerjene k podaljševanju delovne dobe, k zmanjšanju višine pokojnin in k tesnejši povezanosti med višino vplačanih prispevkov in višino prejete pokojnine. Večjo razliko je opaziti v zvezi z zasebnimi shemami. Udeležba v teh je v Sloveniji le prostovoljna, medtem ko je na Madžarskem obvezna za vse, ki na novo vstopijo na trg dela.

V drugem delu smo s pomočjo kvalitativne analize pregledali prevladujoče ideologije, ki so vplivale na sprejete politike, ter moč in interese posameznih, nacionalnih in supranacionalnih, političnih akterjev.

Izvedena analiza je pokazala, da so bili prvi predlogi v obeh državah pretežno pod vplivom liberalne ideologije, pri čemer pa je zaskrbljujoča ekonomska situacija na Madžarskem zahtevala bolj radikalne reforme, katerih izvedba je bila zaupana nacionalnemu Ministrstvu za finance. Predlagana trosteberna struktura je imela močno podporo Svetovne banke, ki je Madžarski nudila finančno pomoč in svetovanje strokovnjakov. Pred sprejemom v parlamentu je bil madžarski predlog dopolnjen s predlogu sindikatov, vendar v zelo omejenem obsegu. Omejeno število vpletenih političnih akterjev se kaže v številnih predlogih, do katerih je ob spremembah sestave vlad prihajalo po sprejeti reformi.

Prvi predlog reforme v Sloveniji je bil pripravljen s strani Ministrstva za delo, družino in socialne zadeve. Analiza kaže, da je bil omenjeni predlog v času reforme predmet pogajanj in vplivanja številnih akterjev. Predvsem je bila pomembna vloga socialdemokratske ideologije sindikatov; njihova neformalna možnost veta je povzročila celo spremembe osnovne predlagane strukture novega pokojninskega sistema. Neoliberalni predlogi Svetovne banke so bili zavrnjeni, prav tako tudi njihovo posojilo. Finančna pomoč je bila prejeta s strani Phare programa Evropske Unije, ki je zagotovila tudi pomoč svojih strokovnjakov. Ti so v času reformiranja pokojninskega sistema z izpostavljanjem slabosti obvezne udeležbe v drugem stebru predstavljali pomembno protiutež predlogom Svetovne banke. Do danes, v tedaj sprejetem sistemu, še ni prišlo do večjih sprememb, kar je po vsej verjetnosti ravno posledica aktivnega sodelovanja akterjev različnih ideoloških prepričanj.

MASTERS DEGREE

IN

EUROPEAN SOCIAL POLICY ANALYSIS

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Executive Summary

The last decade in Europe has been characterised by a rapid demographic transition which was a result of rising life expectancy and decreasing fertility rates. This transition has led to ageing of population and consequently represents a heavy financial burden for pension systems. In CEEC financial sustainability has additionally been pressured by changes in the economic environment in terms of transition from centrally-planned to market economy.

Reform of pension policies appears to be an indispensable tool to respond to the above mentioned demographic and economic situation. In this respect, different countries have chosen different policy responses. Two major, ideologically contradictory, options have appeared on national and global agendas; one advocating the maintenance of public social security systems of corporatist conservative nature, even though some adjustments would be needed, the other more in favour of marketisation of pension provision and establishment of a three-tier structure with minimum benefits arising from public schemes and the rest from supplementary second- and third-tier private pension funds. National policies have usually taken the middle way, whereby the Slovenian reform has gone more in the first direction, whereas the Hungarian pension system has gone more towards privatisation with introduction of mandatory participation in second-tier private funds.

The main task of this paper is to find an explanation for the identified differences between the reformed pension systems in Hungary and Slovenia. For this purpose we have examined the reforms of pension policies in two ways; firstly, by comparing the changes implemented with regard to particular pension policy parameters, and secondly, by looking at the policy process

in each country with a special focus on ideology and power of the most influential policy actors. Before that, we analysed a broader demographic and economic context of the policy process.

In the first phase we analytically compared the parameters of the pension systems aimed at:

- re-balancing working and retirement periods, such as tightened qualifying conditions, strengthened incentives for prolonged participation on labour market and the level of benefits, and
- responding to the challenge of balanced resources in retirement, by diversifying the risks between public and private schemes and by introducing incentives to take part in the private ones.

The changes implemented within public schemes in both countries are directed towards prolonging the working period, towards decreasing the level of benefits and towards the closer linkage between contributions and benefits. Systems differ more as far as the introduction of private pension provision is concerned, which is only voluntary in Slovenia, but mandatory for all new entrants in the labour market in Hungary.

The second stage of the analysis qualitatively examines the main ideologies behind the adopted policies and the power and interests of particular, national and supranational, policy actors, respectively. The original proposal in both countries was the product of a prevailingly liberal ideology, whereby the worrying economic situation in Hungary called for more radical changes entrusted to the Ministry of Finance. The proposed three-tier structure was strongly supported by the WB that offered Hungary financial assistance and expertise. Before the adoption in the Parliament, the proposal was compromised with trade unions, but to an only very limited extent. The original proposal in Slovenia was prepared by the Ministry of Labour, Family and Social Affairs. During the reform process, it was negotiated with and influenced by numerous veto actors. In particular, the social-democratic ideology of the trade unions has played a very significant role; their informal veto power even caused changes in the basic proposed structure of the new pension system. Neo-liberal proposals of the WB were refused and so was their loan. Financial assistance was received by the EU's Phare program, though, which also provided some experts. During the reform process they were, as counter-balance to the WB's proposals, exposing the most conspicuous weaknesses of the mandatory second tier.

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ABBREVIATIONS

CAS	–	Country Assistance Strategy
CEE	–	Central and Eastern Europe
CEEC	–	Central and Eastern European Countries
DESUS	–	Pensioner's Democratic Party of Slovenia
EC	–	European Commission
EU	–	European Union
FDI	–	Foreign Direct Investment
GDP	–	Gross Domestic Product
FIDESZ – MPP	–	Alliance of Young Democrats – Hungarian Civic Party
FKgP	–	Independent Smallholders' Party (Hungary)
HUF	–	Hungarian Forint
ILO	–	International Labour Organisation
IMF	–	International Monetary Fund
IRC	–	Interest Reconciliation Council
LDS	–	Liberal Democracy of Slovenia
MDF	–	Hungarian Democratic Forum
MF	–	Ministry of Finance
MHSFA	–	Ministry of Heath, Social and Family Affairs (Hungary)
MISSOC	–	Mutual Information System on Social Protection in the Member States of the EU
MoLFSA	–	Ministry of Labour, Family and Social Affairs (Slovenia)
MPPF	–	Mandatory Private Pension Fund
MSZP	–	Hungarian Socialist Party

MW	–	Ministry of Welfare (Hungary)
OECD	–	Organisation for Economic Co-operation and Development
ONYF	–	National Administration of the Pension Fund
PAYG	–	Pay-As-You-Go
PDIA	–	Pension and Disability Insurance Act
PDII	–	Pension and Disability Insurance Institute
PIF	–	Pension Insurance Fund (Hungary)
SKD	–	Slovenian Christian Democrats
SLS	–	Slovenian People's Party
SSPS	–	Social Security Pension Scheme
SSPTW	–	Social Security Programs throughout the World
SURS	–	Statistical Office of the Republic of Slovenia
SZDSZ	–	Alliance of Free Democrats (Hungary)
UK	–	United Kingdom
USA	–	United States of America
US DSSA	–	US Department of Social Security Administration
WB	–	World Bank
WEF	–	World Economic Forum
WWII	–	Second World War
ZLSD	–	United League of Social Democrats (Slovenia)

1 INTRODUCTION

The characteristic of all developed societies nowadays is that life-cycle is not very closely connected with working-cycle anymore; the period of active participation in labour market is getting relatively short in comparison with average lifetime. The latter has been prolonged significantly in the last decades and thus, in addition to lower fertility rates, causes notable changes in demographic structure of societies.

Discrepancy between the high level of pension rights granted in the 1960s and 1970s on one hand, and new demographic trends together with the decreasing level of economic growth, high unemployment rate and early retirement on the other hand, causes serious problems in a great majority of the states that have introduced old-age pension systems. Since the existing pension systems do not seem to be a match for recent circumstances anymore, new comprehensive social programmes aimed at helping people in their old age are becoming necessary. Within the ongoing reforms all around Europe, governments have to find new solutions to be able to meet these challenges and at the same time to guarantee income security of the retirees.

In CEEC these unfavourable conditions were even worse due to the transition crisis calling for completely new economic and political environment. The common feature of all pension reforms in CEEC was the need to adapt the pre-transition policies to the conditions within the states and at the same time to respond to new trends in global society, such as stronger economic competition, international migrations, common labour and capital markets etc. The circumstances in which the prior system was established changed significantly. In general terms, until 1989 there was a similar system of welfare policy across the whole CEE (Deacon, 2000). In all cases, the reform meant a move away from contribution-based redistributive policies towards a system in which benefits are more individualised and earnings related. However, there are differences in particular elements of the pension system, through which the two main goals, economic sustainability and old age security, are to be attained. In this respect we notice strong controversy between two different approaches, one supporting privatisation and marketisation of pension provision, while the other favours public provision as the main source of old-age security.

This paper seeks to examine these differences by comparing changes in the pension systems that have occurred in Hungary and Slovenia during the last decade as policy reactions to the challenges given. Interestingly enough, despite numerous similarities between the two countries, some elements and outcomes of the reform seem to differ considerably. This paper therefore seeks to find a comparative explanation of the policy choice made by the governments in the two countries.

1.1 Research Questions

The aim of this study is to analyse actual policy measures comparatively and to explain the factors that have most possibly affected such decisions. In this respect, this paper tries to answer the following research questions:

1. *How do particular pension system elements differ between Hungary and Slovenia?*
2. *How can the difference in approach to the reform of pension system be explained? What are the macroeconomic and demographic variables and who are the policy actors that determine the direction of the reform?*

1.2 Structure of the Analysis

This study consists of two parts, whereby the fist part offers theoretical background for better understanding of the following analysis of policy content and policy process. It starts with a definition of old-age insurance and places it, firstly, within the broad scope of social security systems, and secondly, within various social insurance systems.

Since the study represents the analysis of changes that have taken place recently - most of the pension system reforms have been carried out during the last decade, some of them are still under way – Chapter 3 of the paper presents the main challenges, currently posed to the existing form of old-age security. Within this chapter, various policy options, available to governments in order to respond to challenges given, are depicted. This is followed by analysis of current debates on this issue, which indicate the existence of two different ideological approaches, which are applied to a different extent in different countries as shown in the last part of this chapter, examining general trends within the EU, in particular in CEEC.
The presentation of the applied analytical framework and the discussion on most appropriate methodology serves as an introduction to the analytical part. It also includes an introduction of the instruments of data collection and an explanation for the selection of countries under examination.

The paper continues with a comparative analysis of decisive macroeconomic and demographic variables that have caused and partly also determined the changes in pension systems in Hungary and Slovenia.

This is followed by a description of historical development of basic structures of the former and present old-age insurance in both countries. It gives the reader a general framework for better understanding of the analysis that follows. Namely, in the following chapter the differences and similarities between the particular pension system elements of the two countries are analysed.

On the basis of three main challenges posed to old-age security (OECD, 2001) various factors are being considered. The first section analyses reforms aiming at re-balancing work and retirement, whereby I focus on retirement age and other qualifying conditions, on incentives to reduce early retirement, such as the level of replacement rates, existence of the so called "bonus-malus" system, relationship between contributions and benefits and availability of benefits from private schemes before the retirement age. In the second section the response to the challenge of balanced resources in retirement is being explored. Thereby, the way of pooling the risks between public and private pension provisions is examined. Within this framework shifts in public expenditures on pension benefits, deficits of pension funds and different ways of encouraging private occupational and personal provision, in particular replacement rates, ceilings on benefits, and tax-incentives, are being analysed. The policy content analysis concludes with an analytical comparison of changes introduced to the pension system. The latter is also the answer to the first research question.

The second set of research questions is answered by a policy process analysis, which is expected to explain the findings of the policy content analysis. Criteria used to examine possible causes of particular policy choice are identification of relevant national and supranational policy actors together with macroeconomic and demographic indicators analysed earlier. This is concluded with a comparative analysis of the policy process and relevance of the factors influencing its outcomes.

The Conclusion summarises all of the relevant findings with respect to the research questions set.

2 MAIN FEATURES OF PENSION INSURANCE

2.1 Pension Insurance as a Form of Social Security

In Europe social security systems have become very important and complex social institutions and nowadays represent the cornerstone and a significant characteristic of European states. Within the scope of social security numerous provisions and schemes can be found, which more or less differ from one country to another. Nevertheless, they are all aimed at preventing, repairing or compensating contingencies of social risk. Social security, as defined by Berghman (1991), is a state of complete protection against human damage. Namely, there is a risk of damaging human resources, which consequently causes loss of labour income and loss of well-being. The ILO Convention No. 102 that embraces all the major branches of social security classifies social security schemes according to their intent as follows:

- medical care,
- maternity benefits,
- sickness benefits,
- employment injuries,
- invalidity benefits,
- old-age benefits,
- survivors' benefits,
- unemployment benefits and
- family benefits.

A dynamic development of social security protection in Europe can be discerned from the industrial revolution on. It was firstly introduced in Germany within the Bismarck legislation of 1883-1889 (Berghman, 1991). Legitimacy of social security schemes was rapidly spread around Europe. The first schemes were related to professional injuries and occupational diseases and were soon followed by other schemes in the following order: sickness and maternity benefits, old-age, survivors' and invalidity benefits, family allowances and unemployment benefits. Their development was and still is subject to, in Berghman's words (1991), a whole set of structural and cultural factors.

On the basis of the extent of social insurance Novak (2003: 279) distinguishes three main types of social security systems, depending on which target groups formed the core of welfare regimes. The first is the so-called industrial achievement welfare regime, which is based on mutual aid initiatives and social insurance schemes for the employed population with earnings-related benefits and financed through contributions of employers and employees. It is typical in particular for Germany, France and Belgium. Target groups in the residual welfare regimes, such as the British welfare system, are the only vulnerable groups, whose minimum income protection is financed through progressive taxation. The latter is also used in institutional redistributive welfare regimes, typical for Scandinavian countries, where the entire population is entitled to flat-rate benefits.

The first national pension scheme as an important part of social security systems was first introduced in 1907 in Denmark (Novak, 2003: 280) and followed by other European countries in the first half of the twentieth century. Since then, this part of social security has expanded considerably and in most countries nowadays represents the predominant part of social security expenditures. These benefits were and still are either based on the need, which opens eligibility in social assistance schemes, or on recognised social contingencies, which are crucial for insurance based schemes (Berghman, 1991: 14). Since both of the examined countries have a long tradition of applying the Bismarckian industrial achievement approach, this paper mostly focuses on the latter - insurance based old-age security schemes.

2.2 Pension Insurance as Insurance for Old Age

The first statutory social insurance scheme was introduced in Great Britain in order to spread particular risks. Social risks can either arise from sickness, invalidity, retirement, loss of support, unemployment or from inadequate financial resources for bringing up children.

Taking old-age insurance as an example, an incontestable fact is that nobody can avoid getting old and not being able to produce goods anymore. People of working age produce goods in order to make money that enables them a more or less decent living. The question that arises in this context is: what can be done so that people could count on satisfactory level of well-being and on their financial independence in old-age after having left the labour market.

The first simple answer would be that the most rational decision is to save or borrow money by using private institutions in order to have it available after the retirement. However, during the decades of employment and retirement a worker can face radical increases and decreases of income, low and high interest rates, fluctuations in prices, economic growth and recession, unemployment, fluctuations in the value of currency, not to mention armed conflicts and natural disasters. At the same time nobody can predict how many years he or she has to rely on those savings. Imperfect information, numerous unpredicted risks, uncertainties and external shocks are the assumptions which are not taken into account in the simple answer above and are, according to Barr, key factors that imply the need for social insurance (Barr, 2000: 13). The failure of the market to insure against uncertainties called for creation of public and private insurance institutions and opened up possibilities for state intervention. Therefore, as a response to the risk of not being able to produce goods anymore due to old-age, pension insurance systems were introduced. This way, to some extent, the acquired standard of living can be guaranteed to the beneficiaries by using a specific contribution or earnings related formula.

The most common ways of organising pensions are: funding and PAYG schemes. Funding is accumulation of money, which is being invested in financial assets. Collected contributions together with their rates of return can be exchanged for goods after retirement. These schemes can be either defined-contribution (also called individual funded accounts), where level of contributions is fixed and the benefits reflect strictly the amount of accumulated money during the working time, or defined-benefit (usually run on a firm or industry level), where benefits are paid on the basis of employer's wage. In the funded scheme an individual or a generation as a whole gets out of the funded scheme no more than they have put in. On the other hand, in case of PAYG schemes the benefits need not necessarily match the contributions paid, especially when there is a steady population growth or technological progress, both of which cause output growth (Barr, 2000). The claim of contributors to a pension is based on the promise from the state or intergenerational solidarity respectively. The state raises taxes or contributions from working-age population and transfers them to older people. Thus there are no accumulated funds by the state and consequently no effect of interest rates on pension costs.

Pension insurance systems across the world are organised in various fashions, but in every case they are consumption allocation mechanisms, whereby a portion of the goods and services produced by workers are distributed to older people, who have completed their working careers (WEF, 2004: v). The following chapter depicts the ongoing discussions on optimal organisation of retirement programs, especially in the light of population ageing, which currently represents the primary challenge posed to the existent pension systems.

3 RECENT TRENDS IN REFORMING PENSION SYSTEMS

This section starts with an identification of main challenges pension systems are faced with. After that, some possible policy responses and their application in EU countries are presented. This offers a broad context for the following analysis of the specific situation in Hungary and Slovenia.

3.1 Challenges Pension Insurance Systems are Faced with

Over recent decades pension reforms have been implemented in most of the developed and also in many developing countries. The main challenge that needs to be addressed is rapid demographic transition leading to ageing of population. Namely, life expectancy is rising; partly because of lesser succumb to illness when people are young, and partly because people live longer after reaching old age. Accelerated advances in hygiene and health sciences during the twentieth century do not only extend life, but also improve its quality (WEF, 2004). In addition, fertility rates are in decline and the proportion of old-age population outside labour force is growing rapidly.

Reforms of pension system are of the primary importance on the political agenda in virtually all European countries, especially because implications of ageing for not only social but also their fiscal and economic policies are significant. In Europe prevailing public pension systems are expected to become unsustainable and thus represent a threat to fiscal stability, since fewer people will be producing goods and services and at the same time a considerable increase in public expenditures for pensions will be required. Namely, the situation in the 1960s, with low interest rates and high productivity improvement rates, implying rapid wage growth, favoured generous PAYG pension systems. On the demographic side, high fertility rates have also created a favourable environment for such systems. Towards the end of the twentieth century, however, these conditions reversed in virtually all developed countries.

Therefore, the challenge is to devise a new system and a transition path that is acceptable for the old, who have been led to expect more, while also being sustainable and growth-enhancing for the young. In the WB's opinion, alternative policy options should take into account a dual standard: what is good for old population and what is good for the whole economy (1994: 4). Pension programs would therefore become an essential linkage between macroeconomic prosperity and the welfare of all segments of aging societies.

The definition of the point of optimal balance between the well-being of elderly and the economic development varies among different countries, policy options, among numerous scholars and international actors. Although, before analysing different views on the ideal form of pension systems, some important features, specific for CEE after the collapse of communism, need to be pointed out.

Namely, in comparison with the EU countries, the economies of CEE are facing additional challenges arising from the recent fundamental transformation of their societies and economies calling for a completely new economic and political environment. The circumstances in which the prior system was established have changed significantly. Pessimistic demographic projections were thus associated with falling output, high inflation rates at the end of the 1980s and the beginning of the 1990s, large increase in unemployment and consequently, early retirement and reduced financial viability of public pension systems, decrease in GDP per capita and widening income inequality[1]. Recession, which lasted until the mid-nineties, was triggered mainly by changes in the economic system and comprehensive structural adjustments.

On basis of the challenges given, a number of principles and policy options for the reform were identified. The following section examines some of the main alternatives that are being considered around Europe and beyond.

3.2 Major Policy Options

In order to discern current trends in the field of reforming pension systems in Europe a number of criteria can be used to define the type of occurring and expected changes. These criteria at the same time represent the main policy questions that each government has to consider by implementing reforms of pension arrangements. I will only focus here on the changes most commonly discussed in political and academic arenas.

The first is the decision on introduction of the first, the second and the third tier of pension system, whereby the first is a basic old-age protection, the second is a supplementary protection (often organised by employers as occupational pension schemes) and the third is an additional private saving for old age (EC, 2003: 35).

Within the three tiers, the distinction has to be made according to their mandatory or voluntary nature and also between defined benefit and defined contribution plans. While the difference between the latter was already briefly explained in the previous chapter (Chapter 2), some facts regarding the voluntary and mandatory nature of these schemes need to be explained.

[1] The demographic and macroeconomic trends in Hungary in Slovenia are analysed in Chapter 6.

Namely, since voluntary action due to numerous reasons can not reach certain people, and can thus not ensure a decent living for retirees, all industrial countries have mandatory schemes with broad coverage and extensive government management and regulation as the core of their pension systems. Table 1 shows mandatory institutional arrangements of pension insurance schemes that represent the main point of discussion in this paper. We can see that the first-tier benefits have three basic forms. While flat-rate schemes used to characterise the residual and institutional redistributive types of social security systems and earnings-related schemes industrial achievement welfare regime, in recent years this strict differentiation seems to have been disappearing. An important change that has occurred in many countries during the last decade is the introduction of mandatory nature of occupational (second tier) and individual (third tier) retirement schemes, which supplement the first tier schemes with their traditionally mandatory character. In countries where this is not the case, occupational and individual retirement schemes are of a voluntary nature. The shift from the first tier schemes as a single source of income in old-age to multiple schemes is evident across the whole of Europe.

Table 1: *Mandatory institutional arrangements of pension schemes in various countries in 2002*

	Flat-rate	Earnings-related	Means-tested	Occupational retirement schemes	Individual retirement schemes
Estonia	X	X*			X
Poland	X	X			X
Latvia	/	X	X		X
Hungary		X			X
Sweden	/	X	X		X
Denmark		/	X		X
Lithuania	X	X			
Czech Republic	X	X	/		
Norway	X	X			
Slovenia		X			
Germany		X			
Austria		X			
Spain		X			
Greece		X			
Finland	/	X		X	
Slovakia		X	X		
Portugal		X	X		
Belgium		X	X		
Italy		X	X		
France		X	X	X	

Source of data: U.S. Department of Social Security Administration (1995, 2002)
**Red-coloured signs represent the changes that occurred between 1995 and 2002*

Another important distinction needs to be made regarding privately and publicly managed pension funds, which can be financed either on a funded or a PAYG basis. In most of the countries the tradition of publicly managed schemes, financed on the PAYG basis, is retained in the first tier schemes. However, the essential feature of the second and third tier is that they are prevailingly financed on a funded basis and privately managed, although to a particular extent regulated by governments. A private-public mix in pension provisions is emerging in practically all European countries but has developed to different extents (EC, 2003).

There is also a whole set of other elements[2] of the pension system linked to those mentioned above, which are too often neglected (Augustinovich, 2002). Most of them shall be examined in detail in the following chapters where the reforms of pension system in Hungary and Slovenia are compared.

3.3 Current Debates

Opinions concerning optimal features of old-age security differ above all regarding various combinations of the elements above described, which, consequently, cause a different division of roles and responsibilities among individuals, states and market. In line with this, there are advocates of pension privatisation on one, and those supporting the continuation of the public PAYG system as a main provider of old-age security (the so-called called first tier scheme), even though some of its parameters need to be adjusted, on the other side.

In this respect, Holzmann, Mackellar and Rutkowski (in Whiteford, 2004: 9) distinguish between "parametric changes" to social insurance systems as further development of existing schemes (altering retirement age or replacement rates, but leaving the basic structure of the system unchanged), and "paradigmatic changes", more radical shifts to private and advance funded second tiers of mandatory nature.

[2] Among other elements are: the role of the state as a provider and regulator of pension schemes, organisation of pension scheme (a part of state budget or separate insurance budget), financing (contributions or taxes as a source of benefits), calculation and indexation of benefits, level of redistribution and linkage between contributions and benefits etc. Various combinations of these elements in a particular pension scheme show whether they are mainly designed for smoothing of individual income over a life-cycle or whether they are to provide adequate retirement income for all. The former option highlights the insurance aspect while the latter the redistribution aspect.

Current controversy, as described by Fultz (2003), exists between two general models. The first is characterised by pension benefits that result from pooling of risks and contributions across the covered work force, which prevents loss of earnings resulting from various risks. Such schemes are commonly earnings-related, administered by government and financed on a PAYG basis. Under the second model benefits reflect only individual worker's contributions and losses or gains through interest and other financial return. These contributions are commonly managed by a number of private enterprises, which hold and invest worker's contributions and maintain an account of the performance of his or her personal portfolio. In this model the risk is personalised and the management of worker's portfolio is commercialised. The second model is typical for savings within the second and the third tier that, to a different extent, supplement the first tier schemes.

The question that arises on the basis of the models given is, whether pension design should be shifted from the first model to the second and in what manner and to what extent this should be done in order to avoid financial crisis as population ages. Since the third tier of voluntary savings is actually always present and can thus not be considered as a distinguishing feature of a particular pension system, most of the debates on the ongoing reforms are focused on the changes within the first and the second tier.

Regarding the first pillar, the main dilemma is, whether its objective should be strictly limited to poverty relief, designed mainly for those in need, or should it remain the main source of income in old-age and ensure an acquired living standard to pensioners. In the former case, as suggested by the WB, modest benefits from the first tier are to be supplemented by the introduction of mandatory second pillar scheme. Within the second pension policy approach a special form of means-tested social assistance is used as a corrective measure for the poorest in some countries.

Even more questions have arisen in debates about organisation of the second pillar. The main question is, whether the mandatory second pillar schemes should be introduced at all. The libertarian approach that argues for such policies has been adapted in some European countries that agreed upon paradigmatic changes of the existing systems. Once the second pillar schemes are introduced, the opinions differ; above all, regarding its organisation.

Holzmann, Mackellar and Rutkowski (in Whiteford, 2004) offer a number of arguments in favour of radical changes, including the fact that individual accounts have desirable work incentives and that funding can increase a nation's savings and investment under the right fiscal conditions and also accelerate the development of capital market institutions and efficiency in capital allocation, therefore leading to higher growth, which is highly needed in CEE countries in order to catch up with the EU.

On the other hand, those, who are more in favour of parametric changes, point out that although there is some empirical evidence showing that funding contributes to higher savings in the USA, there is no robust evidence of a similar effect elsewhere (Barr, 2000). Although funding is one of the sources of growth, the whole set of conditions has to be fulfilled beforehand; it should lead to higher rate of saving than PAYG, higher saving should be translated to better and larger investment and consequently increase the output. Barr argues that an increase in savings depends on the extent to which any increase in mandatory saving is offset by a reduction in voluntary saving and on the level of reduction of pensions of older generations; if they are reduced, consumption will fall and savings will increase, whereas if not, they will have to be paid from taxes or debt, which will exert downward pressure on saving. He also highlights a complicated link between savings and growth in post-communist countries. Namely, funding only contributes to growth if it increases domestic investment. In transition countries domestic investment may be low yield and high risk, which is in contrast to what pension fund managers look for and may thus put old-age security at risk. This shows that even though through introduction of privately managed funded schemes the risks are diversified because of public and private management, political and market determination of benefits and investment in wide range of securities, it simultaneously causes additional market and investment risks.

Furthermore, while some argue that the key advantage of radical reform is that 'ultimately the taxpayers and economy will be relieved of the largest single item of public spending' (UK Department of Social Security in Barr, 2000: 104), the actual results in some countries show that transition to new schemes in the short to medium run even increases the financial burden on public pension spending and can only be seen as a solution in the long run, when the schemes are mature (Barr, 2000).

3.4 Trends in Reforming the Pension Systems in the EU

The direction of adjustments and changes of pension systems[3] within the EU seem not to correspond to the traditional distinction among regime types regarding the question who is responsible for an individual's welfare in old-age. Although we have to be aware of the fact that various types are only a simplification of reality, we will use Esping-Andersen's typology here, which distinguishes among a liberal, a corporatist and a social-democratic regime, and supplements it, as suggested by Ferrera (1996), with a southern regime. In the liberal regime

[3] It has to be noted, however, that the public and policymakers are very reluctant to changes in the direction towards reducing public benefits, towards privatisation and individualisation, and that makes new pension policies hard to implement. The difficulty of, in Hinrich's words, moving elephants (2000) was evident, for example, in workers' strikes and protests against the pension reform in France in 2003 and in Gerhard Schröder's threat to resign as the Chancellor of the German government unless members of his party support new rules in the fall of 2003 (WEF, 2004: 12).

an individual him/herself takes care for his/her welfare through workings of the market, in the southern regime type welfare is a responsibility of the family, in the corporatist regime it is a responsibility of a social groups or corporation, whereas in the social-democratic regime the state is responsible for an individual's welfare. When looking at changes currently occurring, we can discern that countries as diverse as Germany, Sweden and the UK have all enacted public policies to encourage greater funding of their pension systems and adopted measures to reduce the benefits paid out of by their public pension programs as a response to recent economic and demographic changes (Fourage, 2003).

Also the CEEC have enacted a wide range of adjustments and changes of pension systems. A recent OECD study (Whiteford, 2004: 10) defines two stages of the reform strategies in CEE. The first, in early the 1990s, involved transformation of inherited systems towards social insurance models common in the EU. The second stage, in the late 1990s, addressed escalating costs of social insurance and has thus involved either "parametric" or "paradigmatic" changes to social insurance system. The report also states that all of the countries have reformed some of the parameters of their public PAYG systems, such as retirement age, benefit formulas etc. In addition, some have opted for radical reforms to enhance the role of private, second tier pensions of mandatory nature. These include Hungary (1998), Poland (1999), Latvia (2001) and Estonia (2002). Similar arrangements are still being considered in Slovakia, whereas Czech Republic and Slovenia[4] have declined to adopt them.

It is evident that the current pension reform developments reflect considerably the controversy between the strategy of scaling down public PAYG schemes on behalf of commercially

[4] With the exception of mandatory participation in a private fund for those who perform particularly demanding and hazardous jobs and people who perform work they can no longer perform professionally after a certain age and is financed by their employers.

managed individual savings schemes and the strategy of combining adjustments of the public PAYG system with the development of voluntary supplemental retirement schemes. The following chapters seek to examine these differences by comparing changes that occurred in Hungary and Slovenia during the last decade. Despite numerous similarities between the two countries, interestingly enough, some elements and outcomes of the reform seem to differ considerably. Hungary on one hand is considered to have been opting for paradigmatic approach, whereas the changes in the Slovenian pension system are usually viewed as incremental, parametric changes. Prior to the analysis, however, the analytical tools and methodological approaches used to answer the research questions set are presented.

4 ANALYTICAL FRAMEWORK AND ITS THEORETICAL BACKGROUND

The main goal of this study is to answer some questions regarding the nature of decisions, adopted in a particular policy subsystem[5] and to find explanations for the difference in the decisions made by the governments of the two countries in question. Therefore, the most appropriate analytical tool appears to be policy analysis.

By using policy analysis a researcher seeks to provide description of or prescription for specific decisions on specific policies and can thus not ignore the overall policy process, which is created by interaction of decisions, policy networks, organisations, actors and events. Nor can he avoid the broader environment within which the policy process is located (Hill, 1993: 11).

Different analysts have attempted to develop different conceptual tools and analytical frameworks in order to analyse policies. These have been used to various extents, depending on the nature and objectives of the studies. Inter-relationships can be dealt with by simplifying them into systematic models, which can, however, due to their often ahistoric approach, downgrade the significance of cause and effect and can thus be very unreliable. For example, the simplest and most frequently used model offered by Laswell (in Hill, 1993: 35) assumes that policy emerges via logical path; an issue moves through political system from the point of entry, through decision and implementation, until the final choice is made to proceed with. Furthermore, Easton (in Hill, 1993: 35-37) has supplemented the model by placing a political system into the environment and has taken into account its inputs and policy outcomes. Hill,

[5] An easy definition of a policy subsystem is, according to Papadopoulus, the mix of actors, institutions and resources that operate in a particular policy area (2004).

however, argues that even this is oversimplified, since the environment is not structureless; it is made up of individuals, groups and organisations, with values and interest, operating alone or together over time. Therefore, he suggests a more detailed focus on environmental variables.

Gordon distinguishes two parts of policy analysis, which will be used for the purpose of this study. The first is an analysis of policy content and the second relates to policy determination (Gordon et al in Hill, 1993: 54-55). By using them, this research focuses not only on a policy system by itself but also on influential environmental variables that have determined the form of the policy response.

4.1 Policy Content Analysis

Policy content analysis is defined as a prescription of a particular policy and possibly, how it developed in relation to earlier policies (Gordon et al in Janouškova, 2003: 32). The analysis of the policy content in this research is used for analysing changes of particular elements of pension system in Hungary and Slovenia. It includes comparative description of current pension policies in the two countries and its development in relation to the policy situation before the reform, which is very much in line with Gordon's definition of policy content analysis.

Identification of similarities and differences in policy content will be based on two traditional models of decision making, the rationalist and incrementalist (Papadopoulus, 2004), and at the same time on controversy between parametric and paradigmatic changes, strongly present in recent debates on pension policy reforms[6] ; depending on comprehensiveness of the adopted changes.

4.2 Policy Determination Analysis

Various theories that examine what determines a policy issue have been put forward. Their main question is: how and why do problems or issues enter the agenda. This refers to a specific part of the policy-making process, prior to making decisions on policy content, the so-called agenda setting process. It is at this stage that an issue is socially and politically constructed or ‘emerges’ as a policy issue (Papadopoulos, 2004) and it thus significantly determines the consequently adopted policies. The analysis of policy determinants can be divided in two parts[7]; the first focuses on macroeconomic and demographic variables whereas the second includes analysis of policy actors together with an illustration of shifts in the policy community during the last decade.

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[6] See Chapter 3.3

[7] The two parts are analysed separately; the macroeconomic and demographic situation is examined in the beginning since it does not only determine the policy response but also has to be understood as one of the main challenges facing the retirement schemes.

5 METHODOLOGY

The most distinctive aspect of comparative science is a wide gulf between quantitative and qualitative method (Ragin, 1987: 2) and between variable-oriented and case-oriented analysis. While the classic quantitative method is essentially case-oriented and aimed at deep understanding of social phenomenon, the quantitative method is variable-oriented and tends to produce generalisation about relationships among variables for a large number of cases. Both methods and both ways of analysing have certain advantages and disadvantages.

Quantitative method is usually used to test hypotheses derived from theories. Since it is mainly concerned with discernible relationships among variables on one hand, and theoretical images on the other hand, it is often described as a theory-centred, deductive method. It is applied when researchers try to asses an average impact of a certain cause across a big number of cases. Its intention is to make generalisations about a particular social phenomenon, whereby it usually fails to take into account relevant historical, social, cultural, economic and political factors. Due to the use of large number of cases generalisations, it can be quite reliable. At the same time, limited consideration of contextual information can make the findings less valid.

Qualitative method, nevertheless, looks at cases as wholes and as configurations of variables. It tends to be historically interpretive in order to account for specific historical outcomes or sets of comparable outcomes or processes chosen for study because of their significance for current institutional arrangements (Ragin, 1987). Units of analysis are examined in their broad context. In contrast to quantitative methods, qualitative methods seek to explain and interpret characteristics of historically defined macrosocial units as a complex social phenomenon. It offers a reader a full understanding of a small number of examined cases; however, generalisations on the findings are not reliable.

5.1 Synthesis of Case Study and Comparative Research

Due to a small number of cases within this analysis, which have to be studied as complex entities, the conduction of a case-oriented comparative analysis between both countries seems to be the most appropriate methodological approach. For purpose of our study, a distinctive, prevailingly case-oriented research strategy, the so-called case study, will be applied. It can be based on any mix of quantitative and qualitative evidence. The essence of a case study is that it tries to illuminate a decision or a set of decisions: why they were taken, how they were implemented, and with what result (Schramm in Yin, 2003: 12). Its utilisation has a distinct advantage in a situation when 'how' or 'why' research question is being asked about a contemporary set of events, over which an investigator has little or no control and when the boundaries between phenomenon and context are not clearly evident (Yin, 2003). All these characteristics imply usefulness of a case-study for the examination of the process of changing the pension system in two countries and for finding an explanation of reasons behind the adopted policies. In accordance with numerous critics on explicit use of either qualitative or quantitative method this option offers a strategy that can apply both methods, depending on aims of the study, and at the same time enables in-depth examination of the cases.

The comparison of macroeconomic and demographic indicators before and during the reform process is based on quantitative methods, mainly in a form of trend analysis. Namely, trends are examined in order to discover the developments since the early 1990s concerning old-age and system dependency ratios, the level of GDP, inflation rates, budgetary balance, level of FDI and the extent of foreign indebtedness.

Policy content analysis in this study is a typical case of combining both methodological approaches; qualitative method is used by examining the historical background of the reforms and by comparing particular parameters of the pension system, such as qualifying conditions, incentives to prolong participation in the labour market and to take part in private funds, calculation and indexation of pensions, before and after the reform. Trend analysis, as a form of a quantitative method, is again applied when looking at the developments in the level of replacement rates and pension expenditures.

Policy process analysis has been carried out exclusively through the use of qualitative method, mainly in the form of textual analysis (see Travers, 2001). Among the examined texts were mainly the existent secondary literature, web pages, documents and publications of political parties and international organisations. In addition, contacts with the representatives of the Ministries, trade unions and international organisations have been established in the form of interviews and written correspondence.

The applied methodology is thus very much in line with Mill's study (1993), where he suggests that a major task facing policy studies might be a synthesis of comparative theory and case study. In this way, analysis of cases in isolation can be avoided due to use of comparative research, while case study approach enables us to find a relevant historical explanation.

5.2 Instruments of Data Collection

In order to carry out the comparison of the development of the pension system in each country, I will rely on data already present, collected by different international organisations and institutes. These data will be supplemented with using national statistical databases and provisions included in the current and former pension legislation of Hungary and Slovenia. In this context, it has to be noted that data coming from different sources, ones from national and others from international databases, might not be completely comparable[8]. In addition, some contacts with experts in the field will be established.

National and international statistical databases will also be used while explaining demographic and economic situation as determinants of policy content. In the case of national and supranational actors, relevant working papers, strategic documents, seminar conclusions, newspaper articles and other documents will be collected from different kinds of textual and multi-media products. In addition to the sources already mentioned, I will also examine the existing secondary literature on the issues in question and establish personal communication with the representatives of the relevant policy actors.

5.3 Selection of Countries

This paper is based on comparison of changes that have occurred during the last decade in Hungary and Slovenia. Namely, both countries belong to the same region, have a similar historical background in terms of prevailing political ideology and basically the same pre-reform situation in the field of pension policy. In addition, recent developments had to respond

[8] This is particularly problematic when variables examined are calculated from numerous other variables, for example, as in the case of pension expenditures.

to the common challenges posed to both countries arising from the transition to market economy and, soon after that, from the EU accession process. Do Hungary and Slovenia, on the basis of given similarities, follow similar developments in the field of pension policy, or do they, in spite of that, follow different patterns of adjusting and changing the systems? This research not only seeks to analyse the similarities and differences in the development, but also tries to explain them by using various contextual variables that potentially influenced the reform process.

6 DEMOGRAPHIC AND MACROECONOMIC SITUATION IN HUNGARY AND SLOVENIA

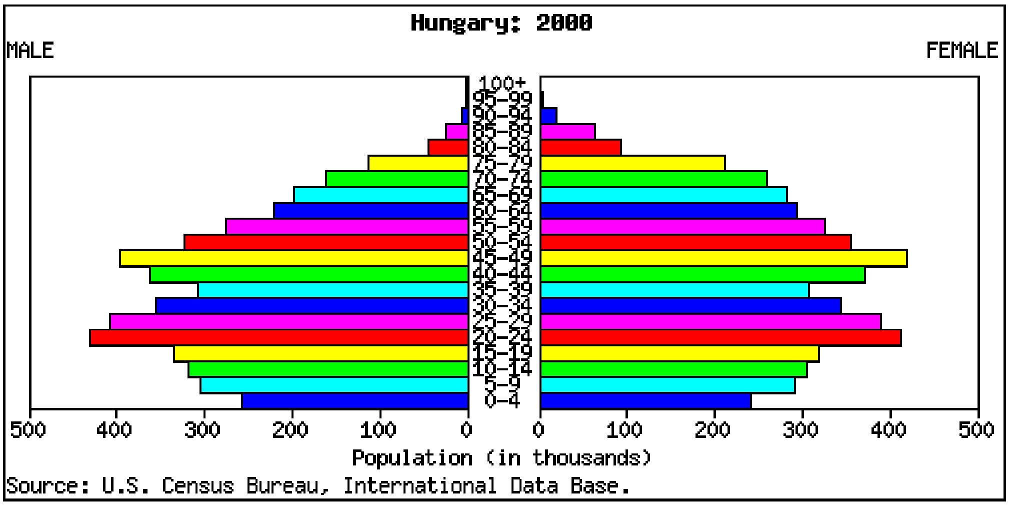
This section, being the first analytical chapter, includes analysis of the main factors behind the need to reform pension systems. Thereby, the paper is focused on the perspectives emphasising economic and demographic determinism. Our comparison starts with the demographic situation and is followed by the examination of the macroeconomic context before and during the reform period. The findings of this chapter will be used by explaining different outcomes of the reforms between Hungary and Slovenia. Many authors (Wilensky, Cutright, Aaron in Papadopoulus, 2004) argue that the structure of nation's economy determines the types of public policies its government would adopt. Demography, on the other hand, has become an important issue recently and is, as a policy determinant, strongly involved in current debates on social policy.

6.1 Demographic Situation

Recent demographic trends and their close linkage to sustainability of pension systems have become a serious concern in academic and political circles due to the occurring phenomenon called population ageing. It is basically a result of a two-dimensional demographic transformation: on one hand, mortality, on overall, declines, resulting in longer life expectancy; on the other hand, decline in fertility results in decreasing proportion of children and young adults (Kalache in Sen, 1994). The proportion of life time that people spend in retirement to the time of participating in labour market has changed considerably. This consequently generates large pressures on public expenditures[9], and also provokes serious labour shortages and thus slower economic growth.

Nowadays, population age structure in the developed and also in many developing countries is moving towards the regressive model, which is characterised by a low basement of young cohorts and a high proportion of population of higher age[10]. The predicted moves in population age structures in Hungary and Slovenia are illustrated with the figures below. As evident, the number of people of higher age is increasing in both countries although the population ageing process is stronger in Slovenia.

Figure 1: *Population Age Structure in Hungary, 2000*



[9] In Hungary and Slovenia the deficit that arises within the public pension system has to be financed from the budget.
[10] There are three demographical models of population according to its age structure: progressive – young society, stationary – balanced society, and regressive – old society (Sundbärg in Janouškova, 2003).

Figure 2: *Population Age Structure in Hungary, prediction for 2050*

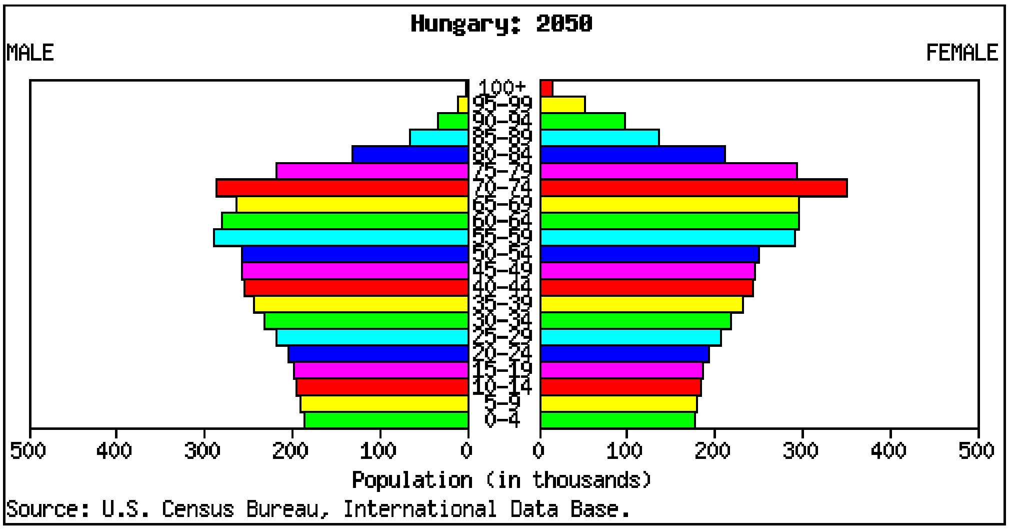


Figure 3: *Population Age Structure in Slovenia, 2000*

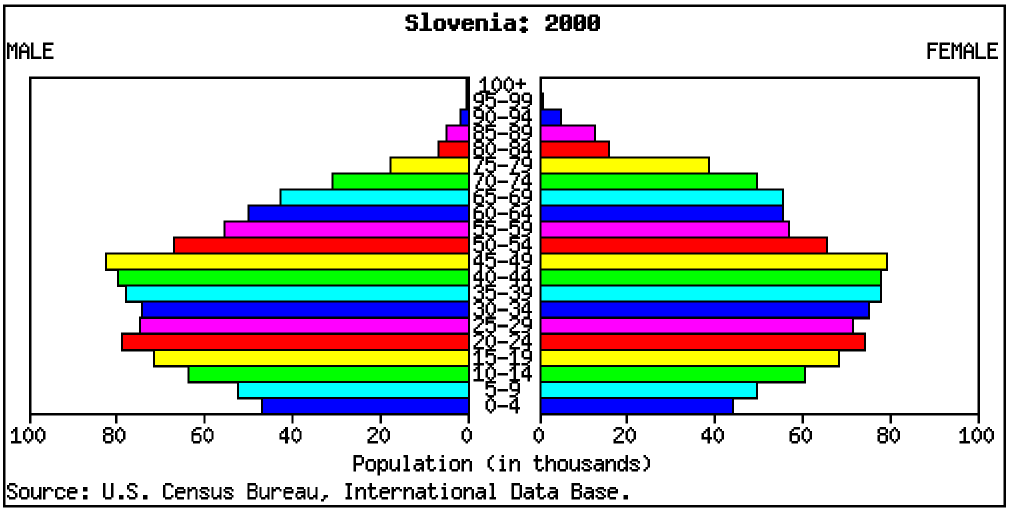
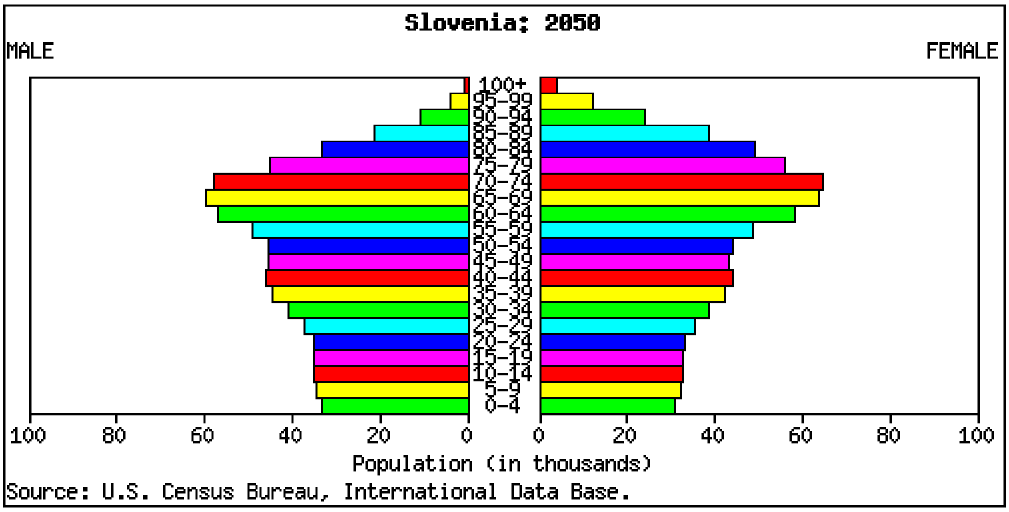
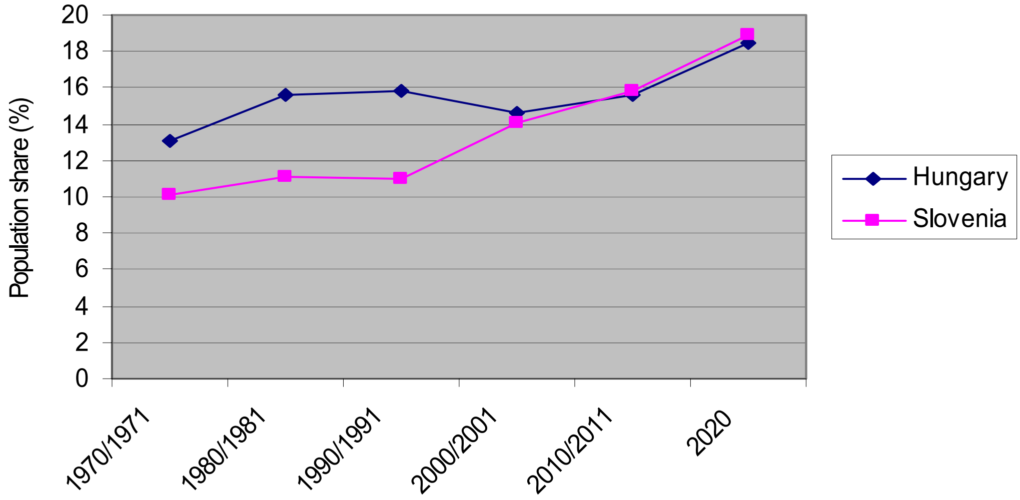


Figure 4: *Population Age Structure in Slovenia, prediction for 2050*



According to Stanovnik (2002b: 29) a worsening demographic structure of Slovene population was the main reason for the government's decision for more fundamental changes in the early 1990s. As indicated in Figures 5 and 6 the share of elderly in the whole population kept increasing and simultaneously, the old-age dependency ratio has been continuously deteriorating for some forty years, and is expected to worsen in the period to 2020.

Figure 5: *Population structure – share of people older than 65 – with projections up to 2020*



Source: SURS, CSO Yearbooks and Hablicsek v Augussztinovics (2002: 27)

The ageing of population in Hungary was relatively slower and the situation in the final decade of the 20th century even improved. From Figure 5 we can infer that in Hungary it is not yet the demography that is putting pension schemes under pressure. It still has a comparatively favourable age structure, with delayed and less rapid population ageing as well as with low life expectancy rates. Namely, the effects of low fertility are amplified by poor mortality figures, which are expected to remain significantly lower than the OECD-average even in the long term (Gal and others, 2003: 8)[11]. Nevertheless, the old-age dependency ratio is projected to increase, but will, if viewed in European context, remain relatively moderate (Augusztinovics, 2002: 28).

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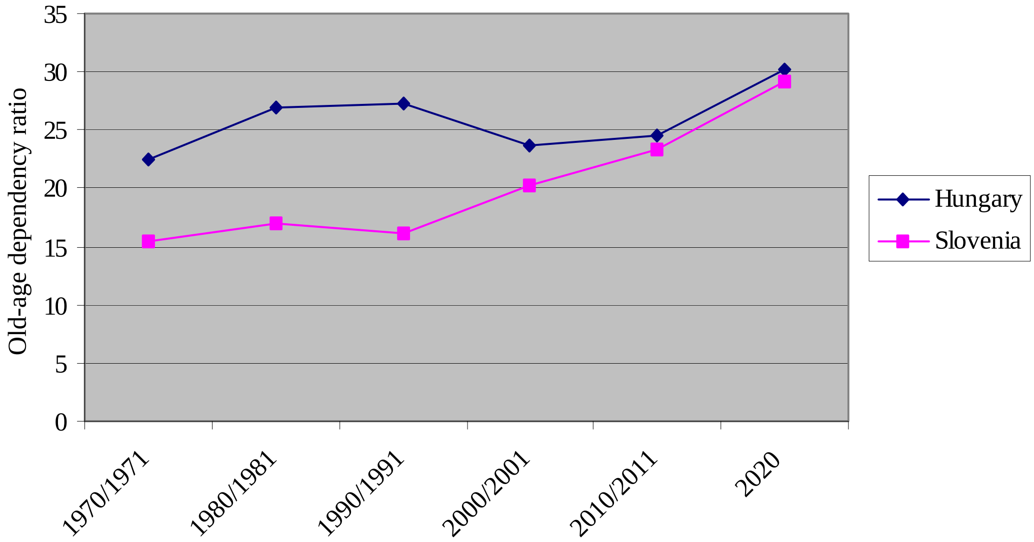
[11] Life expectancy at birth was 70,9 years on average in the period of 1995-2000, only exceeding Turkey's among the OECD countries (Gal et al, 2003: 8).

Figure 6: *Old age dependency ratio (population aged 65 or over per population aged 15–64)*



Source: Statistical Yearbooks of Slovenia, CSO Yearbooks and Hablicsek v Augusztinovics (2002: 27)

This is also confirmed in a study of the EC (2003), which, on the other hand, shows a significant difference between the favourable old-age dependency ratio and less favourable pensioner or system dependency ratio[12]. Namely, for the pensioner ratio, which is much more problematic, the decisive element is effective average retirement age and not statutory retirement age.

In CEEC the effective average retirement age is much lower than the statutory due to early retirement schemes and other pathways to earlier retirement, which have been examined in the previous chapters. Although demography is in general not a crucial problem for all the pension schemes today, ageing of population will be a challenge for nearly all CEEC in the future.

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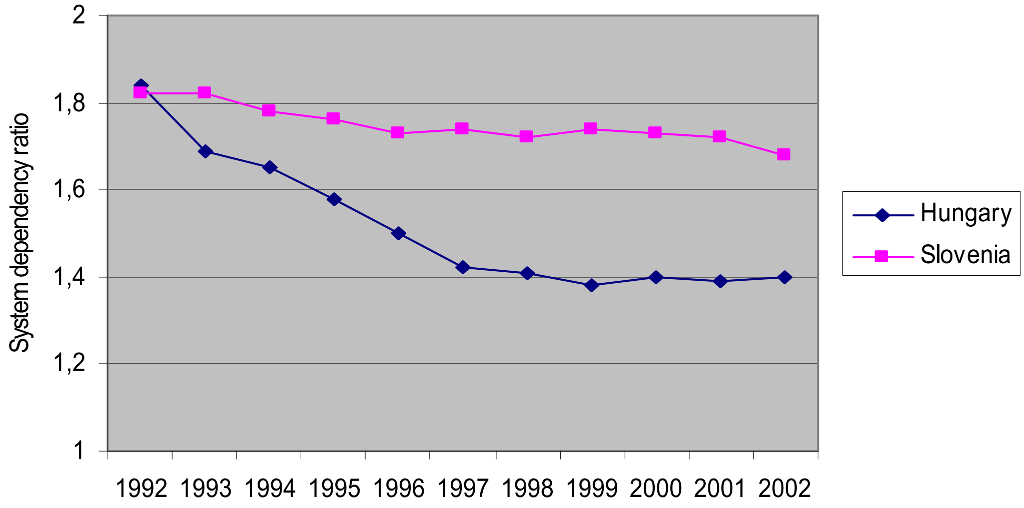
[12] Pension system dependency ratio is estimated as the ratio of contributors to pensioners (EC, 2003).

Figure 7: *System dependency ratio (1992-2002)*



Source: PDII (Slovenia), ONYF (Hungary)

Looking at the system dependency ratio, we can see that in Slovenia it has not changed as much as in Hungary since 1992. Falling number of contributors in the early 90s was among others the consequence of high unemployment rates as a result of implemented structural adjustments (Table 2). In Hungary, on the other hand, the system dependency ratio continued to decrease considerably throughout the 90s and is thus showing an urgent need to act in response to the consequences of structural adjustments also in the field of pension policy. Despite falling number of contributors, the number of recipients of pension benefits kept increasing simultaneously. The unfavourable ratio between contributions and benefits consequently caused increasing public expenditures for pensions in both countries (Figure 11).

6.2 Macroeconomic Background

A pension system can only be analysed completely when set in its macroeconomic context (Barr, 2000). Therefore, the aim of this section is to look at the variables that indicate the conditions under which the pension reforms were carried out and is thus very likely that they had a significant impact on direction of the reforms. In line with this, we will analyse the level of GDP as the main indicator of economic situation, inflation rate, unemployment rate and balance of budgets as important elements of sustainability of the pension systems, and finally the reliance on foreign direct investment and foreign indebtedness as not only economic indicators, but also as indicators of the ideology behind the governmental answers regarding the pension policy.

Starting with GDP per capita, it is evident from Figure 8 that GDP in Slovenia has been much higher than in Hungary throughout the 1990s[13]. Except for the period from 1990 to 1992, when the negative trend can be discerned in Slovenia, GDP has been continuously increasing in both countries. In 2002 GDP per capita (PPS) amounted to 13420 in Hungary and 17710 in Slovenia, indicating that general economic situation in Slovenia is still relatively better.

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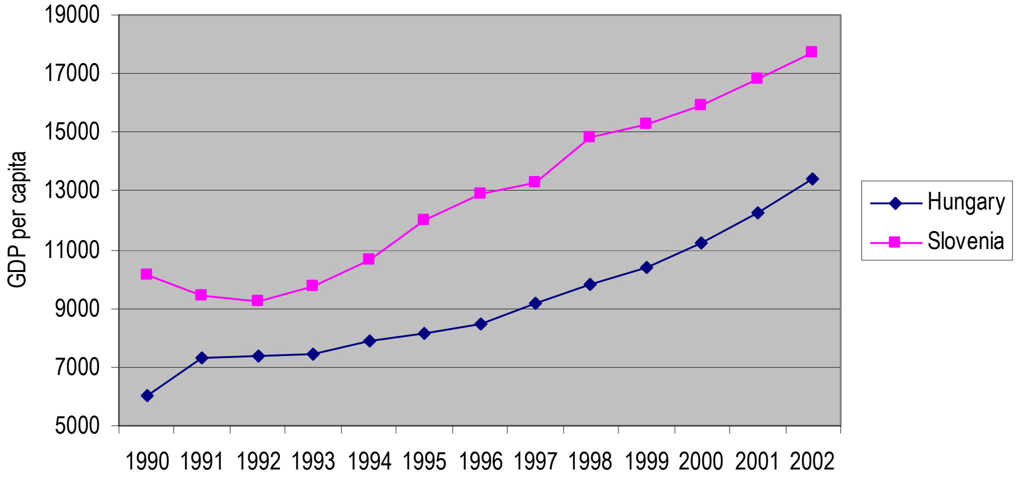
[13] According to GDP per capita, a very unfavourable situation in Hungary in 1990 was comparable to the current economic situation in Bulgaria, whereas Slovenia could then be compared to the current situation in Estonia.

Figure 8: *Per capita GDP (PPS)*



Source: Hungarian Central Statistical Office

Table 2: *Unemployment rates (1992 – 2001)*

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Hungary	9,8	11.9	10,7	10,2	9,9	8,7	7,8	7,0	6.4	5,7
Slovenia		9,1	9,0	7,4	7,3	7,1	7,7	7,4	7,2	5,9

Source: LABORSTA

The early 1990s in all CEEC were characterised by high unemployment rate of structural nature[14], caused mainly by closing down ineffective production and withdrawing subsidies to companies. Both countries have adopted measures to meet the challenge of high unemployment, among others, already described generous possibilities of early retirement. Gradually they have managed to decrease the unemployment rate, but not necessarily also the costs of social security system. Especially in Hungary, an important feature of their labour market is the divergence of unemployment and inactivity, which normally operate more or less

[14] Restructuring industry removed around a net 30 percent of jobs (Gal et al, 2003:9).

in parallel. In case of Hungary, the falling unemployment rate is combined with one of the highest inactivity rates (Gal et al, 2003). In Slovenia, the situation on the labour market was somewhat better during the 1990s.

Inflation is another important factor in the area of social protection schemes since the real value of cash benefits declines significantly in times of high inflation rates, as was the case in all CEEC in the late 1980s and early 1990s. Slovenia's starting point in the beginning of the 90s was extremely unfavourable, but improved considerably in the mid 90s (Table 3). Hungary, despite better starting position in the early 1990s, still suffered from comparatively high inflation rates in the mid 90s. Since the purchasing power of the pension benefits continued to deteriorate rapidly the pension issue in Hungary became pressing (Grimmeisen, 2003: 22).

Table 3: *Inflation rate (1992 – 2001)*

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Hungary	23	22.5	18.8	28.2	23.5	18.5	14.2	10	10	9,2
Slovenia	207.3	32.3	21.0	13.5	9.9	8.3	7.9	6.1	8,9	8,5

Sources: European Parliament (1999), EC (2003)

Besides the negative impact of the inflation development, the problems of the Hungarian pension system were also accelerated by severe budget imbalances as indicated in the table below. Slovenian budgetary balance remained relatively constant during the 90s. Since both governments were obliged to make up deficits that arose within pension systems because of the unfavourable ratio between contributions and benefits, the budgetary balance represents an important factor for the policy strategy.

Table 4: *General Government budgetary balance as a percentage of GDP (1993 – 1999)*

	1993	1994	1995	1996	1997	1998	1999
Hungary	-7.8	-8.4	-6.8	-3.1	-4.8	-4.9	-4.6
Slovenia		+0.2	0	+0.3	-1.1	-1.0	-1.0

Source: European Parliament (1999)

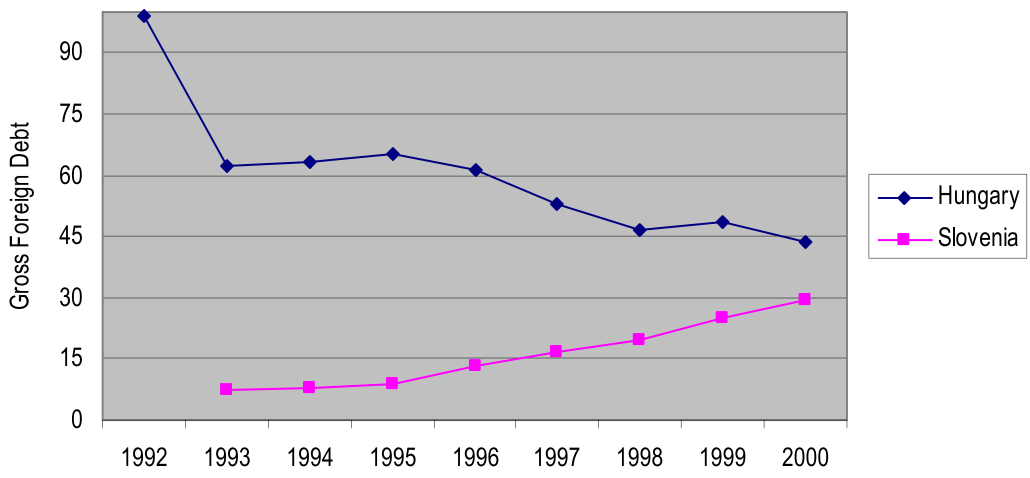
Table 5: *Reliance on Foreign Direct Investment*

	1991	1992	1993	1994	1995	1996	1997
Hungary	5,55	9,71	16,01	18,87	29,40	33,98	38,26
Slovenia	0,00	0,88	1,77	2,36	3,27	4,19	5,67

Source: WB (2004)

From the table above we can see that Hungarian government in comparison to Slovenian relied heavily on FDI. It therefore feared that non-reform of the pension system would cause an even deeper macroeconomic and fiscal crisis and thus lead to diminished confidence of the international financial community (Gedeon in Grimmeisen, 2003: 23). In addition, fiscal deficits emerging during the last decade in Hungary have contributed to extremely high government foreign indebtedness (see Figure 9), especially in the early 1990s. That made the country very vulnerable to the policies imposed from the international community, in particular to the international financial organisations, such as the WB and the IMF.

Figure 9: *Gross Foreign Debt (percentage of GDP)*



Source: Eurostat (Newcronos)

6.3 Concluding Remarks

A critical demographic situation in Slovenia, together with its projected consequences for sustainability of the pension system in the near future, was a decisive factor for the government's decision for pension reform. In Hungary, on the other hand, it was not yet demography that was pressuring the pension systems. Namely, the old-age dependency ratio has even improved in the last decade. However, their system dependency ratio is not as favourable; Hungarian pension system was burdened by increasing expenditures, which were aimed at solving the consequences of structural adjustments, in particular very high inactivity rates. Severe consequences of the transition to market economy in Hungary were also evident in high inflation and high budgetary deficit that lasted throughout the 1990s. These were partly solved by strong reliance on FDI and by high foreign indebtedness, but still called for other measures. Slovenia, on the other hand, has managed to face the new economic situation without such severe and long-lasting consequences. To a large extent the situation was stabilised by the mid 1990s, with a negligible reliance on foreign investments and loans.

7 POLICY CONTENT ANALYSIS

Having examined the differences in macroeconomic and demographic situation before and during the pension reform process in a particular country, the paper continues with the analysis of the policy responses to these specific circumstances. In this way, the differences between the two countries, in terms of changes in particular elements of the pension system can be discerned. In this respect my hypothesis is as follows:

Due to specific macroeconomic and demographic situation and due to different actors that have influenced the reform process in each country, policy responses in terms of introduced changes of the pension system elements between Hungary and Slovenia differ to a certain extent.

For better understanding of the changes implemented this section starts with a historical background of old-age insurance in Hungary and Slovenia.

7.1 Development and Structure of Old-age Insurance in Slovenia and Hungary

Hungary and Slovenia both have a long tradition of social insurance, which is not surprising, since both were a part of the Austro-Hungarian Empire, where the origins of social insurance can be traced back to 1854 (Stanovnik, 2002b: 19). Having been a part of the Austro-Hungarian Empire, Hungary and Slovenia both built industrial achievement welfare regimes. In the socialist regime, however, the previously fragmented welfare regimes on the basis of occupations were unified for all categories of insured persons, with a later inclusion of farmers on basis of the universalistic principle (Novak, 2003: 294).

In Hungary a unified, unfunded PAYG system for wage and salary workers was introduced around 1950, after all Hungarian funded schemes collapsed during and after the WWII. The coverage gradually extended from about 50% coverage in 1950s to almost 100% by the 1970s. Also, the range of benefits was extended to old-age, survivors' and disability benefits. Consequently, the proportion of aggregate pension expenditure rose from 3,5% in 1970 to 6,9% in 1980 and to 8.8% of GDP in 1990 (Augusztinovics, 2002: 29). Therefore, some significant changes were made during the gradualist reform process in the early 1990s, followed by a more radical reform package in 1997 that split the unified mandatory system into two schemes.

Similar historical development can be traced In Slovenia – within the Kingdom of Yugoslavia – where a general scheme for old-age insurance was firstly introduced in 1937. Between the two world wars, insurance based on mutuality and solidarity, i.e. forms of assistance provided at the levels of fraternal funds, brotherhoods and support societies, was developing faster than 'state' insurance (Belopavlovič, 2002). After the WWII, old-age security system in Yugoslavia underwent numerous fundamental changes: new legislation provided a uniform classification system for all groups of people and workers from all industrial branches, assets of the former pension funds were nationalised and the system was transformed into PAYG system. In the former Republic of Yugoslavia the Federal Insurance Institute was formed in 1952 and contribution financing became the main principle of its social security system. The most important federal legal Act on Pension and Disability Insurance was adopted in 1982 and soon complemented by corresponding laws at the republican level. Generosity of the pension system under this act, as well as rapidly deteriorating economic conditions, resulted in a large increase in number of pensioners and soaring pension expenditures (Stanovnik, 2002b: 23) and consequently in numerous changes carried out throughout the 1990s, after Slovene independence.

After the first legislated changes in 1992 a more thorough reform of the pension and disability insurance system in Slovenia commenced in 1996 when the Government prepared and adopted the Starting Points for the Reform of the Pension and Disability Insurance System, and continued in 1997 with the White Paper which explained the reasons behind the changes and their purpose and outlined the most important solutions (Belopavlovič, 2002).

During the 1990s both countries adjusted the parameters of the existent mandatory PAYG system based on intergenerational solidarity (first tier) in order to decrease financial burden pension benefits were posing to the state. PAYG systems are still run by the state, which guarantees benefits to the contributors. The state regulates the system by determining the conditions for retirement, ways of adjusting benefits, the level of benefits and contributions.

In Hungary, successfully introduced private arrangements consist of the so-called second and third tier; a mandatory private scheme (second tier) is compulsory for those entering the labour market for the first time and optional for others[15]. Those, who have decided for new pension schemes, redirect a portion of their pension contributions to the commercially managed savings accounts. Providers of the mandatory supplementary schemes are some of the Mutual Pension Funds, established in 1994. Third-tier voluntary private schemes are also organized within these funds and provide an additional source of income to the insured persons.

In Slovenia a new form of pension insurance was also introduced in the new PDIA in addition to the public scheme restructuring and introduction of income-tested state pension. The act provides for two types of supplementary insurance. Voluntary insurance (third tier) is very

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[15] In the transition period it is only optional for those, younger than 47 years (MHSFA, 2004).

similar to that in Hungary, whereas supplementary insurance (second tier) is mandatory only for those who perform particularly demanding and hazardous jobs and people who perform work they can no longer perform professionally after a certain age and is financed by their employers.

Ever since the changes were legislated[16], individuals without other sources of income in Slovenia and Hungary have been entitled to income-tested minimum pension, which is guaranteed by the state, has a nature of social assistance and does not arise from the insurance schemes.

7.2 Comparative Analysis of Pension System Reforms in Slovenia and Hungary

This chapter presents changes of particular elements within the above-described development of the pension system. By looking at the changes implemented over the last decade, the way of acting in response to two major challenges facing retirement income systems, outlined by the OECD (2001), will be examined;

- growing imbalance of time spent in work and in retirement, resulting from demographic change and possibilities for early retirement, and
- the changing mix of different forms of retirement income provision caused by scaling down public pension schemes to reduce fiscal pressures.

[16] New legislation was adopted in 1997 in Hungary and in 1999 in Slovenia and enforced in 1998 and 2000, respectively.

7.2.1 Reforms to re-balance work and retirement

The first segment of changes has arisen from specific demographic structure and its pessimistic projections for the future, decreasing dependency ratios between active and passive labour force, low average retirement age and easy access to generous public retirement benefits. Among the most important measures to meet these challenges are stricter qualifying conditions, reduced incentives and tightened access to early retirement, closer linkage between contributions and benefits and lower level of replacement rates.

7.2.1.1 Qualifying conditions

In comparing the qualifying conditions I have tried to quantify the following indicators: required age and the number of years of contributions for retirement without suffering reduction in benefits. At the same time the minimum age and minimum number of years of contributions required to obtain reduced benefits will be examined.

Table 6: *Eligibility criteria for retirement before and after the implementation of the pension reform*

	Hungary	Slovenia
BEFORE THE REFORM		
Age	60 (M), 56 (F)	60 (M), 55 (F)
Contributions	20 years	20 years
Minimum age	n.a.	58 (M), 53 (F)
Minimum contributions	n.a.	15 years → 65(M), 61 (F)
AFTER THE REFORM		
Age	62 (M+F)	63 (M), 61 (F)
Contributions	20 years	20 years
Minimum age	60 (M), 57(F) ← 38 years	58 (M–40 years, F–38 years)
Minimum contributions	15 years → 62 (M+F)	15 years → 65(M), 63 (F)

Source: SSPTW, PDIA (1999), EC (2003)

Retirement age

Not surprisingly, in order to reduce high costs of pension system, both countries tend to keep their work force employed as long as possible. According to simulations carried out by OECD (2001) a relatively small increases in retirement age can have large payoffs from the fiscal point of view. In case of Hungary and Slovenia one can notice two general trends; firstly, the retirement age has increased significantly and secondly, the differences in retirement age between men and women are disappearing. However, there are important differences between both states. Hungary approached this issue earlier[17] and also more radically. According to the new Act the retirement age for women has to be gradually increased to 62 and placed on the same level with the required age for men already by 2009. Slovenian legislation foresaw increase in retirement age in 2000 PDIA. Although the differences between genders were decreased, it has kept the right for women to retire earlier despite the initial

[17] In Hungary already the 1992 Act foresaw equalisation of the retirement age between genders.

proposals to equalise the retirement age. The raise in retirement age should be implemented gradually to 63 years for men by 2008 and to 61 years for women by only 2017.

If a person has a contribution period long enough, he/she can obtain an old-age pension earlier. This pension is reduced and remains such throughout the whole retirement period[18]. Required age is currently 60 years for males and 57 for females in Hungary (EC, 2004: 34) and 58 years for both genders in Slovenia. This should, however, coincide with 40/38 (M/F) years of insurance period in Slovenia and 38 years in Hungary. Interestingly enough, the difference between genders has remained in both countries.

Period of paying contributions

Since pension benefits in both countries are based on work merit (Palme, 1990), another criteria that has to be fulfilled is the number of years of paying the contributions. The reforms of the 1990s have not brought any changes in this respect. The length of contribution periods required for those who retire with full pension has remained 20 years in both countries. However, this relatively short period does not cause any changes in the retirement age, as both criteria have to be fulfilled.

7.2..1.2 Reducing early retirement incentives in other schemes

Early retirement is a phenomenon, which should, in CEEC, not be overlooked; it was a very common and important feature of the pension systems in both countries in the beginning of

[18] This is known as the malus system.

the 1990s. It caused some temporary deductions in benefits that were abolished when age criteria were fulfilled[19].

Lavish retirement schemes helped to bridge – at least in social terms – massive decline in economic activity rates in the early transition years (from 5 to 3,5 million people in Hungary in 1989 – 1995) (Czaba, 2000). In addition to early retirement pension there were also other alternatives and relatively easy accessible pathways to withdraw from the labour market. Among those that have also stimulated early retirement we can place disability benefits[20], unemployment-related benefits, generous private occupational pension schemes in combination with severance payments of firms. These schemes have offered relatively high replacement rates and have at the same time imposed an implicit tax on continuation of work.

Tightened access to early retirement

In order to delay retirement, a number of countries, including Hungary and Slovenia, have started to restrict access to early retirement pensions, disability benefits and/or unemployment-related schemes and/or making less generous and strengthening job-search requirements for older unemployed workers. As far as the changes within the pension system are concerned, the new Slovene legislation abolished the possibility of early retirement completely, while in Hungary it remained possible in order to reduce unemployment (pre-retirement). However, according to the National Administration of the Pension Fund (ONYF), the number of those who retire early dropped from 17127 to 3186 between 1993 and 2002. Pre-retirement pension is now based on a tripartite agreement between the representatives of

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[19] In contrast with the newly introduced malus system, deductions because of early retirement were only temporary, whereas they remain reduced throughout the whole retirement period in case of malus system.

[20] In Hungary since 1994 the number of newly entitled invalidity pensions has always exceeded the number of new old-age pensioners (Marin and others, 2001).

employers, workers and the ONYF and can be paid 5 years before the pensionable age (EC, 2002). The costs of the pension paid during this period are reimbursed by the employer.

Bonus – malus system

The main novelty introduced to motivate people to stay in active labour force longer is a so called bonus–malus system. It means that the longer a person works past the full retirement age the higher the pension will be, and people who only meet the minimum age requirement and not also the full retirement age will get a lower pension (Belopavlovič, 2002). This approach represents not only a more flexible retirement, but most importantly, reduces incentives to retire early by strengthening the connection between the paid contributions and received benefits.

In Slovenia an insured person who continues to work and pay contributions after achieving the full pension qualifying period - 40 years (m) and 38 years (w) - acquires an increase of pension that amounts to 0,3 per cent for each month in the first year after the conditions are fulfilled, 0,2 in the second year, and O,1 per cent per month in the third year (Article 53 of the PDIA). In contrast, before the reform, the total accrual rate for the entire insurance period had an upper limit of 85 per cent. For insured persons who continued to work and pay contributions after achieving the pension qualifying period - 40 years (m) and 35 years (w) - the total accumulated accrual rate did not increase but remained at 85 per cent (Hanžek et al, 1999).

Similar approach has been adopted in Hungary; after accruing at least 38 years of service and reaching the age of 62, it is possible to continue working without claiming a pension and to receive an increased pension. The increase is equal to 0,3 per cent of the old-age pension after each period of 30 days (3,6 per cent of the old-age pension per year) of additional service and can exceed average monthly earnings upon which the old-age pension is calculated (EC, 2002). In contrast with Slovenia, in Hungary there is no provision on the maximum age until when the bonuses can be acquired.

Partial pension

As an additional motivation to stay longer in labour force in Slovenia, the concept of partial pension - an old-age pension payable to an employed person who continued or re-entered part-time employment after retirement, in proportion to reduction of full working hours - has been introduced (Article 8 of the PDIA) Its successfulness is not yet known and will depend on labour market conditions and preference of employers and employees[21]. There is no possibility of such pension in Hungary (MHSFA, 2004)

Availability of benefits from private schemes

The last incentive to remain in labour force longer, which will be discussed in the following chapter, is unavailability of benefits from private schemes before the retirement age. In this respect in Hungary the raise of statutory retirement age will simultaneously affect second tier (Marin et al, 2001). Also in Slovenia a person, included in a supplementary scheme, is entitled to benefits only after the retirement according to the rules regulating PAYG scheme.

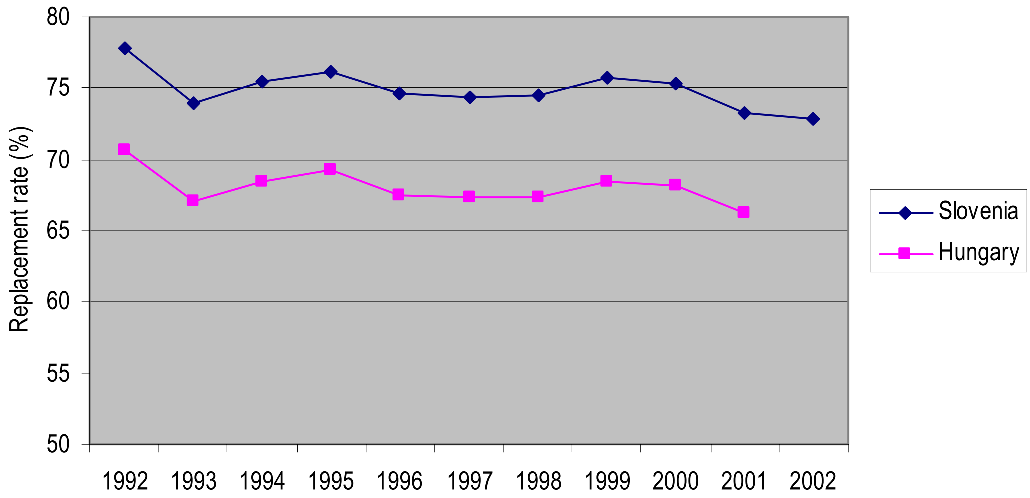
[21] According to the estimations of the Pension and Disability Insurance Institute, in 2003 around 30 men and 50 women decided for partial retirement (PDII, 2004).

7.2.1.3. Level of benefits from public schemes

Level of benefits

Figure 10 shows that the developments of the average level of pension benefits in relation to average wage in Hungary and Slovenia were following the same trend throughout the last decade. However, the important difference is that the replacement rates in Slovenia were about 7 per cents higher in relation to those in Hungary.

Figure 10: *Average replacement rates (%)*



Source: Stanovnik (2004), EC (2004)

Calculation of benefits

Old-age pensions in Slovenia and Hungary are calculated from the average monthly salary received by an insured person, or the insurance basis on which contributions were calculated. In several countries, including Hungary and Slovenia, attempts are being made to strengthen the contribution-benefit link by various changes in the formula for calculating pensions.

The difference between the pre- and post-reform period in Slovenia is that instead of the insurance basis covering 10 most favourable years for an insured person, today insurance basis of 18 most favourable successive years after 1 January 1970 is used to calculate the pension. This is a measure that will consequently reduce the level of pension benefits.

In Hungary an average monthly income during the best 4 years in 5 years preceding (US DSSA, 1995) used as reference earnings was modified to an average monthly income earned since 1988. This similarly implies a gradual extension of the period for calculating reference earnings and thus means a step towards gradual reduction of benefits, which are not even calculated on the basis of the most favourable years as it is the case in Slovenia. When this provision was enacted in 1997 this meant an average income during the last 9 years of employment and until today the reference period has been prolonged to 16 years and this trend will continue until the reference period comes to 20 years of insurance. The extension of the calculation basis at the same time represents an introduction of closer linkage between benefits and contributions and therefore reduces incentives to retire early.

Nevertheless, this measure was still less radical than switching to defined-contribution mandatory funded scheme in 1998, which abolished interpersonal redistribution completely. Redistribution within public schemes was reduced only partly by extending the calculation basis in PAYG scheme; otherwise it was retained, especially due to defined minimum and maximum pensions.

The scale used to calculate old-age pensions in Slovenia is different from the scale laid down under the previous law, both, in terms of the initial level of accrual rates laid down for the minimum insurance period, with which it is possible to obtain the right to an old-age pension, that is a 15-year insurance period, and in terms of the level of annual rates for the pension qualifying period. The initial rate is unchanged for men at 35 per cent of the Pension Rating Basis[22], while the rate for women has been reduced from 40 to 38 per cent, indicating that a certain difference is retained between the sexes in the initial rate. Each subsequent year of completed pension period is given a value of 1.5 per cent (instead of 2 per cent), and each six months 0.75 per cent. According to this data, for 40 years of qualifying period a Slovenian pensioner will receive 72,5 per cent of the Pension Rating Basis instead of 85 per cent that was obtained in line with previous legislation. Replacement earnings will be lowered gradually; 0.5 per cent yearly from 2001 onwards.

In Hungary the initial rate for both genders is the same; 53 per cent of average monthly net income earned since 1988 for 20 years of insurance period. Insured people are given additional 2 per cent for each of the insurance years between 21 and 25, 1 per cent for each year from 26 to 36, 1.5 per cent for years from 36 to 40 and 1.5 per cent for each of the insurance years after 40 years (EC, 2002 and Gal et al, 2003). For 40 years of qualifying period, according to the valid legislation, a Hungarian pensioner will therefore receive 80 per cent of the pension basis. After 2013, however, tha same pensioner will receive 66 per cent of the gross average salary. Due to the different pension base and different methods of calculating, those two replacement rates are not comparable (MHSFA, 2004).

[22] Pension rating basis (PRB): monthly average earnings in any consecutive 18-year period (phased-in until 2008: 12 years in 2002) of insurance following 1 January 1970, whichever is the most favourable for the insured person. Calculation of PRB is based on earnings (net of tax and other contributions) upon which pension contributions have been paid (EC, 2002).

Indexation of pensions

With reforms directed towards achieving fiscally sustainable pensions, many countries have changed the way pension benefits are up-rated. Indexation mechanisms play an important role for the economic well-being of the pensioner relative to the working population and can therefore also affect the decision to remain active in labour market after achieving the retirement age.

The way in which pensions are adjusted in Slovenia has been changed to follow the adjustment of wages agreed on by social partners during each agreement on wage policy better (Belopavlovič, 2002). Thus, pensions are adjusted twice a year in accordance with statistical data on monthly growth of an average national salary of an employed person and at least with the rate of growth of the basic costs of living.

For the same purpose, Hungarian government is obliged to adjust pensions once a year according to the planned increase in consumer prices and net national income, following the Swiss example (half of the sum of planned increase in consumer's prices and in average income).

7.2.2 Responses to the challenge of balanced resources in retirement

Risk diversification

Due to the heavy fiscal burden arising from the obligation of the state to cover the deficit of the public pension schemes[23], many countries are considering the possibilities of risk

[23] In connection with this it would be interesting to look at the data regarding fiscal balance of the pension system, but the figure available reflect only official balance of the pension funds, which serve for administrative

diversification. Therefore, many reforms include not only changing of the parameters of the first tier but also designing the second tier and its supplementary pension schemes. According to an OECD study (2001), this way, risk can be diversified since PAYG systems suffer from risks associated with uncertain demographic and labour trends, whereas a fully capitalised system, where each cohort saves for its own retirement, is on the other hand subject to investment and rate-of-return risk. This approach is analysed by Barr (2000), who is sceptical about the argument that the principal advantage of a three-tier scheme is risk diversification. In this respect he concludes that private pensions may or may not diversify the risk, but what is certain is that they always introduce additional risks.

Public pension expenditures

Another important reason for introducing private provision is the need to reduce public pension expenditures, which are, among others, because of a higher standard and higher replacement rates (see Figure 10), considerably higher in Slovenia than in Hungary (Figure 11). One of the reasons for decreased expenditures was the then existing indexation of pensions that was supposed to prevent the real increases in pensions (Stanovnik, 2002a).

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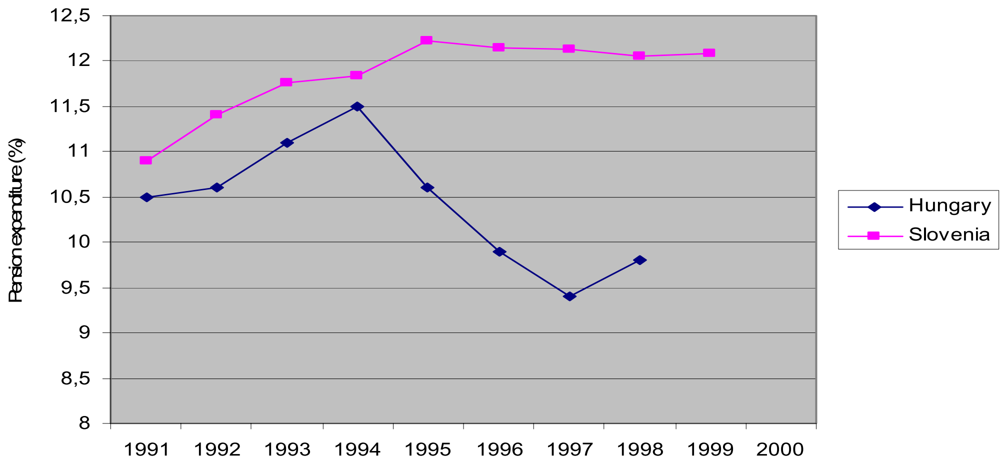
purposes and are not a good indicator of the real financial situation. Namely, the extent of state subsidies and other extra financial sources differ considerably from one country to another.

Figure 11: *Pension expenditures (% of GDP)*



Source: PDI Institute (Slovenia), Luxembourg Income Study (Hungary)

Considering the introduction of mandatory funded schemes it also needs to be highlighted that fiscal costs of undertaking a shift from PAYG to a fully funded scheme may be very high (IMF in Barr, 2000: 104-05). This shift, whatever its other merits, should not be undertaken as a short-term solution, especially not in countries without sound macroeconomic environment – despite the existing theory that the introduction of second-tier mandatory scheme causes increase in savings, in investment in domestic productions and hence in output growth (James in Barr, 2000: 101), certain conditions in terms of socio-economic development have to be fulfilled prior to that.

Supplementary pension schemes

The 1999 PDIA enabled the development of supplementary pension schemes in Slovenia. They can be divided in two parts: second-tier mandatory occupational pensions and third-tier collective and individual voluntary supplementary schemes. The former cover insured persons in certain occupations, for whom employers are obliged to pay higher contributions in order to finance early retirement. The employers have to pay normal contribution to the first tier and additional contributions to the mandatory supplementary pension scheme. Voluntary schemes, on the other hand, are designed for individuals and employers setting up their own collective schemes. PDIA sets certain conditions for operation and management of these schemes (guaranteed rate-of return, minimum number of members in a scheme).

In Hungary the formerly unified mandatory pension system was split into two schemes in 1998; one remained public and PAYG, while other is private and funded. Voluntary pension funds were already established in 1992. Unlike in Slovenia, mandatory scheme is not limited to only those working in hazardous occupations. It is obligatory for all new entrants to the labour market and optional for those already employed, implying that in the very long run, a mixed system would become universal. Employer's contributions to social security pension scheme have decreased from the pre-reform 24 per cent to 22 per cent in 2000 and to 18 in 2002 and continue to be invested only to the public scheme. On the other hand, employee's contributions increased from the pre-reform 6 per cent to 8 per cent in 2000 and to 8,5 per cent in 2003. Out of this, members of the mixed system[24] are to pay only 0.5 per cent to the public scheme and the rest to the mandatory private pension funds.

Extremely high number of people participating in public pension insurance system in Hungary decided or had to channel part of the contributions to commercially managed pension funds. Participation in private fuds is increasing also in Slovenia but still comprises only a small proportion of population (Table 7).

[24] Employees, who were obliged to join the mandatory private schemes, and those, who opted for it, are known as members of the mixed system (Augusztinovcs, 2002).

Table 7: *Development of supplementary pension insurance*

	2001	2002	2003
Slovenia	81.895	173.044	220.000 + 150.000*
Hungary	2.253.000 + 1.153.000**	2.214.000 +1.180.000	2.304.000 + 1.219.000

Source: MoLFSA (Slovenia), ONYF (Hungary)
* Public employees
** Participation in supplementary voluntary schemes

Incentives for use of private schemes

Several incentives to increase interest in mandatory and voluntary private schemes can be observed when analysing the pension reforms in Hungary and Slovenia. Among most important are tax incentives. In Slovenia they are more favourable for collective schemes than for individual ones. They are deductible for purposes of corporate income tax, social security taxation and personal income tax while employee's premiums remain subject to social security taxation (Stanovnik, 2002b: 36). While compulsory contributions in Hungary are not tax-deductible, voluntary supplements paid by an employee enjoy 30 per cent tax credit, whereas supplements paid by an employer are exempted from tax (EC, 2004: 36-37).

There are also other ways of stimulating people to decide for private schemes, for example, lower level of benefits from public schemes and introduction of ceilings on benefits. In a recent study of EC (2003) it is argued that in countries with a minimal differential between a minimum and a maximum pension level or low level of benefits there is generally a mandatory second tier pension scheme mandated by law, while in countries with more generous public first tier schemes supplementary second tier arrangements are voluntary. This surely holds for the cases of Hungary and Slovenia. As we have seen in Figure 10 above, the level of average pension benefits in comparison with the average wage is considerably lower in Hungary than in Slovenia[25]. Mandatory and voluntary private funds, therefore, especially in Hungary, represent an important source of additional benefits for people who want to and who can afford it. In Slovenia only voluntary schemes were introduced to fund part of people's old-age security, while mandatory schemes are supposed to meet other challenges, concerning only specific working places.

As far as the ceiling on income is concerned, in Hungary it equalled twice the expected annual average gross wage until 2003, and was increased to three times the expected annual average gross wage by 2004 (MHSFA, 2004). In Slovenia, following the 1999 PDIA, the ratio between comparable maximum and minimum pensions is set at 4:1 (the previous act stipulated the ratio at 4.8:1). In the context of more redistributive system it also needs to be mentioned that social security contributions are not capped. Stanovnik (2002a) points out that unlike in Slovenia, where pensions were compressed by lowering the income ceiling, the main reason for much more compressed distribution of pensions in Hungary was indexation of pensions that was supposed to prevent the real increases in pensions. As the rate of increase was not proportional, in January 1999, 75 per cent of all pensions fell in a narrow band between 30 and 40 thousand HUF, the average being 32 900 HUF.

[25] For example, the average replacement rate in 1999 in Hungary was 68.5 per cent of the average wage, while in Slovenia it amounted to 75.8 per cent.

7.3 Concluding Remarks

As suggested in the hypothesis, elements of the pension systems after the reform do differ between Hungary and Slovenia, despite the same situation before the reform. Two different sets of changes can be discerned; those within the existing PAYG system and those related to the introduction of supplementary schemes.

Within the first tier both countries have adjusted certain elements in order to balance time spent at work and in retirement. Thereby, Hungary undertook more fundamental changes as regards:

- the retirement age, which is equal for both genders,
- the introduction of bonus system without the upper limit on acquired bonuses,
- the replacement rates that are lower than in Slovenia, and
- the insurance basis for the calculation of benefits, which is longer than in Slovenia and does not include only the most favourable years.

Slovenia, on the other hand, went further by introducing partial pension and by completely abolishing the possibility of early retirement. A question that can not yet be answered is, whether by abolishing early retirement the pensioner ratio is going to improve or will these measures simply cause higher unemployment. Having in mind the pessimistic option and at the same time not facing such severe demographic challenges, Hungary has decided to retain the possibility of early retirement, despite the fact that it represents the main reason for worsening of the pensioner ratio[26].

[26] In spite of these efforts Hungary still has by far the lowest participation among OECD countries among people aged between 55 and 64 years, namely 26,4 per cent in 2002 (ONYF, 2004). The only available data for Slovenia divide this age group between those aged between 55 and 59 and those between 60 and 64.The activity rate of the former group amounted to 36,7 per cent, and of the latter group to 15,7 per cent in 2002 (SURS, 2004).

Slovenia has, in order to solve the problem of a threatening heavy fiscal burden that pension expenditures are going to represent, focused mainly on considerable changes within the existing PAYG system, while Hungary has seen the solution in a more radical approach - in balancing of the resources between mandatory public and private schemes (see Chapter 6.2.2.). Therefore, it is also evident that much stronger incentives to join mandatory (for those, who can chose) and voluntary supplementary schemes have existed in Hungary. Since Hungary decided for "structural reform[27]" most of the efforts were put to the introduction of new schemes. Therefore, much higher than the number of people expected (more than two millions) participating in public pension insurance system decided to channel part of the contributions to commercially managed pension funds. This has, however, led to the higher-than-expected deficit in the first tier, which has to be financed from the state budget. In short term the introduction of second tier scheme has not proved to be a good option. Nevertheless, better results can be expected in the long run, but only in conditions of better macroeconomic situation that would enable low-risk investments in domestic production, and thus output growth. Due to a disappointing economic growth performance during the first half of the 1990s in Hungary, with less than half the annual economic growth rate of the one in Slovenia, some authors reproach Hungary with "premature" welfare system relative to socio-economic development (Marin et al, 2001).

[27] Labelled as »structural reforms« are reforms implemented recently that clearly rejected the previous pension arrangement. On the other hand, the reforms that developed the already existent schemes are labelled »parametric reforms« (EC, 2003).

8 POLICY PROCESS ANALYSIS

This section puts in parallel, the changes of the pension systems, identified in the previous chapter, with the activities of various relevant actors during the reform process. Examination of interests and ideology as well as the roles of government coalitions, ministries, responsible for finance and for social security, pension insurance institutions and of trade unions in the policy process of changing the pension system in both countries will enable determination of the most influential actors and thereby answer the main research question.

In addition to some decisive national actors, Deacon (1997) argues that in explaining the changing of social policy more attention needs to be given to international and global actors. In this respect, he points out different forms of supranationalism. These include different forms of legal obligations and financial dependency of states towards supranational and global agencies, which together with threats and opportunities of the process of economic globalisation directly affect the room for manoeuvre for national policy makers and make various policy options more realistic than others. Therefore, in the second part of this section, the role of the WB, the EU and the ILO when reforming the pension systems will be discussed.

My hypothesis, based on the implemented analysis of the changes of particular pension system elements, is:

Pension system reform in Hungary was mainly influenced by (neo)-liberally oriented policy actors, whereas in Slovenia the degree of change, in particular the size of the private provision, was limited as a result of a balanced compromise of various political interests.

8.1 National Policy Actors

8.1.1 Hungary

The development of Hungarian pension policy can be divided into three stages, characterised mainly by dominant interests and ideologies of government coalition; socialist-liberal period (1994 – 1998) was interrupted by dominance of the right wing coalition from 1998 to 2002, which was again replaced by socialist-liberal thinking.

Two fundamentally different proposals on how to reform the pension system emerged in Hungary in the first phase. The first concept was advocated by the PIF's Self-governing Body, trade unions and individual pension experts. They proposed a two tier public mandatory pension system. The first tier would consist of social assistance; basic, flat-rate pension available to the citizens as a right and financed from general taxation. Pension insurance would create the second tier and would be earnings-related and actuarially fair and would incorporate fair rewards and penalties for postponed and early retirement, respectively. The main result of this proposal was the creation of a viable, accountable and flexible public system of PAYG pensions, with effective incentives to contribute (Auguzstinovics, 2002: 35-36).

The second proposal was prepared by the Ministry of Finance (MF) and later reconciled with the Ministry of Welfare (MW). This support was only possible after the resignation of two prominent leftists, the Minister of Welfare and the Minister of National Security, in protest against major cuts envisaged in social sector expenditures[28]. Namely, as Hungary edged closer to a fiscal and currency crisis, in 1995 the Finance Minister was appointed to implement

[28] At that time the Socialist-Liberal government supermajority coalition consisted of the Hungarian Socialist Party (MSZP) and the Alliance of Free Democrats (SZDSZ).

an austerity plan[29], which eventually set context for a more radical social sector reform. The concept of pension reform proposed within this plan relied mainly on the WB's concept and foresaw a public, contribution-related PAYG system, private mandatory funded scheme and a supplementary, voluntary third tier. Thereby, the reformed PAYG scheme would have to bear the costs of the transition to a three-tier system. There were even ideas, coming from those who controlled the voluntary third-tier funds, to eliminate the PAYG system completely. Other members of the working group, however, considered this as financially and politically unfeasible (Orenstein, 2000).

The 1998 pension reform in Hungary was the result of certain compromises, firstly between the MF and the MW and later also with the Socialist-affiliated trade unions, who had a decisive voice within the Interest Reconciliation Council (IRC[30]) and were represented in the board of the PIF. A rather polarised debate between the MF and MW eventually led to development of a unified pension reform proposal. Due to great differences between the proposals, PIF, however, remained outside this government compromise. After social partners within the IRC were satisfied with the compromises, parliament moved quickly (Ibid.). The need to compromise on the basic design of the reform has partly limited the degree of change, in particular the size of private provision.

Among the most important changes in Hungary there are tighter eligibility in the first tier, introduction of the Swiss indexation, increase in retirement age and the establishment of a legal framework for mandatory private funds. Those already employed could either remain full members of the public scheme or opt for MPPF of their choice. In the latter case the

[29] The plan of the Finance Minister Lajos Bokros became known as the *Bokros Package* (Orenstein, 2000: 28).
[30] IRC is a Hungarian tripartite body and can be placed in parallel with the Slovenian Economic and Social Council.

contributions to the public funds and pension rights[31], arising from them, were diminished. Those switching to mixed system were allowed to return without loss to full SPPS membership up to the end of 1999. For new entrants to labour market membership in private mandatory schemes became compulsory. The contributions were adjusted to the new system by reallocating two percent of contributions from employers to employees. The former were to contribute only to the public scheme (22 per cent by 2000), whereas employees were to pay one percent to the SPPS and the rest to private funds (8 per cent in 2000).

However, after the elections in 1998, a new coalition government was formed that partly voted against the reform while it was still in opposition. The elections were won by a new Right wing coalition that emerged from the reconstruction of previous ruling parties of the early 1990s[32]. Their legislative proposals significantly changed some parameters of the pension reform during their mandate.

The PIF lost its independence to some extent and was placed under direct government supervision, mainly under the MF; the contributions were collected by the State Tax Collection Agency and deadline for the transition of people from MPPF back to SSPS was extended. In November 2001 the parliament made it voluntary to join the mixed system, even for new entrants to labour market. The new government also considered the new indexation rule as not affordable and therewith slowed down the planned increase in benefits. The contribution rates (Table 8) were decreased for five percentage points; the employers' contributions were decreased for six percentage points (instead of envisaged two) and employees' contributions were increased for one percentage point (instead of envisaged two). As the mandatory private

[31] Members of mixed system surrendered 25 percent of the pension rights that had accrued to them in the SPPS (Augusztinovics, 2002: 38)

[32] From 1998 to 2002, Hungary was governed by a coalition government made up of the Alliance of Young Democrats – the Hungarian Civic Party (FIDESZ-MPP), the Independent Smallholders' Party (FKgP) and the Hungarian Democratic Forum (MDF) headed by the Prime Minister Viktor Orbán (FIDESZ-MPP).

tier depends completely on the employees' contributions, the 1997 legislation envisaged gradual reallocation of two per cents of contributions from the employers to the employees that would widen the field for the second tier. The new government did, however, increase the rate of employees' contributions to be paid to the MPPF for only one percent (instead of envisaged two) and increased the rate to be paid to the public scheme to two per cent (Augusztinovics, 2002).

Table 8: *Pension insurance contribution rates (gross wage = 100)*

	Employers	Employees	to MPPF	to SPPS	Total
1998	24 (24)*	7 (7)	6 (6)	1 (1)	31 (31)
1999	22 (23)	8 (8)	6 (7)	2 (1)	30 (31)
2000	22 (22)	8 (9)	6 (8)	2(1)	30 (31)
2001	20 (22)	8 (9)	6 (8)	2(1)	28 (31)
2002	18 (22)	8 (9)	6 (8)	2(1)	26 (31)
2003	17,5	8,5	7	1,5	26
2004	17,5	8,5	8	0,5	26

Source: Augusztinovics (2002: 50) and MHSFA (2004)
* Rates legislated in 1997 are shown in brackets.

From January 2003 onwards the distribution of contributions between the two tiers has been re-regulated again due to another change in government. The socialist-liberal coalition which introduced the mixed system in 1998 is likely to proceed with their policy and with stabilising the new funds (Gal et al, 2003: 47). In 2003 they already raised the employees' contributions to private funds to seven percent of the gross wage whereas in 2004 this level was additionally raised to 8 percent at the expense of reduced contributions to the public scheme. Another new rule from 2004 relates to the return of the MPPF members back to the SSPS; the return is still possible for those who will be members of the MPPF for maximum of 120 month until 2013 and for those whose annuities in the MPPF would not reach 25 per cent of the amount of their state pension. This could have a considerable impact on distribution of contributions and risks between the two tiers (MHSFA, 2004).

8.1.2 Slovenia

Pension reform related activities of particular national policy actors in Slovenia are clearly depicted by Stanovnik (2002b). Some of his findings are summarised in this chapter. Following the parliamentary elections in 1992 the United League of Social Democrats (ZLSD) was in charge of the MoLFSA. The party's preference to retain the existing social rights prevented any activities related to the need for fundamental changes within the pension system. After the proposal of the government to establish a new indexation rule that was less favourable for pensioners and to reduce certain social expenditures the ZLSD withdrew from the coalition, which at that time also included the Liberal Democrats (LDS) and the Christian Democrats (SKD).

The post of the Minister of Labour, Family and Social Affairs was given to the LDS. Staring points for the pension reform and disability insurance system had been prepared by July 1996. These were clearly in favour of minimum security provided by the first pillar and a mandatory fully funded second tier, as advocated by the World Bank.

In 1997 a new coalition, led by the LDS was formed. Other members were also the People's party (SLS) and the Pensioner's Party (Desus). The LDS continued their work on the pension reform with preparation of the White paper on the reform of pension and disability Insurance that was coordinated by the Phare[33] team. Within the recommended structure of the new system was again a mandatory fully funded second tier, as advocated by the LDS and the SLS. The only concerns of the other ruling parties were the introduction of the means-tested national pension (SLS), preservation of the indexing to net wages, introduction of widows' pensions, and recreational supplement for pensioners and financing the future pension deficits by the government (Desus).

The first strong criticism only emerged after forming of the tripartite negotiating working group in January 1998 from the side of trade unions. Consultations with social partners in Slovenia are formally not obligatory, but adoption of relevant legislation is practically impossible without their consent. They opposed the pension reform plan, in particular pensionable age of 65 years, sex equalisation, and introduction of the mandatory second tier and the proposed calculation of the pension assessment base from the best 25 years. This led to several demonstrations and even to a serious threat of a general strike. Eventually most of their arguments were taken into account, except their key proposal that the required contribution period (38 or 40 years) would suffice for full pension, regardless the age (Ule, 1998). Minister of Labour, Family and Social Affairs, Anton Rop, declared this proposal was not acceptable and not in line with the EU legislation (Obzornik, 24 July 1998).

The government therefore gave up the mandatory second tier and at the same time proposed gradual introduction of voluntary fully funded supplementary tier. The main fears of the trade unions were that the transition to the mandatory second tier would cause a large deficit of the first tier and therewith seriously reduce pensions from public provision. These fears were

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[33] The Phare team operated in Slovenia within the framework of Phare programme, which is one of the three pre-accession instruments financed by the European Union to assist the applicant countries of Central and Eastern Europe in their preparations for joining the European Union.

shared with the Desus and the opposition party ZLSD. Even the MF opposed this move as a mandatory fully funded tier would worsen fiscal position in short and medium term.

As far as the other proposals of the trade unions are concerned, instead of 65 years for both sexes, the statutory retirement age was set in line with their proposal; at 63 for men and 61 for women, and the period relevant for the computation of the pension assessment base was lowered from 25 to 18 best years. Some elements of the new pension system are based on the compromise between the government and trade unions: the values of bonuses and maluses were diluted, transition period stretched and for certain groups of people retirement prior to the full pensionable age does not entail penalties (Stropnik et al, 2003:73).

After a year of tough negotiations, two social agreements with employers' and workers' organisations were signed in April 1999. They included the basic elements of the first tier. The only issue not solved remained tax treatment of supplementary pension schemes. While Minister Rop advocated the most favourable tax treatment – exemption of employers' premiums from all forms of taxes, the MF considered that these premiums should be given the same treatment as other fringe benefits granted by the employer. Eventually Minister Rop's suggestion got its way. With strong tax incentives, it can be regarded as an important step towards the universal use of the second tier and consequently as paving the way towards introduction of the mandatory second tier. The new PDIA was adopted in December 1999. It does not only deal with social security but also sets a framework for supplementary schemes, which is usually a responsibility of the MF.

According to Minister Rop the legislation envisaged should ensure financial sustainability of the pension system for at least 15 years (Kranjec, 1998). Pension expenditures in demographically most critical years would gradually decrease for 7 percent of GDP with regard to the existent system (Repovž, 1998). However, despite the abolished idea of introducing the mandatory private tier, Rop was of opinion that after the implemented changes of the public system, Slovenian government should again consider the introduction of the mandatory private pension funds (24 ur, 22 July 1998).

8.2 Supranational Policy Actors

Despite the fact that not many studies about the influence of global actors on national social policies have been carried out, there are some experts on social policy, who argue that "more attention needs to be given to supranational and global actors in explaining the changing of social policy" (Deacon, 1997), including national social policies. In this respect, Deacon points out different forms of supranationalism; supranational and global agencies contribute to shaping of national policy and terms of international competition by:

1. laying down social policy conditions on governments for the receipt of financial assistance,
2. redistributing resources among governments,
3. offering technical advice and assistance as a step towards legal social regulation and
4. empowering citizens to appeal to an authority above the state.

In addition to the abovementioned direct interventions, some international organisations strongly influence social policy through their contributions to global social policy discourse.

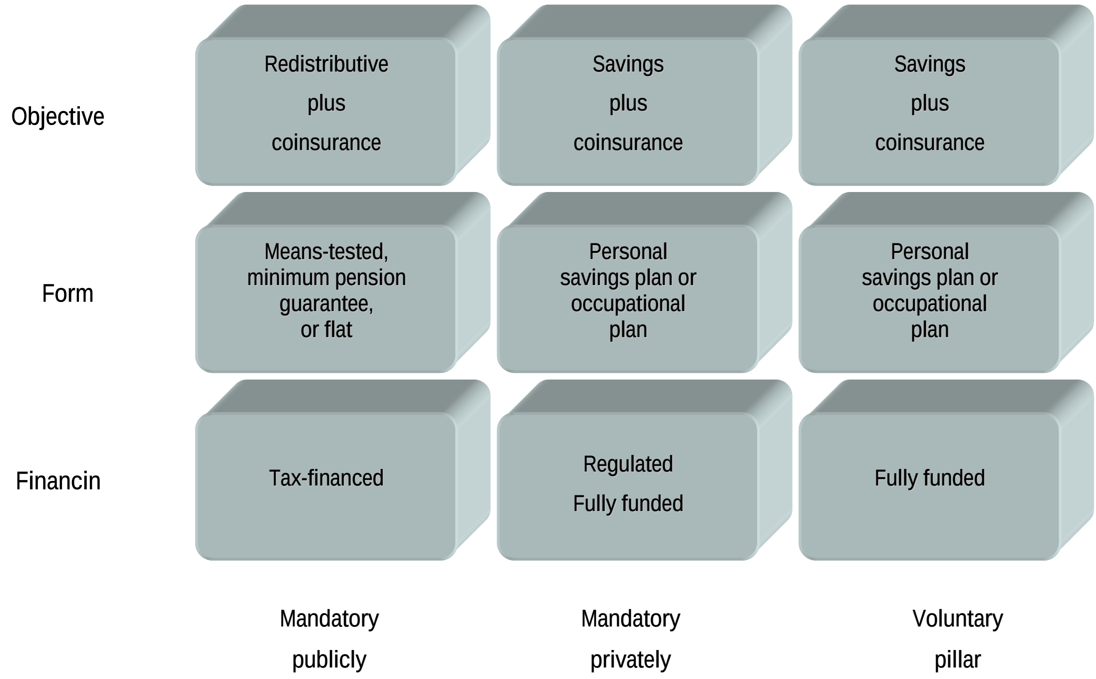
In their struggle for better global and national social policies international agencies work in contradictory directions (Ibid.) and therefore try to influence national policies in different ways. I have decided to base my work on analysis of the role of various approaches of three particular international actors; the WB, the ILO and the EU, the extent of their involvement and their final impact on reform proposals in each country.

8.2.1 World Bank

The WB played an important role through shaping terms of discourse about social welfare, in particular in an intellectual debate on the most appropriate direction of pension reforms. In this discourse the main controversy concerned desirability of wage related PAYG state social security systems, advocated by the ILO and the ISSA, versus fully funded and privately managed individual accounting schemes, advocated by the WB. This debate was above all evident in case of pension reforms in South America and Eastern Europe. The WB's publication Averting the Old Age Crisis revealed their views and provoked a lively intellectual debate around the world.

A dominant approach of the international monetary institutions was the need for free trade and deregulation. In the WB's opinion, the existing systems in Eastern Europe are financially unsustainable and thus intensify intergenerational conflict, discourage work, saving and productive capital formation – thus contributing to economic stagnation. As a solution to these problems the WB (1994: 15) offers a model (Figure 12), separating the saving function from the redistributive function and placing them under different financial and managerial arrangements in two different mandatory pillars – one publicly managed and tax financed, the other privately managed and fully funded – supplemented by a voluntary pillar for those who want more.

Figure 12: *The WB's Model of the Pillars of Old Age Income Security*



Source: WB (1994: 15)

Within the recommended framework[34] the public pillar would be very modest in size and would have limited objective of alleviating old age poverty and co-insuring against a multitude of risks arising from long spells of low investment returns, recession, inflation and private market failures. It could take either a form of means-tested or flat-rate benefit.

The second, mandatory, fully-funded and privately managed pillar would link benefits actuarially to costs. It could take the form of occupational or personal savings plans. It would require careful regulation and should reduce the demands on the first pillar. When choosing between personal and occupational savings plans governments have to be aware of the advantages of occupational plans, which can start up on a voluntary basis before the market

[34] The details about the above depicted recommended framework are presented in the WB's publication *Averting the Old Age Crisis* (WB, 1994)

and the government are ready for a mandatory plan. Despite the advocated advantages of privately managed, mandatory schemes, governments should not rush to establish one, but rather firstly assess carefully the market and regulatory capacities required.

In line with the model described the following steps are recommended for CEE countries:

1. the reform of public pillar by raising the retirement age, eliminating rewards for early retirement and penalties for late retirement, downsizing benefit levels, and making the benefit structure flatter, and tax base broader
2. launching of the second pillar, which should be accompanied by downsizing the public pillar (reallocating contributions), raising contribution rates for public schemes, while holding the benefits constant, or
3. calculating the implicit social security debt that is owed under the old system, and figuring out how to finance it all in a way that is both politically and economically acceptable.

In this way, the WB model would help countries to reduce perverse redistribution and poverty, to achieve a close relationship between contributions and benefits in the second pillar, to increase long-term savings and growth, to diversify risk and to reduce political pressures. Mechanisms used by the WB to achieve these goals in individual countries will be discussed in the rest of this chapter.

8.2.1.1 Hungary

As described by Borbély (2000: 11), the WB has laid down the following pension policy conditions on the Hungarian government for the receipt of loans in the early 1990s:

- stricter eligibility rules for old-age pensions (1992), and
- stricter eligibility rules for disability pensions, pensioners' stimulation to re-enter the labour market (1995).

Since the middle of the 1990s, when the WB's study Averting the Old Age Crisis was published, the idea of privatisation was underlined. It was mainly advocated by the Hungarian MF. Its activities were therefore funded by the WB and thus, due to better opportunities and resources, had a dominant impact on the reform process (Ferge in Orenstein, 2000: 29). The conditions set by the WB in that period included (Borbély, 2000:11):

- reduced public pillar and lower standards,
- multi-pillar pension system with a minimum pension, PAYG social security scheme, compulsory private pensions based on individual savings accounts and voluntary insurance,
- increased role of market forces and decreased role of the state,
- growing role of individual responsibility and decreased solidarity, and
- decreased burden on budget and employers.

Thereby, it needs to be mentioned that total commitments of the IBRD[35] to Hungary from 1991 to 1998 amounted to 1,959 million US dollars, whereas the commitments to Slovenia came to total of 129 millions from 1991 to 2000 (WB, 2004a, 2004b). Comparing these numbers with population figures, we can see that the loans from the WB Group per capita were about three times higher in Hungary.

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[35] The World Bank Group consists of five closely associated institutions, all owned by the member countries that carry ultimate decision-making power. Each institution plays a distinct role in the mission to fight poverty and improve living standards for people in the developing world. IBRD aims to reduce poverty in middle-income and creditworthy poorer countries by promoting sustainable development, through loans, guarantees, and nonlending—including analytical and advisory—services (www.worldbank.org, 16.08.2004).

The WB was not only heavily involved in funding, but also in directly assisting the Hungarian Interministerial group for pension reform, where government reform proposals were elaborated and legislation drafted. Interestingly, the PIF also had access to a WB loan that had been processed earlier and used the technical assistance component of this loan to conduct its own agenda (Orenstein, 2000: 33) that differed significantly from the MF proposal.

8.2.1.2 Slovenia

The first cooperation of the international monetary institutions in Slovenia; the IMF and the WB team, can be traced back to 1995 when they produced a report on new challenges confronting social insurance system in Slovenia. It suggested a pension reform in two stages, whereby the first one would be a parametric reform of the first pillar, whereas in the second stage a multi-pillar system could be developed. According to this report, gradual reform should be in line with the nascent development of the Slovenia's capital market. The report also discusses various options for introduction of the second mandatory pillar, but does not recommend it directly. The report gave a strong impetus to the reform process and had a significant impact on the draft version of the White paper on pension reform (Stanovnik, 2002b).

Another influential element for the process of reforming legal social regulation in Slovenia was the WB publication Averting the Old-age crisis. Working group that prepared the policy paper on pension reform (Starting points for the reform of the pension and disability insurance system) in July 1996 was chaired by Minister Rop. The paper was strongly influenced by the WB publication and came out clearly in favour of a mandatory fully funded second pillar.

Despite its strong interest, the WB was not that actively involved in preparation of the pension reform as their loan was not available at the right time. Therefore, technical assistance for the preparation of the White paper was received through the Phare programme. Nevertheless, in 1997 the WB and the government of Slovenia approved a Country Assistance Strategy (CAS), which included the following activities regarding the pension reform in Slovenia:

(a) assisting the Government in elaboration of an overall reform proposal that would place the PAYG system on a sound financial footing, and introducing the second and third pillars;

(b) preparation of two models to compute various reform simulations and training of staff in the Ministries of Finance and Labor as well as the Institute for Macroeconomic Analysis in their use;

(c) organizing conferences, workshops, study tours and seminars for technical specialists, policy makers and opinion makers designed to present key reform options and enhance public awareness of the need for reform (WB, 2000: 7).

However, not all of these activities were implemented. The WB has installed two models for pension reform simulations and trained staff at the IMAD. Their grant co-financed a study-mission of members of the Parliament and experts to Switzerland and Netherlands. The WB experts took part in the process by attending and co-financing the international conference on pension reform in November 1997, after the White paper had already been prepared. Most of the papers at the conference advocated a multi-pillar approach, whereby the second fully funded pillar would be mandatory. In March 1998 the WB prepared and financed a workshop on Second Pillar Issues. Mr. Bole, one of the most influential economists in Slovenia, was commissioned a paper in which, at a bitter surprise of the WB, he did not favour introduction of s mandatory second pillar. After this workshop the idea of a mandatory second pillar ended in failure and the Bank and Government agreed to drop plans for a Bank loan that would have helped implement the pension system reform (Stanovnik, 2002b: 45, 63).

An assessment of the CAS states that although the new pension legislation fell short of the Bank team's recommendation, it removed projected deficits in the PAYG system in the next 15 years or so, and introduced a third pillar - a voluntary fully funded system. Nevertheless, progress in the creation of occupational funds by many large employers also on a voluntary basis could, in the WB's opinion, eventually lay the groundwork for a more broadly defined contribution pillar (WB, 2000: 7).

8.2.2 European Union

During the pension reform processes in Eastern European countries, it is hard to say, in the light of polarised political discourse, that the EU took a specific stand in the debate. Their advice to the East through Phare and Tacis[36] programs is not a systematically European conservative corporatist advice[37]. This is mostly due to competitive tendering: reliance on

[36] Launched by the EC in 1991, the Tacis Programme provides grant-financed technical assistance to 12 countries of Eastern Europe and Central Asia (Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine and Uzbekistan), and mainly aims at enhancing the transition process in these countries.

[37] Commonly agreed goals of the EU, set by the Council of the EU (2001) only after the implemented reforms in Hungary and Slovenia, can be understood as general views of the EU regarding the development of pension systems. According to these, pensions should be adequate and not only ensure that older people are not placed at risk of poverty but that they also enjoy a decent standard of living. Thus, public and/or private pension arrangements should allow them to earn entitlements that would enable them to maintain, to a reasonable degree, their living standard after retirement. The EU also speaks for solidarity within and between generations. Secondly, financial sustainability of pension system can be achieved through high level of employment and comprehensive labour market reforms. In addition, pension systems should include incentives for longer participation of older workers and facilitate the option of gradual retirement, which would lead to a fair balance between the active and the retired. Private and public funded pension schemes can provide pension with required efficiency, affordability, portability and security only through sound management. Thirdly, pension systems should be modernised and compatible with requirements of flexibility and security on labour market. Thereby, pension systems should take into account across-borders and non-standard employment, encourage self-employment and equal treatment of women and men.

consultancy firms of unknown policy persuasion lead to depoliticisation of globalised social policy (Deacon, 1997).

Concerning harmonisation of national legislation with the EU legislation, it is important that social security systems are largely under the authority of the Member States, while the EU has no overall authority (Oksanen, 2004: 92). There is only an indirectly binding legislation within the framework of co-ordination of economic policies. Namely, serious imbalance in public finances is dealt with at the EU level and public pension systems represent an important part of public finances. The EU study (2001) demonstrates that all EU countries are facing serious financial problems as a result of population ageing and the same can be said for the new member states[38]. Increase in pension system deficit, higher expenditures for pensions[39] and increase in system dependency in Hungary and Slovenia after 1991 have also threatened the sustainability of fiscal system. Therefore, the implementation of the pension reform was necessary for the countries to fulfil the conditions for membership set by the EU.

Another requirement posed to the future EU Member states was to include social partners in preparations for the EU membership and to foster dialogue and active participation of social partners. In July 1998 this requirement was pointed out by representatives of workers' and employers' organisations. Their comment was that by then these preparations, including those for pension reform, had mostly been in the hands of governments, not only in Slovenia but also in other candidate countries (Repovž, 1998).

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[38] Pension expenditure in EU-15 now amounts to 10.4% of GDP, and it is expected to increase to 13.6% of GDP in 2040 (Economic Policy Committee, 2001).
[39]Pension expenditures in Slovenia increased from 10.9% in 1991 to 12.13% of GDP in1997 (Stanovnik, 2004).

8.2.2.1 Hungary

According to MHSFA (2004), In Hungary there were no Phare programs focused on the pension reform carried out. Although there were some initiatives in this direction right after the structural pension reform in 1997, they have never been carried out.

As the EU membership was one of the main objectives in the period of reforming the pension system, Hungary had to make a great effort to fulfil the conditions required. Among these, was to solve the problem of increased deficit in pension system, higher expenditures for pensions[40] and increased system dependency, which threatened the sustainability of the fiscal system. Therefore, implementation of the pension reform was necessary also from the EU's point of view[41].

8.2..2..2 Slovenia

Slovenia's decision for the Phare programme as a provider of technical assistance during preparations for the pension reform was not ideologically motivated. The main reason for it was that the Phare grant appeared just at the right time.

The Phare team started their work with a critical assessment of the Starting points for the reform. However, the final version of the White paper included only few of their suggestions. According to Stanovnik (2002b) the Phare team more or less played a role of a coordinator, while the other tasks were left to the Slovenian experts. As evident at the presentation of the White paper at the international conference in 1997, co-financed by Phare, the paper did not

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[40]Pension expenditures in Slovenia increased from 10.9% in 1991 to 12.13% of GDP in1997 (Stanovnik, 2004).
[41] From 2005 on, the compliance of the national pension policies with the commonly agreed goals of the EU will be subject to peer-review within the Open method of co-ordination.

include much of the European conservative corporatist views and the idea about introduction of a mandatory fully funded second tier prevailed.

However, the role of the Phare team in Slovenia should not be neglected. Its main role was to draw attention to the essential points that needed to be explained or resolved. In this respect, it represented some kind of counter-balance to the strongly present WB's proposals (Fultz, 2004), by exposing the most conspicuous weaknesses of a mandatory second pillar.

8.2.3 International Labour Organisation

In contrast to the neo-liberal orientation of the WB, the ILO is aiming at securing the common international labour and social standards set and derives from the social democratic climate of the period after the WWI. The ILO activities are anchored in relevant ILO social security standards and in concept of decent work. According to the ILO's view, establishment of systems based on individual savings accounts should not weaken solidarity systems, which share risks between all insured persons. The ILO also highlights a crucial role that social partners have to play in this field and a general responsibility of the State for proper administration of the institutions and services concerned in securing protection envisaged in the ILO Convention (Humblet and Silva, 2003).

Another important distinction with the WB has to be made with regard to the instruments available for influencing the national social policies. The ILO can offer technical assistance programmes, but cannot give any loans, which could, to some extent, involve social conditionality. Sources for financing the particular programmes on the national or regional level have to be found outside the organisation. However, the ILO has the ability to impact national social policies through its international labour legislation. Namely, there are two conventions concerning the pension policy; ILO's Social Security (Minimum Standards) Convention (No. 102) has been ratified by 41 countries, among others also by Slovenia, and the Invalidity, Old-Age and Survivors' Benefit Convention (No.128) which has only been ratified by 16 countries. This gives the ILO the power to report on shortcomings in member country's social old-age policy where the particular convention has been ratified. Both conventions are aimed at guaranteeing protected persons, who have reached certain age, the means of a decent standard of living for the rest of their life[42].

8.2.3.1 Hungary

Hungary has not yet ratified neither the ILO Convention No. 102 that lays down the minimum social security standards nor the Convention No. 128. It has thus not accepted any obligations arising from them.

With regard to the involvement of the ILO in the Hungarian pension reform process, it has to be noted that the reform proposal was mainly the responsibility of the national MF. As the ILO co-operates mostly with the national Ministries, responsible for labour and social affairs, its

[42] The Convention No. 102, adopted in 1952 provides for a minimum level of benefits in each branch of social security. Convention No. 128 is, however, drawn up on the model of the Convention No. 102, although offering a higher level of protection in terms of population covered and the level of benefits. For example, while the Convention No. 102 stipulates that the level of benefits must attain 40 per cent of the reference wage, Convention No. 128 raises this percentage to 45 per cent. Both conventions set forth the principle of adjusting the rates of benefit following substantial changes in the general level of earnings or the cost of living, the maximum qualifying period for obtaining the benefits which may not exceed 30 years of paying contributions or being employed or 20 years of residence. The minimum qualifying period for reduced benefits is set at 15 years of contribution or employment. With regard to the retirement age, both conventions prescribe not more that 65 years of age. The Convention No. 102 allows the possibility to fix a higher age with due regard to the working ability of elderly persons in the country, whereas the Convention No. 128 adds the possibility of fixing a higher age due to demographic, economic and social criteria, which shall be demonstrated statistically. In addition, the latter Convention lays down that the pensionable age must be lowered in cases when people have been engaged in arduous or unhealthy occupations.

impact in Hungary has been limited from the beginning. Therefore, no assistance was received from the ILO (MHSFA, 2004). Due to then neo-liberal political orientation of the MF, closer ties were established with the WB. This close co-operation eventually led to adoption of the three-tier pension system.

8.2.3.2 Slovenia

Slovenia has taken over the obligations arising from the provisions of the Convention 102 relating to the old-age benefits from ex-Yugoslavia. Nevertheless, it has not yet ratified the Convention No. 128. By now, the ILO's supervisory body, the Committee of Experts for the Application of Conventions and Recommendations has not given any comments on implementation of the Convention No. 102 provisions.

As regards the ILO's technical assistance, there was no funding at that time provided for the programs aimed at assisting to the pension system reform in Slovenia. However, the advice from the ILO experts was not neglected. Not only informal contacts of the individual ILO experts with the MoLFSA, but also participation of the former ILO officials in the Phare project dealing with of the Slovenian pension system reform, both had a significant impact on cautious balancing of different ideas, received from the international community (Fultz, 2004). Namely, as already mentioned, the Phare experts were chosen through the competitive tendering and were thus of unknown political persuasion. They could therefore more or less independently advocate their own views and Mr. Giovanni Tamburi from the selected French consortium happened to be an ex-ILO official[43].

[43] Mr Tamburi was the director of the Social Security Department of the ILO in 1969 – 1989.

The outcomes of the Slovenian pension reform were eventually very much in line with the ILO views. Therefore, the ILO often gives it as an example of the successful reform to the countries of South-East Europe that are currently going through the process of reforming their pension systems.

8.1 Concluding Remarks

The findings of this chapter have revealed that various policy actors, on national as well as supranational level, have influenced the direction of the reform with their ideology, interests and power. By summing up the conclusions of this chapter I will divide the reform process into three stages.

Looking at the national level, we can confirm that originally, in the first stage, reform proposals in both countries were liberally oriented. This coincided with intensive involvement of the WB. The major difference that existed from the beginning of the process is that the task in Hungary was entrusted to the MF whereas in Slovenia to the MoLFSA.

The second stage of the process in both countries was characterised by inclusion of various veto actors. In Hungary they were limited to coalition parties and to, though to a very limited extent, trade unions. The WB remained the main source of external pressure. In Slovenia, however, a broader compromise was achieved by considerable influence of social-democratic ideology of the trade unions and of the opposition party, ZLSD. Their informal veto power even caused the changes in the proposed basic structure of the pension system and the refusal of the WB's neo-liberal proposals. As far as the supranational level is concerned, the second stage was denoted by involvement of other international organisations of different political pursuance, such as the EU and the ILO. The number and diversity of the actors involved have without doubt considerably limited the degree of change within the pension system.

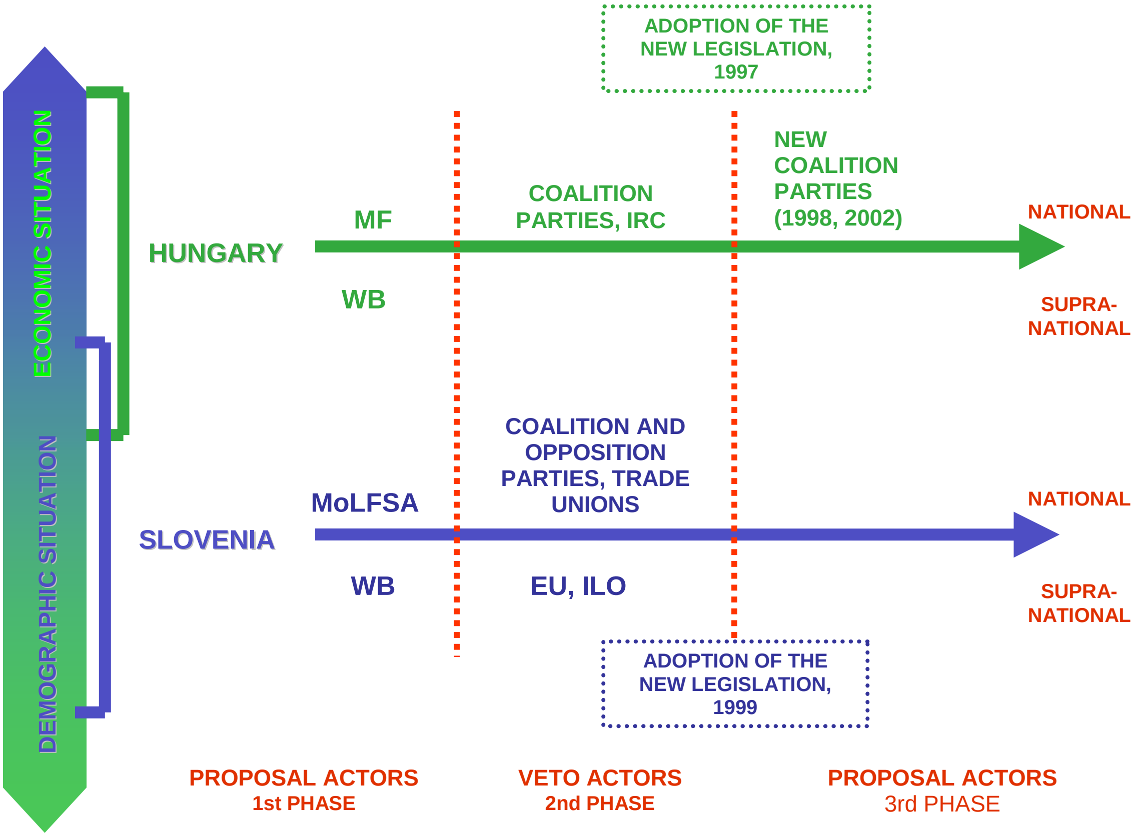
The number and diversity of the actors involved also had a considerable impact on the third stage, the period after the adoption of the new legislation. There were no changes of the pension system elements in Slovenia after a new party became in charge of the MoLFSA. On the other hand, the parameters of the pension system in Hungary have been continuously changing due to the changes in the government. This is in particular the consequence of the fact that in Hungary the opposed opinions concerning the introduction of the compulsory private pension were not taken into consideration (Borbély, 2000: 11).

9 CONCLUSION

The examined analysis has proven strong presence of two opposite ideological approaches in the CEEC. Namely, Hungary and Slovenia are good examples of different strategies undertaken by countries with the same starting position regarding the form of their pension systems. The analysis of the policy content has shown that there are some disparities between the countries within the adjustments made to the already existing PAYG system, but that the main difference is in the relative size of the introduced private arrangements. Namely, prevailingly neo-liberal approach in Hungary resulted in construction of a completely new pension system with partial privatisation of mandatory pension provision, whereas Slovenia, as a result of a broader and more balanced compromise between various political interests, including strong veto actors of social-democratic political persuasion, decided for a gradual approach and supplemented the public PAYG system, newly adapted to the new economic and political circumstances, with only voluntary participation in private pension funds.

And how can this difference be explained? We have looked at two sets of policy determinants; firstly, we have examined the trends in the macroeconomic and demographic situation and secondly, the most influential national and supranational policy actors within the policy process. The analysis of the policy process and of the economic and demographic situation, which are strongly interrelated, clearly demonstrates, that *"social policy is not made in a vacuum, in a "pure" realm of social policy"* (Kangas and Palme, 1992: 231). Similarly as Kangas and Palme (Ibid.) claim for Scandinavian countries, the same is true for pension reforms in CEEC - theydo not only have economic consequences, but are also adjusted to the economic circumstances. At the same time the relationship between private economy and public social policy in CEEC has been patterned in different ways, which reflect differences in political parties, interest group formation, and priorities in economic policy making.

Figure 1: *Factors causing different reform outcomes*



By forming the reform proposals, in the beginning of the process the most influential actor appeared to be each country's ruling coalition, in particular the ideology and the interests of the Ministries responsible for the reform. This coincided with intensive involvement of the WB. In the second stage, their power was to a different extent limited by various veto actors, such as other ministries, trade unions or government opposition, and by pressures, coming from other external actors. From Figure 13 we can see a considerable difference between the number of veto actors involved in each country; inclusion of higher number of policy actors in

Slovenia eventually even resulted in fundamental changes of the original reform proposal. In Hungary, on the other hand, the limited number of the actors involved has did not cause such significant changes of the original proposal. However, in Hungary many adjustments were made after the adoption of the new legislation, firstly, with the election of new government that did not fully support the reform proposal when being in the position of a veto actor, and secondly, after the elections in 2002 due to another change in the government.

According to our findings, one of the main reasons for different outcomes of the pension reform is also an economic situation in a particular country. As a result of severe economic crisis Hungary saw the solution in quickly implemented radical measures, which were, according to the strongly supported WB's view, an important step towards increased savings and consequently, towards increased growth. Pessimistic projections concerning demographic trends, on the other hand, do not require drastic short-term changes. Demography seems to be of less importance in Hungary, whereas it was the main reason for the decision for certain incremental long-term changes within the Slovenian pension system. No radical measures were necessary in Slovenia due to a relatively stable economic situation, allowing for cautious introduction of the new pension system elements.

Due to the gradual introduction of the changes examined[44] the appropriateness and successfulness of the implemented reforms will only be evident after a decade or two and this prevents us to assess the still ongoing reforms. Nevertheless, the main question that comes to my mind at the end of this study is:

Is the new pension legislation, adopted in more or less volatile economic environments, in line with a nascent development of Hungarian and Slovenian capital markets?

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[44] The pension reform will only have been implemented by 2009 in Hungary and by 2017 in Slovenia.

Namely, the less favourable macroeconomic elements and strong reliance on the FDI in Hungary led to a stronger role of private schemes, which even became mandatory. In Slovenia, on the other hand, all social security contributions continued to be invested in the existing PAYG scheme, whereas the decision for private pension accounts is voluntary. At first glance this seems to oppose Barr's theory, stating that second-tier schemes involve additional management, investment and annuities market risks, and therefore require sound macroeconomic situation with adequate financial markets and assets. One could thus argue that the Slovenian approach was more in place and thus reduced the possibilities of exposure to additional risks arising from introduction of private pension accounts. Similarly, in view of adverse factors (weak capital markets, high unemployment), one could also question the wisdom of introducing far-reaching reforms, which require firm long-term commitments, well-functioning capital markets and trust in government and financial institutions (Stanovnik, 2002a).

As even the WB has become more cautious when advising the radical reforms, which have not proved to guarantee economic growth (Fultz, 2004) as suggested earlier, we can conclude that radical changes of pension system are not well-suited to the broader situation in the transition countries, implying that old-age insurance cannot be left to the free market only in such a short time and under inadequate economic circumstances. On the contrary, some kind of state intervention in transition countries, moving on the axis, leading from the collective character of the schemes run by the states in socialist times to more individualistic nature of the western capitalist system, will remain necessary. It will, however, according to the trends in Western Europe, decrease significantly as the economic and political circumstances are becoming mature. Therefore, the continued analyses of the pension reform outcomes are necessary, in order to implement the future pension systems adjustments within the right extent and at the right time.

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