THE MALTA CHAMBER OF COMMERCE, ENTERPRISE AND INDUSTRY

MHRA
MALTA HOTELS & RESTAURANTS ASSOCIATION

Views and recommendations on the Strategic Review on the Adequacy, Sustainability and Social Solidarity of the Pensions System.

1. Preamble

The Malta Chamber of Commerce, Enterprise and Industry and the Malta Hotels and Restaurants Association have constantly been at the forefront of discussions when the national interest was brought to the fore. Individually and collectively they have drafted a number of reports amongst which a highly technical study entitled “Towards Sustainable Welfare Programmes and Pensions in Malta”.

The two organizations believe that the issues mentioned in this study are still valid to this day and should be seriously considered for any changes in the current system. In 2002 and 2003, the two organisations were also actively involved in their feedback to a report by the World Bank establishing the pension situation in the country. Therefore, the contents of this paper have to be seen within the context of the proposals made earlier by the employers.

This subject has already been extensively discussed over the course of the past 20 years, including the time when the new Social Security Act was published in 2006. At the time, Malta took a bold step in increasing the retirement age to 65.

With reference to the consultation process which is currently underway, the two organisations acknowledge the urgency of the situation given that the numbers do not add up. It is no secret that the Pay-As-You-Go (PAYG) system is unsustainable because the first tier adjustments are only short term measures so this needs to be supplemented by a voluntary third pillar and a mandatory second one.

2. Scenarios

The two organisatons are therefore approaching this situation rationally and with an open mind. It believes that prior to further reforms, all the stakeholders need precise information and timeframes with potential social and economic assessments. In particular, the two organisations are asking for the necessary clarifications on the precise impacts of the reform on the competitiveness of different sectors of business, especially insofar as the cost of labour is concerned. It also expects that any further changes be outlined in a blue-print with clear time-frames for business to be in a position to plan ahead for such changes. This will enable us to formulate a better view of the situation.

2.1 Current Scenario - First Tier System (PAYG)

The first-pillar has been recently modified through some parametric changes over the past years in an effort to enhance its sustainability. However, studies show that this pay-as-you-go (PAYG) system is unsustainable even if it is tweaked further. Even so, the room for manoeuvrability is extremely tight. There is a limit as to how many “parametric changes” can continue to be made to the Pay-as-You-Go System. Most of the avenues have been exhausted. To this end:

- Retirement age has already been increased to 65 – and it is arguable as to whether this can be extended any longer. Other European states have increased their retirement age to 67. In relation to this, one must look at the long term effects of indexing retirement age with life expectancy. The latest statistics are showing that in general the Maltese population is living up to the age of 79.
- National contribution rate has been raised to 10 per cent (for both employers and employees)
- Max pensionable income (ceiling) is steadily and constantly increasing (since January 2011)
- Average Pension Replacement Rate has already been significantly reduced to 40 per cent. Reducing it further could lead to significant hardship on beneficiaries if their subsistence would have to rely solely on their pension. In this regard, the two organisations enquire whether the current PAYG system will sustain the incomes and the quality of life enjoyed by today’s pensioners. In particular, it is enquired whether in the study’s assumptions of aiming at poverty line thresholds, the report is assumes the same relative level of: (i) services given by the state (eg. Health) to retirees and (ii) support provided by respective families.

- Gender Issues – Statistics show that, on average, women outlive men. It is intrinsically important that this factor is taken into the equation and see the long term effects this is having on the sustainability of the 1st Pillar.

3. *The Way Forward*

In addressing the pensions dilemma, two extremely important factors must constantly underpin the decision making process, in order to ascertain balance in this highly sensitive area of economic and social policy.

The first of these crucial factors is time. This has been mentioned in the introductory section of this paper wherein it was stated that stakeholders need a blue-print with clear time-frames and all relevant information, in order to be in a position to plan adequately for the future. The time-frames will allow both employers and employees to take the necessary steps to fall in line with the necessary changes, as well as to ensure that any commitments entered into are not rendered unsustainable or unaffordable by any policy measure decided upon and announced at a later date.

The second important element is ensuring that the matter is tackled holistically. The way forward must be charted in a holistic manner to ensure that the effects on stakeholders are well planned and complimentary rather than conflicting. The pensions dilemma is closely related to such areas as health, wage indexation, education and other areas that affect business and the economy.

3.1 Second and Third Tiers (Supplementary Pension)

In the light of the above and given the country's demographic evolution, it would seem inevitable that restoring sustainability to the pensions system requires the introduction of a (Voluntary) 3rd Pillar and if this is not adequately taken up, the (mandatory) 2nd Pillar would also need to be considered.

3.1.1 Direct Measures (3rd Pillar)

The two organisations believe that the first direct measure which can address sustainability to the local pensions system is the introduction of the third tier (i.e. voluntary pension schemes) in the short term and with the necessary safeguards.

There are a number of economic benefits associated with the introduction of the 3rd Pillar Pension. In line with theory, international experience shows that it:

a. Increases the income of individuals once they are past retirement age
b. Alleviates the financial burden on the social security system
c. Stimulates private savings and creates business activity in the Financial Services sector.

Nevertheless, the successful implementation of the 3rd Pillar requires important safeguards in that:

- It must be fully transferrable to the 2nd Pillar (in the event that this is introduced and made mandatory)
- There should be fiscal incentives to encourage people to save more and plan ahead for their pension.

It is also very important that the financial regulatory structure be strengthened to act as a credible and independent 'watchdog' to ensure that funds are being properly invested and administered.

3.1.2 Indirect Measures (2nd Pillar)

The mandatory nature of the second pillar renders its implementation less straightforward and must be considered from a different angle to the introduction of voluntary private pensions. The two organisatons acknowledge the 2nd Pillar as a further step towards achieving sustainability in the pensions system but it is not prepared to consider it unless precise details are made available to allow an exact calculation of the potential impact on the cost of labour to business.

So far, published consultation documents have not been specific about the potential impact on competitiveness particularly on the cost of labour. This information is fundamental particularly because the introduction of a 2nd pillar pension would be expected to result in direct and indirect impacts. Besides an obvious direct effect, a further indirect result would be plausibly expected once workers realise that their disposable income has diminished. Low-income households would obviously be the most affected. Clearly, the second pillar pension requires further study, consultation and negotiation before its implementation can be considered further on behalf of private employers.

Meanwhile, certain policies aimed at economic expansion can mitigate the urgency of implementing the mandatory second pillar. Policy measures aimed at increasing labour supply may help matters in this regard. For instance, the burden of social security contributions could be better spread with measures aimed at increasing female participation or at implementing a careful and selective immigration policy to fill important gaps in high-value added sectors of the local economy.

4. Concluding Remarks

The Sustainability of our Pensions System is beyond debate stage and requires the country's full and constant focus.

In designing the necessary reform, policy makers must ascertain two crucial factors in ensuring balance between the country's economic and social needs. As mentioned above, all stakeholders need a blue-print with clear time-frames and all relevant information, in order to be in a position to plan adequately for the future. The second important element is ensuring that the matter is tackled holistically in line with other social and economic policy objectives such as those related to health, wage indexation and education amongst others. Besides, whilst the reform is underway, stakeholders do not expect conflicting decisions to be taken, such as policies facilitating early retirement in the public sector.

The two organisations remain at the disposal of the authorities to continue discussing the matter as necessary in order to ensure the necessary reform is implemented with the least shocks possible to society, the economy and the business sector.