Social Security and Pensions in Lebanon: A Non-Contributory Proposal
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Upgrading Lebanon’s Economic Analytical Capacity
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Abstract:
The proportion of older adults in Lebanon is currently the highest in the region (7%). Recent projections suggest that the population over 65 years of age will constitute more than 10 percent of the population by the year 2025, similar to contemporary Europe. Yet Lebanon does not have a uniform old-age/retirement pension plan. Rather, such plans are largely dependent on the type of employment. Obviously, those who have never been employed, the majority being women, are not eligible for any type of pension plan or health care coverage.
This study provides an overview of all existing schemes in Lebanon, and studies the feasibility of a universal non-contributory social pension proposal for the elderly with several scenarios and budgetary implications, and provides the basis for a legislative proposal upon which lobbying with key policymakers will take place.

*Keywords: Social security, pensions, elderly, poverty, Lebanon, social welfare, safety nets, noncontributory, proposal.
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The project aimed to upgrade Lebanon’s economic analytical capacity by focusing on key economic and social issues facing the Lebanese society. The project empowered key public officials with the necessary skills and tools to actively engage in tackling current issues, and contribute to putting them at the center of the public policy debate scene. The project focused on two central public policy issues: 1) promoting economic stability by tackling inflation and 2) safeguarding social security and medical care for the elderly through pension reform. Thus, the project established relationships with several related public entities including ministries and public institutions, who in turn selected their representatives. These public officials were divided into two thematic working groups and underwent training, research, regular workshops and seminars to participate in the write-up of the final reports and to engage in the suggested reforms.

This report was written by Mounir Rached, Ph.D. (Public Financial Management Expert, LEA Vice President and Project Working Group Coordinator for Pensions) on the basis of inputs and research done with the valuable support of several research assistants including Mr. Nabil Abdo, Ms. Carole Kerbage, Ms. Soumaya Keynes, Mr. Mario Nassar, and Mr. Raja Sabra. The project team would also like to acknowledge the valuable inputs of Ms. Ola Sidani, Ms. Sawsan Masri and Ms. Claudia Ghanime in the working groups leading to this report.

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“Everyone, as a member of society, has the right to social security...”

(Article 22, UDHR)
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HIGHLIGHTS

WHAT IS THE PROBLEM?
1- Elderly Population is increasing

The proportion of older adults in Lebanon is currently the highest in the region. Recent projections suggest that the population over 65 years of age will constitute more than 10 percent of the population by the year 2025, similar to contemporary Europe. Yet Lebanon does not have a uniform old-age/retirement pension plan. There is widespread poverty among the elderly; over half of the elderly are ‘economically’ deprived, as they face shortages in health services, water, electricity and housing.

2- The current system excludes many elderly from basic coverage

Pension plans in Lebanon are largely dependent on the type of employment. For example, whereas government employees and those in the military service are covered by pension plans and health insurance, those covered by the National Social Security Fund- the majority of whom are employees in the private sector- ironically lose such benefits upon retirement, at the time when they are much needed. Obviously, those who have never been employed, the majority being women, are not eligible for any type of pension plan or health care coverage.

WHAT DID LEA DO?
LEA designed a project with the support of the International Development Research Center (IDRC) - Canada, to increase the capacities of a governmental team selected from related public institutions including the ministry of Finance, the ministry of labor, the ministry of social affairs, and the National Social Security fund. The team aimed to provide an economic analysis to the feasibility of a universal non-contributory social pension for the elderly in Lebanon.

The initial phase of the project included extensive training to the governmental team on public economics principles and methodologies, statistical techniques for decision making and writing policy papers. The team led by Dr. Mounir Rached from LEA held regular meetings between 2010 and 2012 to brainstorm, discuss, and analyze the new scheme. The main findings of the report include a critical revision of the current pension system in Lebanon; a socio-demographic analysis of the need for pension reform and a public financial perspective on pension reform, and a proposal for non-contributory pension schemes for the elderly with its budgetary implications and international benchmarks.

WHAT DOES LEA PROPOSE?
LEA proposes that the government pays a monthly pension to people ages 65 and above who have no other source of income. To capture this segment of the population, the team subtracted all government and military pensioners, as well as those benefiting from pensions through a syndicate (doctors, engineers, lawyers…). This portion of the elderly receives a certain percentage of the minimum wage on monthly basis without having to pay for it in return. Such scheme exists in countries with similar income levels as Lebanon (such as Brazil) and in poorer countries such as Mali.

WHAT WILL THIS NEW PLAN COST?
While there are different possible scenarios varying with the age and the generosity of the monthly payments, the average cost of such a scheme is around $ 542 million. This number is less than half the amount of annual transfers to Electricite du Liban.

This number also represents 3.6 % of our national budget and 1.2 % of GDP

AREN’T THERE EXISTING PROPOSALS FOR PENSION REFORM?
True. While new schemes are being proposed, they are all contributory in nature (i.e. they target workers who have to pay part of their income every month). This will benefit future generations as these schemes have a minimum number of years of contribution before one can
benefit (ex: 20 years). Elderly people, who are seventy and above today, will not benefit from such schemes.

**There is no existing scheme that is non-contributory under consideration.**

**WHAT WILL HAPPEN NEXT?**
LEA will start a lobbying campaign in 2013 to encourage the implementation of a non-contributory pensions scheme in an attempt to reduce poverty and improve the welfare of elderly citizens in Lebanon.

**HOW CAN YOU STAY UPDATED?**
For more information on this project, visit LEA’s website: [www.leb-econ.org](http://www.leb-econ.org)
Like “Lebanese Economic Association” on Facebook: [www.facebook.com/joinlea](http://www.facebook.com/joinlea)
Follow LEA on Twitter: #LEBECON
Videos can be found on [www.youtube.com/theleaproject](http://www.youtube.com/theleaproject)
I. Introduction

Globally, the debate to address old age social safety continues to receive central attention in both advanced and developing countries. The issue is certainly more critical for less advanced economies due to more meager means and the sheer magnitude of the numbers. It is estimated that by 2050, there will be nearly 90 Africans, Asians, and Latinos aged above 60 for each European in the same age range. This is certainly a significant spread even after accounting for population ratios.

Pensions play a key role in providing old age support, but attention has so far focused on contributory pensions. In most developing countries, the majority of older people are not covered by contributory pensions. Such schemes have been restricted to workers in the public sector, and some of those in formal employment.

Lebanon’s private social security system (National Social Security Fund-NSSF) has provided very limited services to the elderly. As you will read in chapter three, Lebanon’s social security system is based on an indemnity scheme that is terminated upon retirement and all health provisions end as well. The NSSF is thus a temporary social safety net that provides care during employment. The end of service indemnity which provides the sum of a month’s salary for every year of service does not provide the beneficiary with sufficient savings to provide security for the remainder of one’s life. The fact that all benefits end with retirement at a time when they are much needed raises concern that the current social safety net is not advanced to care for the vulnerable segment of the population.

The government, therefore, has not developed a global social safety net. Current plans are mainly dependent on the employment affiliation. Whereas government employees enjoy a generous coverage, those in the private sector have limited access to comprehensive pension and health schemes. Syndicates (such as engineers, lawyers) have set up their own pensions and health schemes that extend beyond retirement. However, this pension segment constitutes a small fraction of their average pay scale due in part to the limited self-contribution imposed by the syndicates.
The older population, and those exceeding 65 years of age, constitutes a relatively large segment of the population (about 8%), and it’s projected that its share will rise with time as has the trend been in many countries with the rise in life expectancy.

The government is considering revising the current private sector pension plan but will take many years (approximately 20) of contribution in order to have an impact and provide permanent services to a much larger population. A non-contributory plan would still be needed in order to provide coverage for the current and future gaps that are not likely to diminish before at least a number of decades. Furthermore, Lebanon as in many MENA countries has still a large number of the population that has never participated in the labor force, and certainly needs to be covered by the proposed non-contributory scheme.

The government of Lebanon has repeatedly indicated its intention to improve social and welfare services. In particular, the Paris III recovery document highlighted the government’s intention to take concrete measures to reduce poverty by improving existing social programs or introducing new ones, including considering cash transfers to poor senior citizens, female-headed poor households, and the disabled poor. Such schemes, however, could easily succumb to abuse and don’t necessarily have a significant impact on poverty alleviation as such benefits are not targeted and are temporary in nature.

In the health area, the government has contemplated adopting an optional “contributory” and subsidized scheme for the elderly but was never activated. The scheme required a contribution of 6% of the minimum monthly wage by each subscriber. The health services to be provided conform only to the second section of NSSF scheme which limits benefits to preventive treatment but does not well define treatment benefits. It also addresses disability benefits for working beneficiaries.
II. Social Security in Lebanon

1. The Existing System for the Private Sector

The design of a public pensions system depends on its primary objective, namely whether it is intended to provide individuals with insurance, or to attain a redistribution of income to the poor. Lebanon’s social security currently aims at providing insurance, rather than redistributing towards the most vulnerable. However, it faces many problems, most notably poor coverage, which means that a large proportion of the population is not even offered insurance.

In 1956 an ILO expert introduced discussion of a Lebanese social security system, following on from the international success of providing social benefits. This ultimately led to a bill in 1959, which formed the basis of current social security law, and then on the 26th of September 19631 the Lebanese social security system was established. It included four different branches:

- Health & Maternity Insurance (HMI): offers cash benefits and medical services in case of sickness.
- Family & Educational Allowances (FEA): benefits for the families of the sick to help with costs of education.
- End of Service Indemnity System (ESI): a lump-sum cash benefit, received upon retirement.
- Security of Accidents of Labor and Sickness due to Work Injury (though this branch has not yet been implemented).

This social security is only available to private-sector wage earners, non-permanent government employees and the self-employed; those working abroad and the unemployed are excluded.

1Decree 13955.
The scheme is optional for the self-employed and mandatory for the employed. Total obligatory contributions amount to 23.5% of wages, with 21.5% coming directly from the employer, and 2% from the employee. The system is funded rather than being a Pay as You Go scheme (PAYG). Contributions are made to a fund, and then benefits are allocated according to need (e.g. the HMI) or according to contributions (e.g. the ESI).

The ‘fund’ is called the National Social Security Fund (NSSF), which has financial and administrative independence, though ultimately it is controlled by the Council of Ministers (COM) and the Ministry of Labor (MoL). Its administrative hierarchy consists of: a board of directors, including representatives from the government, employers and employees; a secretariat, which enjoys executive powers; and a technical commission, which submits special reports and proposals for the development of the fund. The main four functions of the NSSF are covered sequentially below.

i. Health & Maternity Insurance:

This branch has four sub-sections: Medical Care; a Health Indemnity; a Maternity Indemnity; and a Funeral Expenses Indemnity.

*Medical Care* includes preventive and treatment services, such as medical consultations, hospitalization, medication, analysis, radiology and maternity care. The *Health Indemnity* offers insurance for nonpayment of salaries in cases of temporary absence from work for health reasons. The *Maternity Indemnity* is offered only in cases where employers do not pay for maternity leave, and finally, the Funeral Expenses Indemnity covers funeral expenses of the insured and their family members.

The HMI branch of social security operates on a funded basis, with contributions going into a fund and then paid out to individuals when they need help.

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3 The branch is governed by decree No. 14035 issued in 16/3/1970; it was lastly amended by decree No. 5101 dated 24/3/2001.
Benefit levels are set so that incentives to return to work are greater for shorter-term illnesses, i.e. generosity increases with the length of the illness. However, this means that individuals are better insured for medium-term illnesses, as they enjoy a better replacement rate if their illness lasts for more than a month.

Benefits are independent of past contributions, and so the insured are well-protected against short to medium term illness. However, those with long-term illnesses or disabilities are not covered, and neither are those who have retired. Thus the health insurance branch does not cover some of the most vulnerable individuals.

ii. Family & Education Allowances

This branch provides extra needs-based help to those with children in education, or individuals with an unemployed spouse. It is not insurance in the usual sense, as this branch represents redistribution to those who are faced with unexpected difficulties with paying for education (because of poor health). The benefit formula includes a cap of 5 children per family, so families with more than 5 children receive less help per child than smaller families.

iii. End of Service Indemnity

Coverage: Originally beneficiaries of this branch were restricted to those in agriculture, services, academia or cooperative institutions, excluding the self-employed that are usually insured by private pension schemes. With time, this list of beneficiaries was extended to incorporate new groups such as taxi drivers, newspaper and magazine vendors, and local councilors.

The group of insured defined above constitutes just 8.3% of the population, of which 70% benefit from sums deposited in their individual accounts, though families of the insured can benefit from this indemnity, and special treatment is provided to the disabled.

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4 Governed by decree No.2957 dated 20/10/1965
5 Governed by decree No.1519 dated 24/4/1965
Contributions: Employers are required to contribute 8.5% to the scheme, 8% of which goes into the employer’s account, and 0.5% of which goes to administration costs. In addition to these contributions, when employees claim their right to their indemnity, employers are obliged to add one month’s salary for every year that the employee has spent with them (up to 20 years), and 1.5 months for every year after that.

Investment: This branch is funded, so contributions are put into individual accounts, and then accrue an interest rate as determined by the investments made by the NSSF. Given that the NSSF invests most of the funds in Treasury bonds, the rate of interest is the rate that the government pays to borrow funds.

The funded nature of the scheme means that there is no redistribution across generations; the scheme only allows redistribution of resources across their own lifetimes. The ESI is clearly intended to provide insurance for its beneficiaries, rather than redistribute to the most vulnerable in society.

Eligibility: There is no specified early retirement age for the ESI, though subscribers can liquidate their indemnity at the age of 60, and are not allowed to contribute after the age of 64. For full eligibility, one should accumulate at least 20 years of service, leave work within 12 months of marriage (female earner), be affected by 50% disability, or experience death (in which case the dependents of the deceased receive six months of the minimum wage).

These contribution requirements mean that there no incentives to retire before the age of 60, though it also means that there are disincentives to move into employment not covered by the ESI scheme.

Generosity: A key feature of this branch is that it is a lump-sum payment, payable once an individual reaches retirement. After this one-off payment, the fund has no more financial obligations to the individual, as there are no more pensions to be paid out, and health insurance eligibility is lost. This system means that individuals bear all of the risk of living for longer than they expect (the risk of longevity), as there is
no opportunity for the ESI to increase with the number of an individual’s post-retirement years.

As benefits are related to past earnings and contributions, the scheme is directed towards providing insurance and a good replacement rate for retirement. There are no supplements for those with insufficient contributions to guarantee a decent standard of living post-retirement, so there is little redistribution taking place.

2. Problems with the Existing System
   i. Problems with the NSSF

There is some disagreement over whether the fund should be considered as independent or a public sector entity. This has contributed to legislative vagueness, particularly with respect to the relationship between the NSSF and the Ministry of Labor, as well as between the main NSSF fund and its sub-funds.6

In addition to this problem, it has been claimed that the fund has relatively high administration costs and low productivity; a 2001 ministerial committee report found overstaffing of 25-30%, and an international comparison of costs per employee revealed that NSSF employees were overpaid.7

In 1990 the devaluation of the Lebanese Pound meant that the social security reserves of the NSSF lost their value. In an attempt to improve its financial position, the NSSF responded by investing in Treasury bonds. A report by the world bank called the reliance of the pension system on Lebanese treasury bonds ‘excessive’ (Robalino, 2005), and it should be noted that by investing so heavily in government bonds, the pension system is implicitly financing government loans and allowing the government to accumulate debt (the Lebanese debt-to-GDP ratio is one of the highest in the region).

7 Antoine Wakim, AlNahar Newspaper, 10 December 2001; P. 3
However, despite this investment decision, the NSSF’s financial difficulties persisted due to deficits in both the HMI and FEA branches, and also the government failing to meet its obligations to cover 25% of the HMI expenses.

Even if the government were to pay its debt to the NSSF, the financial state of the fund would remain risky, which exposes its 200,000 beneficiaries and more than 470 thousand insured. This is mainly due to a reduction in contribution rates implemented in April 2001, which led to continuous budget deficits being generated by both the Health and Maternity and Family Allowances branches.

In 2009, the FEA branch had a total debt of LBP 307 billion, and although there was growth in the HMI branch’s revenue of 44.42%, expenditures still exceeded revenues, leading to debt of LBP 316 billion.

Indeed, the only sub-fund generating positive reserves is the ESI branch, which in 2010, recorded a total of 6400 million LBP worth of reserves. These positive reserves are not really surpluses, as they should be seen alongside the considerable liabilities of the ESI fund, from individuals expecting pension funds after they retire.

The law grants financial independence to sub-funds, so deficits of the Health and Maternity and Family Allowances branches are being unlawfully covered by surpluses generated by the End of Service Indemnity sub-fund - LBP 623 billion were reallocated in year 2009.

This goes against the financial independence of the branches, and also introduces extra risks into the system. The deficits in both the FEA and HMI branches indicate a lack of sustainability, but currently this problem is being hidden by the ESI’s subsidization. As well as discouraging reform to make the system more sustainable, this exposes all those supposedly covered by the ESI scheme to a shortfall in their retirement funds.

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8 Adnan Al Hajj, As-safir, 4 October 2010
Problems with the ESI

The ESI was never meant to become a permanent scheme for protection of the elderly. The following is a list of its key flaws, which draws on those listed by an ILO report on the Lebanese Social Security System:

Coverage is limited, leaving large proportions of the population exposed to risk in their retirement.

- After retirement subscribers (and their families) lose their health insurance, just when they are most in need of it.
- Employers face a large burden from required contributions to the scheme, and the dependence of benefits on earnings provides employers the incentive to pay their employees in the form of bonuses or non-cash benefits rather than a permanent salary increases. This means that the final pension may not reflect an individual’s lifetime earnings, and the replacement rate may be low.
- Benefit levels are insufficient to provide a decent retirement, as they are low relative to the cost of living.
- The indemnity paid is in one installment, which does minimize administration costs, but also allows people to spend it without creating security for the future.
- A distinction should be made here between preferences and “myopia”. If individuals prefer to ‘live for today, rather than smoothing out consumption over their lifetimes, then the one-off payment is efficient as it allows these individuals to spend the money at whatever time they want.
- However, the one-off payment is inefficient if people spend their money today rather than tomorrow--not because this is their preference. In this case it would be more efficient for the government to protect people against themselves by staggering out pension payments.
The lump-sum payment means that individuals are not automatically protected from the risk of inflation and longevity – if they are constrained and don’t have access to good saving instruments then the lump-sum payment represents an inefficient method as the government could save for individuals more effectively.

3. Other Social Security in Lebanon

The Civil Service and Military Pension Schemes—public sector pension

Civil servants and those in the military in Lebanon are covered by a generous (but unsustainable) pension scheme. With expenditures on civil servant pensions at 1.2% of GDP, and spending on military pensions at 2% of GDP, this scheme is a significant component of existing Lebanese social security cost.

Public employees pay contributions of 6% of their wages, which are in turn paid directly to the retired population, i.e. the scheme follows the PAYG method. The government is ultimately responsible for covering any shortfall of funds, i.e. the taxpayer bears the risk of demographic change or an unsustainable benefit formula.

There is no minimum age for retirement (indeed, there are few penalties for early retirement, leading to weak incentives to stay in work later in life), instead individuals must have made at least 20 years of contribution to the scheme.

Military pensions are more generous than those of civil servants, with an accrual benefit rate of 2.66% compared to 2.13% for civil servants. This accrual rate is fixed and not linked to expected or actual return rates on investment. The implicit rates of return from contributions are considered unsustainable by multiple reports from the World Bank, in particular as the population ages, unless there is a dramatic reduction in the benefits in both the civil s and military schemes.

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There is no minimum pension, but the maximum replacement rate is 85% of the final salary (which penalizes those workers whose salaries peak in the middle of their careers). Individuals can either choose a lump-sum pension or a permanent pension paid in monthly installments. A married couple receiving both a military and civil service pension cannot both opt to receive their pension in the same form.

If an individual chooses to receive his/her pension in monthly installments, then the spouse pensioner is obliged to receive his/her pension in a lump sum form.

**Lebanese Universities**

The Lebanese American University, University Saint Joseph, Notre Dame University and Balamand University all require contributions of 5-11% of the employee’s earnings, depending on the number of years served or the level of their salary. The American University of Beirut (AUB) pension plan requires a relatively higher contribution of 15%, though this is still low relative to the ESI’s 23.5%. The AUB in the meantime covers the administrative cost of its program.

These pension schemes are typically funded, with investment of the funds delegated to private insurance companies. Defined benefits rather than defined contributions are preferred, with only one of the universities choosing to make benefits depend purely on the contributions in the fund and the interests earned (and thus expose contributors to asset return risk). The others make retirement benefits depend on the last earned salary and the number of years of service, and thus guarantee a particular replacement rate in retirement.

Some universities require a minimum of 5 years of consecutive service for eligibility. Lebanese universities offer many other subsidized benefits, including life insurance and disability benefits, with no extra fees required. The four non-AUB universities all pay $2,000-4,000 of funeral expenses for their members, as well as educational allowances for both high school and university education. These universities also purchase health insurance from private insurance companies, and subsidize their employees’ premiums by up to 100%.
Syndicates’ schemes

Nearly, all private major syndicates such as lawyers, engineers, physicians, pharmacists, and others have set up their social security schemes. These schemes provide health coverage and a regular pension payment following retirement. Their coverage is extended to the dependent family members. They have been successful in attaining the main objectives of the schemes: primarily providing a minimum permanent social protection to the members and their dependents. The scheme is optional and allows subscription by Lebanese residents and non-residents as long as they fulfill their membership requirements in the syndicates, which is primarily to be licensed to practice their profession in Lebanon. All syndicates schemes are of the defined contribution type. The health service rendered to subscribers and their dependents forms the main incentive to enroll. The pension component is commensurate with the low contribution set for the permanent pension. The government earmarks collection from legal services toward the lawyers syndicate fund. But in general most of the contribution toward funding these schemes id born by membership.

i. The Order of Engineers and Architects in Beirut and Tripoli

The purpose of the fund is to provide a pension for the Lebanese engineers who are no longer working, due to old age or sickness, as well as for their families after their death.

Each member who reaches sixty years of age is entitled, as per his request, to benefit from a full pension if the number of years of his enrollment in the Order amounted to twenty-five years at least. If the number of years is less than twenty-five, the pension he is entitled to is then part of the full retirement, and is calculated as the ratio of his years of enrollment over twenty-five; he is not entitled to the pension in case his registration falls short of twenty-five years.

Each member who has been enrolled in the Order for thirty years has the right to benefit, as per his request too, from the full retirement pension, even if he did not reach the age of sixty.

The member is not entitled to retire before at least 15 years of the actual enrollment in the Fund.
The Ordinary General Assembly determines the monthly retirement pension based on the Fund Management Committee’s proposal and the approval of the Order’s Council.

Each engineer who is a member of the retirement fund and who has a permanent sickness or a disability that prevents him from resuming the engineering practice, has the right to benefit upon his request from a partial retirement pension - in case his enrollment years in the Order was not less than fifteen years.

The pension, which the deceased retired engineer benefited from, or the retirement pension that the deceased engineer could have benefited from, had he been liquidated at the date of his death, is passed on to his family, according to what is specified in the following articles, and the right holder members of the family of the deceased refer to:

1- His wife or wives.
2- Legitimate children, acknowledged children and adopted children, at least ten years prior to the maturity of the pension, of which males under eighteen years of age and females under twenty one years of age.
3- His parents, in case they have no other provider than the deceased engineer.

The right holders, members of the family of the deceased engineer, are granted the following pensions:

1- For the wife or wives, one third of the salary of the deceased, divided equally among them.
2- For the children no matter what their number is, the third of the salary of the deceased, divided equally among them.
3- For each parent, one twelfth of the pension.

The right of the engineer’s widow to the pension is lapsed following death or marriage, and her share is transferred equally to her beneficiary children. In case she does not have any, the share is returned to the retirement fund.

The right of the underage sons is lapsed following death or when they are eighteen years old, and in case they are unable to work, once this inability disappears, and if they are studying, once these studies are finished, or when they are twenty-three years old.
The right of the daughters is lapsed following death, when they are twenty-one years old or when they get married, and in case they are unable to work, once this inability disappears, and if they are studying, once these studies are finished, or when they are twenty-eight years old.

The lapsed share of the child returns to the retirement fund.

The right of the parents is lapsed following death, whereby the share of the deceased parent returns to the surviving parent. When both parents are deceased, their shares are returned to the retirement fund.

The death of one of the beneficiaries of the deceased’s retirement pension prior to its maturity does not deprive, from his share, those who were entitled to it in the event where the death occurred after the maturity of his retirement pension.

The beneficiaries’ retirement pension is exchanged, in case they live abroad, according to the international regulations applicable in such cases.

**Beirut and Tripoli Associations**

Every Lebanese lawyer who is above sixty years of age and who has been enrolled in the association he belongs to for at least thirty years can benefit from the retirement pension provided that he requests to go into retirement. The internship period is included within the practice period up to three years at most, unlike the period during which the lawyer abstains from practice.

Every Lebanese lawyer, who has been enrolled in Beirut or Tripoli Association for at least fifteen years and had a permanent disability that prevented him from practicing law or any other profession.

As for the lawyer who has been enrolled in the Association for less than fifteen years and had a permanent disability that prevented him from practicing law or any other profession, benefits from one fifteenth of the retirement pension for each year of law practice.

The Lebanese family of the deceased lawyer, who are:

- His legitimate non-divorced wife or wives.
- His legitimate sons who are not 18 years of age yet, who have a permanent disability that prevents them from working or who are
successfully pursuing education in an educational institution, are not 25 years of age yet and do not have a paid job.

- His legitimate single daughters who do not have any paid jobs.

- Either his parents or one of them, in case they did not have any other provider other than the deceased lawyer.

- His single sister who still lives with him, who has no other provider and does not have any paid jobs.

**Will not benefit:**

- The lawyer who was permanently removed from the Association by virtue of a disciplinary decision.

- The lawyer who was enrolled past the age of forty-five is exempt from retirement fees.

The Fund Management Committee sets the retirement pension by virtue of a resolution taken by the majority of seven votes from the Beirut Association and four votes from the Tripoli Association, according to the Fund’s capabilities.

The Retirement Committee may, by the said majority and within the said capabilities, increase the retirement pension or decrease it in case of deficit.

No beneficiary, whose pension is decreased due to the reason mentioned in the previous paragraph, is entitled to object or claim any right due to this decrease.

The retirement pension is paid once at the end of every three months.

The retirement pensions may not exceed the annual Fund revenues.

**The Army, Internal Security Forces and Public Security Cooperatives**

A subsidy, set by virtue of a decree adopted by the Council of Ministers, can be granted to the Army, Internal Security Forces and Public Security Cooperatives. As long as these cooperatives provided for the dependents on their subscribers the same health services provided by the cooperative of government employees to the dependents on its members, provided that the members of the said cooperatives contribute to their
funding as much as the members of the cooperative of government employees contribute in return for these services.

The decree sets the amount of subsidy by a percentage of the members of these cooperatives that is equal to the percentage estimated from the subsidy granted by the government to the employees’ cooperative for these health services.

**Private school’s solidarity and pension funds**

Private schools have set up their own optional pension and health scheme. The scheme has two components: an indemnity and a health scheme similar to that of the NSSF, however, the indemnity can be converted into a regular pension.

The indemnity entitlements pay a lump sum at the end of service. The indemnity provides one month salary for each of the first 10 years and 2 months for each of following 20 years, and three month salary for each year beyond the first 30 years.

The pension scheme provides persons with regular payment after serving for at least 30 years. The pension then amounts to 85% of the last salary.

The indemnity/pension plan is being financed by a 6% of salary direct contribution by members, and an equivalent 6% contribution by the school.

The solidarity fund, on the other hand, is a health and services plan. It comprises 11 benefits that are health services related such as hospital bills, medical consultations, and preventive medical services; in addition it provides other family support services such as maternal support, marriage grants, educational loans etc.

**Informal Insurance**

It is important to consider those who do not have access to the End of Service Indemnity or any other kind of social insurance. When they reach retirement they will only have their own savings to survive on, or any help available from their families. A 2007 study showed that the chances of an elderly person living on their own in Lebanon increased with wealth. The study showed that most of the elderly derive much of their income
from transfers from their children (74.8%), with a relatively small share derived from pension schemes.\textsuperscript{10} This is to be expected in the absence of state safety nets.

4. Effectiveness of the Existing NSSF System

Nowhere in the present system is there any redistribution between individuals, other than through the subsidization of the HMI and FEA branches by the ESI branch. The fully funded accounts mean that individuals are allowed to redistribute resources across their own lifetimes, but there are no transfers from the rich to the poor in the current scheme. Indirectly, a transfer is implied when additional taxes are levied to cover any shortfall in the scheme.

In addition to criticizing the poor coverage rate of the current scheme, the ILO has stated that the replacement rate provided is too low to provide a decent standard of living at retirement. Furthermore, the withdrawal of health insurance upon reaching retirement leaves a considerable proportion of the population exposed to health risks.

5. Need for Reform

It is clear that the existing social security in Lebanon is inadequate. There is widespread poverty among the elderly; over half of the elderly are ‘economically’ deprived, as they face shortages in health services, water, electricity and housing (see figure 1).

The expected demographic change, with the elderly population rising, implies that social protection could deteriorate overtime. With the oldest demographic structure in the region the elderly dependency ratio in 2010 was 11%, and is projected to increase to 17% by 2030 (Robalino, 2005).13

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12 The ratio of over-65s to those aged 15-64.
13 http://data.un.org/
1965 law asserted that the ESI is just a temporary measure, and should be used for the transition between the ‘Indemnity Payment’ and a proper old-age pension. However, the ESI is still in place today, despite widespread economic vulnerability among the elderly. The ESI does not protect many of the elderly against poverty, though it is unclear whether the figures presented below arise from poor coverage or low generosity of the ESI scheme. Whatever the case may be, there is a clear need for reform.

Percentage of deprived elderly according to the living conditions index and its fields by sex 2004 (%)

III. System Transition: Attempts at Reform

In 2004 and 2011 there were attempts aimed at reforming the existing social security system. Draft bills were presented to parliament to substitute the ESI with a pension scheme, though neither of these bills has yet been ratified.

1.2004 Draft Bill

In 2001, the office of the Prime Minister initiated work on a draft pension bill and appointed an overseer committee from the MoL, which included representatives of local employers and employees. This committee produced the 2004 bill, which, proposed changes to the insurance component of the ESI, as well as two key redistributive measures.
The first was a flat indemnity payment to individuals who have not made enough contributions to the scheme, and the second was a minimum pension for those who had made sufficient contributions, but whose accounts had not accumulated enough funds for a decent retirement. This marked a clear change from the previous system, where contributors were not protected against the risk of poor earnings, longevity risk, or unemployment, and there was no redistribution.

It was proposed that this safety net would be financed by an extra 2% contribution of those earning between 10 and 20 times the minimum wage. Thus the scheme would redistribute from people in this income bracket to the poor. The proposal did not include an extension of the scheme’s coverage, so those in the informal sector would still have no available social security.

Other proposed reforms included the transformation of the lump-sum payment into an annuity, but with the option of receiving 10% of the sum in the account as a lump-sum transfer upon retirement. Those who had made less than 20 years of contribution would still receive a lump sum indemnity, equal to the amount in their accounts. Overall contributions toward the new scheme would be lowered to 17.5% of wages (12.5% from employers, and 5% from employees).

This system would be self-financed, and the annuity feature would reduce the impact of longevity risk on the elderly. However, administrative costs relative to the old system would be increased, and there would be a large burden on employees as they would be forced to settle all accounts before the implementation of the new regime. Individuals would still be exposed to the risk of poor asset returns, as there would be no guarantee of a particular replacement rate. Thus, it is unclear that the new scheme would be much better at achieving the insurance goal than the original one.
2. The Response of the ILO

In 2003 the Lebanese government requested the International Labor Organization’s (ILO) help to evaluate the draft bill proposed by the pension committee. The ILO responded by issuing a report entitled *Analysis of the Draft Bill Concerning Retirement, Pension Reform & Alternative Solutions*.

Building on its core principles, the ILO made several remarks on the 2004 proposal. They were critical of the capitalized individual accounts, as these are against their principle of solidarity, and they criticized the limited coverage of the adjusted scheme, which was far from their ideal of a universal safety net. They believed that the minimum number of 20 years of contribution was too high, and that 15 years should be sufficient for pension eligibility.

Their report noted that there would be few incentives for private fund managers to insure those on low wages, i.e. they would not have the incentive to protect the most vulnerable members of society. Furthermore, the report questioned the ability of Lebanese financial infrastructure to be able to cope with the investment of the funds, pointing to the underdevelopment of the life annuity market in Lebanon.

Instead of maintaining the system of capitalized accounts, the ILO suggested implementing a ‘notional accounts’ system. This is essentially a PAYG system, where the working population pays for the benefits of the retired, however any contribution made by a working individual would be put into a ‘virtual account’, and their final pension would correspond to the accumulated sum in this account. Benefits could be automatically adjusted to ensure financial sustainability, and there would be no massive fund to be invested, which would help to restore fiscal imbalance and decrease investment risks for contributors.

Finally, although the report commended the minimum pension scheme, the proposal was criticized as being too vague about the replacement rate for those receiving the minimum pension.
In response to these criticisms, the government changed parts of the proposal, though nothing major with respect to the redistributional branch. An amended draft bill was approved by the council of ministers in 2004 and referred to Parliament for study.

What was changed?

The World Bank was called to help Parliament study the 2004 bill, and its recommendations led to disputes between political parties that ultimately halted voting on the bill.

3. 2011 Draft Bill

5 years later, the MoL restarted the debate on the ESI and the need to substitute it with a pension plan and in 2010 submitted a draft proposal to Parliament.

The Ministry arranged for an agreement between different parties on the specifications of the proposed scheme, particularly between the ILO and WB, though there was still some opposition to the proposal, from groups such as the General Labor Union.

The proposal outlined the adoption of a “Notional Defined Contribution” system; where individuals pay contributions from their salary and fund the benefits of the retired population. Each individual has a ‘notional account’, and upon retirement, beneficiaries receive at least 40% of their wages after contributing 30 years to the scheme, so benefits correspond to contributions.

To protect the value of contributions from inflation and other risks, and to ensure a fair benefit formula, a real (but ‘notional’, as the funds are not actually being invested) 2% annual rate of return is granted, along with an annual inflation-proofing measure equal to the rate of inflation as computed by the Central Administration of Statistics. Contribution rates depend on actuarial studies, to ensure sustainability, and any funds that do not go directly towards benefit payments should be invested in treasury bonds.
The plan suggested three extra features: a continuation of medical insurance for pensioners after their retirement, to be covered by the Health and Maternity branch; a contributory minimum wage, to be specified to ensure sustainability according to actuarial studies; and finally the establishment of non-contributory pension scheme covering all citizens. In this final scheme there would be no contributions, instead the system would be funded through taxation.

This third feature is the focus of this paper. By introducing a universal non-contributory pension scheme, Lebanon would be moving away from a system of pure insurance to one of redistribution and protection for the most vulnerable groups in society. However, there are many choices over the precise design of such a scheme, which will have to depend on how closely one subscribes to either the WB or the ILO’s principles, and of course the Lebanese economy and demographic structure.

4. Systems overlap

It’s quite clear that Lebanon is experiencing a multiplicity and overlapping systems that stems from the ineffectiveness and inefficiencies existing in the public sector social security. Even the public sector is lacking a unified system. Substantial resources are being wasted due to unrealized economies of scale in the current systems. Management cost of the spending, collection and of the funds (reserves) must carry a large burden on the economy.

For instance, all syndicates provide health services even before retirement overlap with the provisions of the NSSF. The main incentive for the private initiative to emerge is the inability of the public sector to provide for members after retirement.

A lack of consensus among different professions on provisions and cost probably has led to a surge in numerous private sector social security schemes. There is no
evidence also that the various schemes have attempted to unify certain services to benefit from scale economies such as health insurance, asset management etc.

A non-contributory pension and health schemes could save substantial resources. It can also be realized at a much lower cost to the government by encompassing the existing private systems. The private sector contributions to their own schemes could be channeled to a unified scheme through a restructured tax system or even an earmarked tax. For an employed person joining more than one scheme the combined cost born by the employer and the contribution of the employee is reaching 35 percent of income; the highest in the world and at the same time the least efficient.

IV. Benchmarks

International practices in pension schemes could provide some benchmarks for contributory and non-contributory schemes in other countries and their relative merits. Common problems faced by governments around the world are aging populations, underdeveloped financial sectors, and unsustainable benefit formulas. The following should help to highlight where governments have made mistakes in the past, so that these difficulties may be avoided in Lebanon, and an efficient, sustainable and flexible minimum income scheme may be designed.

Although the main focus in this report is on non-contributory schemes, we will examine international social security schemes and how they use contributory schemes to offer protection to their populations. These examples illustrate the wide coverage some countries have managed to achieve, and how, with time, Lebanon might hope to achieve protection through a similar system. Furthermore, some countries have merged contributory and non-contributory schemes in order to provide a more comprehensive social coverage. Contributory schemes could as well provide guidelines to the services and the system set up. Both schemes should be essentially structured in a similar manner. With contributory social security being more synoptic and have served a
broader social security objective, it could provide a good insight into structuring a non-contributory pension scheme. After all, the striking divergence is the cost and financing. Non-contributory plans tend to be based on the objective of realizing a safety net rather than a saving scheme.

1. Key Contributory Pension System Features

This section provides a brief discussion of some key features of pension systems, and then an overview of factors to be considered in pension design.

i. Funded vs. Unfunded

A pay as you go system relies on intergenerational redistribution, as the young can pass on the gains from their higher wages or incomes to the old. The PAYG schemes are, therefore, perceived to attain redistribution and equity objectives. This is in accordance with the ILO’s principle of solidarity, as the gains from growth should be distributed across society. Of course, with an ageing population, this is made much harder as the number of dependents rises relative to the number of contributors, thus a funded system is less vulnerable to demographic change than an unfunded system.

Transition between the two schemes becomes cumbersome, particularly from a PAYG to a funded scheme. The transition would expose a large group of the elderly who had never saved for retirement, in anticipation of receiving benefits from the working population. They would not be covered by a funded scheme, so there must be some interim payment, requiring those working to pay for the pensions of the retired as well as their own pensions.

A PAYG system has been criticized on the grounds that it leads to a lower aggregate savings than in a funded system, as contributions are
transformed directly into benefits. This might, in turn, lead to less capital formation than the case with a funded system, where contributions could have been invested. Funded systems have as well provided a cushion to government financing as in the case of Lebanon. The Lebanese NSSF is almost totally invested in government bonds.

**ii. Defined Benefit vs. Defined Contribution**

A defined benefit scheme leaves individuals vulnerable to earnings risk, whereas defined contribution schemes expose individuals to asset return risk. Accordingly, defined contribution schemes are usually supplemented by a minimum income component, which gives individuals more protection against earnings’ risk and redistributes to the poorest elderly, thus combining the insurance and redistribution objectives.

Defined contribution schemes are less vulnerable to problems of unsustainability as payments can be closely linked to available funds, whereas defined benefit schemes can lead to a large imbalance between assets and liabilities if the benefit formula is too generous\(^\text{14}\).

A system of ‘notional accounts’ is a defined contribution scheme, as individuals make contributions into virtual accounts and then get a return on these based on what is sustainable for the pensions scheme. This approach provides one solution to the problem of un-sustainability, as sustainability can be factored into the benefit calculation formula.

**iii. Actuarial vs. Non-actuarial**

\(^\text{14}\) It is possible for defined contribution schemes to be unsustainable, e.g. if the benefit formula is too generous and the return promised is too high. However, with a defined benefit system, the government makes a promise to individuals that their pensions will be a certain level, so that if funds fall short they are forced to raise contributions from the working population. It is clear that demographic risk falls on the working age population rather than the pension population.
Whether a pension scheme is actuarial or non-actuarial has two main different meanings. One refers to the financial sustainability of the scheme (on the macro level), and the other refers to the relationship between contributions and benefits (on the micro level). Here we shall focus on the micro-level definition, i.e. the labor market distortions arising from the scheme.

In an entirely non-actuarial model, benefits would be a flat-rate, and would not change depending on when retirement occurred. The marginal rate of return to an individual’s contributions would be zero, though with a fully funded system the average rate of return would be equal to the market interest rate. In contrast, in an actuarially fair model, the marginal and average rates of return would be equal, thus minimizing labor market distortions and incentives to retire early.

Non-actuarial features of many European pension systems have faced financial problems, as the incentive to retire early is embedded within the benefit formula, while effective penalties penalize those deferring retirement (see Gruber, 1997a). Though one must be careful to minimize distortions, it should be noted that even though an actuarially fair system may be more efficient in its insurance provision, as the possibilities for redistribution could be limited.

Most countries therefore choose a combination of the two, with a minimum income component supplemented by a contribution related component, so that there is a positive marginal rate of return for all but the worst off in society.

The minimum component in a non-actuarial scheme carries similarities to a non-contributory pension scheme as both ensure a minimum of social security.

iv. Other Pension Features
There are many other features that contribute to the design of a public pensions system. The list below gives details of many of the options available to a pension designer. It should be noted that many countries have multiple components in their pension scheme, for example a contributory one designed for the general public and a non-contributory one designed for the neediest in society. Thus the features listed below can be combined so that one pension scheme can fulfill several different objectives.

<table>
<thead>
<tr>
<th>Components of the Pension Scheme</th>
<th>Design Options</th>
</tr>
</thead>
<tbody>
<tr>
<td>How are contributions made?</td>
<td>• employers/employees make social security contributions</td>
</tr>
<tr>
<td></td>
<td>• general taxation</td>
</tr>
<tr>
<td>What happens to these contributions?</td>
<td>• <strong>Funded:</strong> they are invested by the government/an autonomous organization/private bodies to get the market rate of return.</td>
</tr>
<tr>
<td></td>
<td>• <strong>Unfunded:</strong> contributions/taxes are converted straight into benefits.</td>
</tr>
<tr>
<td>Who is covered?</td>
<td>• <strong>universal:</strong> residence/nationality requirements</td>
</tr>
<tr>
<td></td>
<td>• only employees of the public/private sector are covered</td>
</tr>
<tr>
<td></td>
<td>• sector-specific schemes</td>
</tr>
<tr>
<td></td>
<td>• spouses/families of the insured</td>
</tr>
<tr>
<td>Who is eligible for benefits?</td>
<td>• those passing a means-test</td>
</tr>
<tr>
<td></td>
<td>• those with sufficient contribution/earnings history</td>
</tr>
<tr>
<td></td>
<td>• those older than a certain age</td>
</tr>
<tr>
<td>How generous are benefits?</td>
<td>• <strong>defined benefit:</strong> generosity depends on earnings</td>
</tr>
<tr>
<td></td>
<td>• <strong>defined contribution:</strong> generosity depends on past contributions</td>
</tr>
<tr>
<td></td>
<td>• contributions, with some rate of return, which might depend on prices, wages, or a factor maintaining the sustainability of the scheme</td>
</tr>
<tr>
<td></td>
<td>• benefits might be adjusted for periods of unemployment, sickness</td>
</tr>
</tbody>
</table>
or maternity leave
- minimum income component
- supplements for dependants
- non-cash benefits alongside the basic pension, e.g. healthcare

Coverage decisions should be made bearing in mind how different groups will be affected by the decisions. For example women and long-term unemployed will be less likely to satisfy earnings/contribution requirements, though they are perhaps most vulnerable to poverty in old age. The more fragmented the coverage, the harder it will be for individuals to move professions and retain their pension, and the greater the overall administrative costs.

Having a means-tested component of the pension scheme involves careful targeting, costly administration, and has the potential to become very complicated. Furthermore, an asset test may induce under-saving, as individuals change their behavior to become eligible for benefits.

Finally, the age of eligibility should depend on the average age of withdrawal from the labor force, as well as the average length of time spent in full retirement – and this will have a significant impact on the overall cost of the scheme.

The benefit formula will depend on the aims of the pension scheme, and could be constrained by financial sustainability requirements. Decisions about who exactly is meant to be covered by the scheme, how the scheme is funded, whether it is actuarially fair and whether it is defined benefit or defined contribution will all influence how benefits are calculated.

Non-cash benefits such as healthcare are clearly more important where free healthcare is not already available. Offering health insurance through a pension scheme could solve some of the adverse selection problems
faced by the elderly, though this could add to the value of the pension dramatically, both in terms of the cost and also in terms of incentives for individuals to gain eligibility.

2. European Experience

Even though European schemes could be clearly seen as prioritizing either redistribution or insurance when they were first implemented, over time they have combined different pension scheme features to offer a decent replacement post-retirement rate to the rich, as well as protection to the most vulnerable.

Typically there are several ‘pillars’ to European pension schemes. The first is a non-contributory (means-tested) flat benefit. Its primary objective being redistribution (providing social security), which is the basis of the “Beveridgian” welfare state. The second pillar is a mandatory contributory benefit offering earnings-related benefits, i.e. offering benefits closer to social insurance. The third pillar is a voluntary pension supplement, whereby individuals can choose to contribute more and get a higher pension. Finally, the fourth pillar encompasses the private sector. The government might subsidize private pension plans by offering tax deductions or simply make the public pension scheme less attractive than those offered by the private sector.

The following exposes the experiences on the experiences of several European countries (Germany, Sweden, Poland and Austria), that are traditionally closer to the “Bismarckian” (insurance scheme) than the “Beveridgean” system.

i. Coverage

The dominance of the formal sector in Europe means that it is not difficult for European pension schemes to achieve universal coverage.

It is standard for all employees to be covered by a mandatory public pension scheme, though some groups with their own occupational pension schemes are exempt (e.g. in Poland where there are special
schemes for soldiers, prosecutors and judges). There are usually different rules for the self-employed, as obviously they don’t have the benefit of employer contributions. Whereas national pension schemes generally do not have residency requirements, those with guaranteed minimum incomes do (e.g. Sweden requires a minimum residency of 40 years). Reducing coverage is an obvious way to reduce the burden on government finances, as is done by Sweden through requiring a longer period of residence for eligibility for the earnings-related scheme. There is some welfare loss with such tightening as vulnerable groups can lose coverage. Overall coverage decisions depend on the purpose of the pension scheme; if the intention is social insurance and the smoothing of income into retirement, then it is less sensible to restrict eligibility far beyond minimum contribution requirements.

A pension system that is integrated across sectors has the advantage of facilitating labor mobility, as individuals will not lose their pension if they move from the public to the private sector. Developed institutions allow this mobility throughout the EU, as either the job type has no implications for the pension administration, the pensions can be transferred directly, or the old pension can be realized as a lump-sum and then reinvested according to the new plan.

**ii. Contributions**

Contributions as a percentage of income hover around the 20% mark, and they split fairly evenly between employers and employees. Lebanon’s contribution rate is still relatively high at 23.5%, compared to Germany’s overall rate of 19.9% and 22.8% in Austria, though not compared to Italy’s rate of 33% of gross wages. It should be noted that mandatory contributions to public pension schemes are often supplemented by contributions to a voluntary ‘pillar’.
This reflects trust in the managing institutions to invest funds efficiently, thus providing a strong incentive to save for retirement. In the countries being considered there is no widespread tax evasion, particularly in comparison to many developing countries. Although Eastern European countries had problems in their transition period in the 1990s, today, in countries such as Poland and others, governments has been able to generate sufficient revenue.

iii. Investment

Nearly all European pension schemes have a PAYG component for their public pension scheme. Whereas a country like the UK, which is closer to the “Beveridgian” model, relies entirely on the PAYG method of financing public pensions. Countries like Sweden rely on a combination of PAYG and a funded system. Often the PAYG branch of a pension system is aimed at redistribution, whereas private or occupational (funded) pension plans are aimed at providing a decent post-retirement replacement rate.

Funded pension schemes require a developed financial infrastructure, as well as an investment body (or bodies) to ensure a decent return on individuals’ contributions. Within the European countries being considered, financial markets are highly developed, and have developed advanced private schemes offering attractive alternatives (and complements) to public pensions.

In both Sweden and Poland there are funded components of the pensions system, though the funded component is relatively more significant in Poland. In Poland, employees contribute 9.76% of the gross wage, with 7.3% going to an individual pension account. These accounts are managed by specialized pension fund companies, which are regulated to guarantee minimum returns and not to expose the fund-holders to
excessive risk. Here the private sector is responsible for generating return on investments. Alternatively, the funds can be managed by a centralized body, as in Sweden. 2.5% of taxable income is contributed to a funded pension scheme, though individuals can choose who controls the account. The choice is between a fund managed by an independent fund manager and an investment fund managed by the ‘Seventh National Swedish Pension Fund’ (AP7). At the beginning of 2008, just under 30% of assets invested in this way were managed by the AP7, showing that the public investment body can be a viable alternative to smaller independent bodies.

One of the European solutions to the fiscal burden placed on public pension schemes has been to encourage reliance on the private sector. In Germany, although having a private/occupational pension is not mandatory, the government offers tax breaks on such occupational and private pensions. The promotion of the private pension schemes was intended to offset reductions in the generosity of the public sector pensions, and accordingly the tax breaks were only offered for funds offering annualized rather than lump-sum payments. The incentives include both tax relief and subsidies to saving. While Borsch-Supan and Wilkes (2003) assess that the emphasis on the private sector will sufficiently compensate younger cohorts, they claim that older generations will not be so lucky. Thus increased emphasis on the private sector is a long-term rather than a short-term solution.

iv. Eligibility

For most unfunded European pension schemes, there are minimum contribution requirements. In Poland there are two pension schemes, one with no guaranteed minimum pension, for which there are no minimum contribution requirements (but benefits are still defined contributions), and another with a guaranteed minimum pension where eligibility
requires 25 insurance years (20 for women). The insurance period is not necessarily made up of periods of continuous employment, as time on maternity leave, sickness benefit and even unemployment benefits all count towards the overall insurance period. However, these ‘non-contributory’ periods can make up a maximum of a third of the overall insurance period. Similarly, Austria requires 180 ‘insurance months’ (15 insurance years), 84 of which must be from employment. In Germany eligibility is less stringent by this measure, as only 5 years of contributions are required for eligibility, while Sweden provides the broadest coverage as it offers the earnings related pension with no minimum contribution threshold, although eligibility for the minimum income scheme does require a minimum of 40 years of residence.

For defined contribution schemes, minimum contributions are less important than for those with defined benefits. The tighter the eligibility criteria for the contributory scheme the broader the coverage of the non-contributory scheme, as generally those not covered by the contributory scheme will have low income.

The choices of minimum contribution requirements often involve an element of arbitrariness, but should be chosen bearing in mind the average labor force attachment over the life cycle. Men usually have more ‘insurance years’ by the time they reach retirement age than women, and accordingly most countries have a lower minimum contribution for women.

An important factor in the design of any pension scheme is the expected number of pension years an individual will draw. The population of the EU is aging quickly as life expectancies are rising and birth rates are falling. In the 10 years between 1996 and 2006, the life expectancy for German males increased from 73.6 to 77.2 and from 76.6 to 78.8 for Swedish men. This reflects trends both for women and men and across
the EU (Source: Euro stat). In response to the increased burden this has placed on the pension scheme finances, the retirement age has been increased from 65 to 67 (e.g. in Germany), and the retirement age for women has been increased to be in line with the male retirement age (e.g. in Germany and Sweden).

In notional accounts systems in Poland, Italy and Sweden, the life expectancy is automatically taken into account when calculating the return on investments. whereas in other unfunded systems, when there is demographic change the administering agency has discretion regarding how to maintain sustainability. A major advantage of the notional accounts scheme is that the political decision of reducing generosity in response to a demographic change is made much easier.

Deferred retirement schemes have been a major problem for many European pension systems, as actuarial unfairness has led to in-built penalties for later retirement. Consequently, many countries have adjusted their benefit formula so that there are appropriate reductions in benefits should an employee decide to retire early. In Poland early retirement is being phased out entirely.

v. Generosity

The more actuarially fair a pension scheme is, the lower the opportunities for intra-generational redistribution. At the bottom of the income/contribution scale, benefits are usually less closely related to earnings or contributions, as countries impose a guaranteed minimum on those who satisfy the contribution requirements but who have had such low lifetime earnings that their retirement income would be below the subsistence level. This is the case in Austria, Poland and Sweden, but not Germany, where minimum income benefits can be applied to supplement a public pension. Reform across the EU has been moving to more
actuarially fair benefits in order to encourage individuals to retire later and thus reduce the financial burden of the pension system.

Whereas the normal pension generosity does not change with dependents in Sweden, Poland, Austria or Germany, in Austria the minimum pension level increases if someone has a spouse or children under the age of 18 to support. This disconnection between household size and benefit generosity reflects the purpose of the pension scheme to insure the individual rather than the household. Means-tested minimum income benefits for the elderly are oriented to the household and therefore benefits change according to the family structure; though in Germany each individual in a household applies in their own right.

Recently several countries are either shifting or considering shifting from defined benefit to defined contribution pension plans, a transition that generally harms those who have an unequal earning distribution throughout their lifetimes (benefits go from being related to the best X years of income to all income), or a regularly interrupted work history. The transitions of Italy and Sweden from defined benefit to defined contribution notional accounts pension systems are the most extreme examples of this case. The case of Greece is less extreme, which in 2005 changed its reference calculation so that for those insured after 1993, the earnings of the 5 years before retirement were taken into account, whereas those insured before 1993 were able to choose the best 5 of the last 10 pre-retirement years. Clearly, the longer the reference period of earnings, the less progressive the scheme becomes.

3. **Experiences in MENA Countries**

It is useful to look at other countries in the Middle East and North Africa, as societal norms as well as the role of the state are closer to Lebanon than in European countries. As with the analysis of contributory schemes in European
countries, the discussion of MENA pension schemes shall be broken down into the following components: contributions; coverage; investment; eligibility; and generosity.

i. Coverage

Coverage tends to be poor in MENA countries due to the size of the informal sector. Normally pensions are related to earnings or wages, but this is clearly impossible in the informal sector. This means that in case pension benefits are funded through taxation, for example from VAT, then a formal sector pension scheme penalizes the informal sector. This is because those in the informal sector will effectively be paying for the pensions of those in the formal sector. A universal pension system would reduce this imbalance, as those in both sectors would receive benefits.

No MENA country offers a pension to the unemployed, and most don't have schemes to cover the self-employed. Only a few countries have tried to tackle these low effective coverage rates, such as Tunisia, which has as many as 10 different pension schemes for different groups, including students, Tunisians working abroad, artists, intellectuals, and low income earners such as domestic workers, persons employed in the public sector and not covered by another scheme. Although Tunisia has offered a solution to low coverage rates, the many different pension schemes have led to fragmentation across different occupations. This has the potential to negatively affect labor mobility between sectors, and makes redistribution across sectors more difficult.

Jordan is another example, where there is a mandatory public (PAYG) pension system, which is supplemented by voluntary occupational and personal pension arrangements (though the latter two are small and undeveloped). The PAYG system is compulsory for those in the military, civil servants, and employees of companies that employ more than 5
workers. This leaves a large proportion of uncovered citizens, only 55% of the working population was covered in the ‘00s (Lowe, 2009). Although there is low coverage, these rates are comparable to other countries with similar economic performance, such as the case for coverage in Tunisia and Egypt. However, countries such as Morocco, Iran and Yemen, which have no compulsory pension schemes for employers or the self-employed, have much worse coverage than other countries with similar economic performance (Loewe, 2009).

MENA countries are notable, in contrast to European countries, in that they do not rely on resource-tested schemes, where the vulnerable are targeted. The lack of availability of formal pensions for large proportions of the vulnerable means that social protection often takes place through informal mechanisms such as family structures. However, increased migration both abroad and from rural to urban areas mean that in many cases these family structures are becoming weaker, and formal pension schemes are becoming more important.

ii. Contributions

Employees, employers and the government contribute to public pension funds throughout MENA countries, with rates ranging from 11.9% in Morocco to 25% in Kuwait, and the burden is split between employees and employers, but with employers bearing a larger proportion of the pension cost (91% in Lebanon). Private pension schemes are relatively undeveloped, due to weak financial infrastructure and the generosity of public pension schemes (Demarco, 2010). Therefore, even though there is sometimes the opportunity to make voluntary contributions to a private pension scheme, public schemes dominate.

Even with a mandatory public pension scheme, low monitoring may result in individuals not contributing to their pension plan. For example,
in Egypt enrolment is compulsory for all workers, however just over half actually make contributions. Some do not understand that their employers do not make the contributions for them, or else they do not know how to contribute (Demarco, 2010).

In Egypt, Jordan and Saudi Arabia, the state covers any possible deficit of the pension system, so tax payers fund any shortfalls, usually via VAT. This means that tax-payers bear any risk of demographic change or any other risk that would result in a shortfall in funds. Also, since the average taxpayer is poorer than the average pension recipient (due to coverage being restricted to specific occupations in the formal sector), this implies that the scheme contributes to a redistribution from the poor to the rich.

iii. Investment

The PAYG method of funding is favored throughout the region, though many pension schemes have ‘buffer funds’ in case of a shortfall. These public pension reserves can be extremely large, for example in Jordan, Egypt and Morocco where public pension reserves are around a third of GDP. Despite these large buffer funds, aging populations throughout the region will soon place heavy burdens on benefit levels, as the ratio of contributors to dependents falls.

The dominance of the public sector and the lack of developed financial infrastructure mean that in MENA countries public entities are mostly in charge of investing any surpluses. One exception is in Egypt, which recently implemented a compulsory funded pension component managed by private managers, though the public sector still dominates. A recent WB publication (Demarco, 2010) states that having a funded pension scheme would not itself increase saving, though it should encourage development of financial infrastructure, which would encourage development.
Pension funds are largely invested in treasury bonds, with Jordan being a key exception, where over 60% of pension wealth is invested in equities. In other MENA countries, buying treasury bonds means that the public pension funds are implicitly financing government debt. This, strains the funds’ liquidity in case of a shortfall as governments may not be able to secure alternative financing.

The rates of return on contributions promised by governments are rarely sustainable, as shown in figure 2 below:

**Figure 2. Implicit rates of return on contributions of mandatory pension schemes in MENA**

![Graph showing implicit rates of return](image)

Source: Robalino (2005)

Although Lebanon has one of the most unsustainable implicit rates of return, a tiny minority of pension schemes in the region offer rates that are below the long term sustainable level. This illustrates the urgent need for reform in the region, as raising taxation to fund the imminent shortfall redistributes from the poor to the rich, as noted above.

iv. Eligibility

Eligibility conditions for full pension withdrawal include a minimum number of contribution-months, as well as a minimum age of retirement. This minimum age is often far below the ‘normal’ age, as for example in Jordan, where the ‘normal’ age is 60, the minimum age is 45 for men and
35 for women, and the minimum number of contribution-months is 180 (15 years).

Often there are no monetary penalties for early retirement, for example if the upper limit on contributions is reached. In Jordan, for a male at the age of 45, the internal rate of return on his contributions is estimated at 7%, but it declines steadily to 3% for males retiring at 70 (Loewe, 2009). This implies that, in the later stages of their working lives, individuals are provided with fewer incentives to remain employed (Robalino, 2005). The withdrawal of health insurance in Lebanon is an example of one such incentive, though it is unclear that it is a main reason for withdrawal, particularly as there are clearly more efficient ways of offering such incentives.

v. Generosity

It is widely recognized that pension schemes in MENA countries are overly generous and unsustainable in the long run. An international comparison of replacement rates (below) reveals that MENA countries offer the highest relative standard of living in retirement compared to OECD countries, Eastern and Central Africa, and Latin America and the Caribbean. This not only crowds out private sector pension provision, but also indicates that individuals have little incentive to save for retirement, leaving populations exposed to the risk of pension funds depletion.

<table>
<thead>
<tr>
<th>Earnings level</th>
<th>MENA</th>
<th>OECD</th>
<th>ECA</th>
<th>LAC</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low</td>
<td>81.3</td>
<td>74.6</td>
<td>63.7</td>
<td>77.7</td>
</tr>
<tr>
<td>Average</td>
<td>77.9</td>
<td>56.4</td>
<td>56.4</td>
<td>57.2</td>
</tr>
<tr>
<td>High</td>
<td>75.7</td>
<td>46.4</td>
<td>50.4</td>
<td>48.3</td>
</tr>
</tbody>
</table>


Even though there are high replacement rates, in many countries pension levels are not automatically adjusted for changes in the cost of living or
wage inflation. Only in Tunisia, Algeria and Yemen pensions are updated according to changes in wages or public sector employee pay. This leaves pensioners throughout the region exposed to changes in the cost of living, and limits the redistributive objective pension schemes.

Most pension schemes supplement their earnings/contribution with a minimum income component, though two different approaches are employed. The first subscribes to Beveridgean principles of redistribution, and benefits are a percentage of the minimum wage (as in the case Syria and Tunisia). The alternative fits better with Bismarkian insurance, and the minimum pension is set to be a percentage of the last wage earned (as in Jordan and Egypt where it’s set at 50%). This is to protect individuals against the risk of insufficient lifetime earnings, and to ensure a sufficient income in retirement.

In a report on pensions in the region, the World Bank stated that minimum pension levels should be related to the poverty line, and chosen according to assistance available from family structures, as well as affordability. The graph below from the report clearly shows minimum pension levels are far above the general poverty line, thus reducing incentives for individuals to save to meet their subsistence needs in retirement.
V. Non-contributory pension schemes

1. Poverty Reduction Impact of Non-contributory Pensions

All evidence suggests that a large number of the elderly in developing countries has no access to pensions and are either poor or at risk of poverty. As the percentage of the world’s elderly in developing countries increases, the risk of poverty increases as well. The poverty rates for single elderly men range from 20% in Tajikistan to 63% in Bulgaria. The poverty rates for single elderly women range from 18% in Tajikistan to 69% in Peru. For elderly couples, the lowest poverty is in Panama at 14%, with the highest in Peru at 53%. The elderly who live in larger households are less likely to be poor than elder-only households, ranging from 19% in Nepal to 32% in Nicaragua. The comparison between multi-generational households with elderly and households with no elderly shows that with the exception of Panama, household with elderly are generally poorer than nonelderly households, with the poverty rates being anywhere from 1% to 29% higher in households with elderly. The elderly get even poorer when they are deprived of a pension income. Other studies have shown similar results. In Malaysia

A well-designed non-contributory pension scheme has a number of advantages and has proven effective in reducing poverty and ameliorating living conditions of the vulnerable segment of the population and the elderly poor in particular. Non-contributory pensions are more likely to provide adequate protection for low-income and poor rural residents and be effective in reducing old-age poverty in rural areas.

For example, in 2002, Argentina’s non-contributory pension program reduced the household poverty rate by 31 percent below what it would have been without that pension and the extreme household poverty rate by 67 percent (Bertranou & Grushka, 2002). Similarly, in Costa Rica, nearly 15 percent of beneficiaries were able to measurably improve their economic status due to the additional income provided by the country’s social pension plan (Duran-Valverde, 2002). Based on evidence from other developing countries, a non-contributory pension would help alleviate rural poverty, increase the status of older people within the family, and promote political stability (Shen & Williamson, 2006).
The Bonosol in Bolivia was a godsend for the poor. It is well-known that intra-family safety nets can fail, especially when entire families live in poverty. Martinez (2004), estimated that rural households increased their consumption of food on average by nearly 165% of the value of the Bonol grant. This multiplier effect is possible because families in rural areas are able to invest the Bonosol in animal stock and vegetable gardens. In urban areas, the effect on food consumption is smaller and the effect on non-food consumption higher. The World Bank and the Inter-American Development Bank concluded that the Bonosol scheme had a strong redistributive effect with minimum fiscal impact.

Brazil’s social security had a substantial positive income redistribution effect in a country with one of the highest income concentration rates in the world. The states in the northeast of Brazil benefit from the social security expenditure scheme (INSS).

Two independent studies, carried out in 1998 (Schwarzer, 2000), in the state of Pará (Delgado and Cardoso, 2000) and in the Brazilian Northeast and South) showed that for 80 to 90 percent of rural beneficiaries’ households, social security benefits were responsible for at least 50 percent of the monetary household income.

This leverage effect on the monetary household income has numerous consequences:

1) *Poverty alleviation*. The rural pension scheme significantly contributed to poverty prevention and reduction as is demonstrated when households with access to rural benefits are compared with those without. In the three southern states, for example, only 14.3 per cent of the households of rural social security beneficiaries is below the exogenous (natural) poverty line of one-half of an official minimum wage per capita family income. If an endogenous poverty lines applied (i.e. adjusted for local prices), then only 0.4 per cent of the households of rural beneficiaries suffer from extreme poverty, 8.8 per cent are in poverty, and 2.7 per cent are just able to meet the very basic needs for all household members with the available income. The remaining 88.1 per cent of households have an income surplus, which is spent on agricultural production and on the improvement of living standards within the household (Delgado/Cardoso Jr. 2000).
2) Access to and substitution of social services. The social security benefit partly replaced or improved access to further social services. The monetary income allows the aged and the disabled to afford private, less precarious medical services in urban areas, which very often are not available in quantity or quality in the substandard public health care facilities in rural areas and small municipalities. The additional income also enables the beneficiaries to buy medicine, normally lacking in the public free health care service. It is noteworthy that expenditure for medical services and pharmaceutical products is an important part of the beneficiaries’ household budgets.

3) Quality of life. Receiving social security benefits dramatically improves the quality of life of the household members. The income allows the acquisition of household appliances such as refrigerators, televisions, dish antennas, and the like. Moreover, households with monetary income are able to afford the installation of electricity cables in their land, the payment of an electricity bill, and may even have access to telephone services. (Schwarzer, 2000)

4) Housing improvement. The monetary income also allows the improvement of the beneficiaries’ residences since the needed materials—bricks, tiles, sanitary facilities, etc.—are now affordable. The rural pensioners’ residences are usually among the best houses in the village (Schwarzer, 2000)

5) Agricultural development. As Brazil moved away from agricultural development policy instruments during the 1990s, the importance of pensions as a safety net for the peasant economy increased. Regular income, independent of the weather—unlike the income from agricultural production—allowed the acquisition of working instruments, seeds, and the capitalization of the family production units, offering a basis on which the rural peasant economy subsisted throughout the decade.
6) Reduced rural-urban migration. All the aforementioned positive consequences prevented further migration to large cities. During the field research in the state of Pará, stories were often told about persons who were eager to leave major crisis-prone urban centers and return to rural areas, where they frequently found support from relatives who receive a social security benefit.

7) Changes in social roles. The fact of receiving a social security benefit redefined the role of the aged within the household and the rural communities in Brazil. The redefinition is particularly evident in the case of women, who now have an income source of their own. Although aged women continue living with their children, the relationship is qualitatively different. It is also important to stress that instead of an erosion of family ties, the family solidarity has usually been strengthened under this non-contributory pension scheme. (Rocha, 2000 and Delgado/Cardoso Jr. 2000)

8) Regional income redistribution. For a large number of municipalities and even states in Brazil, the rural pension scheme had a strong regional income redistribution function. In approximately 40 per cent of Para’s municipalities, for example, the volume of income transfers to families via social security is larger than the fiscal equalization transfers received by the respective municipal administrations from the official Federal and regional funds (the “Fundo de Participação de Municípios” and the “Cota-Parte do ICMS”) (Schwarzer, 2000).

9) Support of the local economy. The pension income transfers support the local economy. The beneficiaries receive their monthly pension on schedule at a commercial bank or at the post office, in accordance with a payment scale. On pay day the beneficiaries purchase the goods needed for the month and pay back the granted loans. The electronic banking card that each beneficiary receives is often used as a proof of creditworthiness, since retired workers are among the few persons in small villages that can count on a regular income. Therefore, pension payday is when the wheel of the local economy goes
round in rural Brazil. Several firms are viable only because of the income transferred by social security. The commercial banks are a special case. Banks are remunerated for the payment service by social Security. Their branches in small towns quite frequently depend on this remuneration to be profitable and keep open.

Without banking infrastructure, local economic development would face great difficulties in accessing rural credit and development programs sponsored by the Government. (Schwarzer 2000a).

**TABLE 4: Poverty headcount and gap measures with and without non-contributory pension income (using adult equivalent household income per capita)**

<table>
<thead>
<tr>
<th></th>
<th>Brazil (n=3523)</th>
<th>South Africa (n=5560)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>With Pension</td>
<td>Without Pension</td>
</tr>
<tr>
<td>Poverty Headcount</td>
<td>58.5</td>
<td>63.9</td>
</tr>
<tr>
<td>Poverty Gap as % of Poverty Line</td>
<td>22.3</td>
<td>30.0</td>
</tr>
<tr>
<td>Indigence Headcount</td>
<td>22</td>
<td>30.9</td>
</tr>
<tr>
<td>Indigence Gap as % of Indigence Line</td>
<td>5.1</td>
<td>12.7</td>
</tr>
</tbody>
</table>

In a comparative study of Brazil and South Africa, Help Age International Concluded that in the absence of non-contributory pension income, and assuming no off-setting effects, the poverty headcount and gap in the two countries increases (table 4). In the absence of non-contributory pension income, the poverty headcount among members of households with older people would be 5.3 percentage points higher in Brazil and 1.9 percentage points higher in South Africa. In the same situation, the indigence headcount would be 8.9 percentage points higher in Brazil, and 2.3 percentage points higher in South Africa. The poverty gap would be a third larger in Brazil, and two-thirds larger for South Africa, if the non-contributory pension income is removed and the indigence gap would be 1.5 times larger in Brazil and one-fifth larger in South Africa. More
detailed analysis showed the impact to be greatest for the poorer households. The result also identifies the impact of non-contributory pensions on the probability of becoming poor, in a multivariate setting that controlled for other factors. The analysis showed that having a non-contributory pension recipient in the household reduces the probability of poverty among household members by 21 per cent in the Brazilian sample, and by 11 per cent in the South African sample.

Several authors have supported the positive impact of a minimum pension on poverty. Professor Pestieau (2010) has shown a significant decline in poverty in a broad sample of Latin American countries. His data shows a decline from 55 to 13 percent in Argentina, from 52 to 6 percent in Brazil, and from 51 to 8 percent in Uruguay.

2. Country Practices

Countries have adopted a number of variants of non-contributory pensions including the universal pensions, means-tested, residence based, and social assistance pensions. Some developing and middle income countries were a head in considering protection within a non-contributory framework rooted in theories of socioeconomic and social development. It was foreseen as an effective policy intervention to help reduce household poverty and vulnerability. Today there is an emerging consensus that non-contributory pensions have the potential advantage of reaching vulnerable groups with relatively low administrative and overall cost.

Universality

Some governments (very few-Bolivia and Botswana) opted for universal pensions especially when targeting is constrained by many elements. Universal pensions have some advantages relative to targeted pensions especially when a country lacks adequate resources to implement a sophisticated targeting process. A major impediment to universal pensions is the higher cost of government contribution toward the pension while in the mean time the administrative cost has declined. A pragmatic way to assess
Universality feasibility is to implement cost/benefit analysis of alternative schemes. For instance, the additional cost of universal pension (payments to any residing person 65+) has to be compared to the incremental benefit accrued from targeting. In many developing countries the absence of reliable data may seriously handicap the process of filtering.

A country may as well follow a simple universality rule that precludes those who benefit from other pensions, in particular public pensions of civil servants. This has been tested for Lebanon (see following chapter) and preliminary calculations show a cost decline of 24 percent. Elimination of civil service pension recipients shouldn’t be costly and can be available from the data base of the ministry of finance.

Universal pensions form a lesser administrative challenge for developing countries, but it is important to keep in mind that any pension scheme requires, at a minimum, evidence of age and proof that a beneficiary is still alive. Non-universal schemes require additional information, such as a record of earnings and contributions, or knowledge of current assets and income; this increases administrative cost and increases may encourage fraud.

Universality’s other benefits as well may preclude the immersion in extended debates on how to determine beneficiaries. The eligibility issues have retarded, and in many cases blocked the implementation of social pensions in many countries. It also precludes corruption and circumvention of the system.

Universal pensions are less common than other pension schemes. At present, they exist only in eight countries: New Zealand, Mauritius, Namibia, Botswana, Bolivia, Nepal, Samoa and Brunei. Only one country on this list (New Zealand) is a high-income country. Bolivia is the poorest country in South America and Nepal is one of the poorest countries on the planet. The other five countries are developing economies of Africa and Asia, with modest per capita incomes. The preponderance of low-income countries in this sample suggests the importance of administrative simplicity and lack of reliable data needed to execute a targeted plan.

In each country, applying a universal pension, an eligibility criteria was drawn where pensions are paid to all who meet age, residency and (in four counties) citizenship requirements, regardless of other income they receive or assets they own. The qualifying age is 60 years in Mauritius and Namibia, 75 years in Nepal and 65 years in the other three countries. New Zealand requires pensioners to have completed at least 10 years of residency in the country, and Mauritius requires 12 years (15 if the resident is not also a citizen of Mauritius). Bolivia requires applicants to have been citizens residing in Bolivia on 31 December 1995. Other countries in the group require only citizenship and current residency, in addition to the age requirement.

The proportion of the population in these countries that satisfy the age requirement for a pension ranges from a low of 1.1% in Nepal to a high of 12% in New Zealand. Pensions reach only 77% of the age qualified population in Nepal, despite the supposed universality of the program. There are a number of reasons for low take-up of pensions in Nepal, including difficulties in establishing proof of age, delays in processing applications, difficulties in reaching remote areas of the country, and the fact that some of the relatively wealthy do not bother to apply for a pension. At the other extreme, Mauritius and Bolivia record apparent rates of coverage of 103% and 105% respectively.

Namibia’s post-independence pension program suffered at first from low coverage and from fraudulent claims. It was not uncommon for children and grandchildren to collect pensions of parents and grandparents up to ten years after the death of a pensioner (Subbarao, 1998, p. 15). Following outsourcing of cash payments to private firms in 1996, the incidence of fraud decreased, and coverage has increased to what one researcher (Schleberger 2002, p. 7) estimates
as “above 95 percent. Old age pensioners in Botswana initially numbered 84,000, an apparent coverage of 117%. The number fell to 71,000 by 1999 due to better controls on age certification.

Administrative costs are well below 5% of transfers in five of the six countries with universal pensions. The exception is in Namibia, where administrative costs as a proportion of pension payments increased from an already high 18% to 27% when cash payments were outsourced in 1996. Costs are high for two reasons. Fraud, outright theft and administrative cost are the primary reasons.

Relative to per capita GDP, universal pensions are most generous in New Zealand (46% of per capita GDP for a single pensioner, 70% for an elderly couple), followed by Bolivia (26% of GDP). The basic pensions, at 16% of per capita GDP, are less generous in Mauritius and Namibia, but are adequate to ensure that few experience extreme poverty or deprivation in old age. Mauritius provides exceptionally generous pensions (60% and 68% of per capita GDP) to residents older than 90 or 100 years of age. The pensions in Botswana and Nepal at 10% of per capita GDP are clearly inadequate. The modest size of the pension in Nepal may explain why one survey of pensioners in that country found that one in seven continued to work, even though all were 75 years of age or older (Palacios and Rajan, 2004, p. 18).

The total transfer of income to the aged via the universal pension ranges from a tiny 0.08% of GDP in Nepal to half a percent in Botswana, approximately one percent in Namibia and Bolivia, 1.66% in Mauritius and 4.32% in New Zealand. Five of the six countries, finance their universal pension from general government revenue. The tax burden on the non-aged population is less than the pension transfers because many pensioners are also taxpayers. Only New Zealand taxes pension receipts as part of its global income tax.

There are other ways to reduce costs while preserving the universality of a pension system.

The revenue requirement (as a proportion of GDP) of universal pensions is equal to the product of two variables: the proportion of the population eligible for pensions times the ratio of the flat pension to per capita GDP. The first can be reduced by increasing the age of eligibility; the second by decreasing the generosity of the pension. New Zealand some years ago adjusted both parameters in order to reduce the cost of its universal pensions. In 1989 the Government reduced the pension floor for a couple from 80% to 65% of the average wage and indexed
pensions by prices alone until the new, lower floor was reached. At the same time, over ten
years New Zealand gradually increased the age of entitlement from 60 to 65, completing the
process in 2001. With these adjustments, the share of public pensions in GDP fell from nearly 8
per cent to less than 5 per cent within a decade (See Preston, 2001, pp. 16-18).

Table 5 provides some estimates of the cost of providing a universal pension of $1 per day to
those above age 60, 65, 70 and 75 in 40 African countries. The numbers range from a low of .01%
of GDP in Seychelles to a high of 17% of GDP in Ethiopia. The high numbers are driven by the
percentage of elderly in a country, with the older countries costing more, and by the relative
generosity of $1 per day when compared to the per capita GDP in many counties.

<table>
<thead>
<tr>
<th>Country</th>
<th>60+</th>
<th>65+</th>
<th>70+</th>
<th>75+</th>
<th>Pension/GDP per capita</th>
</tr>
</thead>
<tbody>
<tr>
<td>Angola</td>
<td>2.4%</td>
<td>1.5%</td>
<td>0.9%</td>
<td>0.4%</td>
<td>77%</td>
</tr>
<tr>
<td>Benin</td>
<td>4.3%</td>
<td>2.8%</td>
<td>1.7%</td>
<td>0.1%</td>
<td>11%</td>
</tr>
<tr>
<td>Burkina Faso</td>
<td>7.3%</td>
<td>4.5%</td>
<td>2.4%</td>
<td>1.1%</td>
<td>155%</td>
</tr>
<tr>
<td>Burundi</td>
<td>14.3%</td>
<td>9.5%</td>
<td>5.9%</td>
<td>3.1%</td>
<td>225%</td>
</tr>
<tr>
<td>Cameroon</td>
<td>3.6%</td>
<td>2.3%</td>
<td>1.4%</td>
<td>0.7%</td>
<td>60%</td>
</tr>
<tr>
<td>Comoros</td>
<td>4.2%</td>
<td>2.3%</td>
<td>0.7%</td>
<td>0.7%</td>
<td>84%</td>
</tr>
<tr>
<td>Congo</td>
<td>1.8%</td>
<td>1.2%</td>
<td>0.7%</td>
<td>0.3%</td>
<td>37%</td>
</tr>
<tr>
<td>Cote d’Ivoire</td>
<td>2.5%</td>
<td>1.5%</td>
<td>0.8%</td>
<td>0.4%</td>
<td>51%</td>
</tr>
<tr>
<td>Gabon</td>
<td>0.8%</td>
<td>0.5%</td>
<td>0.3%</td>
<td>0.2%</td>
<td>8%</td>
</tr>
<tr>
<td>Ghana</td>
<td>8.8%</td>
<td>6.0%</td>
<td>4.1%</td>
<td>2.4%</td>
<td>97%</td>
</tr>
<tr>
<td>Guinea</td>
<td>3.7%</td>
<td>2.3%</td>
<td>1.3%</td>
<td>0.6%</td>
<td>65%</td>
</tr>
<tr>
<td>Guinea-Bissau</td>
<td>12.5%</td>
<td>7.8%</td>
<td>4.4%</td>
<td>2.0%</td>
<td>156%</td>
</tr>
<tr>
<td>Kenya</td>
<td>4.3%</td>
<td>2.8%</td>
<td>1.7%</td>
<td>0.8%</td>
<td>109%</td>
</tr>
<tr>
<td>Lesotho</td>
<td>5.6%</td>
<td>3.6%</td>
<td>2.1%</td>
<td>1.1%</td>
<td>75%</td>
</tr>
<tr>
<td>Country</td>
<td>6.7%</td>
<td>4.2%</td>
<td>2.4%</td>
<td>1.2%</td>
<td>249%</td>
</tr>
<tr>
<td>-----------------</td>
<td>------</td>
<td>------</td>
<td>------</td>
<td>------</td>
<td>------</td>
</tr>
<tr>
<td>Madagascar</td>
<td>8.3%</td>
<td>5.4%</td>
<td>3.2%</td>
<td>1.7%</td>
<td>142%</td>
</tr>
<tr>
<td>Mali</td>
<td>0.9%</td>
<td>0.6%</td>
<td>0.4%</td>
<td>0.2%</td>
<td>10%</td>
</tr>
<tr>
<td>Mozambique</td>
<td>9.2%</td>
<td>6.3%</td>
<td>3.8%</td>
<td>1.8%</td>
<td>250%</td>
</tr>
<tr>
<td>Namibia</td>
<td>1.0%</td>
<td>0.7%</td>
<td>0.4%</td>
<td>0.2%</td>
<td>16/5</td>
</tr>
<tr>
<td>Niger</td>
<td>8.2%</td>
<td>5.1%</td>
<td>1.6%</td>
<td>0.7%</td>
<td>144%</td>
</tr>
<tr>
<td>Rwanda</td>
<td>5.4%</td>
<td>3.2%</td>
<td>1.7%</td>
<td>0.7%</td>
<td>182%</td>
</tr>
<tr>
<td>Senegal</td>
<td>3.5%</td>
<td>2.1%</td>
<td>1.1%</td>
<td>0.5%</td>
<td>68%</td>
</tr>
<tr>
<td>Seychelles</td>
<td>0.1%</td>
<td>0.1%</td>
<td>0.1%</td>
<td>0.1%</td>
<td>5%</td>
</tr>
<tr>
<td>Sierra Leone</td>
<td>12.2%</td>
<td>7.2%</td>
<td>3.6%</td>
<td>1.6%</td>
<td>190%</td>
</tr>
<tr>
<td>Sudan</td>
<td>5.0%</td>
<td>3.1%</td>
<td>1.7%</td>
<td>0.8%</td>
<td>n.a.</td>
</tr>
<tr>
<td>Swaziland</td>
<td>1.4%</td>
<td>0.8%</td>
<td>0.5%</td>
<td>0.3%</td>
<td>26%</td>
</tr>
<tr>
<td>Tanzania</td>
<td>5.1%</td>
<td>3.1%</td>
<td>1.7%</td>
<td>0.8%</td>
<td>206%</td>
</tr>
<tr>
<td>The Gambia</td>
<td>6.0%</td>
<td>3.7%</td>
<td>1.8%</td>
<td>0.9%</td>
<td>106%</td>
</tr>
<tr>
<td>Uganda</td>
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<td>2.5%</td>
<td>1.3%</td>
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<td>122%</td>
</tr>
<tr>
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<td>1.4%</td>
<td>0.7%</td>
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</tr>
<tr>
<td>Zimbabwe</td>
<td>2.5%</td>
<td>1.6%</td>
<td>0.9%</td>
<td>0.5%</td>
<td>56%</td>
</tr>
</tbody>
</table>

Source: Schwarz, Anita, Old Age Security and Social Reform, May 2003 (mimeograph)

The last column shows the value of a dollar a day with respect to per capita GDP in each country. Countries have to decide whether in an environment of scarce resources, so much of GDP should be spent on the elderly in comparison with other age groups, particularly since not all of this expenditure is going toward achieving poverty relief.

Altering the amount of the pension and raising the age of eligibility may be sufficient to make the universal pension option affordable in most countries at least for the medium term. In the long term, as the cost rises due to population aging, the amount of the pension could be held constant in real terms while GDP continues rising, which allows the system to continue
reducing absolute poverty though poverty among the elderly relative to other age groups could increase.

**Eligibility Criteria**

Eligibility has been at the heart of the elderly pension debate. There are many pros and cons for each of the several criteria that are considered by countries as we have seen in the previous review of country cases. Often, the ideal choice will no doubt depend on several factors, budget constraint, institutional set up, data, social factors, and so on. We enumerate below the most common eligibility criteria. It aims at guiding authorities in selecting the most plausible and feasible criteria deemed to serve the poverty reduction objective which is, after all, the raison d’être of non-contributory elderly pension schemes.

**Means-Tested Social Pensions:**

A means test is based on verifying whether potential beneficiaries possess adequate means to support themselves and what amount of payment, if any, they may qualify for. The means are considered as any income incurred to a person and property (except your own home) or an asset that could provide an income.

A non-contributory old-age pensions can be structured to be means-tested (e.g., South Africa, India) instead of being universal based on a flat-rate scheme (e.g., Bolivia, Botswana). Means-tested pensions are intended to be reserved for those who have a level of income below a threshold level, such as the poverty line or minimum wage.

For most low-income developing countries, one major disadvantage of a means-tested pension is that it requires a substantial level of administrative capacity often lacking in rural areas, including ways to maintain reliable and accurate records of individual income (Van Ginneken, 2003; Overbye, 2005). The means-tested approach is also criticized for its greater vulnerability to corruption, as local level bureaucrats are often able to exercise discretionary power in determining who is deemed eligible to receive the pension. For example, in Brazil in the late
1970s and early 1980s, local politicians often issued documents required for applying for a pension benefit in exchange for votes in the rural areas (Schwarzer & Querino, 2002).

In general, in many low-income developing nations, there are serious problems associated with the means-testing alternative often linked to low administrative capacity, corruption, and paucity of data.

One concern often mentioned by critics of universal pension schemes is that, with uniform benefits and unequal incomes throughout a country, what may be viewed as a reasonable pension benefit by poor rural workers will seem negligible for more affluent workers, particularly those in urban areas. This could undercut popular support for such programs. In many developing nations, a minority of the population pays the general tax typically used to finance universal non-contributory pension schemes. As a result, those paying for the program generally do not expect to benefit in any significant way from it, a condition that can threaten its political feasibility (James, 2000).

Another major complaint against a means-tested pension points to its negative effects on those with incomes close to the cut-off point for eligibility. Evidence suggests that it tends to discourage them from saving, or continuing to work in paid employment, out of fear of losing their pension (Willmore, 2007). In addition, if administrative costs are taken into account in an effort to exclude the few relatively affluent rural elders in these low-income countries, the resources saved are often quite modest (Shen & Williamson, 2006; Heslop, 2002; Johnson & Williamson, 2006).

The issue of contribution avoidance, rather than evasion, is also relevant when the level of the noncontributory pension is so high that it encourages people to avoid contributions. A good example is that of Uruguay where the minimum contributory pension at age 65 after 35 years of service is below that of the non-contributory pension
available at age 70. Why would anyone want to contribute? Consequently, contribution compliance is relatively low in Uruguay.

However, the experience of several countries with means-tested programs for the elderly is that the political support for these programs is limited and their budgets either disappear over time or become diverted to other political purposes. Examples include that of Turkey where a means-tested benefit of 300 Turkish liras per month for the elderly has been in place for many years, despite several years of 100% inflation resulting in monthly pensions worth far less than a penny.

In Argentina, a limited budget for noncontributory pensions has increasingly been used for political pensions, so that by 2000, less than half of the noncontributory pensions were based on poverty and the value of the pensions for poverty relief was below that for the political pensions, resulting in well more than half the budget allocated for other purposes. In 1989, 59% of noncontributory pensioners were poor elderly or disabled. By 2000, only 32% of the noncontributory pensioners fell within this category. As a result, the program resulted in a reduction in poverty of only 0.5%.

In many cases, the requirements are not considered so onerous that individuals cannot comply with them, but there are other cases where applying becomes too costly particularly where bureaucrats demand bribes in order to process the paperwork, as in India. In developed countries, the elderly frequently do not seem to take advantage of the benefits offered to them, particularly when means-tested. The experience from other countries seems to suggest that when the pension is broadly means-tested such that a large percentage of the population receives it, take-up is not an issue, but when a small percentage of people get it, and then take-up is a significant issue.

Another issue that authorities need to guard against is the possibility of fraud. If people are able to receive pensions through fraud, it undermines the fairness of the system. Thus, in addition to the costs of means testing, the public agency also needs to expend resources on fraud control which could have been spent paying benefits.
Finally, individuals will alter their behavior in order to make themselves eligible for the pension whatever the criteria may be. The behavioral impact could include evasion of the contributory system, juggling of assets within the family, as well as decisions on labor force participation. It is often stressed that a means-tested pension can accurately distribute limited resources to the truly needy population, but empirical support for this assumption is rather limited. Identifying the wrong rural residents as being needy is a common vulnerability of means-tested pensions and one that is reported in nearly all of the countries that institute such a pension system; for example, Duran-Valverde (2002) reports that some 40 percent of Costa Rica’s means-tested non-contributory pension recipients belong to households that are classified as “non-poor.” Willmore (2003) studied the short-lived means-tested non-contributory pension in Mauritius. He reports that the “pensioners quickly learned to hide their true income for fear of benefit reduction, which made it difficult to assess the true position of those poor people.”

**Residence based pensions**

Seven countries have residence-based pensions in place: the five Nordic countries (Denmark, Finland, Iceland, Norway, Sweden), Canada and the Netherlands. The age of eligibility is 67 in Norway and 65 in the other six countries. Six countries require forty years of residence as an adult for a full pension; only the Netherlands has a more stringent requirement (50 years). The full pension as a percentage of per capita income varies from 9% in Iceland to 39% in the Netherlands. Five countries provide supplements for low-income pensioners that result in full pensions as high as 30% of per capita income in Norway and Canada, 35% in Iceland, 41% in Denmark and 54% in the Netherlands. In Finland, Sweden and the Netherlands, the size of the pension is reduced when the beneficiary shares accommodation with his or her spouse.

Residence-based pensions are quasi-contributory pensions, each year of adult residence counting as contribution toward an old age pension. A person with fewer than the required years of residency for a full pension might still qualify for a partial pension. Twenty years of residency, for example, earns 40% of a basic pension in the Netherlands and 50% of a basic pension in the other six countries. Three is the minimum number of years to qualify for a partial
pension in five of the countries, but Canada requires a minimum ten years of residence while the Netherlands provides partial pensions with as little as a single year of residency. Denmark requires a minimum of ten years residence instead of three if the beneficiary is not a Danish citizen. There are no examples of residence-based pensions in low-income countries, possibly because such a system is likely to increase administrative costs and produce little or no fiscal saving.

Six of the seven countries with residence-based pensions ‘claw back’ (recover) benefits from the relatively affluent and tax the net benefits as regular income. The exception is the Netherlands, which allows pensioners to retain all benefits, regardless of other income, and, in addition, provides all pensioners with a tax break. The tax break is a consequence of the fact that the Netherlands, unlike the other six countries, finances its residence-based pension primarily with an earmarked tax that is not paid by taxpayers 65 years of age or older.

The tax earmarked by Dutch authorities, for instance, for the basic pension is payable on earnings up to a maximum amount. This payment is described as a ‘pension premium’, but it is very much a tax, since pension entitlements are determined solely by residence, not by how much or indeed, whether a person contributes to the pension scheme. There are income taxes earmarked for health care and other social security benefits as well, but pensioners pay these at the same rate as non-pensioners. In effect, Dutch pensioners receive a global pension determined at nearly half the value of a full basic pension and available to everyone over the age of 65 with no residency requirement. Contributions to occupational pensions are deductible from taxable income whereas pension payments are taxable, so there is a large incentive for workers to delay receipt of their wage income in this way. The availability of tax savings may well explain why more than 90% of Dutch workers contribute to occupational pensions even though they are not mandated by law.

On equity grounds, there is no justification for reduced tax rates for pensioners, and much to justify equal treatment of taxpayers of all ages. In the Netherlands, if the basic pension were increased by 26.7% and the tax break eliminated, those with only a basic pension would be no worse off 14 and the net fiscal cost of pensions would be greatly reduced.
Recovery-conditioned pensions

Recovery-conditioned pensions work very much like a negative income tax, except that the net tax collected is at most zero, and never positive. Each resident or citizen of a country is entitled to a flat pension upon reaching the age of eligibility, but the pensioner is also required to return part or all of it out of other income she receives during the year. The rate of recovery from other income can beset anywhere between 0% and 100%. There is a trade-off between fiscal savings and disincentives: high rates of recovery produce large cost savings but discourage saving for retirement or continuing to work past the age of eligibility for a basic pension. The ‘other income’ subject to recovery can be defined in any way: other pension income, employment earnings, income from savings and investment, or any combination of these. In this case there is no trade-off: a broader definition of income allows recovery of the same amount of benefit with a lower rate of recovery.

Recovery-conditioned pensions require a special income tax regime for those who elect to receive a non-contributory pension from the State. This, in effect, is a voluntary tax, one that can be legally avoided simply by not requesting a non-contributory age pension. Those who take advantage of their entitlement to a non-contributory pension have to reveal all the chargeable income they receive and include net pension benefits in the income they declare for payment of normal income tax. If only mild targeting is desired, no special tax regime is necessary: simply make the universal pension taxable as ordinary income. This is done successfully in New Zealand and Mauritius, two countries with a long history of flat, universal pensions.

There are as many other examples of recovery-based pension systems as there are of residence based systems (7 countries), but the overlap between the two systems is large, with six countries belonging to both sets. The Netherlands is the only country offering a residence-based pension without recovery from other income, and the United Kingdom is the only one offering a pension that is universal in all respects other than its recovery provision.

The UK’s non-contributory pension is neither well-known nor widely-utilized, but it does exist with the name “Category D State Pension”. Beneficiaries must be 80 years of age or older and have resided in the United Kingdom for at least 10 years after age 60. Not all Category D
pensioners receive the maximum benefit of £46.35 a week since the pension is reduced, pound-for-pound, for any income from contributory basic state pensions. Curiously, there is no recovery from other types of income, not even income from earnings-related pensions. In effect, Government in the UK guarantees a minimum basic pension to each person over the age of 80 who satisfies the residency requirement. Affluent elderly are not excluded provided they receive little or nothing from another basic state pension. As of March 2004, 23,000 persons—fewer than 1% of the relevant population—were receiving Category D pensions.

Sweden, like the UK, claws back benefits from other pension income at the rate of 100%, so its scheme also functions as a minimum pension guarantee conditional on years of residency. Finland also claws back benefits only from other pension income, but at the lower rate of 50%. Pensioners in Finland can receive other pension income equal to double their residence-based entitlement before losing all rights to a non-contributory pension. Denmark and Norway take the opposite approach, clawing back benefits from earnings of those who continue to work past the normal retirement age, but there is a large exemption in each case, so only those with high salaries or professional income are affected.

In Norway, claw-back ceases at the age of 70, but the pension still is not universal from that age, and the quasi-contributory residency requirement remains. Canada claw back benefits from all income, including pensions, but the recovery begins at a high level of income. The Netherlands, as discussed above, not only has no claw-back of benefits, it also provides its pensioners with a large tax break. It might appear that claw-back of benefits works best with residency-based pensions, but there is no logical connection between the two methods of reducing fiscal costs.

The United Kingdom is the only example at the moment of a country with claw-back of benefits from what would otherwise be a universal pension, but there are other examples from the past. In 1985 New Zealand collected a taxation surcharge on other income that clawed back the entire benefit from 10% of the pensioners and a portion of the benefit from an additional 13% (Preston, 2001). The surcharge was very unpopular, so universality was restored in 1998. Mauritius in
1965 introduced an “income tax test” that in effect was a draconian claw-back scheme: those with taxable income lost their entitlement to a pension.

**Social Assistance Pensions**

Social assistance pensions are by far the most common type of non-contributory old age pension. They exist almost everywhere in one form or another. Surprisingly, they even exist in the form of means-tested supplements in four of the seven countries with recovery-conditioned pensions. For example, in Denmark, Iceland, Norway and Canada, a person who meets the age requirements and has resided in the country for at least 40 years as an adult is entitled to a noncontributory pension varying from 9% of per capita GDP in Iceland to 21% of per capita GDP in Denmark.

Social assistance pensions target the poor, and are considered preferable to the minimum pension guarantees of contributory systems, which exclude the poorest and most vulnerable members of society. Nonetheless, as a tool to reduce fiscal costs they have no advantage over recovery conditioned pensions, and they have a number of disadvantages. First, ex-ante identification and screening of applicants increases administration costs compared to a system which encourages self selection and ex-post repayment. Second, bureaucrats are given discretion in processing applications, providing opportunity for corrupt behavior. Third, even with efficient and honest officials, it is difficult to determine how much, or whether, a partial pension should be allowed, which can result in perverse incentives, discouraging saving for retirement as well as continued work in old age. Fourth, assistance pensions when tightly targeted come to be regarded as charity, which reduces their political appeal and discourages applications from the eligible poor.

To capture country experiences: India and the United States have tightly targeted social assistance pensions for those aged 65 years and older. India’s National Old Age Pension Scheme provides benefits to 4% of this age group. Supplement Security Income (SSI) in the United States benefits 6% of the same age group in that country. India’s non-contributory pension is
equivalent to 5% of its per capita GDP. The maximum SSI pension is the equivalent of 17% of per capita GDP (13% at the couple rate) and the average SSI pension is 9% of per capita GDP. South Africa and Australia, in contrast, exclude only the relatively affluent, providing basic pensions to 88% and 66% of their respective age-qualified populations (65 years for men and 60 for women). Not only does this coverage exceed by far that of India and the United States, the pensions are also more generous: 32% of per capita GDP for South Africa and 37% (28% at the couple rate) for Australia. Moreover, in both South Africa and Australia, most pensioners receive benefits at the full rate.

3. Budgetary Implications of Pensions

This section is intended to give an illustrative example of budget implications in an economy. In international comparisons, the annual benefit level for a pensioner can be expressed as percentage of a country’s GDP per capita and the cost of a social pension plan as percentage of GDP spent on it (Help Age International, 2007; Palacios & Sluchynsky, 2006; Willmore, 2007). This percentage can be obtained by the following formula:

\[ C = P \times B \]

C is the percentage of the cost of a social pension plan to a nation’s GDP;
P is the percentage of number of pensioners to a nation’s total population;
and B is the percentage of the benefit to per-capita income.

To place things in perspective, it is helpful to provide a case of the cost of a universal non-contributory pension. Antigua (a small island economy was selected) It provides a good example of a small country case. It adopted a universal pension given to all elderly residents, irrespective of other pension and non-pension income. Abstracting from administrative expenses, this cost is the proportion of the population eligible for the pension times the ratio of the pension to per capita GDP. If ten percent of the population becomes eligible for pensions equal to 20% of per capita GDP, the fiscal cost will be \((0.1)(0.2) = 0.02\) or 2% of GDP. In Antigua, approximately 11% of the population is older than 60 years of age, 8.2% older than 65 and 5.6% older than 70. If we begin with any specific figure, for example
EC$255 (US$94) a month amounts to 10.8% of per capita GDP, so the cost of giving this to all citizens over the age of 70, for example, would be (0.056) times (0.108) = 0.006, or 0.6% of GDP.

This is less than the amount that Antigua currently spends on (poorly) targeted non-contributory benefits. Implementation of universal pensions in Antigua is constrained by political will (or perhaps by the strength of favored interest groups) rather than government revenue. If the Government chose to do so, it could provide smaller pensions to all older citizens instead of large minimum pensions to former government employees, many of whom are neither elderly nor poor.

This exercise can be repeated for any combination of monthly pension and age of entitlement. Calculations are shown in the table below (table 6) for five different levels of pension and three ages of entitlement. The levels of pension correspond to the current minimum Age Assistance Pension (EC$255), the current minimum Social Security Pension (EC$350), the previous Minimum Government Service Pension (EC$500), the current Minimum Government Service Pension (EC$750) and the Promised Minimum Citizen’s Pension (EC$1,000). For these 15 combinations, fiscal cost as a percentage of GDP varied from 0.6% (EC$255 from age 70) to 4.7% (EC$1,000 from age 60 up).

The costs listed in the table are costs of a universal pension, not a minimum pension. Costs are reduced if benefits are denied to those with pensions larger than the minimum, and recovered, dollar-for-dollar, from smaller pensions. These fiscal savings come at a price. A minimum pension transforms the first of a worker’s Social Security contributions into payroll taxes, since non-contributors and contributors alike are entitled to the same minimum benefits. This discourages participation in the contributory scheme, which is not the case with universal pensions or, for that matter, with the absence of non-contributory pensions of any kind. This disincentive will be larger, the larger the minimum pension.

One way to reduce the disincentive is to recover the benefit from other pension income at a lower rate, such as 50% (50 cents per dollar of other pension income), rather than the punitive rate of 100%.
To illustrate this method of recovering benefits from other pension income: suppose the minimum citizen’s pension is set at EC$500 a month and the rate of recovery is set at 50%. All other pension income received would in effect be subject to a 50% tax until the full EC$500 was recovered. A person with no other pension income would retain the full EC$500 minimum pension, and a person with EC$1,000 or more in other pension income would have no entitlement to benefits from the minimum pension. A person with EC$100 of other pension income would return EC$50, retaining a total monthly pension of EC$550; one with EC$400 other pension income would return EC$200, retaining a total pension of EC$700, etc.

The Government might want to add employment earnings to other pension income in order to recover the pension also from those who continue to work. The scheme would then become one that guarantees the elderly a minimum income, but not necessarily a minimum pension. When earnings are included in chargeable income, it is very important that the rate of recovery is not set at a high level. A 100% rate would confiscate all earnings from continued work, and rates lower than 100%, but still high, would discourage the elderly from continuing in paid employment. A maximum rate of 50% would probably be a good compromise between labor market incentives and fiscal cost.

It is also possible to add income from investments and savings to that of pensions and earnings in order to recover the non-contributory pension benefit from a larger pool. This is especially attractive since income from investments and savings tends to be more important, the wealthier the citizen. In Antigua, this is not likely to be politically feasible since there is no tradition of taxing investment income; but it remains a possibility.

<table>
<thead>
<tr>
<th>Table 6: ANTIGUA: FISCAL COST OF A UNIVERSAL CITIZEN’S PENSION (% of GDP)</th>
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<tr>
<td>Monthly Age of Entitlement to Pension</td>
</tr>
<tr>
<td>Pension</td>
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<tr>
<td>EC$ 255</td>
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<td>EC$ 350</td>
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<td>EC$ 500</td>
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Determining the beneficiary age is a key element in determining cost given a fixed benefit level. A higher eligibility age reduces the number of recipients and the cost of the program. The benefit level also directly affects the cost of a social pension plan. Keeping eligibility age constant, a more generous pension benefit results in more expenditure and a heavier burden on the provincial or national budget level to a nation’s GDP per capita for each pensioner.

In the 72 countries with social pension schemes, 27 have an eligibility age set at 65, while most of the other countries set it at under 70 (International Social Security Association, 2007). The decision on the cut-off age usually takes into account life expectancy.

Taking the case of rural China, an extreme opposite case of a very large country; life expectancy was approximately 71 years in 2006, setting the eligibility age at 65 is reasonable. In 2007, 8 percent of China’s population was aged 65 or over, and it was estimated that nearly 5 percent of China’s population were rural elders. So a reasonable estimate of $P$ is 5 percent.

As the primary aim of a social pension is to prevent poverty and vulnerability among the elderly, the benefit level of China’s social pension should at least be above its national rural poverty line, which in 2007 was US$107 per person per year. In the same year, China’s GDP per capita was US$ 2,556. Thus, the estimated annual benefit for each pensioner would be just over 4 percent. $B$ can also be calculated on the basis of social programs in a similar country or block of countries. Data on 24 countries provide a $B$ estimate of 4 while $P$ for rural china is estimated at 5 $P$. So the minimum cost of China’s rural old-age social pension would be 0.2 percent of its GDP.

The above calculations illustrate that social pensions in developing countries are affordable where the political will exists, and China’s small-scale rural non-contributory pension program has laid a foundation for the introduction of a social pension for all rural elderly people.

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<td>750</td>
<td>3.5</td>
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<td>1.8</td>
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<tr>
<td>1000</td>
<td>4.7</td>
<td>4.7</td>
<td>2.4</td>
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</table>

Source: Author’s calculations, based on age distribution of population in 2001 and per capita GDP in 2004.
Governments, however, face a trade-off between old-age pension and other public programs, such as primary education and health services for the young, which may help people to build human capital and reduce reliance on social assistance in the long run. They may be concerned that the universal pensions plan might undercut inter-generational transfers and possibly lead to a near total withdrawal of traditional family support for elderly people.

There are empirical studies supporting the conclusion that universal non-contributory pension systems tend to have a positive impact, strengthening intergenerational relationship (Palacios & Sluchynsky, 2006). A rise in the number of children living in pensioner households in South Africa was observed. In Brazil, the co-residence with the grandchildren for elder-headed households increased after the extension of pension entitlements (Camarano, 2002).

In most cases, access to regular pension benefits creates an incentive for younger children to extend the survival of the beneficiary in order to guarantee the continuity of this cash stream, and henceforth improves the status of older people within their household (Barrientos & Lloyd-Sherlock, 2002). However, what does remain uncertain is whether such programs are politically feasible, particularly when introduced in rural areas as in the case of China, as rural residents have relatively little political influence.

V. A Non-contributory Pension Scheme for Lebanon

1. Background

Non-contributory pensions of any sort are not available in Lebanon. The government has not so far considered a non-contributory scheme and new proposals to modify the existing pension don’t address the issue. The government, however, has proposed a universal health scheme with limited coverage but has not been operational until now. A legislative decision on such a scheme has not been taken yet, and it’s less likely to be adopted any time soon.

The elderly can benefit from health services provided by public hospitals located across all regions. However, the existing capacity of such facilities is rather limited and has been
plagued with inefficient management and many other technical problems. The elderly and as well non-elderly could benefit from special ministry of health programs that are being extended free of charge to a specified life threatening medical conditions such as dialysis, by-pass operations, kidney transplants etc. The elderly benefit also from many private charity programs, but such services have lacked consistency and in many cases they are underfunded to be able to respond to large and diverse elderly needs.

2. Budgetary implication

An analysis of budgetary implication has, no doubt, to take into account, the poverty structure of the population of Lebanon. This segment relies heavily on the recent studies by UNDP in collaboration with the World Bank, the Ministry of Social Affairs(MOSA) and the Statistics Center (CAS) on “Poverty, Growth, and income Distribution” that was published in 2008; and draws on recent work by MOSA and CAS supported by UNDP that produced valuable documents on “Comparative Mapping of Living Conditions between 1995 and 2004” (1998); “The Living Conditions of Household” (2007).

The studies’ main conclusions are:

• 28 percent of the Lebanese population can be considered poor

• 8 percent as extremely poor Regional disparities are striking, with the North having the largest concentration of poverty

• The poor are heavily concentrated among the unemployed, and among unskilled workers (the report didn’t single out the elderly)

• The cost of halving extreme poverty is modest, but the cost of reducing overall poverty could be substantial

• The bottom 20 percent of the population accounts for only 7 percent of all consumption

• The richest 20 percent accounts for 43 percent of all consumption
The research of Dr. Hala Riskallah on the age structure of the population of Lebanon (2003) provided, as well, a valuable input leading to the estimate of the segment of the population that could be eligible for a social non-contributory pension.

The cost estimate is closely linked to eligibility, and age structure. The UNDP estimates that about 300,000 individuals in Lebanon (not clear whether Palestinian camps are included) are unable to meet their most basic food and nonfood needs. Since our focus is providing social security to the elderly, then, assuming these numbers are conclusive, one can, as a first step, estimate the percent of elderly among the total number.

The work of the UNDP policy content focused on the growth aspect to poverty reduction by creating employment. Since the elderly were not singled out as a target group, a social benefit scheme was not fully addressed; the study noted that it was not intended to propose a set of polices to reduce poverty of the elderly.

A very useful insight into the cost of alleviation of poverty can build on the study's methodology to develop poverty line through the provision of a food basket with the required calorie intake. This can provide a basis for calculating pension outlays. The study also suggested that the non-food expenditure can be obtained by fitting Engel’s curve of the food share to total expenditure.

Lebanon has a total population of about 4 million. According to the UNDP survey, about 7.5 percent of the population (300,000) lives under conditions of extreme poverty (below the lower poverty line). This number certainly includes all age groups. By considering the “upper poverty line” as defined by the WB, the overall poverty ratio reaches 28.5 percent. Therefore the budget scenarios adopted will consider the budget implication of a social safety net (pension restricted to the lower poverty line, and the budget implication of a safety net covering the upper poverty line). It’s important to note that extreme poverty has declined in Lebanon from nearly 10 percent in 1996 and household consumption has improved over this period.
The UNDP study has focused on growth and job creation in order to stem and reduce poverty. It calculated the needed investment (and the financing gap) to halve poverty by 2015; total investment of about 15 percent of GDP (under the assumption of pro-poor growth) would be needed.

Their focus, therefore, is on job creation that will ultimately benefit the young unemployed segment. The UNDP found that unemployment is particularly high among the poor.

Our concern in this project is to assess how poverty can be reduced among the elderly who are less likely to be positively impacted by a growth oriented policy. However, this does not dilute the importance of the growth approach as it’s a key to limit, or even eliminate the entry to the poverty trap. However, the UNDP has rather mitigated the task to reduce poverty by assuming that it takes only US$ 48 million per year (USD $ 12 per person) to eliminate extreme poverty and US$ 460 million per annum (USD 116 per person) to reduce poverty for those under the upper poverty gap. These objectives that were drawn in 2008 are very optimistic, in particular, that the target year is 2015.

The above draws attention to address poverty through a social security net and to estimate the needed budgetary funds to realize its targets.

First, the following tables can illustrate the burden of the task through initially estimating the number of elderly poor. The table below provides estimates of the age structure and the respective number

| Table 7- Population above 60 years old by age group, 2006, 2011 |
|-----------------|-------|-------|
| Age Group       | 2006  | 2011  |
| 60-64           | 112,736 | 124,148 |
| 65-69           | 97,813  | 102,301 |
| 70-74           | 77,877  | 82,973  |
Most social pensions have been drawn on a strict eligibility criteria, the same can be drawn for Lebanon. The most common eligibility criteria are means-based. These often exclude as non-eligible those you benefit from any other government pension such as civil service pensions. Beneficiaries of other pensions are also excluded. This exclusion is rather means tested as those who are provided with an alternative pension are assumed to have incomes exceeding the poverty line. The means tested approach ought to set an income threshold in order to guide the filtering process. Therefore, those who receive other private pensions are excluded on the basis of the level of their disposable income rather than merely due to the fact that they receive a pension.

The wealth criterion is another common practice used to determine eligibility. Though in Lebanon, the banking secrecy laws renders such criteria implausible. Perhaps, the more meaningful factor is to consider tangible assets as the wealth reference scale. For instance, the scenario could be based on property ownership exceeding a specified area.

<table>
<thead>
<tr>
<th>Age Group</th>
<th>75-79</th>
<th>80-84</th>
<th>85+</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>52,083</td>
<td>28,110</td>
<td>16,099</td>
</tr>
<tr>
<td>Total 60-85+</td>
<td>384,718</td>
<td>418,827</td>
<td></td>
</tr>
<tr>
<td>Total 65-85+</td>
<td>271,982</td>
<td>294,679</td>
<td></td>
</tr>
<tr>
<td>Total population</td>
<td>3,784,779</td>
<td>4,055,922</td>
<td></td>
</tr>
<tr>
<td>60+ as percent of total</td>
<td>10.16 %</td>
<td>10.32%</td>
<td></td>
</tr>
<tr>
<td>65+ as percent of total</td>
<td>7.2 %</td>
<td>7.3%</td>
<td></td>
</tr>
</tbody>
</table>

Source: H.A Abou Rizk, Population Conditions in Lebanon, 2003
The first scenario will consider all those eligible by age exceeding the age of 64, the mandatory age of retirement of private sector social security scheme. A total of 294,679 individuals fall into this category which is about 7.2 percent of the total population.

In case a universal non-contributory pension scheme is adopted, the cost will depend on the poverty coefficient adopted. Often a percent of the minimum wage is considered as a guiding principle.

The following options scenarios provide a guideline to a pension scheme cost. The options presented below are certainly in no way exhaustive. For instance, all have considered the pension eligibility starting at age 65, however, the government may consider an older cutoff age in order to calibrate the fiscal cost into the budget. Governments have used different cut off ages to qualify eligibility with some starting at age 60 and others starting even at age 80. Those that have restricted the benefits to a certain older age have normally extensive benefit private schemes and other generous government services catering to the elderly. In the case of Lebanon, raising eligibility from 65 to 70 plus will reduce eligibility nearly by 35 percent. Therefore, what seems an unaffordable scenario and financially unviable becomes quite feasible

**Pension cost under different scenarios:**

These scenarios are based on a pension scheme linked to the recently adjusted minimum wage which amounts to LL 670,000. The objective of these scenarios is to show the fiscal impact on the budget associated with the extent of possible coverage. Certainly, the overarching objective is to target the most needy and at the same time demonstrate the net savings that could be realized through targeting while taking into account the administrative cost of targeting. The scenarios below are selected to demonstrate overall budgetary cost while maintaining sustainable administrative cost. To this end, the scenarios have computed the cost of a universal pension, a targeted pensions based on a means-tested approach, and residency.
Precise targeting in Lebanon is not an easy task and may engender a cost without being assured of its effectiveness. The paucity of reliable data is a prime limiting factor. Recent studies have relied on the consumption approach to identify the poor. The identification of poverty was broad and by region; while it helps, but individual identification remains elusive. Therefore, the methodology relies on a proxy for means-tested non-contributory pension combined with residency criteria.

The residency criteria can as well be implemented at a low cost. The objective as cited above is to reward those who have contributed to the tax system earlier in their careers. Use of residency criterion has varied among countries. Canada for instance requires 10 years of residency. Lebanon with a large Diaspora population can realize sizable savings by instituting a residency requirement. It provides as well more tangible savings than other eligibility tests. The calculations provided below can justify such exclusion.

The approach followed is based on targeting those that enjoy higher incomes and wealth for exclusion from the poverty basket. The government is undertaking a more comprehensive survey (consumption based) to identify the needy population. The results, assuming having a high rate of reliability, can then be used to have a direct means-tested approach.

The civil service (both military, security, and civil) enjoy a generous public pension (include health benefits) that’s covered and subsidized by the central budget. Their exclusion will allow government to channel larger benefits to the poor. While other groups such as syndicates (doctors, lawyers, engineers) have more austere plans covered by their own contributions, they comprise high income professionals that can provide for their old age needs and allows them to maintain a comfortable standard after retirement.

A recovery-conditioned pension – a flat minimum pension less income received during the year is difficult to implement in Lebanon as data on income is rather limited. For instance, banking secrecy laws prohibit divulging personal accounts and their respective earnings. That’s why, taxes on banks accounts are submitted to the treasury in lump-sum while maintaining the confidentiality of private accounts. Also, recovery conditioned pensions could discourage work and savings when the recovery rates are high. In order to suppress
such incentives, some governments have resorted to low rates of recovery which renders such a scheme less effective.

The elimination (exclusion) approach suggested for Lebanon can avert many of the problems affiliated with a standard means-tested approach such as the cases cited in the previous chapter. In particular, it precludes the high cost that’s often affiliated with means-tested. The absence of reliable data, even on consumption, could compound the problem in Lebanon and reduce the effectiveness of the scheme.

Option I is certainly costly, as it is universal in nature and not designed particularly as a poverty reducing instrument. It will take up nearly 10% of the budget and 2% of GDP (8.7 % of primary budget spending). At 75% each pensioner receives US $ 337 per month. However, it’s more meaningful to consider a pension of 50% of the minimum wage. In this case the total cost drops down to USD 795 million per year, and the total cost is drops to 1.8% of GDP, a one percentage point of reduction.

<table>
<thead>
<tr>
<th>Table 8: Option I full coverage for 65+ based on 2011 data</th>
</tr>
</thead>
<tbody>
<tr>
<td>pension/person</td>
</tr>
<tr>
<td>USD monthly</td>
</tr>
<tr>
<td>75% of min wage</td>
</tr>
<tr>
<td>50%</td>
</tr>
<tr>
<td>30%</td>
</tr>
<tr>
<td>Total pensioners</td>
</tr>
<tr>
<td>Percent of pop</td>
</tr>
<tr>
<td>&lt;Minim wage-USD</td>
</tr>
<tr>
<td>GDP 2011 USD(000)</td>
</tr>
<tr>
<td>Population</td>
</tr>
</tbody>
</table>
Means-Tested Pensions

Means-tested pensions, options II to IV, provide a cost estimate under different means-tested scenarios. The approach attempts to estimate the number of less privileged and the needy by elimination, as noted above, rather than by directly attempting to identify these groups. This approach is frequently practiced when data on the target deprived population is not available, and the cost rendered to obtain the necessary means-tested information is exorbitant relative to the total cost of the scheme:

Option II takes out total civil servants beneficiaries from the total eligible number. The total estimated civil service beneficiaries including their dependants are estimated at 51000. The basis of this option is that the cost of social pension is born by the government and, therefore, excluding civil and military beneficiaries will preclude duplicity in allocating benefits. Excluding such a group will cut the pension population as well as the benefits 17%. (Table 9)

| Table 9: Option II full coverage for 65+ |  |
|---|---|---|---|---|
| Pension/person | Pension/person | Pension/per capita GDP (%) | Total cost per annum | % of GDP |
| USD monthly | USD Annually | | USD(000) | (%) |
| 75% of min wage | 337.5 | 4050 | 38.1 | 986899 | 2.3 |
| 50% | 225 | 2700 | 25.4 | 657933 | 1.5 |
| 30% | 135 | 1620 | 15.2 | 394759 | 1.0 |
| Total pensioners | 294,679 |  |
| Percent of pop | 7.3 |
The third option (III) could be more controversial. Under this proposal all syndicates are excluded. Those above the age of 65 and members of syndicates with their dependants total 7600 and expected to rise to only 8000 by 2017. Syndicate members have paid taxes and believe they deserve inclusion in the plan. However, this plan is meant to address the poverty issue and provides a social safety net, and is not intended to be a copy of a funded scheme (Table 10).

<table>
<thead>
<tr>
<th>Deductions:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Civil service beneficiaries</td>
<td>51,000</td>
</tr>
</tbody>
</table>

### Table 10: Option III full coverage for 65+

<table>
<thead>
<tr>
<th></th>
<th>pension/person</th>
<th>pension/person</th>
<th>Pension/per capita GDP (%)</th>
<th>Total cost per annum</th>
<th>% of GD USD(000)</th>
<th>(%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>USD Monthly</td>
<td>337.5</td>
<td>4050</td>
<td>38.1</td>
<td>956,119</td>
<td>2.2</td>
<td></td>
</tr>
<tr>
<td>USD annually</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>75% of min wage</td>
<td>225</td>
<td>2700</td>
<td>25</td>
<td>637,413</td>
<td>1.5</td>
<td></td>
</tr>
<tr>
<td>50%</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>30%</td>
<td>135</td>
<td>1620</td>
<td>15.2</td>
<td>382,447</td>
<td>1.0</td>
<td></td>
</tr>
<tr>
<td>Total pensioners</td>
<td></td>
<td></td>
<td></td>
<td>294,679</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>------------------------</td>
<td>----------</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Percent of pop</td>
<td>7.3</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Minimum wage (USD)</td>
<td>450</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>GDP 2011 USD(000)</td>
<td>42,500,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Population</td>
<td>4,000,000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Per capita GDP</td>
<td>10625</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deductions:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Civil service</td>
<td>51000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Beneficiaries</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Syndicates</td>
<td>7600</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net beneficiaries</td>
<td>236,079</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Other options:

Most non-contributory pension schemes have also established a residency requirement which could range from few to several years. Some even go up to 40 years. For Lebanon, it would be reasonable to require a minimum residency of 5 years. This will reduce the total number of beneficiaries even further (Table 11). The reduction is very difficult to determine accurately but one can safely assume that it reduce the total by 5 percent.

<table>
<thead>
<tr>
<th>Table 11: Option IV full coverage for 65+</th>
</tr>
</thead>
<tbody>
<tr>
<td>pension/person</td>
</tr>
<tr>
<td>----------------</td>
</tr>
<tr>
<td>USD Monthly</td>
</tr>
<tr>
<td>75% of min wage</td>
</tr>
<tr>
<td>50%</td>
</tr>
<tr>
<td>30%</td>
</tr>
<tr>
<td>Total pensioners</td>
</tr>
<tr>
<td>Percent of pop</td>
</tr>
<tr>
<td>Minim wage-USD</td>
</tr>
<tr>
<td>GDP 2011- USD(000)</td>
</tr>
<tr>
<td>Population</td>
</tr>
<tr>
<td>Per capita GDP</td>
</tr>
<tr>
<td>Deductions:</td>
</tr>
<tr>
<td>Civil service</td>
</tr>
<tr>
<td>Syndicates</td>
</tr>
<tr>
<td>Residency requirement (5%)</td>
</tr>
<tr>
<td>Net beneficiaries</td>
</tr>
</tbody>
</table>
Residency requirement has to be permanent (for instance, so many days per year) and at least for the past 5 years. This will limit the benefits to local residents; eliminate transients until they become full residents. With the Lebanese Diaspora as large as it is, no doubt many return home after a long career particularly in the Gulf and Africa. This may constitute a small fraction of those 65+, but this instrument safeguards the possibility of abuse of the system.

Another compelling, means-tested exclusion is one based on the wealth factor and primarily those possessing wealth in tangible assets such as built property and land. Based on available data, again a benchmark wealth factor has to be determined such as housing property exceeding 200 square meters and productive land of at least 5000 square meters.

Although, the amounts proposed in the above schemes may be considered low, but certainly they allow recipients to overcome the extreme poverty line. Furthermore, in a household with two recipients, the two could have a higher standard of living instead of each living separately by benefiting from scale economies.

The above scenarios provide a guideline to a pension scheme cost. The options presented are certainly in no way exhaustive. For instance, all have considered the pension eligibility starting at age 65; however, the government may consider an older cut off age in order to calibrate the fiscal cost into the budget. Governments have used different cut off ages to qualify eligibility with some staring at age 60 and others starting even at age 80. Those countries that have restricted the benefits to a certain older age have normally extensive benefit private schemes and other generous government services catering to the elderly. In the case of Lebanon, raising eligibility from 65 to 70 plus will reduce eligibility nearly by 50 percent which will allow raising benefits to each receiver. Therefore, what seems an unaffordable scenario and financially unviable becomes quite feasible with even better benefits.

In scenario IV, which is the most pragmatic among the four options, cost could be reduced by nearly one half (in all coverage categories) by raising eligibility age to 70 years.

Scenario V portrays the outcome if pensioners cutoff age is raised to 70 years. As noted above there will be a sharp drop in beneficiaries’ numbers and benefits.
3. Health benefits

Obviously, old people are the most vulnerable group in the community, yet the government does not provide them with sufficient health support services. When retired, private employees lose their health coverage that was previously provided by the NSSF’s Health and maternity branch.
Health conditions of the elderly in Lebanon are not very promising. Almost 71% of this group has chronic diseases and 7.2% are disabled. The top 10 most spread chronic diseases are: eye diseases, ulcers, arthritis and rheumatism, osteoporosis, triglyceride and cholesterol, occupational diseases, diabetes, cardiac and hypertension diseases.

Health bills are very high and many cannot afford treatments. Around 52% of the elderly are uncovered by health insurance, thus, half of the old aged population is exposed to serious health risks. Many of the uncovered rely on their family members for treatment.

Of those insured, 46% are covered by the NSSF, 39%, 11% by Private Insurance and 4% by other methods. Those who are still getting coverage at a retired age from the NSSF are getting health privileges as dependents from their insured family members. The following chart summarizes sources of health benefits in Lebanon.
Table 13: Overview of Existing Schemes in NSSF

<table>
<thead>
<tr>
<th>Branch</th>
<th>Contribution Rate</th>
<th>Beneficiaries</th>
<th>Benefit Formula</th>
<th>Benefit Cap</th>
</tr>
</thead>
<tbody>
<tr>
<td>HMI</td>
<td>9% of wage (7% from employer, 2% from employee)</td>
<td>the contributor and their family</td>
<td>Up to 39 weeks, though possibility of extension through NSSF board of directors.</td>
<td>1.5m LBP</td>
</tr>
<tr>
<td><em>medical care</em></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><em>health indemnity</em></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><em>maternity indemnity</em></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><em>funeral expenses indemnity</em></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>FEA</td>
<td>• 6% of wages</td>
<td>• Those eligible for HMI, and those who are</td>
<td>• 33,000 LBP per month for every child under 18 (or 25 if 1.5m LBP)</td>
<td></td>
</tr>
</tbody>
</table>
| ESI | insured and are at least 50% disabled.\textsuperscript{15}  
- Individuals must also have been working for at least 15 days during the month in which allowances are due. | they are pursuing higher education. Payment limited to 5 children.  
- If an individual’s spouse is unemployed, then they can receive an allowance of 60,000 LBP. |
| --- | --- | --- |
| - 8.5% of wages (8% of this is capitalized in individual accounts, and 0.5% is used to cover administrative costs) | - contributions are compulsory for contractual workers, whether they are paid by commission or fixed salaries | - For every year of service up to 20 years, the insured earns 1 month of his last salary, and every year after that, they earn 1.5 months of his last salary  
- If the 20 year requirement is not completed, then the following reductions are made:  
  i. <5 years contributions means the indemnity is reduced by 50% (relative to the full amount)  
  ii. 5-10 years of contributions leads to a reduction of 35%.  
  iii. 10-15 years of contributions, reduction of 25% |

\textsuperscript{15}specified in decree No. 5102 dated 20/10/1965

A health plan could be an integral part of a non-contributory pension. However, most countries, and in order to avert abuse of free medical services, are more inclined to provide the elderly a national old age health plan. The government of Lebanon has proposed an optional health plan for the elderly, however it has never been approved. The plan didn’t clearly define the medical benefits that could be bestowed on the subscriber. However, it was noted that with a single subscription benefits can be shared with a spouse.

The plan stipulated that beneficiaries are restricted to those who are not eligible to benefit from any other government plan or a syndicate plan. And importantly it was restricted to those who are at least 65 years of age and above.

The proposed cost was estimated at 6 percent of the minimum wage which is equivalent to $240 per person per year; equivalent to USD 52 million per annum.

A health scheme of this kind can be effective in providing basic health services (covering consultation and hospitalization). The plan could be restricted to hospitalization alone. Private medical/health groups have been successful in providing health insurance at a low cost. Current fees vary between USD 70 to USD 100 per annum. These services are restricted to participating hospitals and group medical doctors. These schemes, however, don’t cover the cost of medication; thus limiting their overall benefits.

The government can reap scale economies from managing a group health insurance scheme managed through local or international group health specialists. Significant discounts can be realized and cost cuts can be maintained by well defining the services that could be provided. Expensive and exceptional cases can be excluded and could be covered by the public hospital system. A health scheme for the elderly could be guided by other countries experiences such as Medicaid and others.
The elderly as well as other age groups can benefit from the services provided by public hospitals. The cost of public hospitalization to the public is at a small fraction of private hospitalization. A careful comparative study of public hospitalization versus elderly group insurance can help determine the inherent advantage of widening the role of public hospitalization with a targeting scheme for qualified elderly groups.

4. Administrative Arrangements for a Non-contributory scheme and Financing

Administrative Arrangements

The administrative structure of the proposed non-contributory pension scheme is key to its long-term success. There are important decisions to be made regarding the degree of decentralization, as well as whether different branches are to be merged or kept separately. Specifically, there are the questions of whether or not the non-contributory system should be implemented as part of the NSSF, and if the health and pension components should be administered separately.

There are several options available, including the following:

- The NSSF could assume all responsibility for the management and implementation of the non-contributory scheme (both the pension and health components)
- The non-contributory pension scheme could be managed separately from the NSSF, though still within the Ministry of Finance.
- The non-contributory pension and health insurance components could be separated, with the Ministry of Public Health remaining in charge of the medical part.

There are both advantages and disadvantages to merging the proposed non-contributory social insurance with the existing NSSF.

The advantages first; the merger would make it easy to create a uniform system for individuals’ records, which would facilitate verification of eligibility criteria. Furthermore, the NSSF is an established institution with its own infrastructure, so

18. Our gratitude to Ms. Ola Sidani for her direct contribution to this section

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creating the non-contributory system as a subsidiary of the NSSF might save on the initial administration costs.

The main disadvantage of joining with the NSSF is that it may create an opportunity of cross-subsidization between the different branches and funds. As described earlier, there was cross-subsidization between the health and ESI branches, despite it being illegal, which ultimately hid a dangerous un-sustainability problem.

On the other hand, there is the disadvantage that by inheriting the NSSF's organizational structure, the non-contributory pension system might inherit its inefficiencies. As an independent organization, the non-contributory system could start on its own and avoid its predecessors' mistakes.

If the health and pension components of the non-contributory scheme were separated and headed by different ministries, then it would become necessary to ensure coordination between departments. This may require an inter-ministerial committee, or some other formal structure for checking that the program was meeting its goals of efficiency and redistribution.

In this case, The Ministry of Finance could be in charge of the pension scheme as it is being financed. An identification card could be issued for the beneficiaries by the Ministry of Finance.

Expenses could be entered as a separate current spending item in the budget.

However, leaving the medical insurance component in the hands of the Ministry of Health might allow them to manage the fund more efficiently. For example they would be better placed to index benefits in line with inflation in medical costs, or perhaps even decide who should receive the insurance (e.g. if benefits are to be targeted towards specific illnesses.

Decentralization to local governments is one possibility for the administration of public social security. Local authorities might be better positioned to determine who is truly
deserving of benefits, and they might be able to be more responsive to the changing needs of their citizens.

On the other hand this might make it harder to monitor the officials giving out the benefits, encouraging corruption. A further danger with decentralization is that extreme differences will emerge between areas, encouraging individuals to move for the sake of more benefits. Although this is unlikely to be possible for the poor, the distortion would lead to inefficiency, and so any decentralization should be carefully managed in some central organization. In any case, given that funds will presumably be collected centrally, it would be impossible to obtain complete decentralization.

**Financing**

The government can have several options to generate the needed resources to cover the cost of a non-contributory pension scheme. The approach has to address the overall management of expenditure and revenues. Earmarking is a common practice such as that of the independent Municipal Fund where revenues from value Added tax are earmarked for municipalities. A similar approach could be adopted for the proposed pension scheme. However, a more prudent management of both spending and revenue can generate over a short period of time a 2% percent of GDP savings. Waste in the electricity sector is just one example of the potential that can be generated.

Currently, transfers account for 19% of total expenditure (equivalent to 5.2% of GDP). A better management of subsidies can release the necessary funds for this scheme. Current subsidies and transfers are not targeted and a greater part of their benefit is channeled to higher income groups as their consumption is much higher than the more deprived groups.

Revenue generation has many gaps in Lebanon, income tax in particular. Currently, Lebanon has one of the lowest income tax rates among peer countries; 3.9 % of GDP. Tax evasion is a serious problem as well, particularly among large tax payers. A better management of the fiscal side can generate the needed income.
A Non-contributory pension scheme is viewed as a safety net issue unlike funded schemes. With the proper development of a regular contributory scheme with a broader coverage, could over time obviate/ or reduce significantly the size of a non-contributory social safety net.

Considering that the current contributory pension scheme managed by the NSSF is inadequate and fails to provide a safety net, the government may opt to adopt a PAYG scheme without notional accounts. Collections from the current indemnity scheme could be merged with a government subsidy to finance a global social security.
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