Declaration

International Federation of Pension Fund Administrators (FIAP)

The International Federation of Pension Fund Administrators (FIAP) wishes to publicly express its concern regarding the Bulgarian Government's decision to modify the pension system, undermining the functioning of the mandatory individually-funded program (2nd Pillar).

Specifically, on December 19, 2014, the Bulgarian government (without consulting its citizens or any experts), unilaterally approved the 2015 Budget Law, which includes a series of measures that modify the Social Security Code (SSC), to the detriment of the 2nd Pillar. It specifically states the following:

1. Current contributors to the 2nd Pillar (those born after December 31, 1959), will have the one-off option of choosing whether they want to transfer their private pension funds to the solidarity fund of the National Social Security Institute (NSSI). There is no deadline for members to make this decision. This entails the transfer of the accumulated balance in their individual accounts, as well as future contributions (5%) to the public PAYGO system (1st Pillar, managed by the NSSI). This decision would be irreversible, because the NSSI does not maintain personal accounts.
2. All new participants in the labor market will have to make their contributions to the 1st Pillar, unless they expressly state that they want their contribution (5%) to be managed by a private fund, for which they have a deadline of one year after employment. If at the end of the year these individuals have not exercised their option to contribute to a private fund, they may no longer have the option to participate in the 2nd Pillar in future, and they will have to contribute everything to the 1st Pillar.

The Bulgarian pension system was reformed in 2002. This reform incorporated a second privately managed savings and individually-funded pillar to the existing public PAYGO pillar. This new pension system, of a mixed-complementary nature, is mandatory for all workers born after December 31, 1959 (those born before that date were not given the possibility of participating in the 2nd Pillar, and were only given the option of voluntarily contributing to the 3rd Voluntary Savings Pillar that had been operating since 1994). The total contribution rate to this mixed system is 17.8% of the taxable income of workers, of which the employer financed a rate of 9.9% (7.10 percentage points going to the PAYGO program and 2.8 percentage points to the individually-funded account) and the workers a rate of 7.9% (5.7 percentage points going to the PAYGO program and 2.2 percentage points to the individually-funded account). Thus, the 5% of salary paid into a private pension fund (2.2% funded by the worker and 2.8% by the employer) goes to the individually-funded account.

FIAP considers that the measures that the Bulgarian Government intends to implement will have negative consequences for workers, for their pension system and for the economy of the country, due to the fact that:

1. The proposed changes are in fact an attempt to replace the 3 pillars pension model (introduced in 2000, and widely recognized by international agencies as a successful strategy for diversifying the sources of income for retirement), with solutions that have only a temporary fiscal impact, that undermine confidence in the pension system and that essentially constitute a reversal of the reforms implemented for improving pensions. The fiscal problem facing most of the governments of the Central and Eastern European countries, and Bulgaria in particular, is the result of the erosion of the assets of the former PAYGO system. The demographic factors faced by the PAYGO systems (increase in life expectancy and decrease in the fertility rate) have severely impacted these systems, making them unsustainable.

2. The financial sustainability of pension systems was among the main reasons that the governments of Central and Eastern European countries implemented private, defined contribution individually funded pension programs, since they needed to improve the prospects of the public sector deficit. Hence, the measures proposed by the current Bulgarian government would only exchange one type of debt for another (explicit and implicit debt) and would harm the fiscal status in the mid and long-term.

   In countries with reforms, the "explicit" accounting public debt arises from the acknowledgment by the Government of the benefits of the workers who contributed in the former system and who must receive the pensions promised by that system in future. However, in countries without reforms, this so-called "implied" debt is not registered in the Government accounts, despite the fact that the creditors do exist.

   The changes proposed to the SSC will in the long term result in a larger deficit of the 1st Pillar and will generate even fewer pension benefits for workers, while eroding the ability of the individually-funded program to provide suitable replacement rates.

3. The financial balance of the Bulgarian pension system will also be affected by the loss of the macroeconomic benefits entailed in the operation of an individually-funded program in which workers' contributions are invested in financial instruments of the capital market. Existing international evidence shows that the creation of these systems has a positive impact on the growth rate of the Gross Domestic Product (GDP), through increased savings and investment,

employment and the productivity of factors. The potential positive effect of the accumulation of the pension funds on the economy (higher economic growth, more liquid and deeper capital markets, a greater number of financial instruments available for investment, lower transaction costs) depends to a great extent on the volume of accumulated funds. Thus, the lower the contribution rate to the individually funded 2nd Pillar, the lower the volume of accumulated resources and, consequently, the lower such effects will be.

Studies of the macroeconomic effects generated by the creation of the individually-funded systems have recently been carried out in four countries in Latin America: Chile, Colombia, Peru and Mexico[1]. The reforms generated macroeconomic effects through four main channels: the degree and structure of employment and its formality; savings and investment; the development and efficiency of the capital market; and the evolution of the total productivity of factors (capital and labor). The magnitude of these effects differed between countries, but the average estimate was positive across all channels, particularly highlighting the impact of financial development and the total productivity of factors. It is concluded that in the evaluation period, the creation of the individually funded system contributed to a greater annual growth of the GDP between 0.31% (Mexico) and 0.58% (Colombia). The higher growth rates driven by the birth of the individually funded system were equivalent to between 6.2% (Peru) and 12.9% (Mexico) of the annual growth of the GDP during the evaluation period (see Table No.1).

Table No.1

Macroeconomic Impact of the Creation of the Individually-Funded System

Impact of the Reform	**Chile**	**Colombia**	**Mexico**	**Peru**
Year in which the new system began	1981	1994	1997	1993
Evaluation period	1981-	2006-2010	1998-2012	1993-2011
Annual GDP growth for the period	4.58%	4.55%	2.40%	5.3541%
Effect of the reform on GDP, average scenario (1) (2)	0.37%	0.58%	0.31%	0.3331%
Saving - Investment	0.09%	0.22%	0.16%	0.0167%
Labor Market	0.08%	0.00%	0.02%	0.0129%
Financial development and portfolio (3)	0.20%	0.36%	0.13%	0.3037%
% growth of the GDP explained by reform	8.08%	12.75%	12.92%	6.22%

(1) Greater annual growth generated by the reform.
(2) The average between the two scenarios considered is applicable in the case of Chile and Peru. The Chilean study estimates the increase of the GDP in stationary status. The figure shown is the estimated effect in 30 years, which assumes that half the gap between a stationary status and the other was closed in this period.
(3) Total Productivity of Factors.

Source: Contribution of the Private Pension System to the Economic Development of Latin America. Experiences of Colombia, Mexico, Chile and Peru. SURA Asset Management.

[1] Book "Contribution of the Private Pension System to the Economic Development of Latin America. Experiences of Colombia, Mexico, Chile and Peru". Research carried out by SURA Asset Management.

4. These types of measures harm foreign investment in Bulgaria, since sudden changes in long-term policies increase the perception of the risks of instability in the political and economic status of the country.

FIAP has deemed it important to make its view on these matters known to public opinion, convinced of the importance of the consolidation and strengthening of the new defined-contribution pension programs created in Central and Eastern Europe, mostly with the support of the World Bank and other international agencies, due to their significant benefits for the pensions of workers, the functioning of the economy and the degree of debt and fiscal deficit of these countries. Our organization is at your disposal for collaborating in technical matters and providing our support for halting or preventing these initiatives.

FIAP, founded in May, 1996, is an international agency comprising the Associations of Pension Fund Managers from the following countries: Bolivia, Bulgaria, Colombia, Costa Rica, Curacao, Chile, El Salvador, Spain, Kazakhstan, Mexico, Panama, Peru, Poland, the Dominican Republic, Ukraine and Uruguay. As of December 2013, there were more than 122 million workers enrolled in associations and institutions that are FIAP members, accumulating more than US$ 725,000 million in their respective individual accounts.

Santiago, Chile, January 22, 2015.

Signed by:	Guillermo Arthur, FIAP President, Chile.
On behalf of:	International Federation of Pension Fund Administrators (FIAP)