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THE SYSTEM OF PRIVATE INSTITUTIONS OF SUPPLEMENTARY PENSIONS THE LEGAL FRAMEWORK AND ITS IMPLEMENTATION IN ALBANIA AND KOSOVO

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Abstract
The article that I aim to present in this conference, if you will accept my work has as its object the system of supplementary institutions by private legal persons who receive a special authorization from the Financial Supervisory Agency. The social security right relatively a new branch of law, that is based on the law of year 1993 'On social insurance' .The market of social insurance in Albania is regulated specifically by the Financial Supervisory Agency. The legal framework in Albania regulate the provision of supplementary benefit for the insured in case age pension, disability, and/or family pensions, through the supplementary pension arrangement in addition to those provided by law for obligate insurance. The innovation that is set out by this law is that in addition to the supplementary pension system will be implemented even the public system of the pensions that is administered from the private juridical persons. At the same time I will explain with the comparative method and the legal or the framework regulation of regional countries about their experience in terms of the social insurance system that is one of the most discussed and most problematic in Europe and elsewhere.
Keywords:Financial Supervisory Agency, social insurance, pension

Voluntary loss of your money in exchange for a minimum but guaranteed pension, or the uncertainty to risk and get much more than to contribute to a private scheme. This will be the biggest dilemma of the pensioners of tomorrow. Will be facing that puzzle one day not too distant, when an open private pension scheme will be operating. In this way, the 30-year-olds of today will, probably, not have the fate of their fathers, who receive a monthly pension, which, as they put it, can do no more than pay for a cup of coffee in the morning. Possibilities are, that you can invest your pension contribution money in a scheme where you can receive more. Consequently, it will not be repeated what is happening to today's retirees, who have paid millions of leks for years and their pension benefit , in total, is much less than the money paid. The current scheme, less and less, is making this possible. Even more so in Albania, where the number of contributors in the years of transition has declined drastically. Exit from this vicious circle is, tentatively, through private schemes, but how safe the schemes will be, nobody can tell exactly.To receive a pension today, according to the laws you need meet two conditions: reaching age 65 years for men and 60 for women and corresponding years of contribution, unlike the years of work starting with 20 years for partial retirement and 35 years for full pension. To receive a pension you must pay pension contribution during working years. In this sense, a pension is neither help nor humanism. Pensions are simply the return of money paid for years. But social unrest that the country went through, has made this problem more complicated. In fact, the high rate of births before the 90's has contributed to a very young age country, compared with other countries, even according to UN statistics, the specific weight of the third age in our country is only 9 percent of the population and according to the same statistics, the number of people able to work is four times that of pensioners. If reality is as good as the figures show, that would be a miracle. A number of reasons such as high informality and corruption in the system affect negatively. But the biggest negative impact consists in two other reasons;

* high rate of emigration of skilled people able to work,

*high rate of unemployment in the country, that have eventually reversed this ratio.

Now, for a retiree it is not possible to contribute to the mandatory scheme of an employee. In 2049 it is estimated that a contributor's burden is to pay for 1.5 pensioners. Under these conditions the scheme only suffers and never be able to sustain itself. In front of such a situation, the state is forced to find the solution to improve the scheme in the increase of the contribution paid and the increase of the pension age. Looks like a solution, but in the long run, people continue to lose. High rate of contributions generate higher informality. Thousands of people currently working in the black, while others knowing that they will nottake their money back in old age pay contributions based on the minimum wage. This is without saying a big failure, and has forced the sector specialists to accept it.

In a national strategy aiming at reforming the pension system drafted by a working group headed by the Ministry of Labour and Social Affairs, it is stated explicitly: "The rules of the system are such that low ratio of contributing employees will result very quickly in a low percentage of population covered by the pension system. It is not the financial balance of the system under discussion, but rather its capacity to ensure sufficient income for all pensioners ". How safe are today's contributors to a pension and how will it sustain us tomorrow? A simple calculation puts you in front of the dilemma, to contribute, or not.

Compulsory scheme appears to be marked to fail, in a more moderate variant it will not yield the expected results. This, perhaps is due to the fact that we are dealing with a shift from a generation in time. Put more simply, I, the worker or present contributor pay contribution to an actual pension benefactor and tomorrow when I retire, someone else will pay contributions for me. This is the core of the system "pay as you go." Perhaps it is this time detachment that causes problems. And in the struggle to emerge from these perennial losses, the solution is directed to other variants, in private pension schemes.

How do these schemes work?

Under applicable law, the schemes rely on the principle of voluntary participation of persons wishing to enter them. The benefits obtained from the scheme are subject to contribution paid, which, by law, can not be less than 500 new leks. Also, under special contract with the creator or the scheme manager you may decide on the term and form you can obtain the benefit, which, based on the economic activity of the scheme is equal to the contribution plus an accrued benefit. These private pension funds provide for their contributors supplementary pension, supplementary disability pensions, supplementary family pensions and early retirement pensions. Besides these, from private schemes you can also receive benefits payable in the form of immediate payment and payoff. The law states that private legal entities can raise such a pension funds, upon licensing from the Inspectorate. Same can set up a group of people in the form of a joint stock company registered in court. The law also entitles the private financial institutions, with permanent residence in Albania. Furthermore, with a special authorization from the Council of Ministers, state non-budgeted enterprises can set up a private pension scheme. The number of participants therein depends on the type of the scheme. Thus, if we are dealing with a closed or limited scheme, the number of contributors should not be less than 100 and when the scheme is open, the number of participants should be no less than 500 people. And to start such an activity, the law in 1995 foresaw a bank guarantee in the country of 10 million lek, a figure that, according to the Inspectorate, may increase. Judging from the law and the law enforcement, it seems that our retirement days will have an exit from the vicious cycle of lost pension contributions and often funny pension our grandparents and fathers are taking.

The difference between state and private entities in offering pensions.If not controlled private pension schemes may end up in pyramidal schemes.

What is the risk that such schemes can turn into pyramids, which consequences we, Albanians have already experienced?

This question can be asked for any activity. Any financial institution that lacks the check elements, first and foremost, the legality regulating this institution, and secondly the supervision of this institution, is vulnerable to turn into a pyramidal scheme. But in this case, we refer to institutions, whose activity is regulated by law, and are monitored and checked by an inspectorate set up by the Council of Ministers. Thus the chances for them to become pyramidal schemes are minimum to zero.

Certainly, setting up a private pension institution is not a purely administrative step. It is subject to a number of factors. Namely reliability, capital of the individuals wanting to set up such private schemes, who are the individuals to create the funds and who are contributors and those who will benefit from them. Fulfillment of these conditions is not a one shop thing, but it is a process that lasts.Private schemes have an advantage because they bring benefits more favorable than mandatory schemes, provide greater benefits than the mandatory schemes per unit of contributions paid. Another major advantage is their ability to provide immediate benefits or in the form of payoff. Therefore, paid contributions can not be lost. While in the mandatory social security schemes, a defined working time has to lapse before pension benefit and, this time is substantial.

What are private pension schemes?

In December, the Parliament passed law no.10197, dated 10.12.2009 "On the Voluntary Pension Funds." From the viewpoint of pensions market development, the adoption of this law brings a number of advantages compared to prior law. This law, in the good will to develop private pension funds, makes a radical change in the organization, management and operation of private pension funds, increasing their reliability, their guarantee and therefore interest on them.

In this regard, this law brings some positive changes in private pension market;

First. It is a contemporary law reflecting several years of practical application of the pension law in some countries of Eastern Europe. More specifically, Poland, Czech Republic, Slovenia, Macedonia, and little experience of development in our country.This law regulates the activity of the Voluntary Pension Fund with defined contributions with individual and professional plan, where a pension plan can have more than one product (pension).

The operation of this law, from the administration viewpoint involves three levels.

Level One: Pension Fund, which consists of a group of assets owned by members of the fund, established on the basis of contracts, each member has his share. The assets of the fund include payments made and net profit realized from their investment. Each member has a quote that represents its share of ownership in pension fund assets.

By law, pension funds are of two types:

A) Voluntary Pension Fund, representing physical individuals who can participate in one or more pension plans. In this case, the individual and the Society of Pension Fund Management enters into a contract, setting forth the terms and conditions of the parties, to benefit voluntary pension.Participant in a pension fund, may be any individual, regardless of location, age, size of contribution, etc.., only after a contract has been entered into with the Fund.

A member of the Pension Fund has the right:

- Receive monthly voluntary pension, five years before reaching retirement age established under the law "On Social Security;
- Receive monthly voluntary pension, when he becomes permanently disabled;
- When he passes away before reaching retirement age, his heirs benefit the accumulated assets;
- When, at any time you want to make an early withdrawal of the funds.
- transfer at any moment, his assets to other pension funds.

B) Professional Pension Fund: represents the desire of private or public employers to insure his employees at a pension fund with a professional pension plan. In this case, a contract is entered into between employers and Pension Fund Management Association, specifying the terms and conditions to be met by both parties, names of persons who will benefit from this agreement, the amount of monthly contribution, etc..In this case, the participation in pension plan may be of three types, collective, individual and combined.

Collective Pension Plan: wherein the employer is obliged to voluntary pay all the pension contributions on behalf of its employees. In the individual Pension Plan the employers and employees enter into an annex contract attached to the employment contract. The annex set out the conditions to be satisfied by the employee in labor relations, in order to benefit from the Individual pension agreement, where employees undertake to pay all voluntary pension contribution rate at their personal expense.

Combined Pension Plan, wherein voluntary pension contributions are paid partly by employers and partly by the employees, in percentages as desired. Even in this case, an annex contract is entered into between employers and employees for the rate born by the employers.

Second level.Managing Association. By law, the Voluntary Pension Fund will be administered by the Managing Association, which is established as a joint stock entity in accordance with the Law on “Commercial Association". For the companies to administer one or more pension plans, they must be licensed by the Financial Supervisory Authority. Following main requirements must be satisfied by the companies:Managing Company should be established as a joint stock company with unlimited duration, with no less than 51% of shares, are owned by a bank or financial institution.Managing Company must have a minimum capital of 15,625 thousand lek. When the value of assets exceeds 31.2 billion lek, the capital must be increased by 0.02% of the value of assets.

The main role of the Managing Company shall be the collection of contributions and their investment. But in special cases, the managing company has the right to carry out the activity of managing the Investment funds and Pension Fund Assets, provided that this activity is licensed by the Authority.Managing Company shall administer the Voluntary Pension Fund at a cost not to exceed 3% of the assets of the Fund.

The third level. Depositary is a bank licensed by the Bank of Albania to provide custodian services approved by the Financial Supervision Authority on the proposal of the Managing Company.

Depositary is also responsible for safeguarding the assets of the fund. It has the following tasks:

- Inform Managing Company periodically on net asset value;
- Controls assets administration by the Managing Company, in accordance with the legislation is in force;
- Ensures that the transactions made by the Managing Company return to the Fund;
- Ensures that the Fund incomes are distributes as per contracts and legislation in force.

Secondly, the new law makes the parties participating in the voluntary pension plans more attracted thereof. Both adherents and benefactors are favored fiscally.Tax relieves for the contributions of pension fund members.Contribution made by each member of a pension fund is, for tax purposes, deducted from his personal income.

Profit realized from the investment is not subject to tax, neither for the pension fund nor for the Managing company.Contributions made by the employer on behalf of a member of a pension fund are, for tax purposes, not considered personal income.Contributions paid by the pension fund member are not included in the total income for purposes of calculating social security and health contributions.Acquisition of Shares of a pension fund is considered as a financial service and therefore is exempt from VAT.Services provided by the Depositary for the managing company and its members are considered as a financial service and therefore are exempt from VAT.2. Fiscal treatment of contributions paid by the employer.Contributions paid by employers on behalf of its employees in a pension plan is considered as a deductible expense in the profit tax calculations.

Thirdly, the new law defines certain duties for the existing private pension funds, which are compulsory and to be implemented within one year from its effective date, so;Existing pension institutes licensed in accordance with the law no. 7943, dated 1.6.1995 "On Supplementary Pensions and Private Pension Institutes" will continue to work under conditions they are licensed.

Existing institutes, within one year from the effective date of the new law, shall meet the requirements of the provisions of this law. After meeting the conditions and within a year from the effective date of the law, they should renew their license.

If existing institutions do not meet the requirements of laws, or do not renew the license within a year from the effective date of the law, the license granted is no longer valid from the date of the decision taken by the Authority. In this case, the Authority orders the existing Institute to transfer the assets to another Licensed Pension Institute, or upon the desire of its members liquidate them.

Finally we can say that the new law "On the Voluntary Pension Funds," will give a new development to private pensions in Albania.Noteworthy is the fact that during the approval process of this law it was evidenced the need to develop the system of compulsory private pensions.

State social security system has its problems. In circumstances where birth rates are falling and the average life expectancy is extended, the social security system, is increasingly rendered impossible to meet the financial requirements for third "age" population. Suffice to mention a fact, the degree of substitution which represents the ratio between average pension and average wage, presently is no more than 30% against no less than 70-75%, which is a legal obligation. All this gap, should be covered by private pension schemes.

Referring to the experience of pension system development, particularly in Eastern Europe, after '95, two trends or two models are easily observed, both established in support of the concrete conditions of each country.

The first Model first and most general, of the pension system consists of three schemes.

The first scheme - a state mandatory system, PAYG which covers up to 35-40% degree of substitution, through contributions that each person exercising an economic activity should pay in this scheme.

The second scheme – mandatory private system, wherein part of the total contribution is transferred to this scheme and is managed by the Private Pension Funds. This scheme covers 20-25% of the pension.

The third scheme - voluntary private system, which covers 10-15% of the pension. This model is found in Poland, Bulgaria, Hungary, Croatia, Estonia, Romania, Slovakia, Macedonia, etc..

The second model is the one where the overall system consists of two pension schemes - a state well consolidated base scheme, which bears 55-60% of the pension and a developed voluntary private insurance scheme, giving a chance, through fiscal incentives, to all active population involved in it, which covers 15-20% of the pension. This well-managed system is found in the Czech Republic, Slovenia etc.

I think that in view of the direction, the Albanian economy has taken, the gradual introduction of three columns system would be efficient but would require some modifications and improvements of the pension basic law.

Social security issues in general and of pensions in particular, are quite extensive and complex, because of the fact that it involves directly and indirectly the whole population. I think the first step is taken ie, the law, but it needs to be associated with other important measures that would support the development of this market in Albania.

➢ *A brief overview of the history of pensions in Kosovo.*

Before the 1998 conflict, Kosovo was covered by the Yugoslav pension system. This was a "pay-as-you-go" (PAYG) system in which current workers made contributions to the pension fund, and those contributions were used to pay benefits to current pensioners. Pension levels were determined by a benefit formula based on years of service and salary level. Until 1989, Kosovo had an autonomous pension fund that collected contributions and paid benefits. In 1989, these functions were centralized to Belgrade, and the regional Kosovo fund was disbanded. Many Kosovar workers were excluded from the system as of 1989 when they were removed from formal-sector labor positions. From the beginning of the conflict, Belgrade ceased paying pensions to most past contributors.After the conflict ended, UNMIK began a social assistance program that included

payments to certain categories of elderly on a needs-tested basis. These payments to elderly did not cover a large share of the older population, mostly did not go to those who made past contributions, and were seen as social assistance rather than pension benefits. During 2001-2003, a fundamentally new pension system was designed and implemented in Kosovo.

1. Broad Principles and Specific Objectives of the Reform

In developing a pension strategy for Kosovo, policymakers considered the importance ofthe following four broad pension principles, which are relevant for any pension system:

• Lifetime consumption smoothing. A pension system should allow the working age population to set aside income for retirement years to facilitate consumptionsmoothing. That is, the system should help ensure that people can consumeroughly as much in old age as they did when of working age, even though they nolonger continue to receive wage income. Consumption smoothing can beachieved either through true savings in financial markets or also by givingcontributions to the state in exchange for a promise to pay a future pensionbenefit.

• Insurance function. A pension system should allow participants to insure againstcertain risks: uncertainty of longevity (that is, we do not know how long we willlive), and also the possibilities of becoming disabled during work career, or ofdying and leaving survivors in need of support. Risks of the pension system itselfalso should be well managed—market and institutional risks in funded systems,and demographic, fiscal and political risks in unfunded systems.

• Redistribution and provision of a social safety net. A pension system is one ofsociety's primary means of redistributing wealth across and within generations,for instance, from richer to poorer, and of ensuring that poor elderly receive atleast a minimum income.

• Compatibility with economic growth. While not its primary function, a pensionsystem must be compatible with economic growth, labor market efficiency, anddevelopment of capital markets.

The following specific objectives guided the design of the new Kosovo pension system:

Avoid recreating the old Yugoslav socialist pension system. The old system was atypical East European system with very high contribution rates, frequent delays inpayment of pensions, a high level of evasion, early retirement ages, special categories ofearlier retirement, a complicated benefit formula, and increasing financialunsustainability. Only part of the population was covered. In short, the old system wasineffective on several fronts. Although the Kosovar population is young, it will start toage rapidly and therefore will be subject to the same demographic pressures that plaguethe Yugoslav system. Therefore, it was decided that a clean start should be made with anew, modern pension system. While it was important to address the issue of previouscontributions, it was agreed that UNMIK should not formally assume liabilities of theBelgrade pension fund. Claims on Belgrade should be addressed in discussions with them.

Create a pension system that covers the whole population. European countriespresent a wide array of possible pension schemes, with various mixes of funded PAYG,mandatory and voluntary, private and public components. The one feature common to allEuropean countries is that the systems cover almost the entire population. In contrast, inKosovo, the Yugoslav pension system covered only about half of the elderly in 1998.

-Address the needs of all population groups: The relevant populations groups could becategorized as follows:

1) The elderly who contributed to the past system (up to 25,000old-age pensioners, or less than 1.5% of the population, who felt they are entitled tobenefits based on these past contributions; plus approximately 25,000 over 65 who werereceiving survivor and disability pensions);

2) The elderly who did not contribute to (orwere excluded from) the past system (roughly 90,000, or up to five percent of thepopulation, who may be equally in need of a pension as those who contributed); and

3)The current working-age (up to 1.4 million individuals 16-65, who were not makingcontributions to any pension system and were not earning entitlements to any futurepensions).

- Seek a comprehensive solution. The best pension policy would be one that addressesnot only immediate political pressures and budget constraints, but one that also leadsalong a path to creating a pension system that is sustainable in the long-term, givenchanging demographics, and is consistent with the development of a market economy.
- Take advantage of the political window of opportunity. This was a period whenpolitical pressure to address pension issues was high and the governing authorities hadthe capacity to enact a well-thought-out proposal that recognizes budget constraints andaddresses concerns regarding sustainability.
- Address ethnic concerns. All pensioners and workers should be allowed to participatein the new system on equal terms regardless of ethnicity. An issue arose because somepeople continued to receive pensions from Belgrade while most did not. A politicaldecision was taken to give everyone in Kosovo pensions even if they also receivepensions from Belgrade or have other sources of income.
- Promote economic development. To the extent feasible, the pension system shouldfacilitate savings and investment of the population, rather than relying on mechanismsthat are similar to issuance of government debt. Furthermore, the pension system shouldpromote development of the labor market, suggesting that contribution rates be set atreasonable levels and that pension programs offer participants acceptable returns on theircontributions so that there are incentives to participate.

- *Overview of the Three Pillars*

In December 2001, following extensive policy discussions with all political parties,UNMIK approved the implementation of a three-pillar pension system, as defined in 21UNMIK Regulation 2001/35.

Pillar I, is comprised of a basic pension and a disabilitypension. The basic pension pays a flat benefit to all habitual residents of Kosovo who are65 years of age and older. The decision to opt for a new, universal, flat benefit was basedon:

1) a desire to avoid high contribution rates and to promote long-term fiscalsustainability;
2) the low rate of coverage provided by the old system;
3) the poor state ofcontribution records for the old system;
4) political challenges in determining how toequitably treat those who were forced out of their jobs and denied the opportunity toparticipate in the pension program in the decade following the political changes of 1989.

The new basic pension is designed so that it does not discriminate based on work history,sex, or ethnicity. The benefit is funded from general government revenues, on a pay-asyou-go basis, with universal eligibility upon reaching age 65 regardless of other incomesources. The amount of the monthly benefit is determined annually during the budgetingprocess, based on the methodology set out in Law 2002/1, and is reflective of the cost ofa minimum consumption food basket, initially defined by the World Bank. The disabilitypension is similar in all respects except for eligibility, which is determined based onmedically-confirmed, permanent disability. The implementations of the basic pensionand the disability pension are governed by separate laws that were passed in the KosovoAssembly. These laws were enacted by the PISG rather than UNMIK due to the fact thatauthority over Pillar I of the pension system was "transferred" from UNMIK to the PISG,through the Ministry of Labor and Social Welfare, while jurisdiction over financialinstitutions such as the KPST remained "reserved" to UNMIK.

Pillar II of the system is a mandatory, defined-contribution, savings pension program.The program requires all working, habitual residents of Kosovo to contribute 5% of grosssalary to the pension trust. This worker contribution is matched by an additional 5%payment from the employer.Both workers and employers are eligible to voluntarilycontribute an additional 10% of gross salary. Thus, the maximum total contribution(mandatory and voluntary) for each individual per month is 30% of gross salary.Contributions and records are managed by the Kosovo Pension Savings Trust, anindependent body established solely for the purpose of administering the savings pensionsystem. The intent of the program is that, at the time of retirement (or permanentdisability), an individual's pension savings are used to purchase a pension annuity.

Pillar III of the system provides for supplemental, individual or employer-sponsoredpension schemes. The pension regulation mandates the Banking and Payments Authorityof Kosovo (BPK), Kosovo's financial regulatory body, to license

and regulate all PillarIII pension schemes.