

Finnish Experience of Raising the Employment Rate of Older Workers

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In Finland the development of the employment rate of older workers has in recent years been more positive than in many other European countries. This article discusses the measures taken in Finland to address the effects of the ageing work force. These measures include major reforms of the pension system. For example, employees will have a 4,5% increase in their pension for every day they stay on at work after the age of 63 until they reach 68. The article also discusses the elements which induce people to work longer.

I. General features of the Finnish Pension System

The Finnish pension scheme was established in 1962 with an idea to have a high penetration, to integrate the new system to private pensions, which existed before 1962, and to build the organisation on existing insurance companies and pension funds. The scheme is compulsory: the employers have to take pension insurance for their employees. Self-employed must insure themselves.

The contributions are shared by employers and employees. The employers take the payment of an employee from his/her wage, and forward it to pension insurance company, industry-wide pension fund or company pension fund. The penetration rate of the system

is 100%, since the accrual of the pension does not depend on the type of the employment.

The scheme is of the defined benefit type. However, from 2005 onwards the benefits are based on life time earnings making the system resemble a notional contribution defined system with index linking playing the role of investment return. The benefits include old age, disability and survivor's pension.

The retirement age is flexible between 63 - 68 years. Accrual rate is normally 1,5% up to age 53, 1,9% between 53 and 62 and 4,5 % between 63 and 68. Life expectancy coefficient adjusts the pension to the observed change in life expectancy. For example, the expected

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value of the coefficient in 2030 is about 0.9.

The scheme is partly funded (about 30 % funding rate) and partly as PAYG. The scheme is not based on individual accounts, although the funded part of the accrued pension rights is defined on individual basis. Both contribution and benefits include a well-defined funded component and the corresponding money flows and book-keeping follow. Due to the fact that funded and PAYG parts are integrated, the PAYG part of benefits is the smaller the higher the returns on investments have been.

Private insurance companies, industry-wide pension funds and company pension funds handle pension insurance and they compete with each other within certain limits. They are supervised by the Insurance Supervisory Authority. Each institution is liable for the funded part of pensions insured in that institution and manages the corresponding assets.

Accrued benefits are registered at the Finnish Centre for Pensions (ETK), who is also the clearing house for the money-flows needed between pension providers. Each individual can check his/her accrued benefits via Inter-

net. From 2008 onwards each citizen will automatically annually receive a report of his/her accrued pension and an estimate of the final pension.

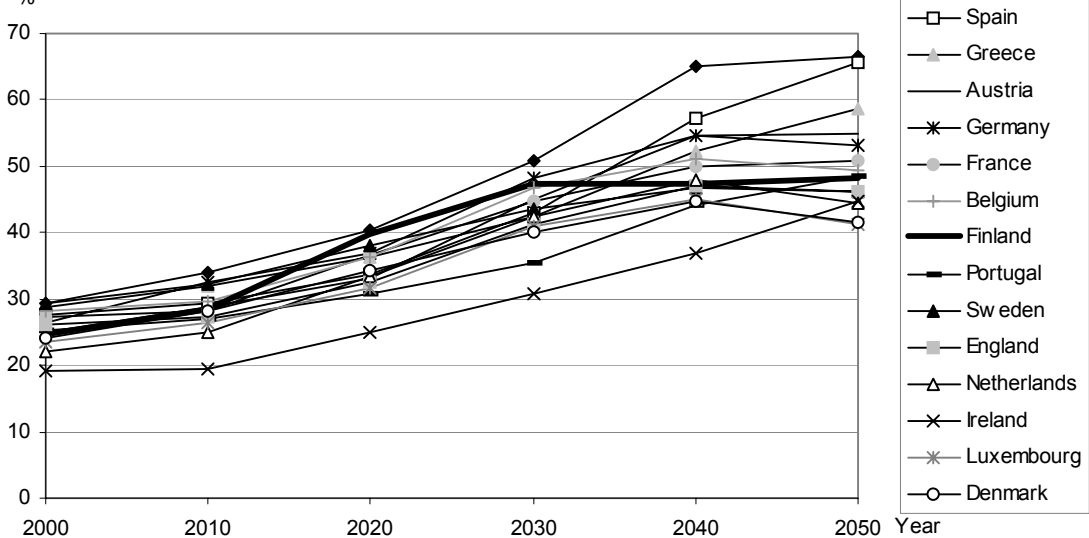
The annual administration and transaction costs of the asset management are approximately 0.3 per cent of the market value of the assets. Total operating expenses of the earnings-related pension schemes are 3.1 per cent of the premiums written. Low costs are due to the fact that the insurance is compulsory plus that it is the employer not the employee who makes the choice between insurance providers.

2. Concern about an ageing population and about employment behind the reforms

The Finnish old-age dependency ratio is deteriorating rapidly and will become the weakest in the EU by 2020 (Figure 1). The reason is the retirement of the post-war baby-boomers.

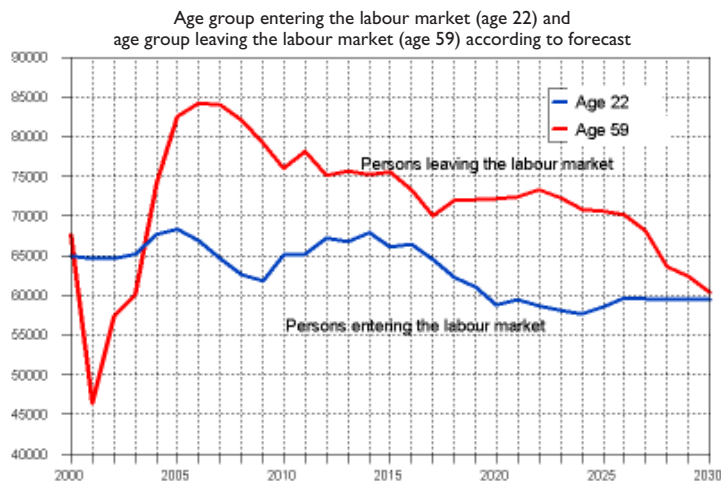
During somewhat over two decades more persons will exit the labour market than young age groups will enter it (Figure 2).

Figure 1. Old-age dependency ratio in EU-15 2000-2050



Source: Eurostat

Figure 2: Change in labour supply potential in 2000-2030



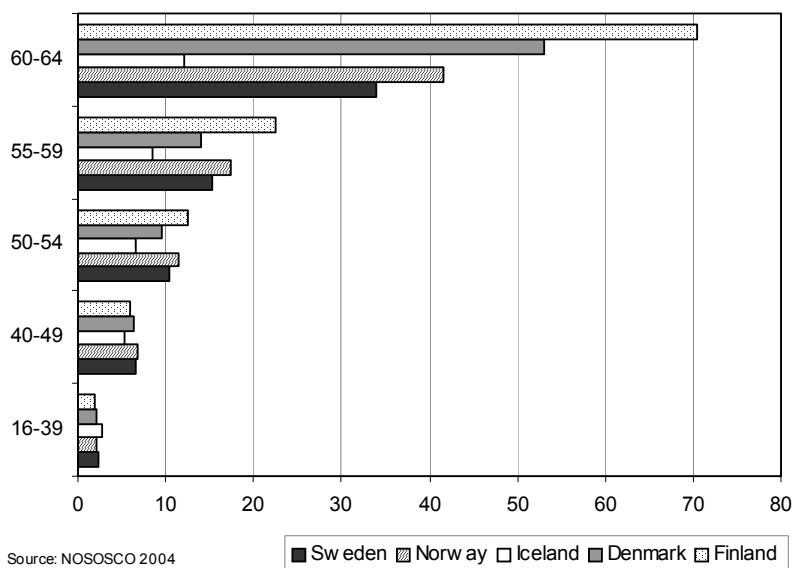
Source Statistics Finland

The concern about sufficient labour force and about the weakening old-age dependency ratio is justified in Finland, since people enter the labour market late and retire early. The average effective retirement age is 59 years. The share of persons aged 55-64 who have retired of the whole age group is high in

Finland from a Nordic perspective. The share is especially high for persons aged 60-64 (Figure 3).

In Finland, of the persons in this age group almost three-fourths are retired, in Denmark about half, in Norway less than half, in Sweden one-third and in Iceland only a good tenth.

Figure 3. Pension recipients by age as percentages of the age group in 2002



Compared to the other Nordic countries the Finnish profile is a country which clearly makes the most frequent use of pre-retirement pensions.

The differences between the countries can be explained by differences in the build-up of the pension schemes and benefits and also by different labour market developments. In Finland the high proportion of retired people aged 60-64 is in part due to the exceptionally deep recession at the beginning of the 1990s. A significant number of persons aged over 60 have retired on an unemployment pension. Every fifth person aged 60-64 receives an unemployment pension.

3. Recent trends in the retirement and older age employment

The Finnish pension scheme has been reformed over somewhat more than a decade with the aim of increasing the effective retirement age and restricting the growth in pension expenditure in the long term. The change from an early retirement policy to postponing retirement occurred already at the turnover between the 1980s and the 1990s. In the 1980s the pre-retirement pension schemes were extended and new benefits were introduced. During the previous decade several considerable changes were made to the earnings-related pension scheme to postpone retirement and to cut the growth in pension expenditure. The reforms were mainly carried out on the basis of the report by the pension committee from 1990. The aim of the measures suggested by the committee was to increase the effective retirement age by three years by 2020. Over the period 1990-2004 the increase has been over one year.

The development work which started with the pension committee in 1990 reached its peak in the private sector in autumn 2002, when as a result of negotiations between the labour market organisations an extensive “pen-

sion package” was agreed on. The aim of the pension reform is to postpone the effective retirement age by 2-3 years, adjust the scheme to the increasing average life expectancy and create the bases for a unification of the private-sector earnings-related pension acts. Parliament approved the private-sector pension reform in spring 2003. As to its main parts the reform took effect from the beginning of 2005. The pension reform was also extended to the public sector as to its main parts with the same contents as in the private sector.

The structure and the incentives of the pension system are important elements in attempts to lengthen the working careers. It is equally important to promote work ability, especially that of older employees. Since the late 1980s employers in Finland have been encouraged to introduce so-called work ability programs. Experiences of them have been very positive. Pension insurance companies usually participate in those programs, by advice and also by financing.

The expected effective retirement age

To measure the effective retirement a new indicator is used, the expected effective retirement age (expectancy). The indicator is comparable to the indicator for the life expectancy. It describes the average effective retirement age for a person of a specific age on the condition that the age-specific retirement risks and the mortality rates stay at the level of the year concerned.

The Finnish Centre for Pensions has developed the expectancy, because the old indicators (the median and the average retirement age) can not be used to measure changes which occur over time. Due to the Finnish age structure, as the population ages also the average age of those retiring increases even if the incidence rate of new pensions for each age group would not change. For instance the average age of those who have retired would

Figure 4. Expected effective retirement age (i.e. expectancy). Persons retired from the private sector



Source: Finnish Centre for Pensions

in the period 2005 – 2010 increase by about one year with no change in the incidence rate. This is primarily a consequence of the post-war baby-boomers nearing retirement age.

The Finnish Centre for Pensions calculates the expectancy for both 25-year-olds and 50-year-olds. The expectancy for 25-year-olds reflects mainly the whole population which is insured for earnings-related pension benefits. Of those retiring, about 15 percent are less than 50 years old. Illnesses and injuries in this group often prevent working. Calculating the expectancy for 50-year-olds is needed because pension policy is most effective beyond this age.

Figure 4 shows, how the expectancy has changed in the last 20 years in the private sector of the Finnish earnings-related pension scheme. In

1986 the expectancy plummeted because new flexible retirement programmes were introduced. As a result an uncommonly large number of persons aged 55-64 retired on these new types of pension. After that the effective retirement age started increasing.

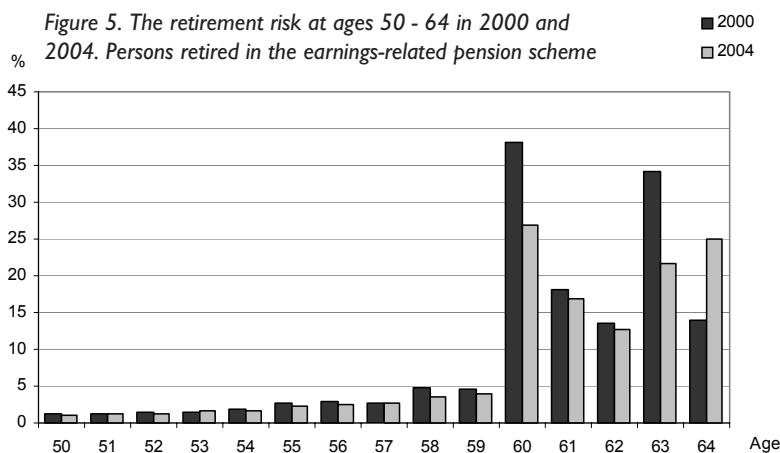
Over the last six years particularly the rise of the expectancy for 25-year-olds has been quite modest. However, for 50-year-olds it has been favourable since the expectancy has

increased by about half a year in the last five years as a result of the decrease in the retirement risk at ages 50 – 64 (see figure 5).

The changes in employment

In the early 1990s Finland experienced a deep economic recession and as a result the employment rate of the elderly decreased dramatically (table 1) from the peak of 1989. In the middle of the 1990s the recession turned into economic boom and since then the em-

Figure 5. The retirement risk at ages 50 - 64 in 2000 and 2004. Persons retired in the earnings-related pension scheme



Source: Finnish Centre for Pensions

ployment rate of older workers has clearly risen. For 55-59-year-olds the improvement has been particularly good and nowadays the employment rate is even higher than before the recession. A similar growth can also be seen in the age groups 60-64.

Table 1. Employment rates in Finland by some age groups, %

Age / year	1989	1994	2000	2004
45-49	90	78	84	83
50-54	83	74	79	80
55-59	58	49	59	66
60-64	26	17	23	29
15-64	74	60	67	67

Source: Labour Force Survey

The main reason for the rise in the employment rate of older workers is the decreased exit rate from employment. An important explanation for this is the strong economic growth and demand for labour. However, there is also good reason to believe that two pension reforms that took place in the second part of 1990s as well as the increasing popularity of the work ability programs have had a significant influence.

Table 2 gives the employment rate of older workers and its recent changes in the EU-15. Finland has experienced the largest increase in the employment rate during 1997-2002.

Long-term scenarios

The Finnish Centre for Pensions publishes regularly reports presenting long-term scenarios of the development of the Finnish statutory earnings-related pension scheme. The latest report extends to the year 2075.

In the baseline scenario the total employment rate is expected to rise modestly from the current approximately 67 per cent by about 3 percentage points by 2025 and by about 4.5 percentage points by the end of the calculation period. The expected effective retirement age for employees is assumed to increase from the current approximately 59 years by 2 years by

Table 2. Employment rate of older workers (55-64 years) and recent changes in the European Union

	2002	Cap below 2010 target	Change 2001-2002	Change 1997-2002
S	68.0		1.3	5.4
DK	57.8		-0.1	6.1
UK	53.5		1.2	5.2
P	50.9		0.9	2.7
IRL	48.1	1.9	1.2	7.7
FIN	47.8	2.2	2.1	12.2
NL	42.3	7.7	2.0	10.3
EL	39.7	10.3	1.8	-1.2
E	39.7	10.3	0.5	5.6
D	38.4	11.6	0.5	0.3
F	34.8	15.2	2.9	5.9
A	30.0	20.0	1.0	1.7
I	28.9	21.1	1.0	1.0
L	28.3	21.7	2.7	4.4
B	26.7	23.3	1.6	4.7
EU	40.1	9.9	1.4	3.7
2010 Target		50 %		

Source: European commission

2025 and by 3 years by 2050. Increase in life expectancy and in expected effective retirement age means that in 2050 the average time in retirement is a good 3 years longer than currently. This can be characterized as a cautious rather than as an optimistic scenario.

4. Features of the Finnish pension system affecting the retirement age

One of the most important factors for a person to improve and maintain work ability is to have possibility to develop his or her professional and vocational qualifications and keep them up to date. This possibility will be undermined if the change of an employer is hindered by disincentives in the pension system. There are several features in the Finnish pension system, which promote the mobility of the workforce:

- the pension accrues from all work and at the same rate irrespective of the employer (private or public, small or large)
- eligibility and vesting period are both zero (practically taken each euro earned gives you a pension accrual)

- the accrual of the pension is independent of structure of the working carrier (public or private employer, short or long working contracts, part-time or full time etc.)
- index-linkage of the accrued benefits more than preserves the purchasing power (index is the mixture of 80% earnings index and 20% of CPI)

There are incentives to the employers to promote work ability:

- The earnings related pension system includes disability benefits. The contribution for them is experience rated for larger employers in order to get them to promote the work ability
- Employers with less than 50 employees pay a flat-rate contribution which is proportional to the wage and independent of the age of the insured. For companies with at least 50 employees the total contribution varies according to the age of the insured and the size of the firm. In firms with exactly 50 employees the contribution is determined as an average contribution on the basis of age, but as the firms become bigger the experience rate based part of the contribution increases so that employers with more than 800 employees pay fully their own disability costs.

Incentives for the employee to continue in the work include:

- Part-time pension is meant to make possible for older people to continue in the work in part time. The age limit for part-time pension has been raised to 58 from 56 for employees born in 1947 and later.
- Vocational rehabilitation became in 2004 a personal right for people at risk of becoming disabled. After pension reform vocational rehabilitation is the primary alternative to a disability pension. The rehabilitee receives full or partial rehabilitation allowance, and the allowances are always higher than plain disability pensions

- The accrual rate increases with age. Pension accrues at the rate of 1.5 per cent on the annual earnings until the age of 53, at 1.9 per cent between the ages of 53 and 62 and at 4.5 per cent between the ages of 63 and 68.
- In the new scheme it is possible to retire on an old-age pension flexibly between the ages of 63 and 68 instead of at the previous fixed retirement age of 65. On the other hand, the possibilities of retiring early were weakened as the age limit for the early old-age pension was increased from 60 years to 62 years. Taking the old-age pension early reduces the pension permanently.
- In the future the decreasing effect of the life expectancy coefficient on the pension amount can be compensated by working longer.

The possibilities to use different forms of early retirement have been reduced:

- The unemployment pension will be gradually phased out, and the income of unemployed people born after 1949 will be ensured through unemployment security.
- Individual early retirement pension (a relaxed form of disability pension) has been abolished and instead, the occupational disability of people over 60 will gain emphasis in assessment of their right to disability pension in cases where they have had a long working career and continued work would be unreasonable.

The employers in Finland have been encouraged to introduce so-called work ability programs as well. Pension insurance companies usually participate in those programs, by advice and also by financing. There are also several government sponsored programmes, which give both general and employer specific support to work ability.

5. What induces people to work longer?

Economic incentives have an effect

The Finnish Centre for Pensions and the Finnish Pension Alliance TELA have made surveys and opinion polls to clarify the employers' and the oldest employees' views to continue at work and to ask their opinions on the pension reform also more generally.

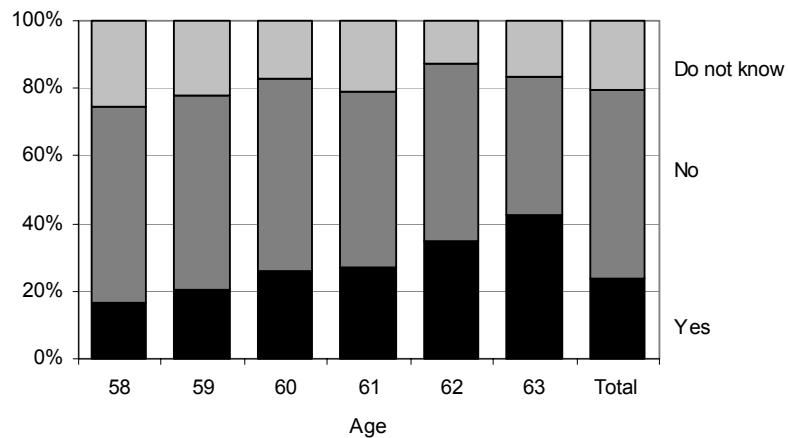
According to the employee survey "Flexible Retirement Age", about a quarter of the oldest private-sector employees thought they would continue working beyond the age of 63 in order to get a higher pension. The interest in continued work increases with age. A partial explanation for this is that the employees with the best work capacity and with the strongest willingness to work have stayed on in working life (Figure 6).

Good health is an important precondition in order to be able to consider continued work in order to get a higher pension. Also the person's education and training has an effect. Highly educated persons think more frequently than less educated persons that

they will continue working after having reached the age of 63.

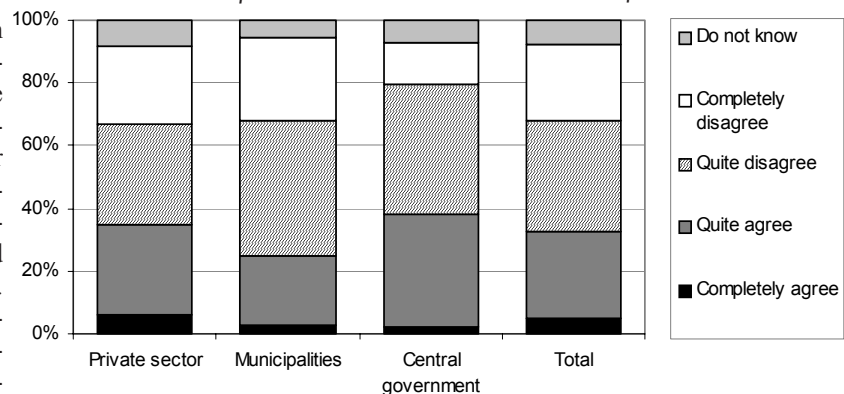
Realising these intentions to continue working would mean an increase in ageing people's participation in working life in Finland. However, we are not talking about a very significant increase in employment rates. The cautiously positive evaluation can also be explained by the employers' view of the significance of the accelerated accrual rate. Par-

Figure 6. Does the accelerated accrual rate of 4.5% increase the willingness to continue working beyond the age of 63



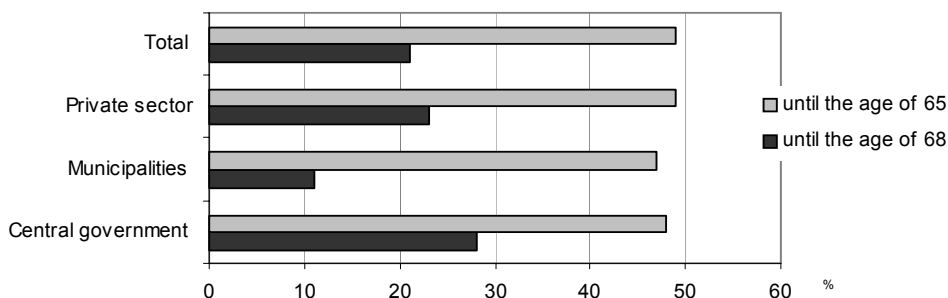
Source: Finnish Centre for Pensions

Figure 7. Employers' answer to the argument: continuing at work will increase at our workplace due to the accelerated accrual rate of 4.5%



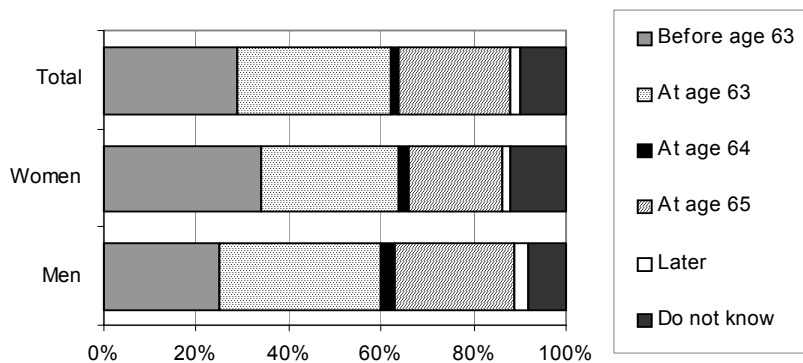
Source: Finnish Centre for Pensions

Figure 8. Proportion of establishments who agree with the argument: at our workplace in most duties employees can very well continue at work until the age 65 / 68



Source: Finnish Centre for Pensions

Figure 9. Retirement intentions by gender, oldest employees in the private sector



Source: Finnish Centre for Pensions

participation in working life among ageing persons is expected due to this factor to increase in about a third of the establishments (Figure 7). In large establishments, belief in the effect of economic incentives is slightly more frequent than in small ones.

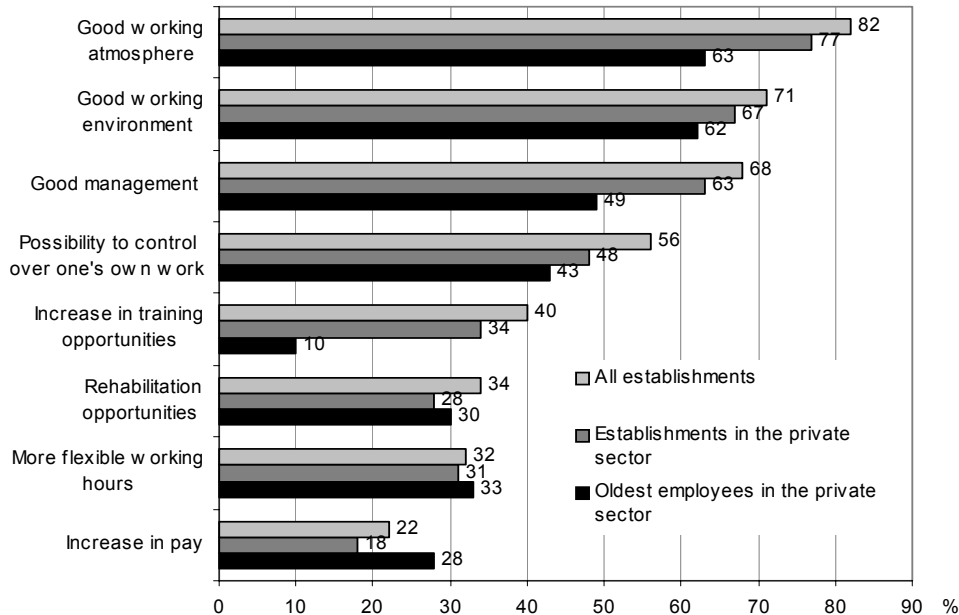
Good chances for longer work histories

The employers find the ageing employees' possibilities of continuing work for a long time as fairly good: at about half of the establishments most employees could well continue working until the age of 65 and at about a fifth of the establishments to the new upper

age limit of 68 years for the old-age pension (Figure 8). At present only about 15 per cent of the age group continues working until the age of 65.

In view of these results there are clearly more possibilities of continuing work than there is an interest among the oldest employees to continue working until the age of 65 or 68 (Figure 9). A fifth of the oldest employees estimate, that they will continue working to the age of 65 and only some two or three per cent to the age of 68. Thus there seems to be more problems on the supply side than on the demand side as regards the labour force.

Figure 10. The proportion of those who consider measures very important for coping at work for as long as possible



Source: Finnish Centre for Pensions

Factors related to wellbeing at work are very significant

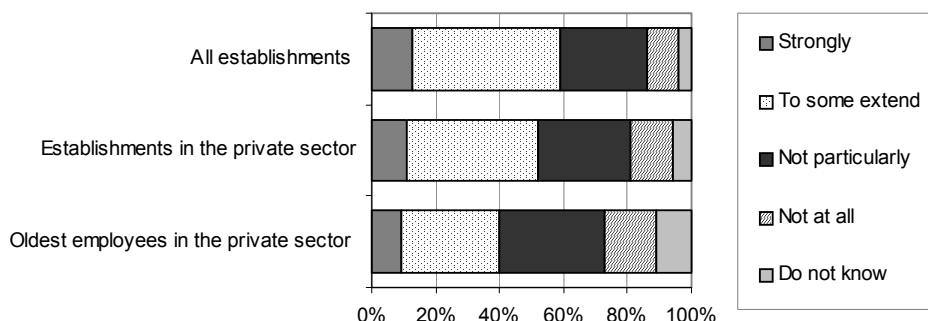
According to the employer and employee studies, more important than economic incentives are factors related to the workplace community. Topping the list of important factors related to the working conditions are a good atmosphere at work, a properly functioning work environment and good management (Figure 10).

The possibility to influence one's own work is also found to be important. It is worth noting the similarity of the views of both employers and employees. On only two issues the viewpoints somewhat differ. Further vocational training is clearly more appreciated among employers than among employees. On the other hand, the employees more generally

than the employers emphasise increases in the wage or other rewards. Still, also in the employees' ranking the remuneration is listed among the issues that are not very important.

The importance of the work ability programs is clear from the studies. According to the employer study, in more than half of the establishments the employees are encouraged to continue working until the retirement age. Strong support is given in about a tenth of the establishments (Figure 11). The same question was also posed in the employee study and the viewpoints were similar also here. However, a slightly smaller proportion of the employees than of the employers were of the opinion that the employees were supported to continue at work.

Figure 11. Do the practices at the workplace support employees' continuing work until retirement age?



Source: Finnish Centre for Pensions

6. Conclusions

The prospects for the aim of longer work histories and postponed retirement are good. According to the employers' assessment there are fairly ample possibilities to continue working compared to the current participation in working life of the oldest employees and the employees' intentions to continue working between the ages of 63 and 68.

Economic incentives including those of the pension system are important but still increasing the attractiveness of working life is the key to longer work histories. It is also important to care for the ageing employees' work capacity and to develop the working conditions while

taking into account the ageing workforce. In this respect the work ability programmes are a useful tool.

Despite the need for and the importance of these measures whether the work histories will become longer depends ultimately on a favourable economic and employment development.

Acknowledgements

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