

Assessment of the Lithuanian State Pension System

Final report
of the project SRSS/C2018/11

Experts:

Lauri Leppik
Magnus Piirits

Tallinn University
Estonian Institute for Population Studies

November 2018

Table of Contents

Executive summary	4
Introduction	7
I. Occupational state pensions	10
1. Description of scheme parameters	10
1.1 State pensions for officials and servicemen	10
1.2 State pensions of judges.....	12
1.3 State pensions of scientists	13
1.4 Benefits of stage artists	14
2. Descriptive statistics on occupational schemes	16
2.1 Number of beneficiaries by gender, age and type of benefit	16
2.2 Employees in covered occupations	18
2.3 Benefit amounts and replacement rates.....	23
3. Legal analysis of Constitutional Court case-law on occupational pensions	25
4. Analysis of policy inconsistencies.....	28
5. Projections.....	34
6. Reform options.....	36
II. Merit-based state pensions	47
1. Description of scheme parameters	47
1.1 State pensions of the first and second degree	47
1.2 Annuities for former sportsmen.....	48
1.3 Annuities for signatories of Independence Act	49
2. Descriptive statistics on merit-based schemes	50
2.1 Number of beneficiaries by gender, age and type of benefit	50
2.2 Mothers of 5 or more children	52
2.3 Benefit rates	54
3. Analysis of policy inconsistencies.....	55
4. Projections.....	57
5. Reform options	58
III. Compensatory benefits	61
1. Description of scheme parameters	61
1.1 State pensions for victims	61
2. Descriptive statistics on compensatory scheme for victims	61

3. Projections.....	63
4. Reform options.....	65
Summary	66
Annex 1: Review of Constitutional Court rulings on state pensions	71
Annex 2: Analysis of international law on social rights as regards supplementary pensions.....	79
Annex 3: Lithuanian State Pension Model LitPen structure and assumptions	81

Executive summary

The report provides an analysis and assessment of state pensions in Lithuania, which constitute special regimes in the Lithuanian public pay-as-you-go pension system. These special state pensions are financed from the state budget and supplement the pension rights arising from the social insurance system.

The state pensions fall into three categories, each serving significantly different social-political aims and functions: occupational, merit-based and compensatory benefits. Occupational benefits are essentially special employer's pensions paid to selected occupational groups: officials and servicemen, judges, scientists and stage art workers. Merit-based benefits acknowledge some special merits for Lithuanian state or society – Signatories of the Independence Act, freedom fighters, resistance participants, Olympic champions and medal winners, World and European champions and record holders, Cultural Prize winners, blood donors and parents of 5 or more children. Compensatory benefits compensate for specific losses the person has suffered – these are mainly victims of Soviet repressions etc.

Structure and content of analysis

The analysis is structured along the three categories of benefits. For each type of benefit, the personal scope, eligibility criteria, benefit calculation rules and payment conditions are described. This is followed by descriptive statistics on the number, age and gender profile of beneficiaries, benefit rates and expenditures. For occupational state pension schemes, an age and gender profile of employees currently earning state pension rights through their employment is also analyzed.

Based on the description of the current scheme parameters and benefit rules, and statistics on beneficiaries, we analyze the policy inconsistencies of the current system of state pensions. As regards the occupational state pensions we also provide a legal analysis of relevant Constitutional Court case-law to identify existing legal constraints on possible reform options.

Using the LitPen model developed within the framework of this project, we simulate the evolution of the number of beneficiaries and expenditures of state pensions by benefit schemes. Projections are provided firstly under the base scenario of maintaining the current legislation. Beyond the base scenario we also analyze some reform alternatives.

Main findings

The general notion emerging from the assessment is that of state pensions cover a diverse spectrum of benefits. There is a considerable variation of objectives, eligibility criteria, benefit rules and benefit rates both across the three categories of state pensions

as well as within each of these categories between different types of benefits for different groups. Even within the category of occupation pensions there are large differences in eligibility ages, qualification periods, benefit determination principles, accrual rates, benefits ceilings, payment conditions and sanctions across occupational groups. Such differences in treatment are not objectively grounded with empirical findings related to the nature and conditions of employment. There are large differences in benefit rates, ranging from 60 EUR per month for victims to over 1200 EUR per month for former sportsmen and Signatories of Independence Act. This may raise questions as to whether there is a balance between the principles of justice, reasonableness and proportionality, emphasized by the Constitutional Court.

Early retirement: State pensions for officials and servicemen allow early retirement with very low effective age of retirement. The median age of retirement in the scheme for officials and servicemen is 47 for men and 53 for women, extending the average retirement duration of eligible men for about 11 years and for women about 8 years compared to persons who retire at the general pension age.

Indexation: The absence of regular statutory indexation of state pensions (with the exception of benefits for former sportsmen and signatories) reduces the purchasing power of state pensions over time during the payment period, compared to social insurance pensions, which are indexed annually.

Relative importance of schemes: The number of beneficiaries is highest in the category of compensatory benefits for victims of repressions – about 65 thousand persons or 62% of the total number of beneficiaries of state pensions in Lithuania in 2017. On the other hand, expenditures are highest for the state pensions of officials and servicemen – about 67,5 mln EUR or 48% of the total expenditures on state pensions in Lithuania in 2017.

Future development: As regards the future evolution of state pension schemes under the base scenario, the schemes have diverging trends related to the fact that the schemes are in different stages of maturation:

1. The number of beneficiaries of state pensions for victims will decline due to mortality, provided the personal scope of the scheme is not extended to other groups and no new categories of victims emerge. As a result, the costs of these state pensions will steadily decline.
2. The future evolution of merit-based state pensions is determined by the largest sub-scheme of second degree state pensions for parents of 5+ children. The number of beneficiaries of this scheme would decrease over the next decade until 2027, but would increase thereafter due to increasing life expectancy unless the general pension age is increased further.
3. The scheme of state pensions for officials and servicemen is expected to see the highest increase in the number of beneficiaries unless any reforms to

contain this increase are undertaken. The number of recipients of this scheme would increase by about 13 thousand persons to reach 35 thousand by 2040 due to low median age of retirement and long period of benefit payment. As a consequence, expenditures of this scheme of state pension for officials and servicemen are projected to increase by about 1.7 times by 2040 years to reach 0.24% of GDP.

Reform options: The report also analyzes some possible reform scenarios, in particular as regards the scheme for officials and servicemen, where the identified sustainability risks are the highest. Based on the analysis presented in the report, the Lithuania authorities may want to consider which reform options to undertake with a view to balance fairness, adequacy and sustainability considerations.

The analysis was financed by the European Commission Structural Reform Support Programme project SRSS/C2018/11.

Introduction

The report contains an analysis of state pensions in Lithuania, projections on the evolution of the number of beneficiaries and expenditures and an outline of possible reform options.

The state pensions may be regarded as special regimes in the overall public pay-as-you-go pension system of Lithuania. These benefits either substitute or supplement the social insurance pensions, which are the core of the Lithuanian public pension system. In contrast to the social insurance pensions, which are financed from the social security contributions, the state pensions are financed from the allocations of the state budget.

It is not unique for Lithuania to have some small special pension schemes for selected groups. However the context, the factors that led to introduction of such schemes in the past, the policy choices as regards the choice of covered persons, eligibility rules and other scheme parameters are unique and specific to the national circumstances.

From the analytical perspective, the Lithuanian state pensions may be considered as falling into three categories:

- 1) occupational benefits;
- 2) merit-based benefits;
- 3) compensatory benefits.

A similar distinction of Lithuanian state pensions was made by the Constitutional Court of Lithuania in its ruling on the state pensions of officials and servicemen from 4 July 2003 (see below).

Each category of state pensions serves somewhat different social-political functions.

Occupational benefits may be regarded as special employer's pensions, in the instant case paid by the state as an employer (or the former employer) to selected occupational groups. State pensions for officials and servicemen of interior affairs and military, for judges, for scientists and for stage art workers fall into this category.

Merit-based benefits acknowledge some special merits the person has in front of the Lithuanian state or society. Such merits may be either achievements accumulated over a longer time period or single acts. Signatories of the Independence Act, freedom fighters, resistance participants, Olympic champions and medallists, World and European champions and record holders, cultural prize winners, blood donors and mothers or fathers of 5 or more children belong to this category.

Compensatory benefits compensate for specific losses the person has suffered. Such losses are socially recognised, but there is no other counterpart accepting responsibility. Victims and persons who suffered hardship during World War II, during the Soviet period or at the time of regaining of independence in 1991 fall into this category.

Given the different nature and social-political objectives these types of benefits carry, the analysis in this report is structured along the three categories of benefits: occupational, merit-based and compensatory.

For each category of benefits the following analytical elements are presented:

- description of the key parameters of schemes
- descriptive statistics on the number and age structure of beneficiaries, pension rates and expenditures
- projections on the evolution of the number of beneficiaries and expenditures
- legal analysis of reform options
- identification of policy inconsistencies

Parameters of schemes of the different types of state pensions are described along a common structure. The descriptive characteristics of schemes serve as a basis of subsequent qualitative and quantitative analysis. It also illustrates the diverse spectrum of benefits under the general umbrella notion of state pensions as well as within a specific branch of benefits.

The law on state pensions, containing the regulation of the first and second degree state pensions and the state pensions for victims was adopted in Lithuania in 1994 and entered into force from 1995. Other types of state pensions are regulated by separate acts.

Legal act	Year of enactment
Law on state pensions	1995
Law on state pensions of officials and servicemen	1995
Provisional law on state pensions of scientists	1995
Law on state pensions for judges	2003
Law on the status of the signatories of the independence act	2004
Law on professional stage art	2005
Law on physical education and sports	2009

Table 1. Laws regulating state pensions and years of enactment.

The date of enactment of respective laws establishing state pensions for designated categories has relevance as regards the maturation of respective benefit sub-schemes, influencing the number and age structure of current beneficiaries. Whereas the occupational schemes for officials and servicemen and for scientists, the merit-based first

and second degree state pensions and the compensatory benefits for victims have been by now in force for 23 years, the occupational schemes for judges and stage art workers, and the merit-based benefits for former sportsmen have a shorter history, having been in force for respectively 15, 14 and 10 years. However, there have also been some later amendments extending the scope of persons eligible to some state pensions. As examples, from 2014 the personal scope of second degree state pensions was extended to mothers of 5 or more children, whereas earlier mothers of 7 or more children were eligible. From 2017 the personal scope of compensatory benefits for stage artists was extended to circus performers, conductors, actors and musicians other than playing wind instruments.

I. Occupational state pensions

1. Description of scheme parameters

The first section outlines the key parameters of four types of occupational state pensions:

- 1) pensions for officials and servicemen;
- 2) pensions for judges;
- 3) pensions for scientists;
- 4) benefits for stage art workers.

1.1 State pensions for officials and servicemen

The scheme is regulated by the Law on State Pensions of Officials and Servicemen, in force from 1995.

Personal scope

Officials of the Ministry of the Interior, the police, the State Border Security Service and other institutions of the Ministry of Interior, officials of the Special Investigation Service, servicemen of professional military service, officials of the system of the State Security Department, officials of the Prosecutor's Office, officials of the Department of Prisons and of the establishments and state enterprises which are subordinate to the latter.

Contingencies as defined by law

- Superannuation (attaining prescribed years of service in qualifying occupations)
- Loss of work capacity due to service
- Redundancy due to results of the medical examination or loss of work capacity unrelated to service

Risks covered

Superannuation, incapacity for work, survivorship

Qualifying conditions

The qualifying length service requirement varies across contingencies, different occupational categories, and time of entering the service:

- 1) 25 years of service for officials and servicemen of the interior affairs, police, defence forces, border security service, special investigation service, the prison department and customs (the qualifying period is lower, from 20–24,5 years for

- officials and servicemen who entered service before 1.1.2016 and by that time had service periods from 11 to 19 years);
- 2) 20 years of service and attaining of statutory pension age for officials of the prosecutor's office;
 - 3) 5 years of service for officials and servicemen who are made redundant as a result of the medical examination or loss of work capacity unrelated to service
 - 4) 5 years of service for official and servicemen who have reached the statutory mandatory retirement age (or in its absence the statutory social insurance pension age)

Benefit calculation

The following accrual rates are applied to calculate a state pension for length of service to officials and servicemen:

- 1% of the reference wage for the first 20 years of service;
- 1,5% for 21-25 years of service;
- 1% for each year of service from 26 years onwards.

The reference wage is the average monthly wage of the most favourable 12 consecutive months from the period of 5 consecutive years.

Beneficiaries under pension age who are unemployed or with insured income less than minimum wage receive a supplement in the amount of social insurance basic pension (152 EUR).¹

To calculate the amount of work incapacity pension, the accrual rates relate to the loss of work capacity:

- 1,2% of reference wage per year of service in case of loss of work capacity 75-100%
- 1% in case of loss of work capacity 60-70%
- 0,5% in case of loss of work capacity 45-55%

To calculate work incapacity pensions for service related reasons and survivors pensions, in the length of service of the person was less than 25 years, the length is assumed to be 25 years for the purposes of benefit calculation.

In case of soldiers of mandatory military service who lost the work capacity due to service, a flat-rate incapacity pension is paid, depending on the loss of work capacity:

- 2 state social insurance basic pensions in case of loss of work capacity 75-100%
- 1,5 state social insurance basic pensions in case of loss of work capacity 60-70%

¹ In 2018 the minimum gross monthly wage in Lithuania is 400 EUR. In 2017 the minimum monthly wage was 380 EUR.

- 0,75 state social insurance basic pensions in case of loss of work capacity 45-55%

Payment conditions

The total sum of state pension and social insurance pension may not exceed 1.5 times the average national wage.

1.2 State pensions of judges

Regulated by the Law on state pensions of judges, in force from 2003.

Personal scope

Persons working as:

- judges of the ordinary and specialised courts of Lithuania
- judges of the Constitutional Court, Supreme Court, Court of Appeal and Supreme Administrative Court
- judges from Lithuania appointed or elected to international courts

Qualifying conditions

- 1) having attained a statutory pension age for social insurance old age pension²
- 2) have at least 5 years of service as judge
- 3) have ceased working as a judge

Contingency as defined by law

Supplementary pension for judges upon attaining old age and retiring from the qualifying occupation

Risks covered

Old age (attaining general statutory pension age)

Benefit calculation

The benefit calculation rules are regulated by an Order of the Director of the National Judicial Administration according to the following scale:

² In 2018 the general statutory pension age to qualify for social insurance old age pension is 63 years 8 months for men and 62 years 4 months for women.

Length of service as a judge (years)	Rate of pension as percentage of reference wage	Marginal accrual rate of one additional year of service (percentage)
5	10	2
6	12	2
7	14	2
8	16	2
9	18	2
10	20	2
11	23	3
12	26	3
13	29	3
14	32	3
15	35	3
16	37	2
17	39	2
18	41	2
19	43	2
20	45	2
over 20	45	0

Table 2. The rate of judge’s pension as a percent of the reference wage depending on the years of service as a judge

The reference wage is the average wage of the judge in the last 5 years before termination of holding the office of the judge.

Payment conditions

The payment of pension is suspended when a person is convicted for a criminal offence or receives a pension from abroad.

1.3 State pensions of scientists

State pensions for scientists are regulated by the Provisional Law on the State Pensions of Scientists, in force from 1995.

Personal scope

Eligible are scientists with a scientific degree (doctor or habilitated doctor) residing in Lithuania.

Qualifying conditions

At least 10 years of academic career in research and educational institutions and reaching the statutory pension age or being incapable to work (loss of work capacity 60% or more)

Contingency as defined by law

Supplementary pension for scientists upon attaining old age or becoming incapable to work and ceasing to work under an employment contract or as self-employed.

Risks covered

Old age, incapacity for work

Benefit calculation

10% of the state pension base for each full year of academic career as a doctor, and additionally 5% of the state pension base for each full year of career as a habilitated doctor

Payment conditions

The payment of pension is suspended when a person receives any insured income from work or is convicted for a criminal offence. The total sum of state pension and social insurance pension may not exceed 1.5 times the average national wage.

1.4 Benefits of stage artists

Regulated by Article 15 of the Law on professional stage art, adopted in 2004.

Personal scope

Creative staff of professional stage art institutions

Contingency as defined by law

Termination of employment due to inability to work in acquired specialty related to specifics of the profession

Risks covered

- Superannuation (long career in a defined profession after prescribed years of service)
- Loss of work capacity (disability) due to traumatizing work or occupational disease preventing to work in the acquired specialty

Qualifying conditions

The qualifying work period varies depending on the profession:

- 1) 18 years of creative work for ballet performers and dancers, and circus performers using force or muscles in their public performances (acrobats, jugglers, balancers, gymnasts and others)
- 2) 20 years of creative work for solo vocalists
- 3) 25 years of creative work for musicians playing wind instruments
- 4) 30 years of creative work for other musicians, conductors choir artists and actors

Benefit

Flat-rate benefit in the amount of 8 basic social benefits (in 2018, 8 x 38 EUR = 304 EUR)

Payment conditions

Benefit is not granted or the paid benefit suspended, if the amount of social insurance pension or other pensions exceeds the amount of benefit. If the person receives a social insurance or other pension, which is less than the rate of benefit, a partial benefit is paid in the amount of the difference between the 8 basic social benefits and the total amount of pensions.

	Officials and servicemen	Judges	Scientists	Stage artists
Contingencies covered	Superannuation, incapacity for work, survivorship	Old age	Old age, incapacity for work	Occupational incapacity
Retirement age	No statutory retirement age for military, police, border, customs and prison staff. General pension age for prosecutors.	General pension age	General pension age	No statutory retirement age
Qualification period	25 years of service for military, police, border, customs and prison staff; 20 years of service for prosecutors.	5 years of service	10 years of service	18-30 years of service depending on specialty
Benefit calculation principle	Earnings-related	Earnings-related	Proportional to the years of qualifying service	Flat-rate
Accrual rate	1-1.5% of reference wage per year depending on length of service	2-3% of reference wage per year depending on length of service	10% of calculation base per year of academic career	None
Reference wage	Average monthly wage of the most favourable 12 consecutive months from the period of 5 consecutive years	Average monthly wage over the last 5 years before retirement	None	None
Replacement rate	20 % of reference wage or over,	10-45% of reference wage	N/A	N/A

	depending on length of service	depending on length of service		
Benefit ceiling	The sum of social insurance pension and state pension not to exceed 1.5 times the national average wage	None	The sum of social insurance pension and state pension not to exceed 1.5 times the national average wage	Benefit is suspended if the amount of social insurance pension exceeds the amount of benefit
Benefit revalorisation	No statutory revalorisation	No statutory revalorisation	Benefits linked to state pension base	Benefit linked to basic social benefit

Table 3. Comparison of the main parameters of occupational state pensions

Table 3 summarizes the main characteristics of occupational state pensions. Despite all of them being based on employment in specific occupational groups, the scheme parameters are significantly different. Given that there are no age criteria on state pensions for officials and servicemen (except prosecutors) and for stage artists, these pensions are effectively early retirement pensions allowing retirement several years before general statutory pension age based on superannuation – the number of years employed in specific occupation (or occupational category). Upon reaching the general pension age these pensions continue to be paid as a supplement to the social insurance old age pension (subject to pension income test in case of state pensions for artists). State pensions for judges and for scientists, on the other hand, operate as supplementary pensions to top up social insurance old age pensions. Moreover, the qualification criteria, pension calculation rules and revalorisation rules differ across all four types of occupational state pensions.

2. Descriptive statistics on occupational schemes

2.1 Number of beneficiaries by gender, age and type of benefit

In 2017, the total number of beneficiaries of occupational state pensions was 24.522, of them 20.972 (or over 85%) received state pensions under the sub-scheme for officials and servicemen.

Recipients of occupational state pension are overwhelmingly men (Table 4) with the share of women only 22%. This relates to the fact that the occupations covered with the right to state pension, in particular those of the sub-scheme of officials and servicemen – military, internal service, investigators, border guards and customs, prison department staff and prosecutors – are male-dominated.

Occupational state pensions	Women	Men	Total
Officials and servicemen	3349	16842	20191
Officials and servicemen survivors	697	84	781
Scientists	1311	1917	3228
Judges	82	85	167
Stage art workers	93	62	155
Total	5532	18990	24522

Table 4. The number of beneficiaries and gender breakdown by types occupational state pensions in 2017

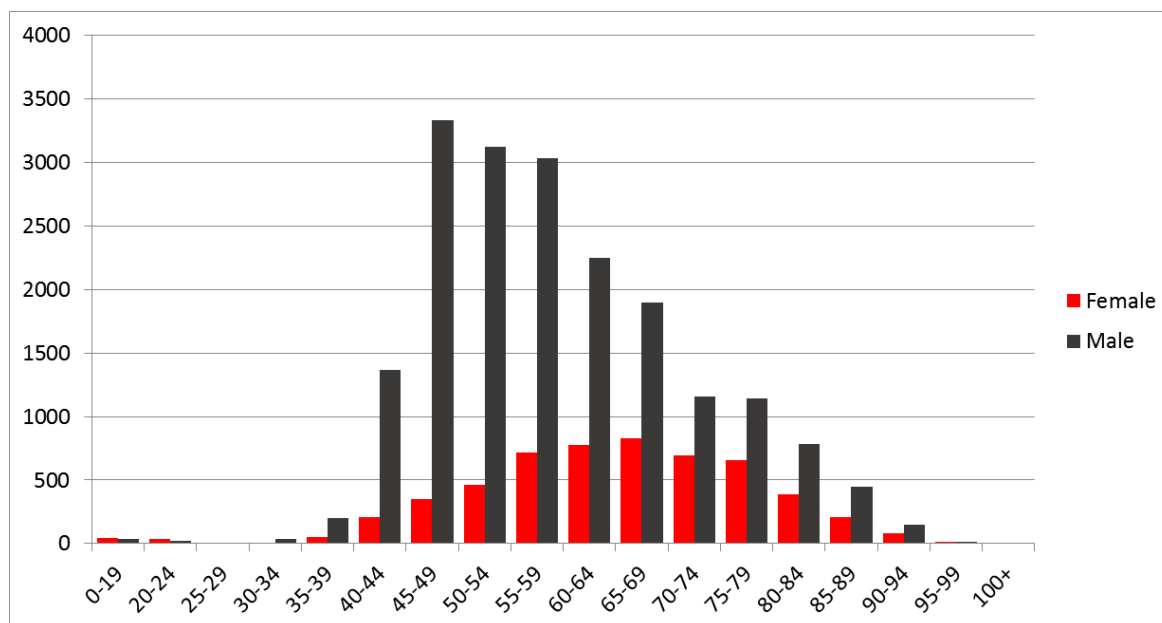


Figure 1. Age and gender profile of recipients of occupational state pensions in 2017

The category of occupational pensions is characterized by a relatively young age structure (Figure 1). 54% of beneficiaries in this category are below the age of 60. Hence the majority of recipients of occupational state pensions are below the general pension age³. Furthermore, there is a considerable number of beneficiaries (over 5000) of the scheme for officials and servicemen, particularly men, who are below the age of 50. On the other hand, in the sub-scheme of scientists' pensions 90% of beneficiaries are 70+ years old.

It is also noteworthy that the age structure of male and female recipients of occupational state pensions is significantly different. Whereas the highest numbers of male beneficiaries are in age bracket 45-60, for female beneficiaries the peak is in 65-69 age group. The gender differences in the age profile of occupational state pensions seem to be related to mainly two factors: men on average enter the qualifying occupations at younger ages than women and accordingly fulfil the length of service criteria earlier; on the other hand, women have had career breaks due to maternity and parental leave,

³ In 2017 the general pension age was 63 years 6 months for men and 62 years for women.

which further postpone the age at which they fulfil the occupational length of service criteria.

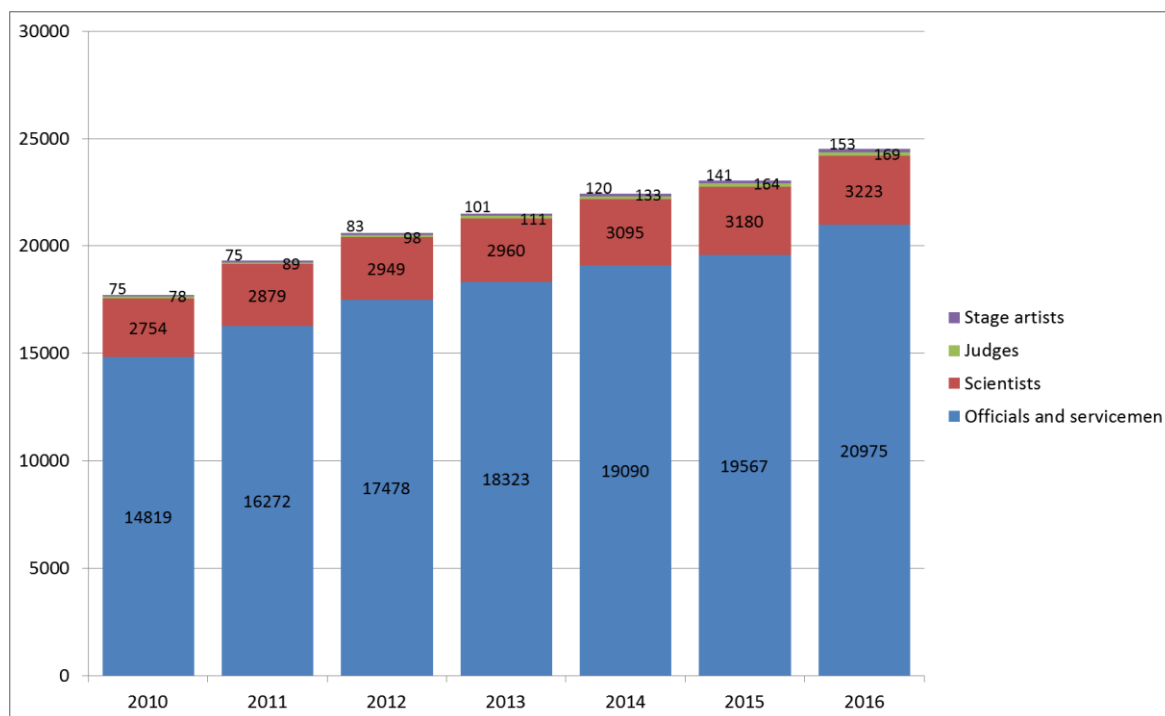


Figure 2. The number of beneficiaries of occupational state pensions 2010-2016

The number of recipients of occupational pensions is increasing. The increase has been across all four types of benefits. However the schemes for stage artists and judges are rather small. The overall increase in the number of beneficiaries can be attributed to the following factors. The largest occupational state pension scheme for officials and servicemen is in continuing maturation, whereby a relatively large number of persons reach the (relatively low) length of service requirements in a relatively young age several years before pension age. Even though the scheme has been in force for 23 years, this is less than the remaining life expectancy at median age of retirement (withdrawal from covered occupations and granting of occupational pension). As a consequence, the number of newly granted occupational pensions exceeds the mortality losses. There is also a cohort effect as the cohorts reaching the qualification period are larger (see below).

2.2 Employees in covered occupations

	Employees		
	Men	Women	Total
Officials and servicemen	22322	7412	29734
Scientists	2406	2254	4660
Stage artists	959	831	1790
Judges	289	472	761
Total	25976	10969	36945

Table 5. The number of employees working in occupations covered by occupational state pensions by gender in 2017

In 2017, the total number of employees working in occupations covered by occupational state pensions was 36945 persons or 2,7% of all employed persons in Lithuania in the same year. Even when compared to the number of general government employees (305 thousand persons)⁴ the share of general government employees covered by these special occupational schemes is only 12%. In other words, the state provides special supplementary pension rights to only a small fraction of general government employees. Obviously, whether the covered employees will actually become beneficiaries depends on if they eventually fulfil the qualification criteria. But they are persons who through their work in covered occupations acquire additional pension rights supplementing those acquired under the general social insurance system.

	Occupational dependency ratio
Officials and servicemen	1,42
Scientists	1,44
Stage artists	11,55
Judges	4,56

Table 6. The ratio of employees to current beneficiaries in occupational groups covered by state pension in 2017

Calculating the ratio of current employees to current beneficiaries in occupational groups covered by occupational state pensions reveals a mixed picture. In the schemes of officials and servicemen, and scientists, the calculated dependency ratio is low, about 1,4. In case of officials and servicemen, the low dependency ratio is related to the low effective age of retirement. In case of scientists, the factor behind is rather the shrinking number of persons pursuing academic careers compared to earlier cohorts. The dependency ratio is currently the most favourable in the scheme for stage artists. However, this is mostly due to the rather short history of the scheme (from 2004 whereas the personal scope was significantly extended in 2017), implying a relatively small number of retirees.

While the calculated occupational system dependency ratios have currently little practical value as the state pensions are financed from the state budget without any direct contributions payable by covered employees, this indicator still illustrates the potential capacity (or rather the lack of it) to operate those schemes as separate DB schemes.

⁴ OECD.stat data from 2015. General government employment covers employment in all levels of government (central, local and social security administration) and includes core ministries, agencies, departments and non-profit institutions that are controlled by public authorities. Data represents the total number of persons employed directly by those institutions.

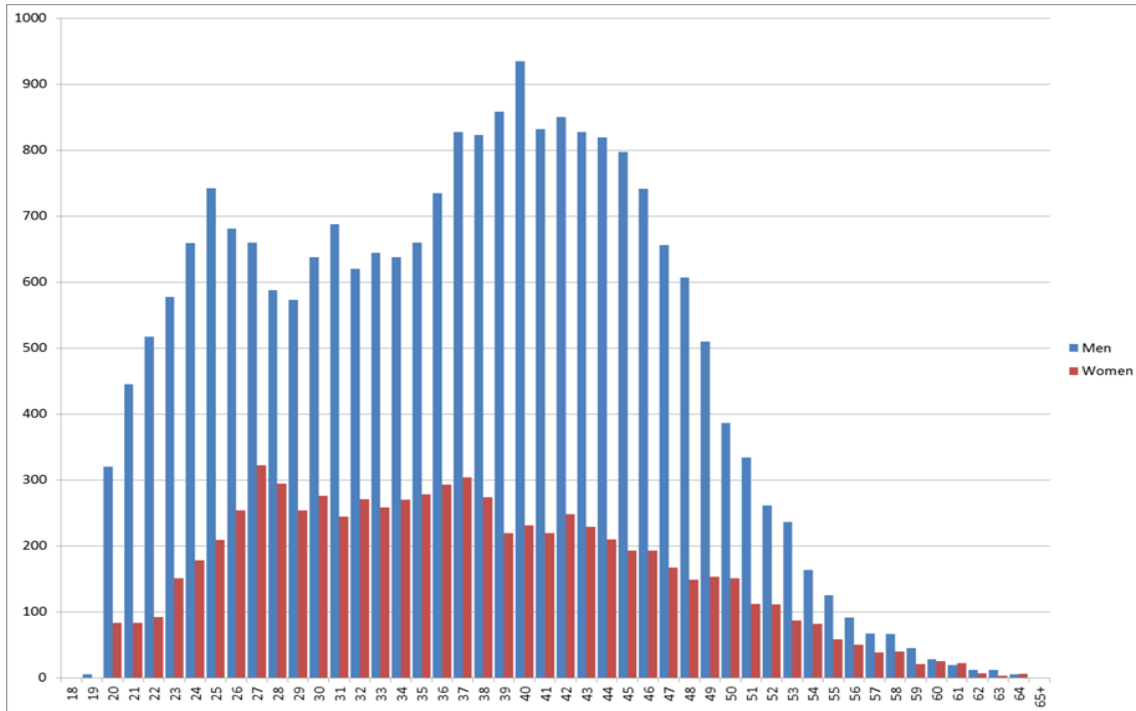


Figure 3. Age and gender profile of employees working in occupations acquiring the right to state pension for officials and servicemen, 2017

Looking at the age structure of employees working in positions covered with the right to state pension for officials and servicemen, we observe that the largest age group is 36-45. After the age of 45 the number of employees starts to decline, indicating a withdrawal from the qualifying occupations after 20–25 years of service. Very few remain in these occupations after the age of 55.

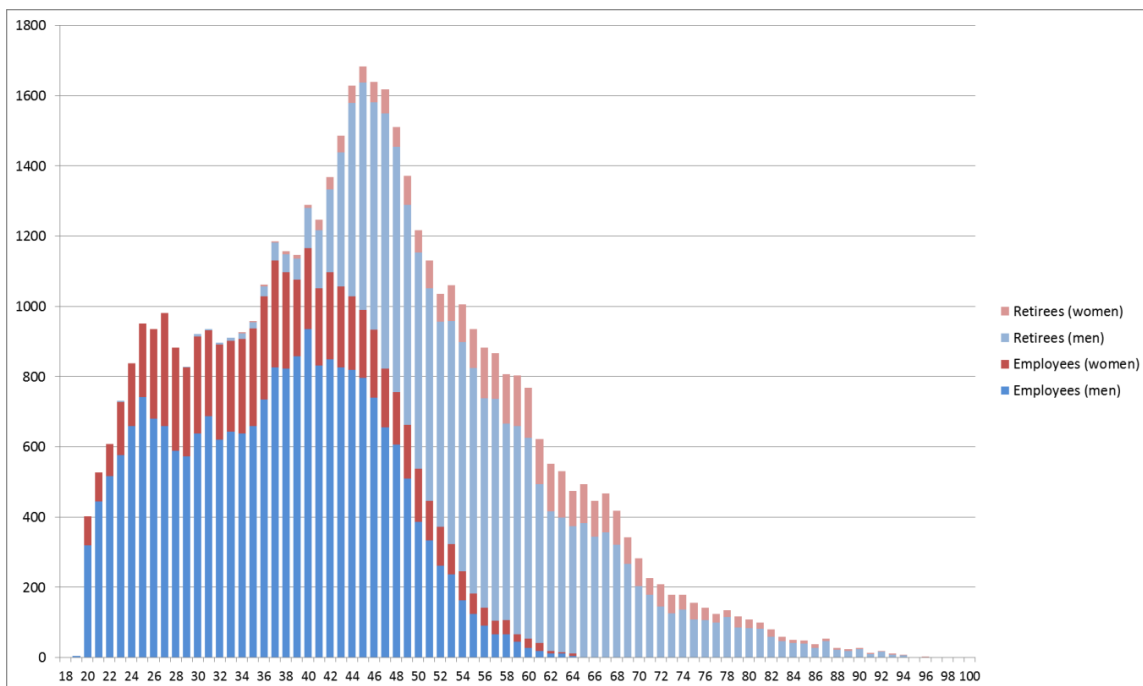


Figure 4. Age and gender structure of retirees and employees covered under the occupational scheme for officials and servicemen, 2017

Merging the age structures of the retirees and employees covered under the occupational scheme for officials and servicemen into a single chart (Figure 4) suggests a particular cohort phenomenon. In the occupations covered by this type of state pensions cohorts born 1968-1975 have been considerably larger than cohorts born earlier and later. This is probably related to restructuring of the police and military forces in the first years after regaining independence with increased hiring of new staff members in early 1990s. About 25% of this age group has already retired, while the others are expected to retire over the next 10-15 years. The ageing of this cohort will also shape the age profile of retirees of the scheme for officials and servicemen over the next decades as the following cohorts are smaller in size.

Figures 5 and 6 illustrate the share of employees as opposed to the share of retirees by gender in single-year age cohorts for the occupational scheme of officials and servicemen. The columns representing the standard pension age are marked with darker colour.

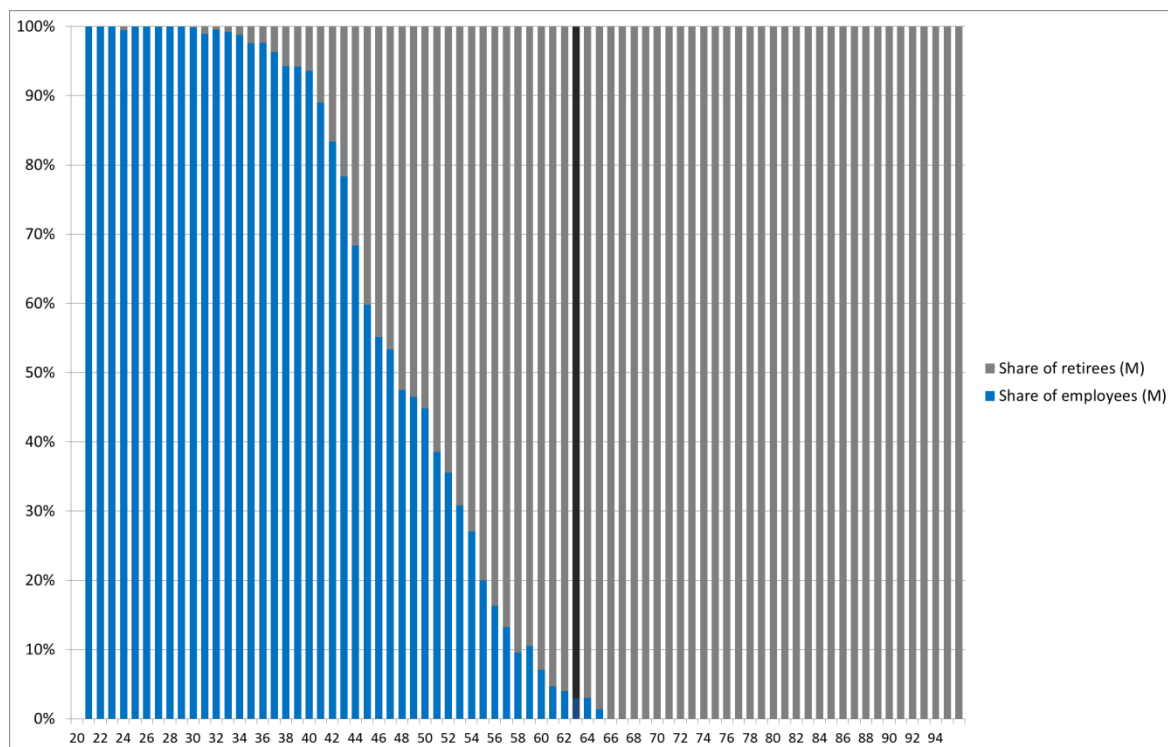


Figure 5. The shares of male employees and retirees in single-year age cohorts for the scheme of officials and servicemen in 2017

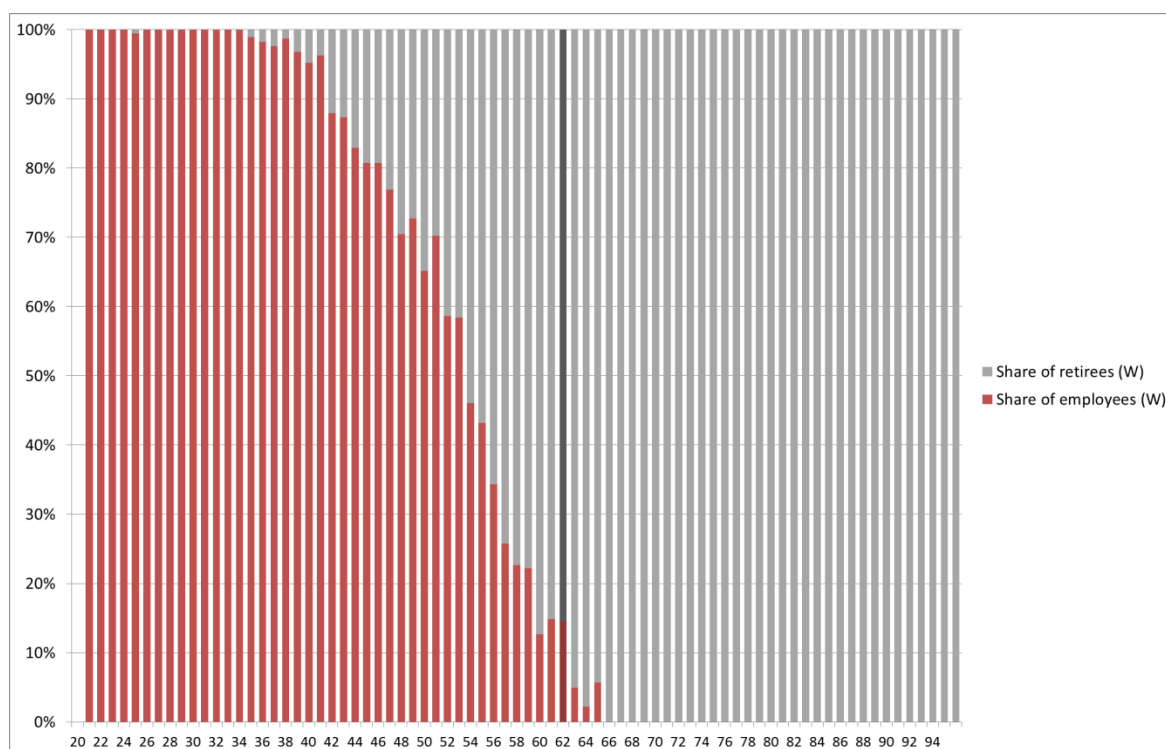


Figure 6. The shares of female employees and retirees in single-year age cohorts for the scheme of officials and servicemen in 2017

The median age of retirement (age at which the share of retirees exceeds the share of employees in the same age cohort) in those occupations is 47 for men and 53 for women. The average remaining life expectancy for men in age 47 is 26 years, while for women in age 53 it is 29 years. The early retirement thus extends the retirement duration for eligible men on average for about 11 years and for women on average about 8 years compared to persons retiring at general pension age.

Occupational groups	Number of employees			Average wage (EUR)		
	Men	Women	Total	Men	Women	Total
Prosecutors	333	339	672	1985	1896	1940
Investigation	142	88	230	1545	1407	1492
Military	7993	1092	9085	1020	1000	1018
Internal service	11525	4449	15974	1000	970	991
Prisons	1606	928	2534	981	879	944
Customs	723	516	1239	913	833	880
Total	22322	7412	29734	1021	1001	1016

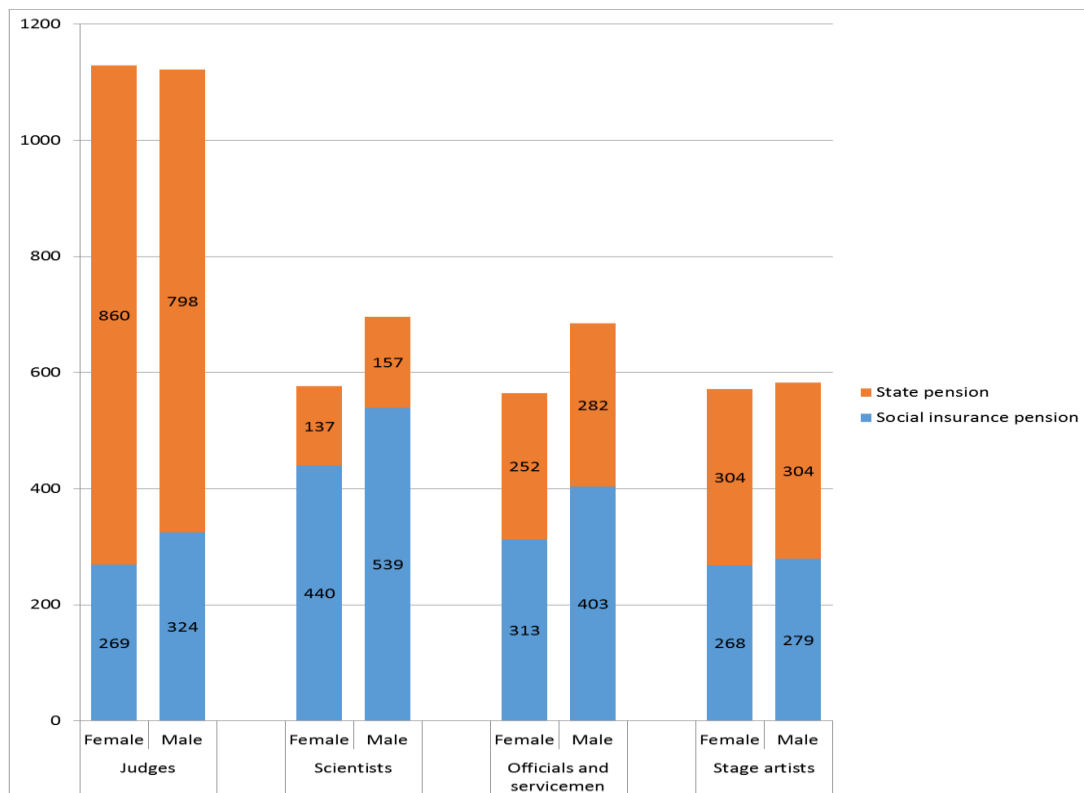
Table 7. The number of employees and average monthly wages of occupational groups covered under the occupational scheme for officials and servicemen by gender in 2017

The average monthly gross wage across all occupational groups covered by the state pension scheme for officials and servicemen was 1016 EUR in 2017 (Table 7). However, between the occupational groups the wages differ by more than 2 times ranging from 880 EUR in customs office to 1940 EUR for prosecutors. The data also indicates a gender

pay gap in all occupational groups, but this is rather small (ranging from 2% in military to 10% in prison department) compared both to the overall gender pay gap in Lithuania (14,4% in 2016) and the EU average (16% in 2016).

2.3 Benefit amounts and replacement rates

Figure 7 illustrates the average amounts of occupational state pensions combined with the amounts of social insurance pensions for beneficiaries who have reached the general pension age.⁵ For judges and for stage artists the state pension is generally higher than the social insurance pension. In other words, for these occupational groups the state pension is actually the primary pension, while the social insurance pension constitutes a top-up. For officials and servicemen, the state pension is the primary pension before the general pension age, while after the pension age it becomes a supplement to the social insurance pension, but still a significant supplement comprising on average 40-45% of their total pension. For scientists, the state pension is a supplement to the social insurance old age pension comprising about 20-25% of their total pension.



⁵ In 2017 the general pension age was 62 for women and 63,5 for men.

Figure 7. Average state and social insurance pension amounts of beneficiaries of occupational pension schemes in general pension age, 2017⁶

Type of occupational state pension	Mean pension		Lowest benefit paid		Highest benefit paid	
	Women	Men	Women	Men	Women	Men
Officials and servicemen	252	282	9	1	952	1258
Officials and servicemen survivors	65	64	11	16	323	242
Judges	860	798
Scientists	137	157	44	58	281	316
Stage art workers	304		304		304	

Table 8. Mean values and the lowest and the highest amounts of payable occupational state pensions by gender in 2017

Using as reference values the average social insurance old age pension (277 EUR in 2017) and the average gross wage (885 EUR in 2017), we observe that the pensions for judges exceed the average wage, while the average state pensions of stage artists as well as officials and servicemen are slightly above the average social insurance old age pension. Combined with social insurance pensions, the average total benefits of recipients of all occupational pension schemes exceed the average social insurance old age pension more than twice.

Type of occupational state pension	Share of average state pension to social insurance pension	
	Men	Women
Officials and servicemen	70%	80%
Judges	246%	320%
Scientists	25%	31%
Stage art workers	109%	113%

Table 9. State pensions as a top-up to social insurance pension by type of occupational pension, 2017

However, the lack of statutory regular indexation of state pensions during the payment period reduces the purchasing power of state pensions over time compared to the amounts of social insurance pensions, which from 2018 onwards are indexed annually based on the 7-year average wage fund growth rate.⁷

⁶ In case of judges the chart reflects the average social insurance pension as individualised data on the amounts of social insurance pension of recipients of state pension for judges were not available. In the reality, the social insurance pensions of judges are likely to be higher than the average social insurance pension.

⁷ However, the index is applied only insofar as the resulting pension costs (in the current year and projected costs for the next year) do not exceed social insurance revenues. Pensions are not indexed if the calculated

The average monthly wage of judges in 2017 was 2473 EUR for men and 2361 EUR for women. The average replacement rates offered by judges' pensions are then 36,6% for women and 32,3% for men. Combined with social insurance pensions, the gross replacement rates for judges reach 50%.

Comparing the values of state pensions for officials and servicemen to the average wage in covered occupations, the average replacement rate of benefits of this scheme in 2017 was 25,2% for women and 27,6% for men. Considering the accrual rates of 1-1,5% per year of service this corresponds on average to 25 years of service in covered occupations for retiring men and 23 years of service for women.

The average gross replacement rate of the total benefit for officials and servicemen taking the social insurance pension and the state pension together (upon reaching the pension age) amounts to 56% for women and 67% for men.⁸

In 2017, a supplement of 152 EUR (social insurance basic pension) was paid to 7039 recipients of state pension of officials and servicemen. As this supplement is paid to persons under the pension age who are unemployed or receive insured income less than the minimum wage, the numbers suggest that nearly half of all recipients of state pensions for officials and servicemen in age group 35-63 were not working or received a declared income less than minimum wage. Different factors may be behind the high share of non-working early retirees – either these early retirees were unable or demotivated to find a new job, while undeclared work or work abroad may also influence the numbers.

3. Legal analysis of Constitutional Court case-law on occupational pensions

Beyond the provisions of legal acts establishing and regulating the granting and payment of state pensions, the legal framework conditioning the provision of and possible reform options includes the case law of Lithuanian courts, in particular the decisions of the Constitutional Court.

The Constitution of the Republic of Lithuania contains several articles which have relevance in respect of granting and payment of state pensions. In particular, these are Articles 52, 23 and 48 of the Constitution which read as follows:

rate of index increase is less than 1% or if the GDP at constant prices or the wage fund declined or is projected to decline in the budget year.

⁸ The gender difference in replacement rates is mostly due to the gender pension gap in social insurance pensions.

Article 52: *“The State shall guarantee its citizens the right to receive old-age and disability pensions, as well as social assistance in the event of unemployment, sickness, widowhood, the loss of the breadwinner, and in other cases provided for by law.”*

Article 23: *“Property shall be inviolable.”*

Article 48: *“Everyone may freely choose a job or business, and shall have the right to have proper, safe, and healthy conditions at work, as well as to receive fair pay for work and social security in the event of unemployment.”*

There have been 3 substantial rulings of the Constitutional Court, which have directly addressed cases related to occupational state pensions:

- 1) Ruling from 4 July 2003 on the state pensions of officials and servicemen (Case No. 46/2001-48/2001-50/2001-2/2002-6/2002-18/2002)
- 2) Ruling from 22 October 2007 on the state pensions of judges (Case No. 38/04-39/04)
- 3) Ruling from 29 June 2010 on the state pensions of judges (Case No. 06/2008-18/2008-24/2010)

The argumentation delivered by the Constitutional Court in these rulings has effectively established a constitutional law framework on conditions governing the regulation of state pensions, as well as restrictions on possible later reforms of such pensions once established. The key points may be summarised as follows (for further details on merits of the case and the line of reasoning of the Court see Annex 1):

- The state pensions for service to the state are legitimate and constitutional;
- The personal scope, the conditions of granting and payment of such pensions shall be regulated by laws, and not by lower level acts;
- The regulation of state pensions for service shall take into account the specific circumstances of service, while the eligibility rules may not be too relaxed and the size of pensions shall not be unproportional for the pension not to become a ‘privilege’;
- Once state pensions are legislated they fall under the constitutional obligation of the state to guarantee their payment to the qualifying persons;
- The state may establish maximum amounts of state pensions;
- Following the principle of proportionality state pensions for a similar service of considerably different durations shall not be equal;
- The system of state pensions may be reorganised and some types of pensions may be abolished, at least in principle, however in such cases the legal regulation shall establish ‘a just mechanism for compensation of losses’ to persons in receipt of such pensions, and there shall be a sufficiently long transition period to address

the legitimate expectations of persons who have acquired service periods in covered occupations.

The argumentation developed by the Constitutional Court appears to make state pensions, which have already been granted and are in payment virtually irreversible, as following the line of reasoning of the Court the just mechanism for compensation of losses is hardly anything significantly less than the previously granted amount under a possibly different name and legal act. The available reform options then may concern persons who have not yet retired from the occupations where pension rights for service are acquired, but any reform shall provide for a sufficiently long transition period and shall not interfere with their legitimate expectations.

A key aspect in the legal assessment of special occupational state pension schemes concerns the notion of a 'privilege'. Privileges can be altered and revoked whereas legitimate rights are protected under the constitutional law.

In its argumentation the Constitutional Court noted that while establishing and regulating special pensions for service for specific groups, the legislature needs to address the specific circumstances of the covered profession striking a balance with consideration to the principles of justice, reasonableness and proportionality. On the other hand, the Court appeared to accept that an arbitrary regulation of state pensions may turn these into an unjust and unreasonable privilege, for example if the conditions of granting these pensions were overly relaxed and *'the person would be able to retire unreasonably early'* (ruling from 4 July 2003) or if the amounts of benefits would violate the principle of proportionality in case of *'groundlessly big or small sizes of such pensions'* (ruling from 22 October 2007).

In practical policy terms, it is not however self-evident which parameters would address *'the specific character of service'* and which circumstances would run in counter of the *'principles of justice, reasonableness and proportionality'*. For example, whether the possibility to retire at age 45 in the scheme for officials and servicemen is *'unreasonably early'* and whether the highest amounts of occupational pensions are *'groundlessly big'* or proportional and reasonable. Ultimately, only the Constitutional Court itself can make such legal assessments. Nonetheless, the legislature elected by people can follow the same principles in its own interpretation when establishing and reforming such pension schemes.

Noteworthy is also the ruling from 29 June 2010 on the state pensions of judges, where the Court appeared to suggest that state pensions for service to the state shall be proportional to the duration of specific service and pensions for the same occupational service of considerably different durations shall not be equal. This principle is currently not applied as regards compensations for stage artists, which are paid at a flat rate. In the ruling from 22 October 2007 on the state pensions of judges the Court noted in respect of

state pensions that *'in the case of the old age pension, the law must establish the age upon reaching which a person has the right to receive the old age pension'*. This principle is currently not applied as regards state pensions for officials and servicemen (except for prosecutors) as there is no established age criteria.

4. Analysis of policy inconsistencies

The analysis in this section aims to assess the coherence of the regulation of occupational state pensions, with a view to identify any policy inconsistencies, e.g. whether the functions of the schemes are clear and justified, whether any differences in benefit eligibility and payment parameters are based on objective differences in the situation of beneficiaries or if there are any arbitrary policy elements which appear difficult to explain and ground rationally.

The identified issues are grouped under thematic topics:

1) Justification for selection of occupational groups entitled to state pension

One of the key policy questions regarding the special pension schemes is whether it is justified to treat some groups of state servants differently than other groups as regards their pension rights, and if so on what grounds and to what extent. This is not only relevant at the time of introducing such schemes, but the question is to be reiterated also later, in view of assessing if the grounds and conditions that led to establishment of such scheme pertain or have changed leading to possible reforms, merging or abolition of special schemes.

The share of occupational groups covered with prospective rights to occupational state pension based on their specific service comprise 2,7% of all employees in Lithuania and 12% of general government employees. Hence a small selected fraction of government employees enjoy supplementary pension rights which are not available to other groups of government employees nor to other workers.

The Constitutional Court when examining cases related to granting and payment of state pensions has held that *'the legislator enjoys the constitutional powers to establish by the law the pensions and/or types of social assistance granted solely to the state servants or individual groups of state servants, the grouping of which is objectively justified'*. Hence the Court has stressed the need for objective justification for selection of particular groups of state servants. However, it is not only a question about why an individual group of state servants is selected, but also why other groups of state servants are excluded.

2) Considerable variation of objectives, eligibility criteria and benefit rules of different types of occupational state pensions

The occupational groups currently entitled to state pensions are judges, officials and servicemen of interior affairs and military, scientists and stage art workers. However, the roles and functions of these special schemes for selected occupational groups vary considerably between those groups, even if all are based on occupational service.

Different functions and eligibility age

State pensions for judges and scientists are only paid upon attaining the general pension age, providing supplementary pensions in addition to social insurance pension. On the other hand state pensions for officials and servicemen and for stage artists allow early retirement based on years of service before general pension age, when persons are not yet eligible to social insurance pension. State pensions for stage art workers essentially fulfil the role of 'bridging pensions' for the period before becoming eligible to social insurance pension and the benefit is withdrawn when the granted social insurance pension is higher.

All four categories are treated differently as regards entitlement to, calculation and payment of state pensions while there is no apparent objective justification, why the eligibility rules, benefit determination principles, accrual rates and conditions of granting and payment differ to such an extent across the occupational groups.

Different benefit determination principles

State pensions for judges and for officials and servicemen are based on their former remuneration, are calculated based on fixed accrual rates and carry the role of partial wage replacement. State pensions for scientists are linked to their length of service, but not to their earnings. State pensions for stage art workers are flat rate even though the entitlement is dependent on the length of service.

Different qualification periods

The qualification periods to become eligible for state pensions are markedly different between occupational groups.

For judges, the minimum period of service giving entitlement to state pension is 5 years. For scientists it is 10 years, for prosecutors 20 years, for other groups of

officials and servicemen 25 years. For stage artists, the qualification periods vary from 18 to 30 years of service depending on specialty.

These differences appear to lack any empirical basis and hence lack an objective justification stressed by the Constitutional Court in its rulings. Effectively in the Law on Professional Scene Art the legislature has defined a particular equivalence scale of years of creative work for different categories of stage artists whereby 20 years of vocal signing are equalised with 25 years of playing wind instruments and 30 years of conducting choirs or orchestras. In the absence of any empirical findings to support such periods, they look arbitrary. It is not established whether a specific length of creative work has a particular deteriorating effect on the ability to continue in the relevant specialty, and if so, whether and to what extent such periods vary between professions.

Different accrual rates

For the earnings-related part of social insurance pension the applicable accrual rate is 0,5% of reference earnings per year of insurance, based on insured income upon which social insurance contributions are paid.⁹ In contrast, in the occupational schemes for officials and servicemen and for judges, the applicable accrual rates are respectively 1-1,5% of reference wage and 2-3% of reference wage. The stipulation of accrual rates mimics a defined-benefit pension scheme while no separate contributions are paid. In addition, the higher accrual rates are earned on top of the 0,5% accrual rate in the social insurance scheme for the same years of service.

Furthermore, there are questionable variations of accrual rates depending on the length of service and across occupational groups entitled to state pension. To calculate state pensions for judges, the marginal accrual rate of one additional year of service varies depending on the length of service as a judge. A higher – 3% – accrual rate is applied for years of service from 11th to 15th, compared to the accrual rate of 2% for the first 10 years of working as a judge and for the years from 16th to 20th. It is not evident what, if any, is the rationale why the mid-career period is valued higher than the starting and later years of career. As after 20 years of service as a judge the marginal accrual rate for any additional years of service is 0, the incentives to continue working as a judge decrease.

⁹ The reference earnings are calculated as the weighted average of a ratio between person's monthly earnings and the average insurable income in the country for the best 25 years of insurance period (with ceiling five times the average insurable income) multiplied with the average insurable income in the country on the month of the pension payment.

As noted above, the annual accrual rates to calculate state pensions for judges are 2% for the first 10 years of service, 3% for 11-15 years of service, again 2% for 16-20 years of service as a judge, and 0% for each additional years of service over 20 years. In contrast, the accrual rates to calculate state pension for prosecutors is 1% for the first 20 years of service, 1,5% for 21-25 years of service, and again 1% for each years of service from 26 years onwards. Notwithstanding any differences in the rates of remuneration between judges and prosecutors, the stipulation of accrual rates implies what share of the remuneration is earned as entitlement towards future pension per one year of service. There is no apparent objective justification why judges accumulate pension rights faster and higher than prosecutors. For a judge, it takes 20 years to acquire a right to a pension of 45% of his/her remuneration. A prosecutor would earn in 20 years a pension right corresponding to only 20% of his/her remuneration. To earn a replacement rate of 45% the prosecutor would need to work in this profession for 43 years. In contrast, with sufficiently long career, the prosecutor has a possibility to increase his/her replacement rate beyond 45% of his/her remuneration, whereas judges do not have such an option.

Different ceilings

On state pensions for scientists and for officials and servicemen, the legislation sets a maximum amount, which is 1.5 times the national average wage. The ceiling applies to the sum of the payable state pension and the social insurance pension. In contrast, as a consequence of the ruling of the Constitutional Court there is no corresponding ceiling applying to state pensions for judges and these are paid regardless of the amount of state social insurance pension. Notably, the payable rates of state pensions with no respective ceilings and restrictions are considerably higher than the rates of state pensions for which such ceilings apply. Occupational benefits for stage art workers are not paid at all if the amount of social insurance pension or any other pension is higher than the rate of benefit.

Different sanctions

State pensions for scientists are suspended if the recipient is convicted for intentional crime, and the payment is stopped from the day the judgment comes into force. In contrast, following a ruling of the Constitutional Court state pensions for officials and servicemen may not be suspended to persons convicted for intentional crimes. As a consequence, recipients of state pensions convicted for intentional crimes are treated differently depending on the type of pension they receive – sanctions are applied on some beneficiaries, but not on others.

Such differential treatments appear to lack an objective justification and it is therefore questionable if these comply with the principles of justice, reasonableness and proportionality emphasised by the Constitutional Court.

3) Low effective age of retirement

In the schemes for officials and servicemen and for stage art workers, the majority of recipients are under the general pension age. There is a significant number (over 1500) of 'retirees' already in the 40–44 age group, whereas the 45–54 age groups are in fact the largest (over 7000 pension recipients). Also the age structure of employees working in occupations covered with the prospective right to state pension on officials and servicemen indicates that the number of employees starts to decline after the age of 45 as a result of withdrawal from these occupations after 20–25 years of service. This considerably prolongs the duration of retirement compared to persons insured under the general social insurance pension scheme. The low median age of retirement (47 for men and 53 for women) in the scheme for officials and servicemen extends the retirement duration of eligible men on average for about 11 years and for women on average about 8 years compared to persons retiring at general pension age.

A typical function of occupational pensions is to maintain a loyal and qualified workforce. In the absence of age criteria to qualify for pensions of officials and servicemen, the length of service requirement alone fosters withdrawal from the occupation once the service requirement is fulfilled. The fact that in the scheme for officials and servicemen the accrual rate for years of service after 25 years declines from 1,5% to 1% gives a further incentive in the same direction.

The data indicates that nearly half of all recipients of state pensions for officials and servicemen under general pension age (in age group 35-63) are not working or receive declared income less than minimum wage. Hence the occupational pensions for this group contribute to early withdrawal from employment and/or to undeclared work. However, even if persons retiring from state service at the age of 40–54 continue to work in some other jobs, the state ought to weight the costs of paying occupational pensions before the general pension age and the opportunity costs of losing specially trained and qualified personnel in relatively young ages against any perceived benefits of higher rotation of police and military officials.

Furthermore, in ruling from 4 July 2003 on the state pensions of officials and servicemen the Constitutional Court expressly noted that when establishing the pension for service of officials and servicemen the constitutional principles of

justice, reasonableness and proportionality could be violated if “*the person would be able to retire unreasonably early*”.

4) Lack of statutory regular indexation

The absence of regular statutory indexation of state pensions reduces over time the purchasing power of state pensions during the payment period compared to the amounts of social insurance pensions, which are indexed annually. As a consequence the effective replacement rate of pensions in payment decline along beneficiaries reaching older ages.

5) Possible age discrimination

According to Article 3 of the temporary law on state pensions for scientists, the qualifying period for entitlement to a pension is 10 years of seniority as a doctor or habilitated doctor. On the other hand, Article 4 stipulates that the academic career is counted from the date of granting the doctoral degree, but not more than until the person reaches the age of 65. Such an age criteria entails a direct age discrimination, as a person who receives a doctoral degree at the age of 55 or later, but several years before the pension age, has no possibility to fulfil the length of service requirement to qualify for a state pension of scientists even if willing to continue to work after attaining pension age. Consequently, persons who defend the scientific degree of a doctor later in their academic career (but still before the pension age) are treated less favourably than persons who defend their doctoral degrees before the age of 55. In the absence of a legitimate aim and objective justification, the less favourable treatment would amount to age discrimination.

6) Regulation by a substatory act

In the ruling from 22 October 2007 on the state pensions of judges, the Constitutional Court noted that pursuant to Article 52 of the Constitution, the conditions for granting and payment of pensions, as well as the sizes of the pensions, including those not explicitly mentioned in Article 52, shall be established only by law and it is not permissible to establish such conditions by means of substatory acts. However, the applicable rules of calculation of the size of judge’s pension are stipulated in the Order of the Director of the National Judicial Administration, which is a substatory act. Whereas the scale of applicable accrual rates coincides with the overruled provisions of the Law on state pensions of judges for the length of service periods respectively 5, 10, 15 and 20 years, the Order the Director of the National Judicial Administration makes the accrual rate function continuous (as opposed to the stepwise regulation of

replacement rates in the Law on state pensions of judges), thus expanding the rules of calculation of judges' pensions compared to the provisions of the law.

5. Projections

The simulation model LitPen developed in the framework of the current study allows running of projections on evolution of the number of beneficiaries and expenditures of state pension schemes over the time horizon until 2080.

Input data and assumptions are described in Annex 3. It shall be stressed though that several assumptions are changeable in the model allowing projections based on alternative assumptions.

The base scenario assumes no further changes in the applicable legislation while taking into account already legislated reforms, e.g. increase of the general pension age. Beyond the base scenario, the model allows to analyse various reform scenarios. Some reform parameters can be altered in the model, but additional reform scenarios may also be defined.

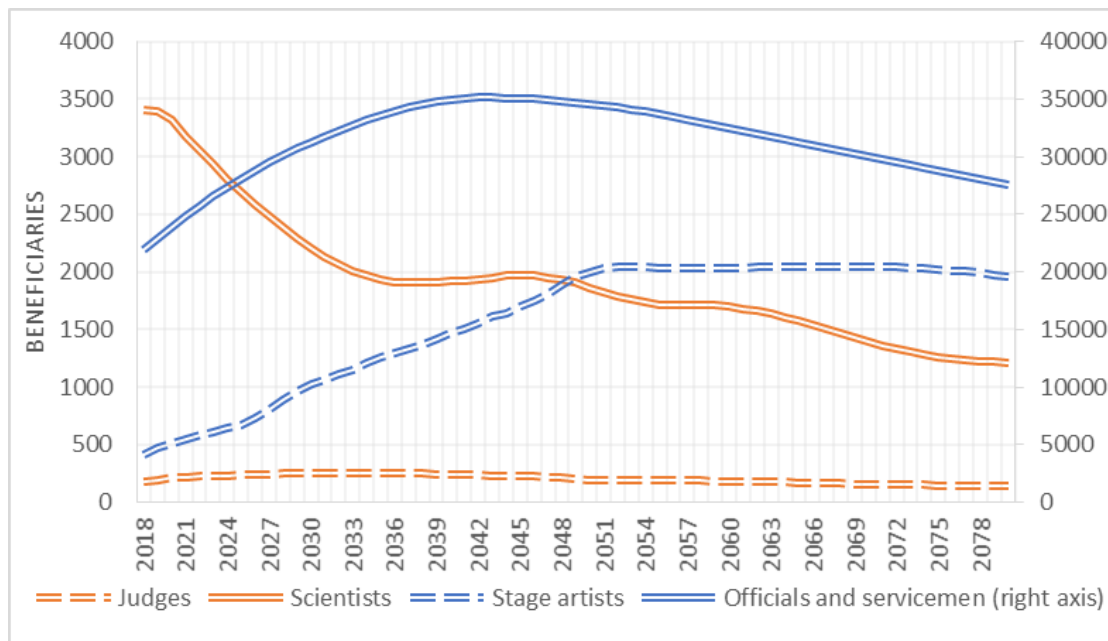


Figure 8. Evolution of the number of beneficiaries of occupational pension schemes under the base scenario

In the largest scheme of state pension for officials and servicemen the number of beneficiaries would increase by about 13 thousand persons to reach the peak of 35 thousand persons by 2040. The smaller schemes have diverging trends. The number of recipients of scientists' pensions is projected to decline by 1,5 thousand persons over the next 15 years, thereafter stabilizing at the level of around 2 thousand persons for about

a decade. On the other hand, the number of beneficiaries of pensions for stage artists would steadily increase over the next three decades, stabilizing at the level of 2 thousand persons thereafter. In the scheme for judges the number of beneficiaries would increase by less than 100 persons over the next two decades.

The average replacement rates (average pension to average national wage) would decline for the schemes of officials and servicemen, scientists and stage artists due to the absence of indexation of benefits combined with prolonged payment periods. In the scheme for officials and servicemen, the average replacement rate would decrease by about 10 percentage points over the period of next 30 years, from 27% to 17%. In contrast, the average replacement rate of state pensions for judges, which is already high close to 100% of the national average wage, would further increase to 160% over the next 30 years.

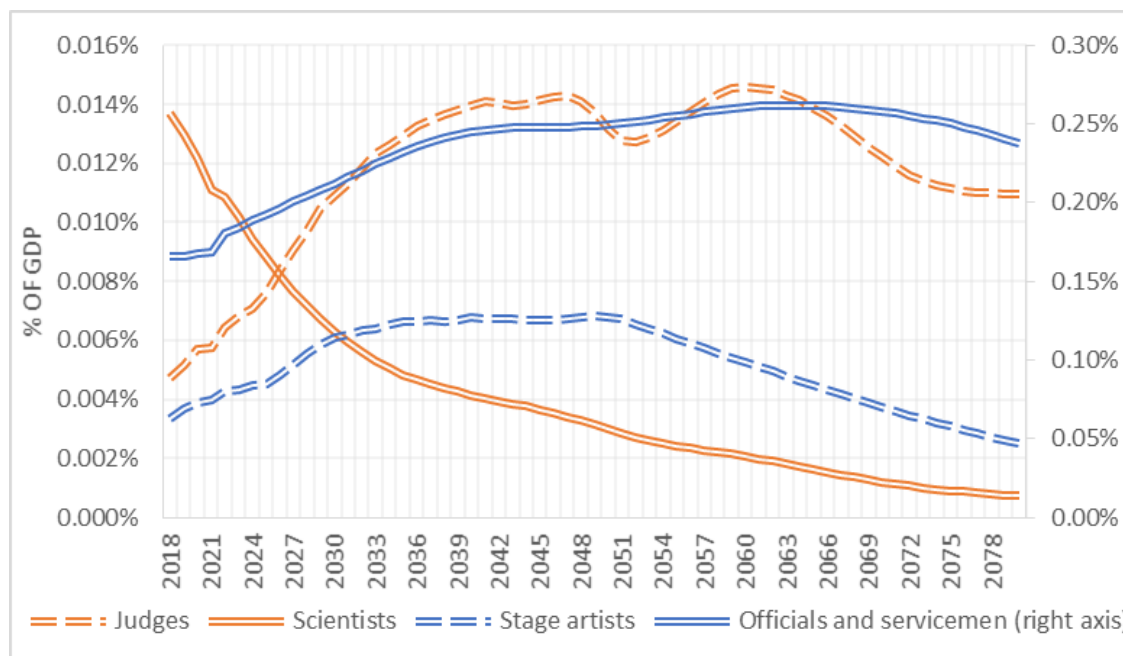


Figure 9. Evolution of expenditures of occupational pension schemes under the base scenario (per cent of GDP)

The evolution of costs of occupation pension schemes (Figure 9) is mostly driven by developments in the number of beneficiaries. Expenditures of the largest scheme of state pension for officials and servicemen are projected to increase by about 1.7 times by 2040 years to reach 0.24% of GDP (or 127 million EUR in discounted values). On the other hand, the total expenditures of the three smaller schemes (scientists, judges and stage artists) would remain nearly constant (in sum at about 10 million EUR) as the decline in the costs of scientists' pensions is offset by increases in the costs of pensions for stage artists and judges.

6. Reform options

To address the identified policy inconsistencies, legal issues and projected increase in expenditures, the Lithuanian authorities may want to consider ways how to reform these occupational pension schemes.

We describe and analyse three possible reform scenarios. Some elements of these scenarios may be modified and/or combined, while obviously there are more reform options beyond those described.

Radical reform

Scenario 1 – abolition of special occupational schemes

This scenario could entail the following reform measures:

- from the onset year of the reform (here taken to be 2020) no new special pension rights are granted to persons entering the occupations (officials and servicemen, judges, stage artists, scientists) which were formerly covered by the right to state pension;
- the rights acquired by current employees under the existing legislation are respected.

Scenario 1 is radical towards new employees in the formerly covered occupations (mostly younger age groups entering the labour market after completing education) while respecting the legitimate expectations of current employees.

As regards the current employees, there are two possible alternative approaches:

- either they will continue to acquire occupational pension rights under the former rules until they retire (with the possibility to fulfil the currently applicable qualification periods), or
- no new occupational pensions rights are granted to current employees from the onset of the reform while previously acquired rights to current employees are compensated based on stipulated accrual rates (but waiving the qualification period conditions).

This scenario would address the requirements of the Constitutional Court as regards the legitimate expectations of persons who have acquired service periods in covered occupations, while over a long period would diminish the costs of these special occupational schemes.

Figures 10 and 11 illustrate the evolution of the number of beneficiaries and costs of the first alternative for the occupational scheme of officials and servicemen.

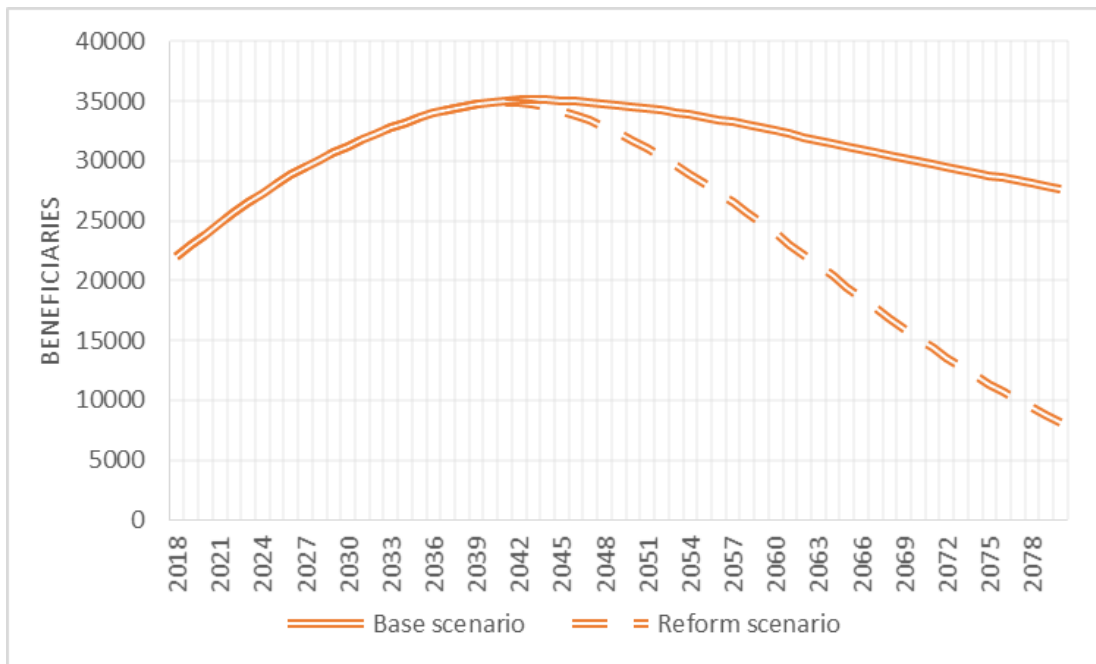


Figure 10. Evolution of the number of beneficiaries of the occupational pension scheme for officials and servicemen: base scenario compared to the reform scenario if no new state pension rights are granted to new entrants to these professions, while current employees continue to earn rights until they retire

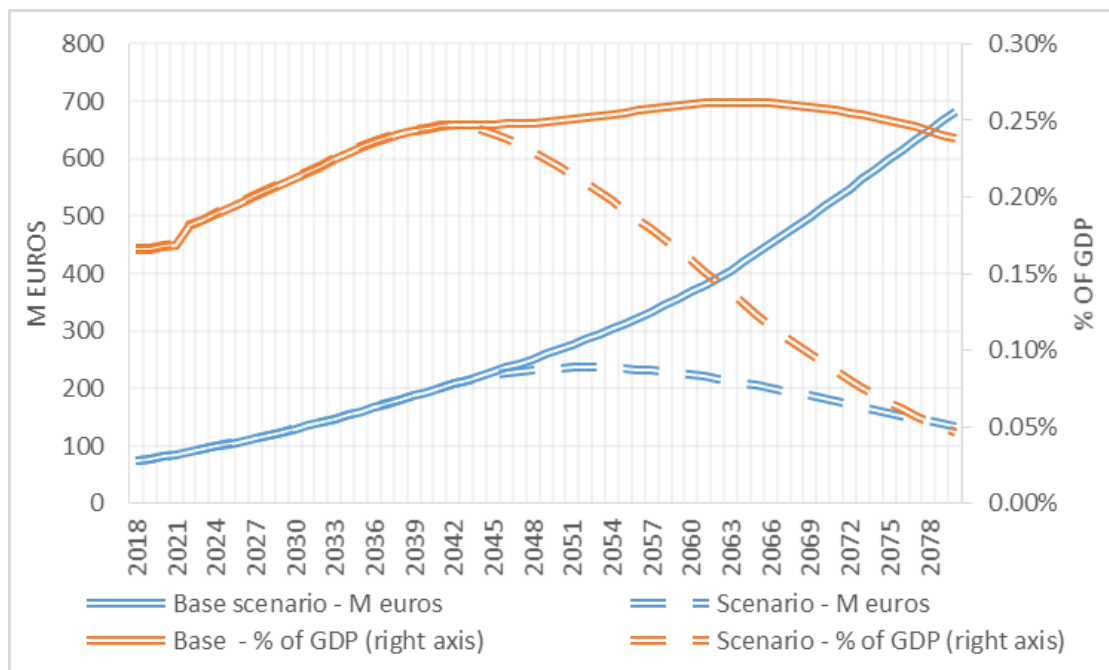


Figure 11. Evolution of the costs (per cent of GDP – right axis; millions EUR – left axis) of the occupational pension scheme for officials and servicemen: base scenario compared to the reform scenario if no new state pension rights are granted to new entrants to these professions, while current employees continue to earn rights until they retire

In this reform scenario there would be no changes compared to the base scenario in the mid-term by 2040 as benefits are continued to be paid under the current rules to those already retired as well as to those who are going to retire over the next two decades, given the qualification period of 25 years. From 2040s onwards the number of beneficiaries and costs would decline.

Systemic reforms of special occupational schemes

Systemic reforms could entail rearrangement of the financing system of occupational schemes and the principles of acquisition of new pension rights under these schemes in order to make the cost of occupational state pensions explicit in terms of the share of the wage bill. There are several options under this branch of reforms.

Scenario 2 – Introducing a separate DB scheme

The first option is to convert the occupational pension schemes into separate pay-as-you-go defined-benefit schemes. There is also possibility to merge the four occupational schemes into a single scheme.

As noted above, the system dependency ratio (the ratio of covered employees to current beneficiaries) of the largest sub-scheme for officials and servicemen in 2017 was 1,42 whereas the average replacement rate is 26,4%. To operate as a separate pay-as-you-go defined-benefit scheme being financed from incoming contributions charged on gross wages of covered employees, the contribution rate to finance current benefits would have to be **18,7%** of the gross wage. This would be on top of the general contribution for financing social insurance pensions, which is 23,3% of gross wage paid by the employer and 3% by the employee. Given that the number of beneficiaries is projected increase as the scheme matures, the supplementary contribution rate would need to be increased to cover increasing expenditures. Already by 2024 the number of beneficiaries of the scheme would exceed the number of covered employees, the system dependency ratio dropping below 1. By 2040 the dependency ratio would decline further to 0,63 (Figure 12). To maintain the average replacement rate, the additional contribution rate would need to be already nearly 42%. It is evident that such a scheme would not be financially sustainable and hence realistic. Nonetheless these calculations illustrate the implicit, hidden burden on labour costs of these special pensions.

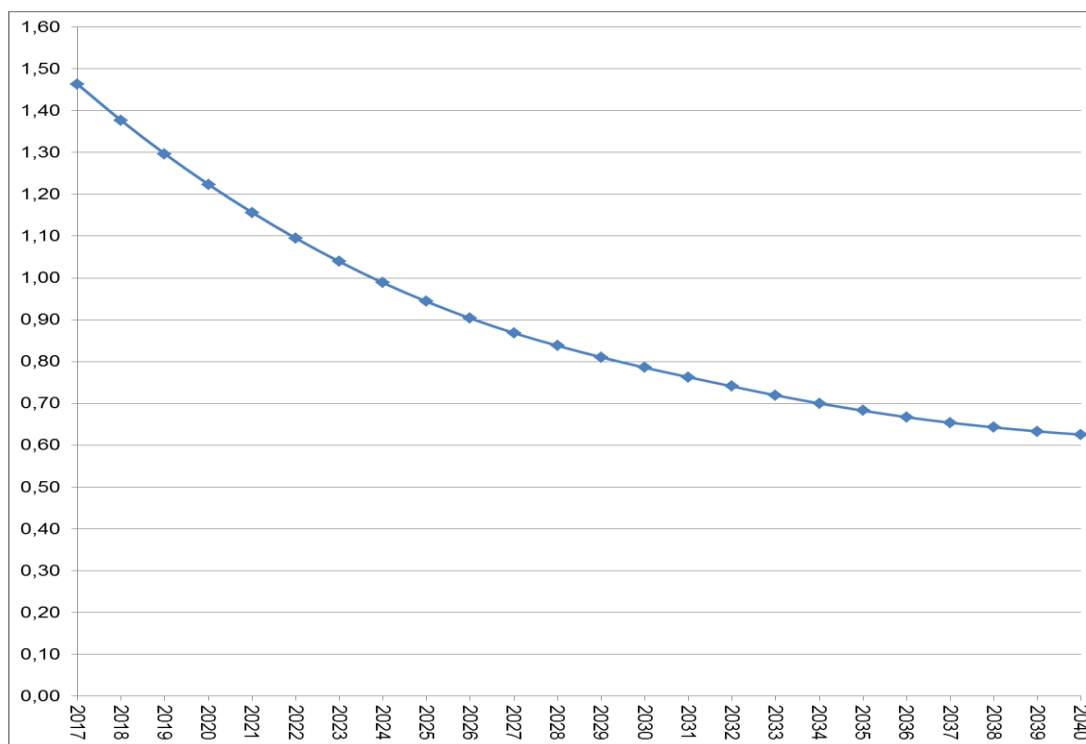


Figure 12. Evolution of the ratio of covered employees to retirees in the occupational state pension scheme for officials and servicemen, 2017–2040

Scenario 3 – Introducing a separate DC scheme

The second option to be analysed under this scenario is to convert the occupational pension scheme for officials and servicemen into a funded defined-contribution scheme with a fixed contribution rate. Here, in turn, are different alternatives as regards which age groups are diverted to the DC scheme and which remain under the current DB scheme.

In the first alternative, all new employees are switched to the DC scheme whereas all current employees remain in the DB scheme. In the calculations we set the contribution rate of the DC scheme at 17% of gross wage, assume an annual 4% net rate of return from the DC scheme during the accumulation phase and 1% net interest rate during the pay-out phase. These parameters are changeable in the model.

Figure 13 depicts the evolution of the number of beneficiaries in this alternative over a time horizon until 2078. Retaining the current qualification period of 25 years also under the DC scheme, the first retirees of the DC scheme emerge only after 2043. Thereafter the number of DB beneficiaries starts to decline while the number of DC beneficiaries increases. Accordingly, the effect on pension replacement rates only appears after 2043 for cohorts retiring thereafter.

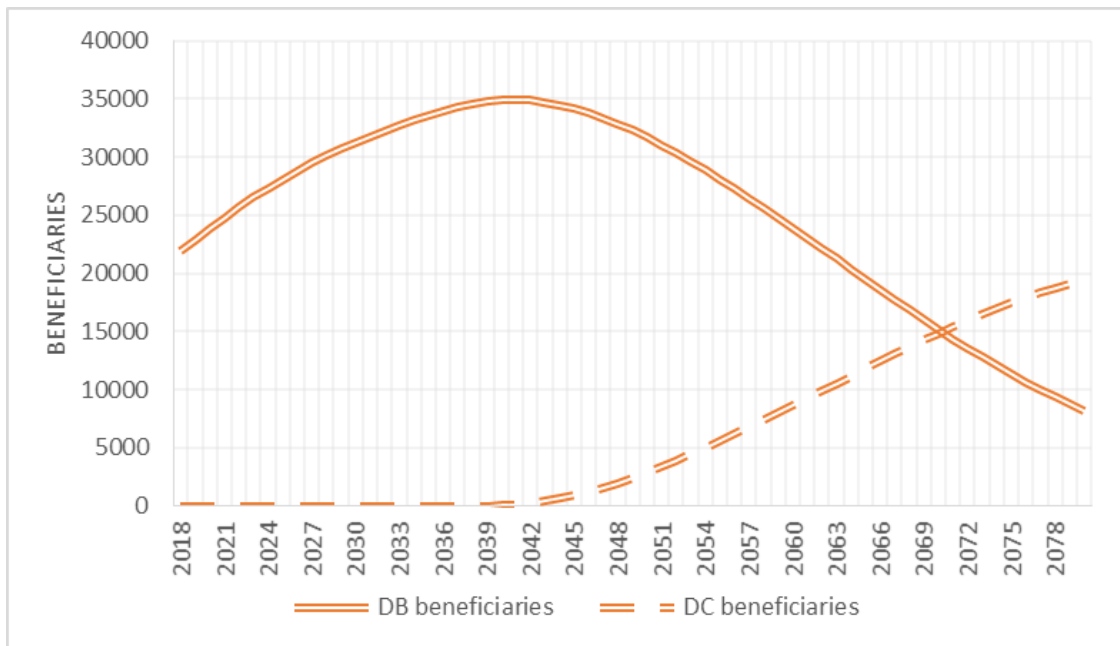


Figure 13. Evolution of the number of beneficiaries the scheme for officials and servicemen under the scenario of switching new employees to a DC scheme

Figure 14 depicts the evolution of costs under the scenario of switching to a DC scheme for new employees as compared to the base scenario.

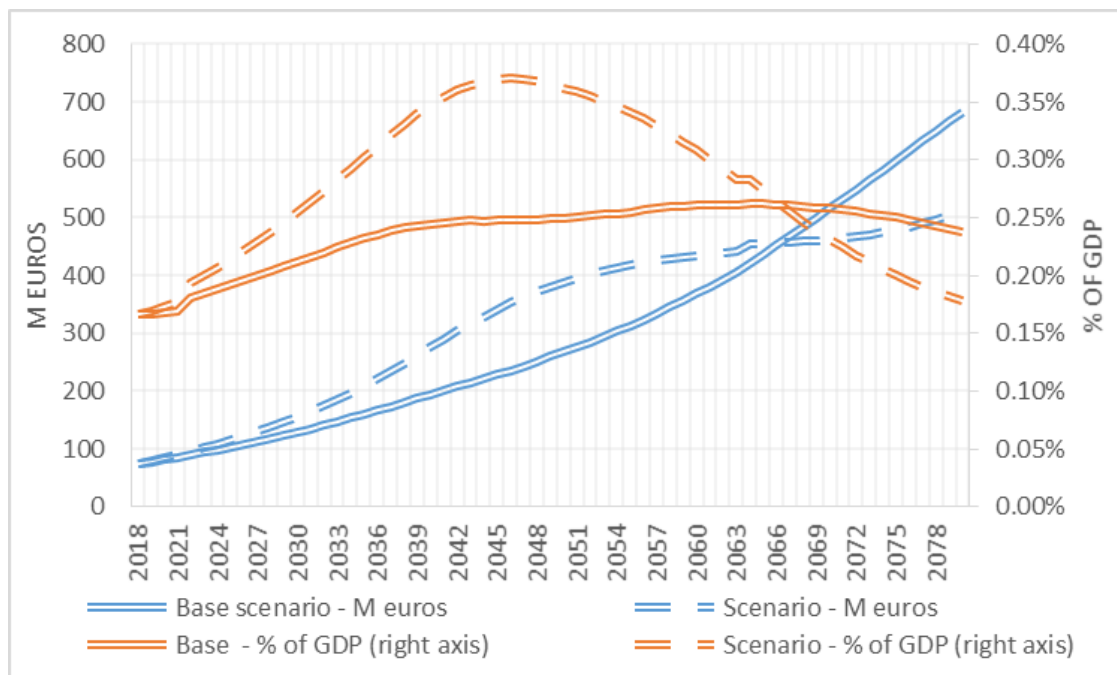


Figure 14. Projected expenditures of the scheme for officials and servicemen (per cent of GDP – right axis; millions EUR – left axis) under the scenario of switching to a DC scheme for new employees compared to the base scenario

Switching to a separate DC scheme for new employees would increase the costs for the next 45 years. This is due to the classical issue of transition costs – the need to finance

simultaneously benefits under the old scheme to current retirees and to future retirees for pension rights already acquired while setting aside contributions to pre-fund new pension rights for new employees. Only from the second half of 2060s this reform scenario would contain costs compared to the base scenario.

Another alternative could be to introduce a DC scheme for all current and future employees to cover new insurance periods from 2020 onwards, but compensate service years acquired before 2020 under the current DB rules.

Figure 15 illustrates the evolution of costs under such a scenario. Comparing the evolution of costs under these two alternative strategies of switching to a DC scheme (Figures 14 and 15), we observe that switching to a DC for all employees from 2020 as regards new insurance periods entails initially higher costs compared to the scenario where only new employees switch. The peak of transition costs arrives about 15 years earlier with total costs nearly doubling by mid 2030s. However, in the longer run the costs would be lower.

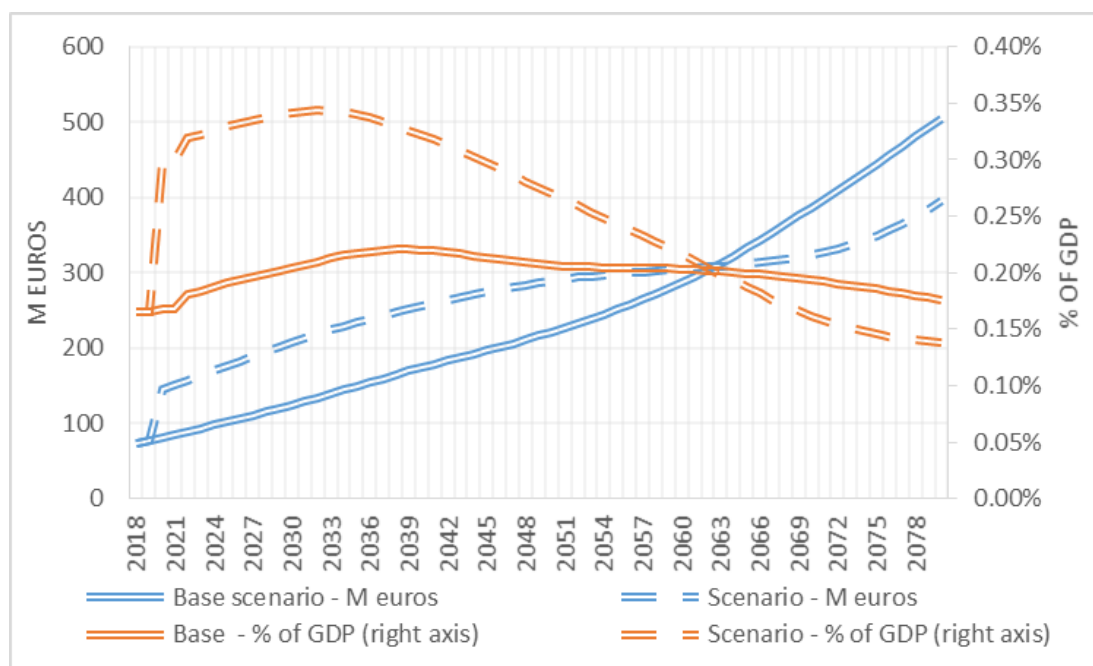


Figure 15. Projected expenditures (per cent of GDP – right axis; millions EUR – left axis) of the scheme for officials and servicemen under the scenario of switching to a DC scheme from 2020 for all employees compared to the base scenario

The other side of the coin is the evolution of the average replacement rate. Switching to a DC scheme for all employees for new insurance periods would significantly reduce the replacement rate already over the next decade (Figure 16).

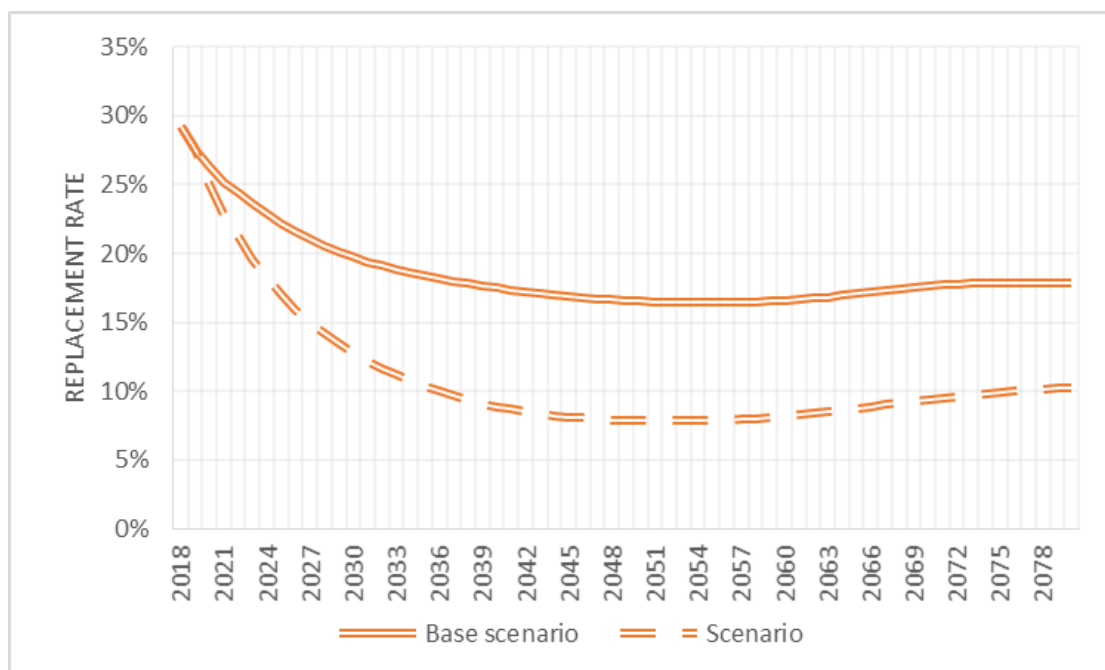


Figure 16. Evolution of the average replacement rate in the scheme for officials and servicemen under the scenario of switching to a DC scheme for all insurance periods from 2020 onwards compared to the base scenario

Alternatively, to maintain the current average replacement rate, the contribution rate would need to be higher – with implications on expenditures – or the yield on assets would need to be higher – with uncertainties on whether this is realistic.

Parametric reforms of special occupational schemes

Such reforms could entail a set of parametric changes in the current rules with a view to curtailing the increase of costs and increase fairness. Such parametric changes could be:

- introducing an age criteria (in addition to length of service criteria) for state pensions of officials and servicemen, and for stage artists;
- introducing a regular indexation of state pensions;
- harmonisation of benefit rules and payment conditions across covered occupational groups by eliminating ungrounded differences.

Scenario 4 – Introducing an age criteria

This scenario would aim to postpone the average age of withdrawal from covered occupations, while maintaining the purchasing power of pensions in payment. The age criteria could be linked to the general pension age, implying it will increase on par with increase of the general pension age.

The following figures illustrate the impact of a parametric reform whereby a minimum age to retire in the scheme of officials and servicemen is set 5 years before the general pension age.

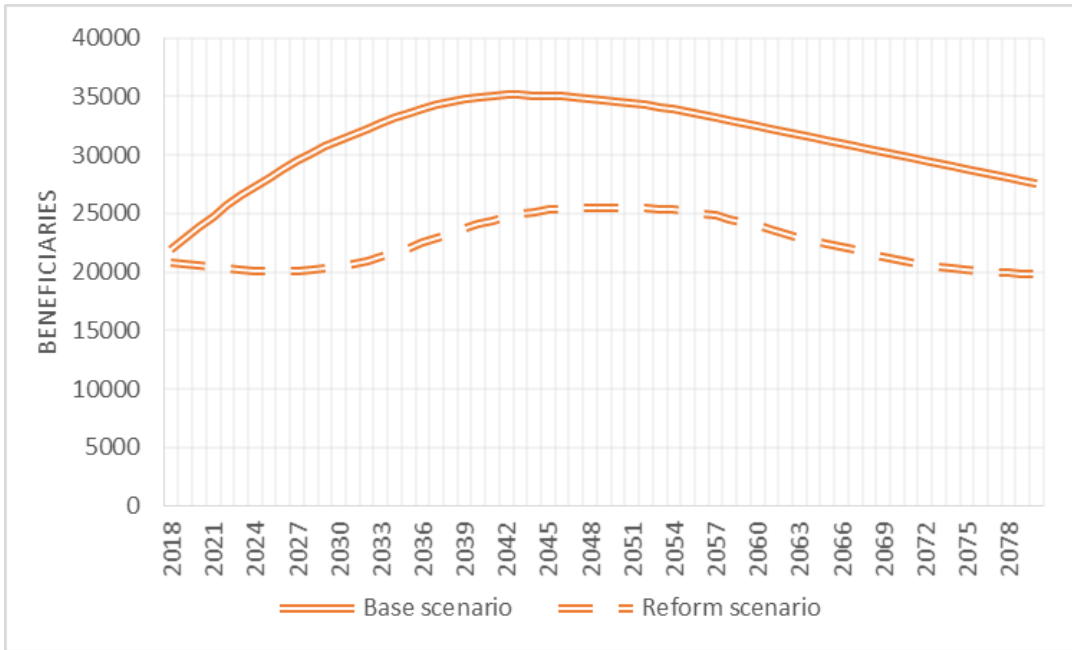


Figure 17. Evolution of the number of beneficiaries in the scheme for officials and servicemen under the scenario of introducing an age criteria 5 years before the general pension age compared to the base scenario

Introduction of an age criteria 5 years before the general pension age would stabilize the number of beneficiaries over the next decade and prevent a significant increase in the number of retirees compared to the base scenario as the employees could not retire so early as currently and would have to continue to work for some additional years. In 2030s the number of retirees would still increase due to increasing life expectancy unless the general pension age is further increased.

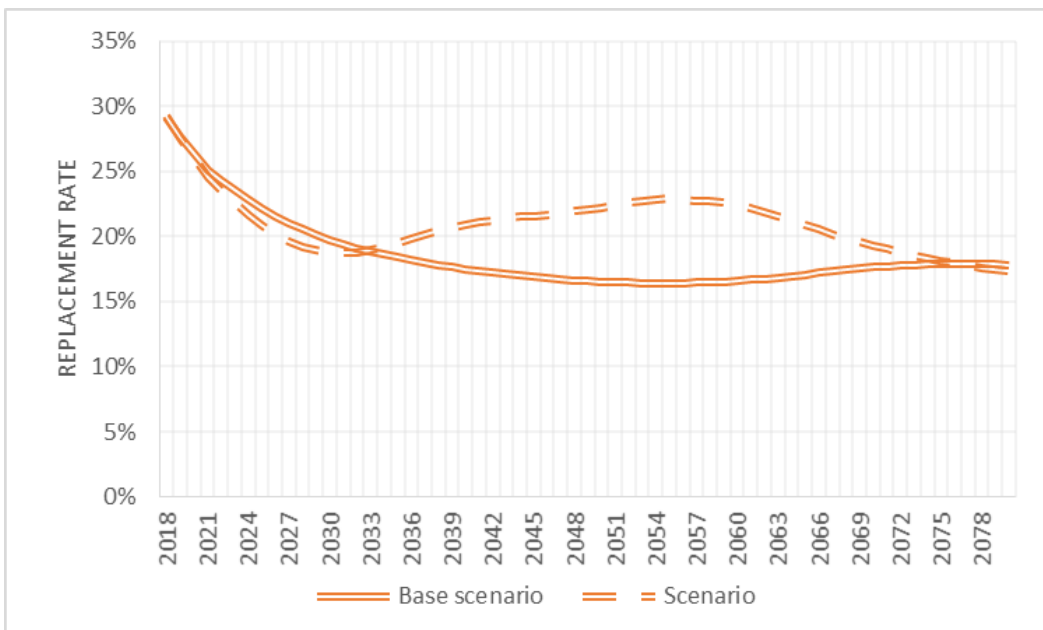


Figure 18. Evolution of the average replacement rate in the scheme for officials and servicemen under the scenario of introducing an age criteria 5 years before the general pension age compared to the base scenario

This parametric reform would increase the average replacement rate from mid 2030s due to longer average accrual periods for new retirees.

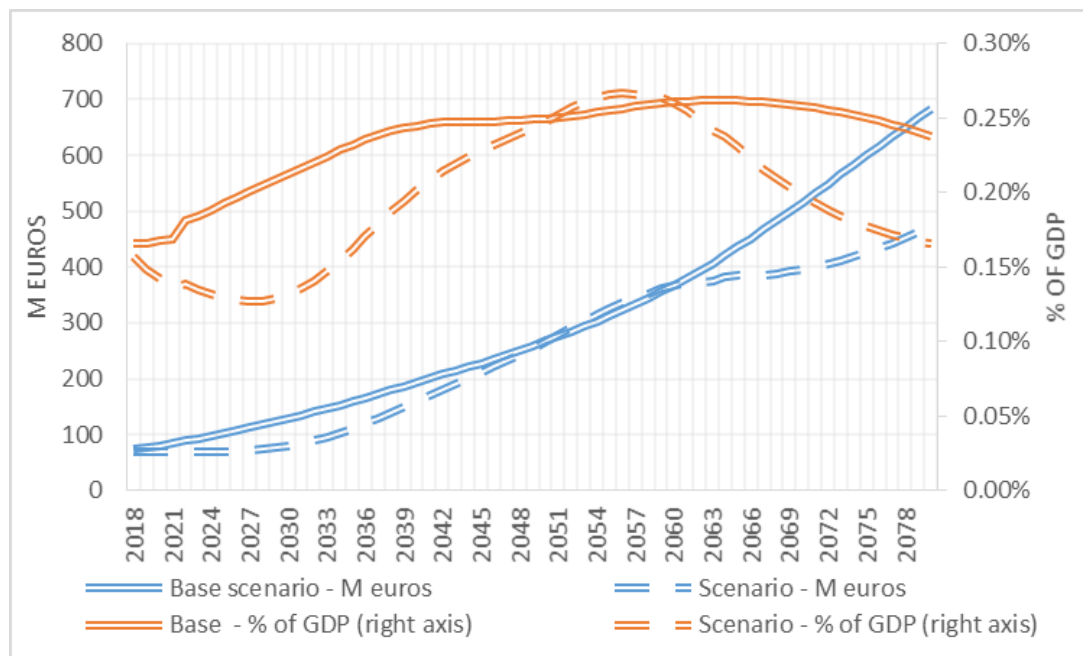


Figure 19. Projected expenditures (per cent of GDP – right axis; millions EUR – left axis) of the scheme for officials and servicemen under the scenario of introducing an age criteria 5 years before the general pension age compared to the base scenario

Introduction of the age criteria would significantly contain the costs compared to the base scenario. The level of costs would stabilize over the next decade. Thereafter the costs would increase as a result of increase in the average replacement rate due to longer accrual periods. However, the cumulative costs over a longer time horizon would still be significantly lower than in the base scenario.

Scenario 5 – Indexation

In this scenario we analyse the impact of introducing a regular indexation of state pensions for officials and servicemen upon the average replacement rate (ratio of the average pension from this scheme to the average national wage) and the evolution of expenditures. We use two alternative indexes in calculations:

- state pensions are indexed annually with the consumer price index (CPI) to maintain their purchasing power; or
- state pensions are indexed annually with the average wage growth.

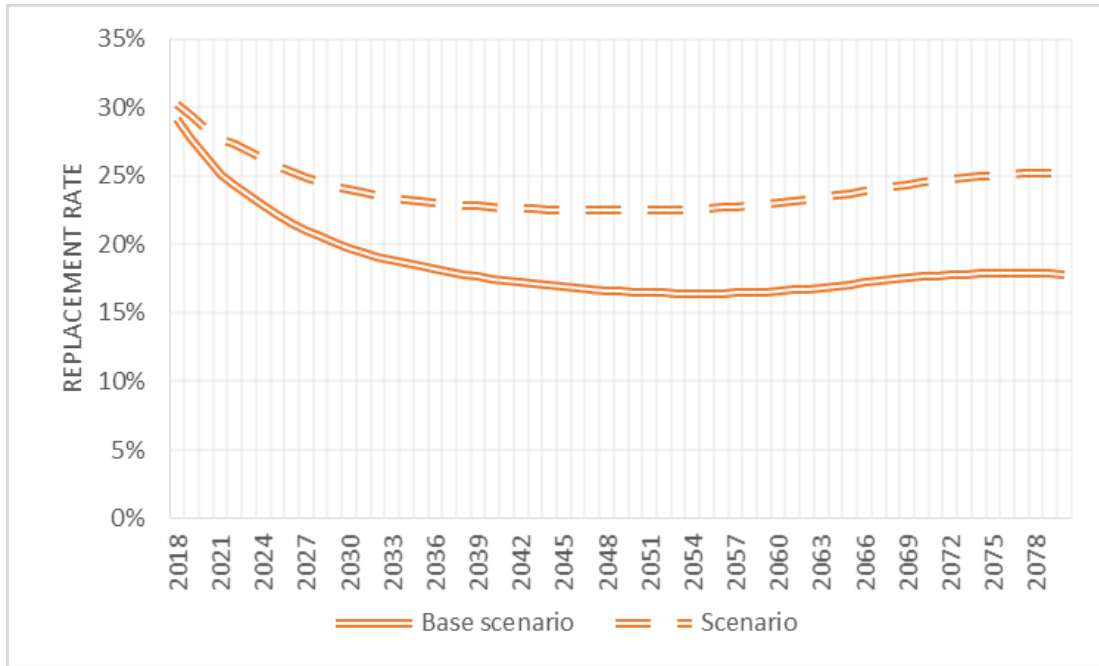


Figure 20. Evolution of the average replacement rate in the scheme for officials and servicemen if pensions are indexed with CPI compared to the base scenario

Annual indexation of pensions with CPI would still imply a decline in the average replacement rate, but the decline is more moderate compared to the base scenario with no indexation. On the other hand, expenditures would increase.

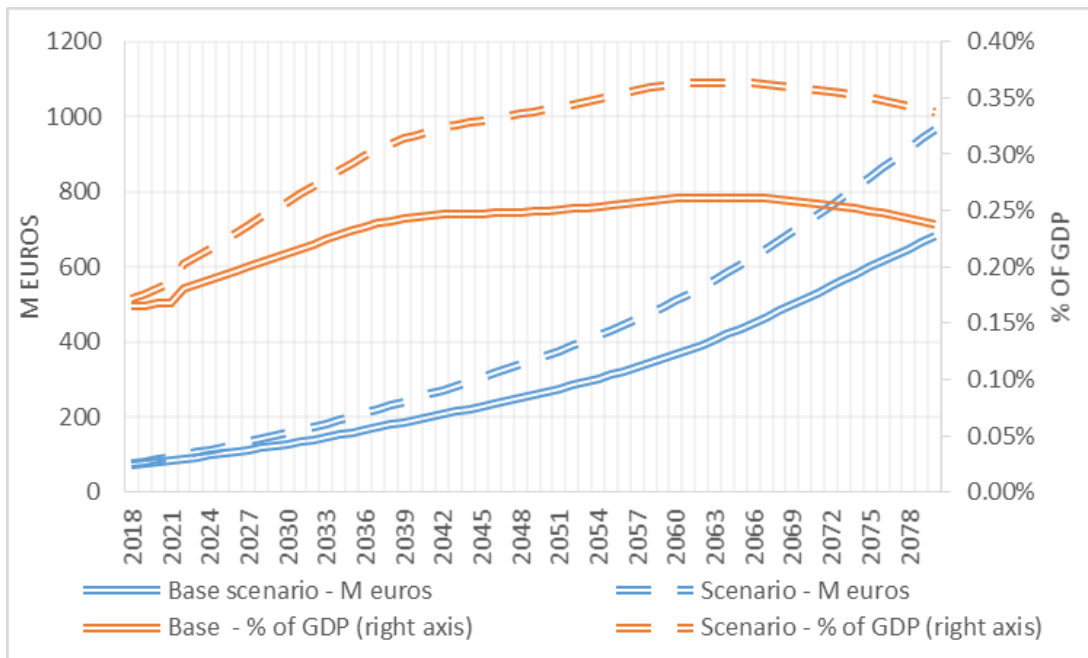


Figure 21. Projected expenditures (per cent of GDP – right axis; millions EUR – left axis) of the scheme for officials and servicemen if pensions are indexed with CPI compared to the base scenario

Annual indexation of pensions with the average wage growth would stabilize the average replacement rate with a slight increase in the longer term.

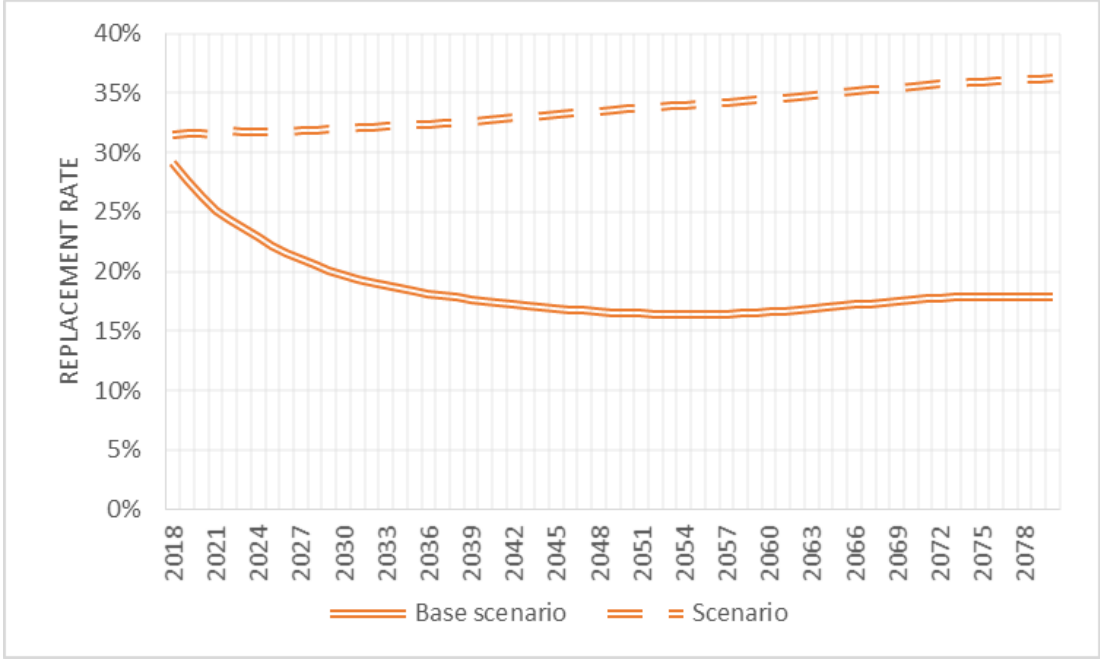


Figure 22. Evolution of the average replacement rate in the scheme for officials and servicemen if pensions are indexed with the average wage growth compared to the base scenario

On the other hand, the increase of expenditures would be much higher than in the case of CPI indexation with the total costs doubling over the next 40 years.

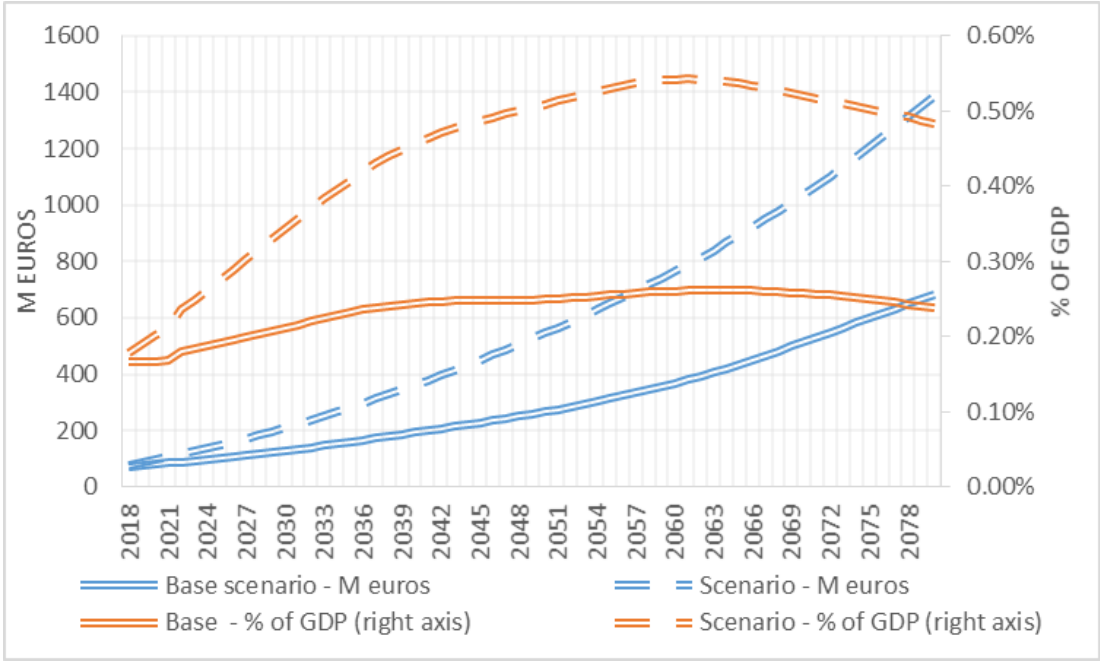


Figure 23. Projected expenditures (per cent of GDP – right axis; millions EUR – left axis) of the scheme for officials and servicemen if pensions are indexed with the average wage growth compared to the base scenario

II. Merit-based state pensions

1. Description of scheme parameters

The key parameters of three types of merit-based state pensions are outlined first:

- 1) first and second degree pensions;
- 2) annuities for former sportsmen;
- 3) annuities for signatories of the Independence Act.

1.1 State pensions of the first and second degree

The first and second degree state pensions are regulated by the Law on state pensions, effective from 1995.

Personal scope

The first degree state pensions are granted to:

- 1) Olympic champions (gold medal winners);
- 2) Winners of the Lithuanian National Prize for Culture and Arts;
- 3) participants of armed resistance.

The second degree state pensions are granted to:

- 1) mothers or fathers of 5 or more children (own or adopted), who have raised them to the age of 8;
- 2) Olympic medallists (silver and bronze medallists), Paralympic champions, world champions in Olympic sports and Deaflympics champions;
- 3) Honorary Donors

To a first or second degree state pension are also entitled:

- 1) freedom fighters (distinguished members of unarmed resistance);
- 2) the highest state officials (Speaker of the Seimas, Prime Minister, President of the Supreme Court, or President of the Constitutional Court)

Contingency as defined by law

Qualifying acts

Risks covered

Merits combined with old age, incapacity to work, survivorship

Qualifying conditions

Attaining pension age or being incapable to work (loss of work capacity 60% or more)

For highest state officials there is a length of service requirement – at least 2 years in qualifying position – combined with attaining the pension age.

Benefits

The first and second degree state pensions are paid in flat rates, the amounts being linked to the state pension base:

- the first degree state pension amounts to 4 state pension bases (in 2018, 4 x 58 EUR = 232 EUR);
- the second degree state pension amounts to 2 state pension bases (in 2018, 2 x 58 EUR = 116 EUR)

To qualifying survivors a survivors' pension is paid in the amount of 20% of the state pension to which the deceased was entitled.

To orphans the amount of pension is 30-100% of the state pension to which the deceased was entitled depending on the number of surviving children and if there is also a surviving spouse.

1.2 Annuities for former sportsmen

The benefits are regulated by Article 41 of the Law on physical education and sports, in force from 2009.

Personal scope

Former sportsmen citizens of Lithuania who are:

- 1) champions or medal winners of Olympic games (gold, silver or bronze medals);
- 2) European or world champions in any Olympic discipline of an Olympic sport;
- 3) before 11 March 1990 a world or European champion of the discipline removed from the Olympic programme prior to the achievement of the result or added to the Olympic programme after the achievement of the result;
- 4) European or world record holders of any Olympic discipline of an Olympic sport, a record holder of Olympic games;
- 5) winners of Paralympic games and deaf games;
- 6) world champions and record holders of a non-Olympic discipline of an Olympic sport;
- 7) world champions of a non-Olympic discipline of an Olympic sport for at least three times.

Contingency as defined by law

A sportsman has finished the sporting career and does not participate in Olympic games, world and European championships

Risks covered

Merits combined with retirement

Qualifying conditions

- 1) Achievement of the specified result (qualifying medals or records)
- 2) Finishing of sporting career

Benefit

A flat-rate benefit in the amount of 1,5 monthly average wage in the national economy.

Payment conditions

The benefit is not granted and the granted benefit not paid, if the person has insured income (except income for work in the field of physical education and sports), a judgement of conviction has become effective for committing an intentional crime, the person has been disqualified for use of doping and the qualifying results have been annulled, or the person has lost citizenship of Lithuania.

1.3 Annuities for signatories of Independence Act

Personal scope

Signatories of Independence Act regardless of age

Contingency as defined by law

Qualifying act

Risks covered

Merit, survivorship

Benefit

50% of the wage of the Member of the Parliament (in 2018, 1285 EUR)

Survivors and orphans are paid 25% of the annuity.

	I degree	II degree	Former sportsmen	Signatories
Contingencies covered	Merits combined with old age, incapacity for work,	Merits combined with old age, incapacity for	Merits combined with withdrawal from sports career	Qualifying merit

	survivorship	work, survivorship		
Retirement age	General pension age	General pension age	No statutory retirement age	No statutory retirement age
Qualification period	2 years of service for highest state officials. No specific qualification period for other groups	No qualification period	No qualification period	No qualification period
Benefit type	Flat-rate	Flat-rate	Flat-rate	Flat-rate
Benefit formula	4 times state pension base	2 times state pension base	1,5 monthly national average wage	50% of the wage of MPs
Benefit revalorisation	No statutory revalorisation	No statutory revalorisation	Revalorised quarterly based on new value of national average wage	Benefit linked to MPs wage, revalorised once in 4 years after Parliament elections

Table 10. Comparison of main parameters of occupational state pensions

2. Descriptive statistics on merit-based schemes

2.1 Number of beneficiaries by gender, age and type of benefit

The total number of beneficiaries of merit-based state pensions was 14207 persons in 2017. Women strongly outnumber men in this branch of state pensions, with nearly 90% of recipients being women. However, among the recipients of the first-degree state pensions the gender balance is the opposite, as 87% of beneficiaries are men.

<i>Merit-based state pensions</i>	Women	Men	Total
First degree	63	427	490
Second degree	12002	855	12857
Second degree survivors	566	75	641
Signatories	7	65	72
Signatories' survivors	15	1	16
Former sportsmen	59	72	131
Total	12712	1495	14207

Table 11. The number of beneficiaries and gender breakdown of merit-based state pensions in 2017

Within the category of second degree state pensions, mothers of 5 or more children constitute the largest subgroup with 9898 beneficiaries (77% of all recipients of second degree state pensions) in 2017.

The age structure of recipients of merit-based benefits is strongly skewed towards older ages. For women, the peak is in age group 80-84, while for men the peak is even higher, in 85-89 age group. Nearly 85% of recipients of merit-based benefits are 70+ years old.

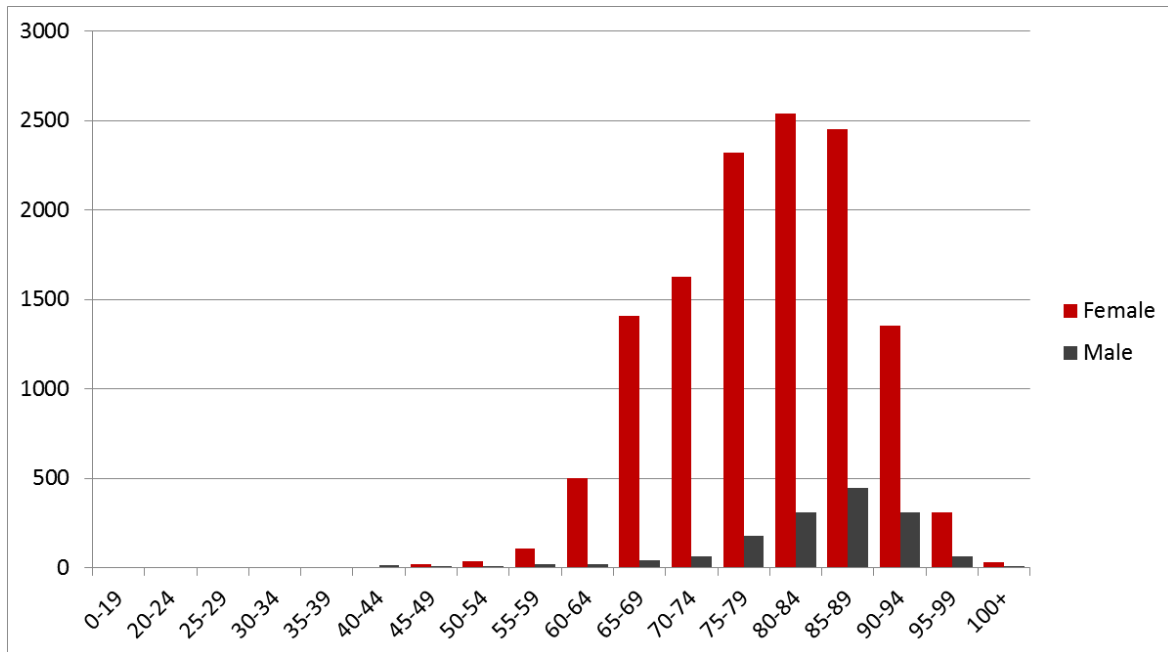


Figure 24. Age and gender profile of recipients of merit-based state pensions in 2017

In 2014 the number of beneficiaries of merit-based pensions increased as the personal scope of second degree state pensions was extended to mothers of 5 or more children (earlier mothers of 7 or more children were eligible). As a result, the number of beneficiaries of the second degree state pensions increased by more than 8400 persons, from 5478 persons in 2013 to 13903 persons in 2014. Nonetheless, after this one-off large increase the number of beneficiaries of merit-based pensions is again decreasing (Figure 25). The age structure of beneficiaries with a large share of beneficiaries 75-89 years old implies mortality losses, as the prevalence of large families in younger age cohorts is lower, implying a declining number of new beneficiaries.

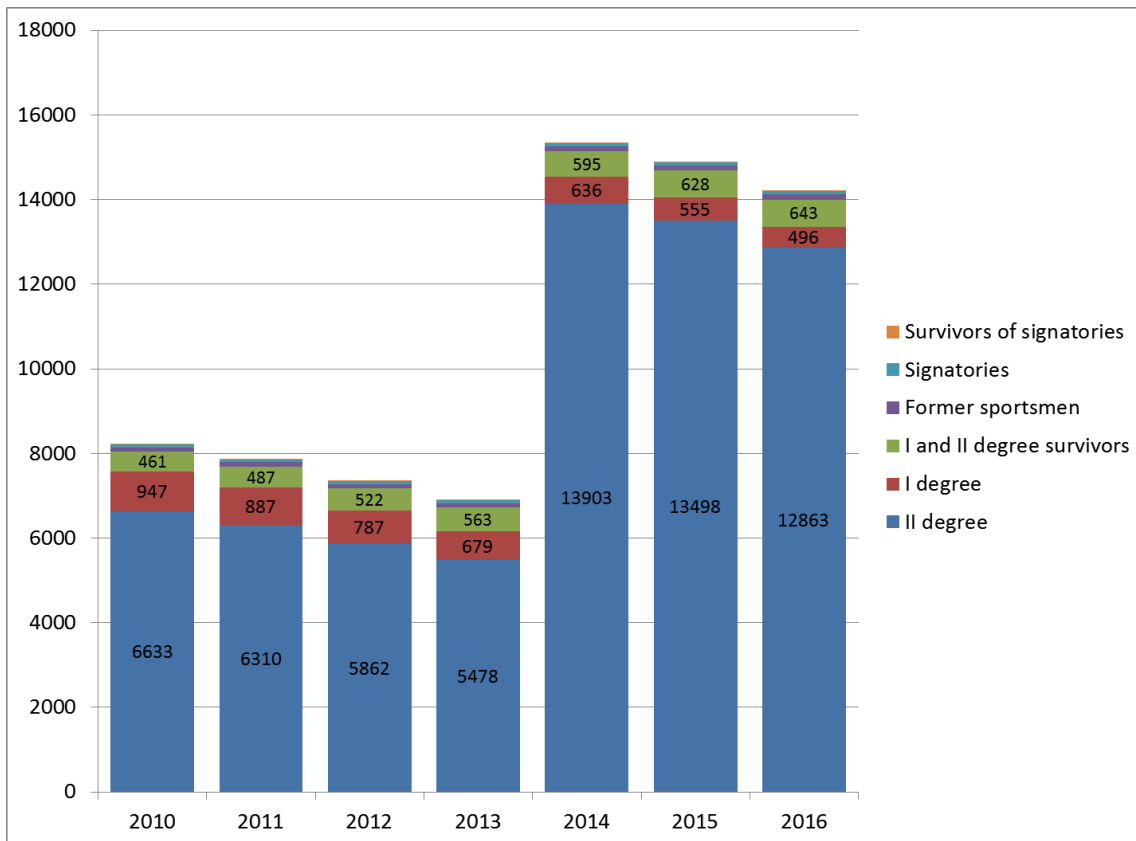


Figure 25. The number of beneficiaries of merit-based state pensions 2010-2016

2.2 Mothers of 5 or more children

Comparing the data on the number of beneficiaries of second degree state pensions for mothers of 5 or more children to census-based data on the number of mothers who have given birth to 5 or more children we observe that the latter numbers are significantly higher. The large difference between these numbers needs to be explained.

In 2011, based on census data, the number of women in pension age (at that time 60+) who had given birth to 5 or more children was 23738. Taking into account mortality (based on gender-specific mortality rates in one-year age cohorts), increase of pension age (from 60 in 2011 to 62 in 2017) and the number of mothers of 5+ children who reached pension age over the period of 2011-2017, we can estimate the number of women in pension age (62+) with 5+ children in 2017. The calculated number of such women is 18493. We observe that the number of women in pension age who have given birth to 5+ children is 1.87 times higher than the actual number of beneficiaries of the second degree state pension for mothers of 5+ children, which was 9898 in 2017.

Possible reasons why some women who have given birth to 5 or more children are not receiving respective state pension for mothers may include:

1) *Child mortality*

Eligible to state pension are mothers who raised the child to the age of eight. A mother of 5 children would not qualify if any of the born children died before the age of 8, as in this case only 4 children were raised to the age of 8. From Eurostat database we observe that the probability of a child to survive until the age of 8 was 97,459% in 1970 (data for earlier periods is not available from Eurostat), increasing to 98,331% in 1995 and 99,426% in 2016. Considering that the children of women currently reaching pension age and those already retired are mostly born before 1975, we can make estimations based on 1970 value. The probability that at that time in a family with 5 children any of the children died before the age of 8 was 12,1% (i.e. $1-0,97459^5$). The group of mothers who have given birth to 5 children constitute about 54,5% of all mothers with 5 or more children. Hence the child mortality effect is likely to count for more than 1200 cases, where a mother who has given birth to 5 children is not eligible for a state pension. However, due to significant decline in child mortality this effect will diminish over time. For children born during the last decade the probability to survive until the age of 8 is over 99%, hence even in a family with 5 children the likelihood of any of the children dying before the age of 8 is less than 5%.

2) *Non-citizens*

The second degree state pension for mothers is granted only to citizens of Lithuania. Non-citizens are not eligible. According to Eurostat, in 2014 the share of foreign citizens in the total resident population of Lithuania was 0,8% (0,1% other EU citizens and 0,7% non-EU citizens). Data on age and gender distribution of non-citizens can be verified, but it is not likely that parents of large families are over-represented among non-citizens. The number of non-citizen mothers ineligible to state pension may therefore be estimated to be less than 150.

3) *Neglect of parental obligations*

To be eligible to the state pension the parent must have been effectively fulfilled parental obligations. If the parent has neglected parental obligations, parental rights have been withdrawn and/or any of the children has been placed in a social care institution, the state pension is not granted. In the absence of specific data, we lack estimation on the share of such parents among large families.

4) *Simultaneous eligibility*

According to the Law on State Pensions, a person who is entitled to receive several state pensions shall only be paid one of them, based on his or her choice. There may be some mothers who are simultaneously eligible to another state pension, which is higher than the amount of second degree state pension. However, their number can't be particularly high as state pensions for victims (which is the only type of state pensions where the number of female recipients is higher than for second degree state pensions) are on

average lower than second degree state pensions. Considering the age structure of female recipients of other types of state pensions and the prevalence of mothers with 5+ children in age groups (about 2% in 45-49 age group to over 5% in age groups over 75), the number of mothers of 5+ children with simultaneous eligibility to another type of state pension is estimated to be about 110.

Also the Law on Social Assistance Pensions stipulates compensations for the mothers of 5 or more children (born before 1 January 1995). The number of recipients of such compensations is 1429. Mother of 5+ children who are not eligible to the social insurance pension mostly choose this compensation rather than the second degree state pension as the compensation is higher (195 EUR in 2018, compared to the second degree state pension which is 116 EUR). However, as the compensation is not paid together with social insurance pension, mothers who are eligible to social insurance pension mostly choose the second degree state pension, if the sum of her social insurance pension and state pension is higher than the amount of compensation, i.e. 195 EUR.

5) *Offences*

State pensions are not granted to persons who have been convicted for committing an intentional offence. However, there is no data on the number of parents of 5+ children who have committed such offences.

6) *Non-take-up*

It is possible that some parents, who are eligible for a state pension, have not applied for it. However, as the poverty risk of older persons and parents of large families in Lithuania is higher than average, the non-take-up is not likely to be particularly widespread.

The reasons with quantified estimations in total would explain about 3 thousand cases where mothers who have given birth to 5 or more children do not qualify for the second degree state pension. However, there remains a gap of more than 5 thousand persons with unexplained reasons for non-eligibility or non-take-up.

2.3 Benefit rates

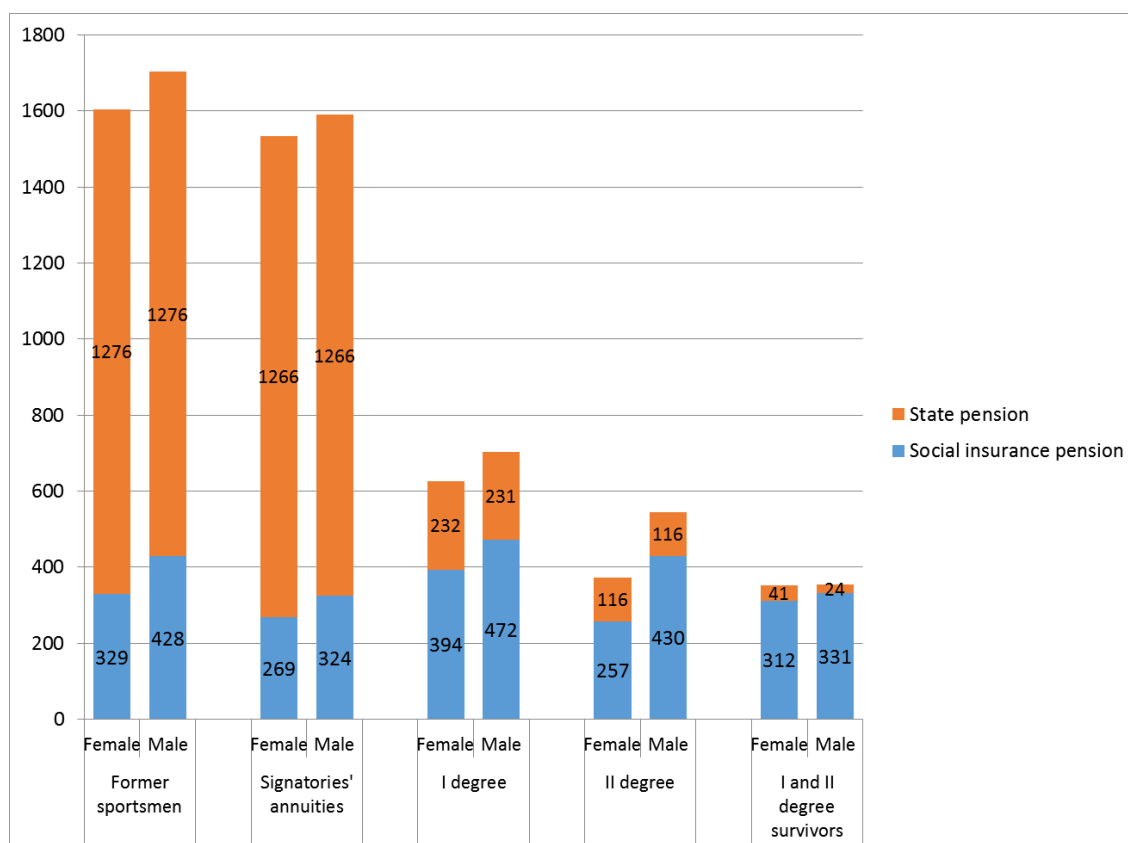


Figure 26. Average state and social insurance pension amounts (EUR) of beneficiaries of merit-based pension schemes in general pension age, 2017

The highest rates of merit-based state pensions are paid to the small categories of Signatories of the Independence Act (72 recipients) and former sportsmen (131 recipients). These benefits exceed the average wage in the country.

As the benefits are paid at flat rates, there is no variation of benefit amounts (including also no gender gap) among beneficiaries receiving the same type of benefit.

3. Analysis of policy inconsistencies

Similar to the analysis of occupational state pensions, the identified policy issues are grouped under thematic topics:

1) Variation of benefit basis, benefit rates and revalorisation

While all types of merit-based state pensions are flat-rate, a number of different calculation bases are applied. First and second degree state pensions are linked to the rate of state pension base. Annuities for former sportsmen are linked to the national average wage. Signatories' and their survivors' annuities are linked to the

wage of the Member of the Parliament. The choice of the calculation base affects the amount of the benefit, but also influences the timing of any revalorizations.

Effectively, the selection of the calculation base and the variation in the benefit amounts reflect the significance attributed to particular merits by the legislator. The highest valued merits then appear to be distinguished sports achievements. The annuities for former sportsmen are linked to the national average wage and accordingly recalculated quarterly along with changes in the national average wage. The larger categories of first and second degree state pensions are considerably lower, but are also adjusted less frequently.

2) Overlapping entitlements under different legal acts

Olympic champions and medal winners (as well as the winners of Paralympic and Deaflympic games) fall simultaneously into the personal scope of two types of benefits: first or second degree state pensions and the annuity for former sportsmen. The criteria of these two types of benefits are somewhat different, but situations of overlapping entitlements may occur. Despite the fact that in case of overlapping entitlements only one state pension is payable (based on the choice of an eligible person) in interests of legal clarity and rationality, the provisions addressing the same persons and the same contingencies could be regulated in a single act.

3) Less favourable treatment of disabled athletes

According to Article 4 of the Law on state pensions, Olympic champions (gold medal winners) are entitled to the first degree state pension, whereas the silver and bronze medal winners at Olympic games, Paralympic champions and Deaflympics champions are entitled to second degree state pension, with respectively lower rate of benefit. While the winners of Paralympic and Deaflympic games are equalised with the lower colour (silver and bronze) Olympic medal winners, at the same time they are treated less favourably than the winners of Olympic games. Hence there is a differential treatment linked to disability. It is not self-evident if there is an objective justification and a legitimate aim that this differential treatment serves. In the absence of an objective justification, the less favourable treatment is not compatible with the principles of the equality and non-discrimination enshrined in Article 5 of the UN Convention on the Rights of Persons with Disabilities.

According to Article 41 of the Law on physical education and sports, the former sportsmen who have finished their sports career are entitled to a monthly annuity in the amount of 1,5 average wage. Among other categories of sportsmen, the right extends to the champions and other medal winners (gold, silver, bronze) of Olympic games, and also to the winners of Paralympic and Deaflympic games. Hence, for the purposes of this law the winners of Paralympic and Deaflympic games are treated equally with Olympic champions. However, the winners of silver and bronze medals of Paralympic and Deaflympic games are treated less favourably than respective medal winners at Olympic games as they are not eligible to a respective annuity.

4. Projections

The base scenario again assumes no changes in the applicable legislation.

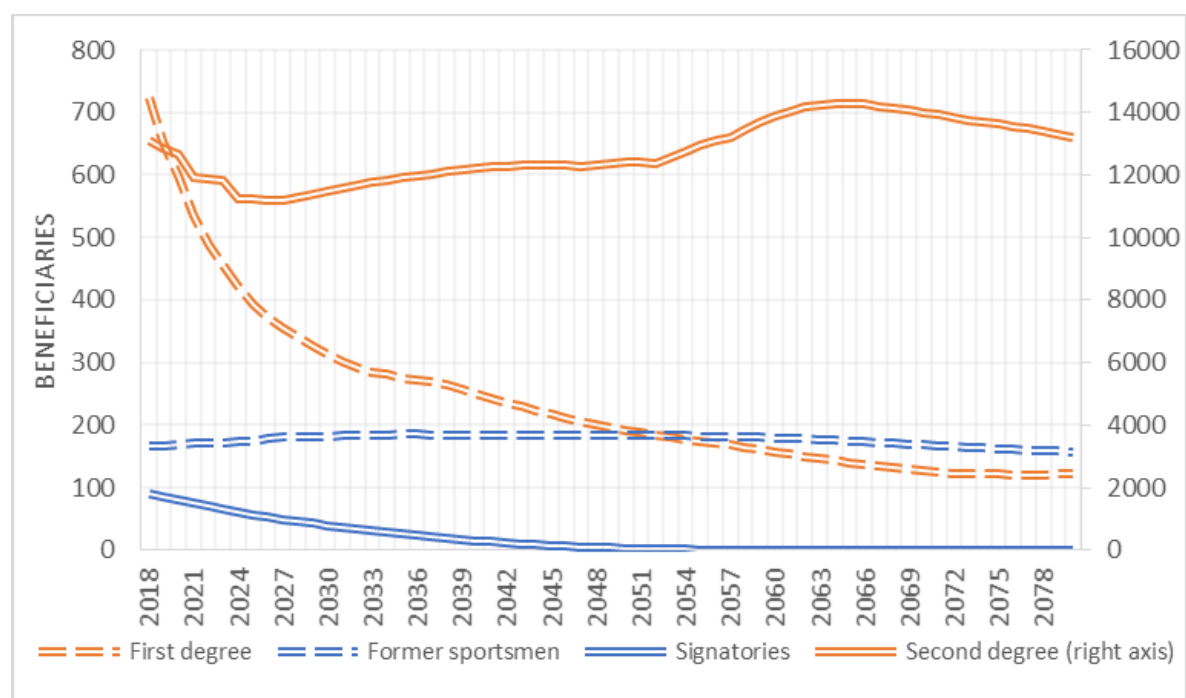


Figure 27. Evolution of the number of beneficiaries of merit-based pension schemes under the base scenario

The total number of recipients of merit-based state pensions is expected to decline. The number of beneficiaries of the largest sub-scheme of second degree state pensions for parents of 5+ children would decline over the next decade until 2027, but would start to increase thereafter. Obviously, such projection is an artefact of the assumptions whereby the share of parents of 5+ children in subsequent cohorts would remain constant (at about 2%) while the life expectancy is projected to increase. The turning point in 2027

relates to the fact that the currently legislated increase of pension age will continue until 2026. The trend could be altered if the pension age is increased further beyond 2026.

The number of recipients of first degree state pensions is expected to decline due to mortality of freedom fighters and participants of armed resistance, assuming the personal scope of these benefits is not extended. Similarly, the number of recipients of signatories' annuities will decline.

Figure 28 depicts the projected evolution of costs of merit-based pension schemes.

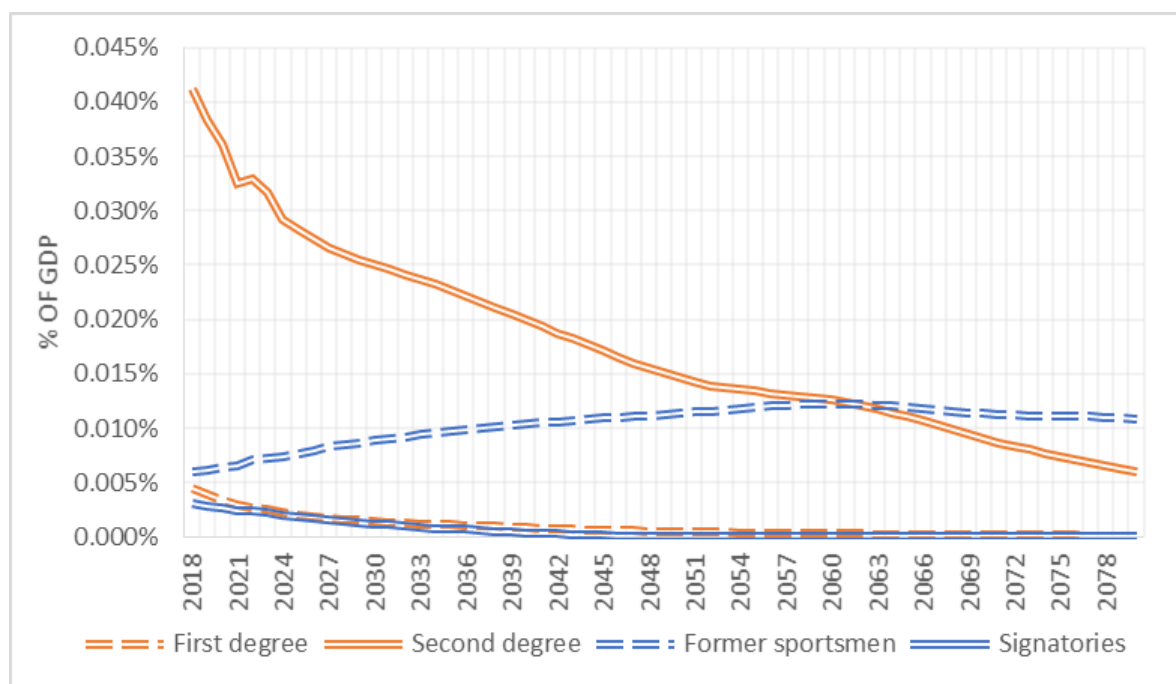


Figure 28. Evolution of expenditures of merit-based pension schemes under the base scenario (per cent of GDP)

The total costs of merit-based state pension schemes are projected to decrease. In the mid-term, by 2040 the total costs of these pensions would decline by about one third from 0.05% of GDP to 0.033% (or from 23 million EUR to 15.5 million EUR in discounted values). In the longer term, the total costs of merit-based pensions would further decline, whereas the costs of annuities for former sportsmen would stabilize at around 0.01% of GDP.

5. Reform options

At the request of Lithuanian authorities we analyse here implications of a policy alternative whereby the personal scope of second degree state pensions would be extended to parents of 4 children.

Scenario 1 – extending second degree state pensions to parents of 4 or more children

Taking as a basis the population data from census and the share of mothers who have given birth to 4 children in single-year age cohorts, estimation is needed on the proportion of such mothers who fulfil all qualification conditions and will take up such benefits. In this regard the analysis presented in section 8.3 is relevant. More specifically, the question is if the eligibility/take-up ratio among mothers of 4 children is the same or higher than among mothers of 5+ children. There are several factors suggesting it may be (substantially) higher: the child mortality effect is lower, the child neglect factor is likely to be lower as the share of risk-families tends to be higher in larger families. The issue of simultaneous eligibility is dependent on if there will be corresponding changes in the Law on Social Assistance Pensions or not.

Figure 29 depicts the evolution of the number of beneficiaries if the second degree state pensions were to be extended to parents of 4 children from 2020.

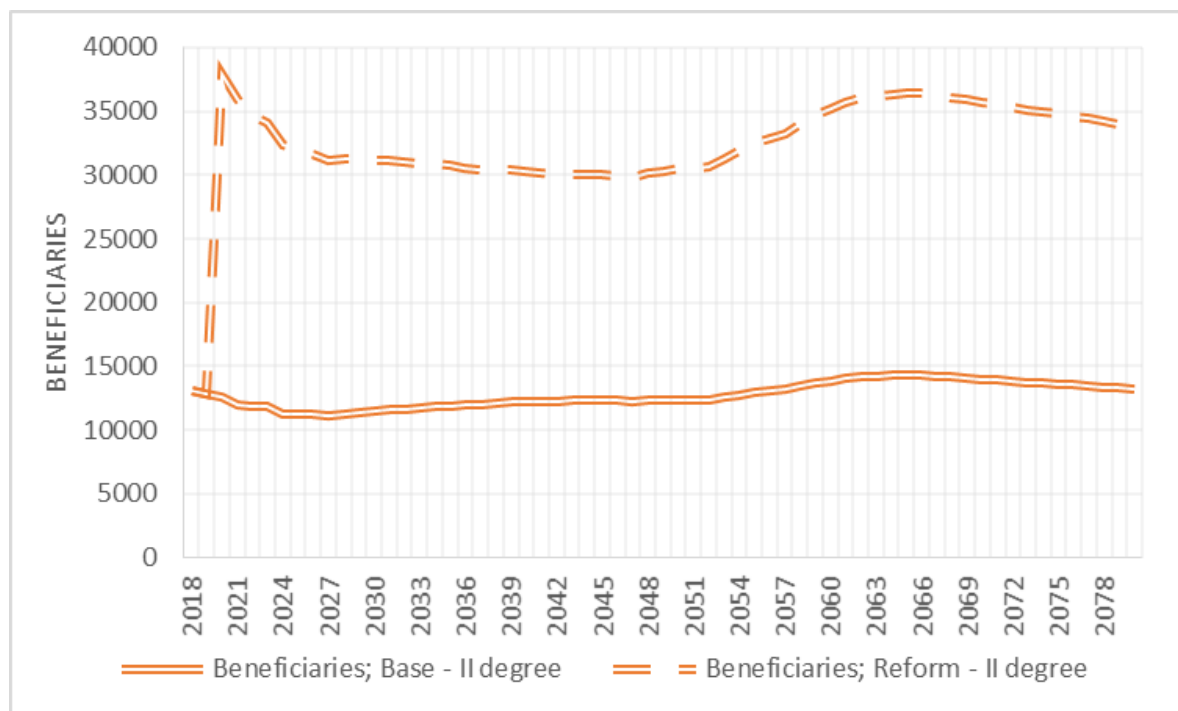


Figure 29. Evolution of the number of beneficiaries of second degree state pension under the scenario if the scheme is extended to parents of 4 children compared to the base scenario

We observe a large increase in the number beneficiaries by about 25 thousand persons at the onset of the reform as also parents who are already in pension age and have 4 children would become eligible. Following the one-off large increase, the number of beneficiaries would again decline due to lower prevalence of families with 4 children in cohorts reaching pension age in the next decades, compared to older cohorts who are currently in pension age.

The expenditure curve follows a similar trend with a one-off sharp increase of expenditures (to over 0.1% of GDP or up to 30 million EUR in 2020) with a subsequent decline over the time horizon of projections.

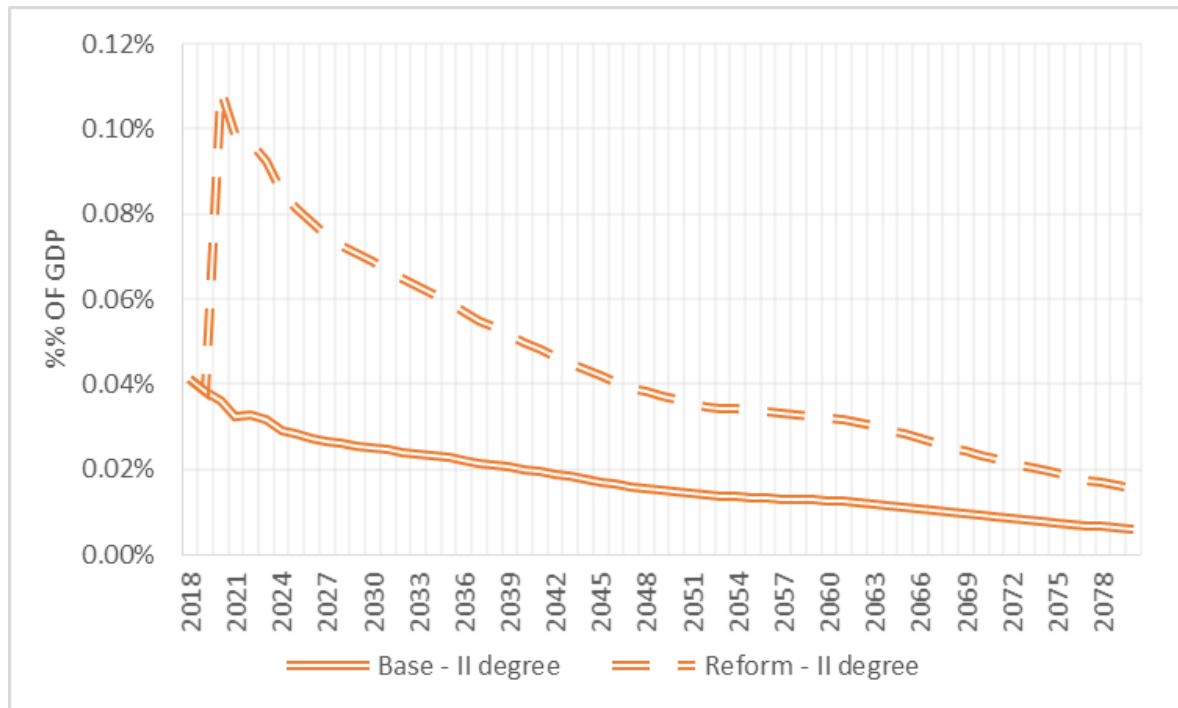


Figure 30. Evolution of expenditures (per cent of GDP) of second degree state pensions under the scenario if the scheme is extended to parents of 4 children

Scenario 2 – parametric reforms of merit-based pension schemes

Such reforms could entail some parametric changes in the current rules with a view to increasing legal clarity and fairness. Such parametric changes may include harmonisation of benefit calculation basis and benefit revalorisation rules across different types of merit-based state pensions.

The purpose of such reforms would be to increase fairness and eliminate ungrounded differences in scheme parameters, while possibly retaining justified differences of benefit rates at the discretion of the legislator. Such reforms are not analysed here in further details, as the reforms parameters would need to be specified first. However, the model permits to run projections upon defining such reform scenarios.

III. Compensatory benefits

This category covers state pensions for victims.

1. Description of scheme parameters

1.1 State pensions for victims

Personal scope

Victims of aggression, repressions and other defined circumstances and their survivors

Contingencies covered

Defined situations of victimisation

Benefit

The amount of pension is linked to the state pension base. The rate of pension varies depending on the legal status, level and reason of incapacity for work as ranges from 0,8025 state pension base to 8.56 state pension base (or from 46.55 EUR to 496.48 EUR in 2018).

Payment conditions

The pension is paid regardless of other income the victims may have.

2. Descriptive statistics on compensatory scheme for victims

The total number of recipients of victims' pensions was 65045 persons in 2017.

<i>Compensatory benefits</i>	Women	Men	Total
Victims	27498	17062	44560
Victims survivors	17573	2912	20485
Total	45071	19974	65045

Table 12. The number of beneficiaries and gender breakdown of compensatory state pensions in 2017

Women outnumber men in a ratio about 70:30 among the recipients. The gender balance is related to the age-structure of recipients of victims' pensions combined with the higher longevity of surviving women. In other words, due to shorter life expectancy, many

former male recipients of victims’ pensions have passed away, while their spouses and female victims survive.

As a result, the age structure of recipients of compensatory benefits is skewed towards older ages with the peak in age bracket 75-84.

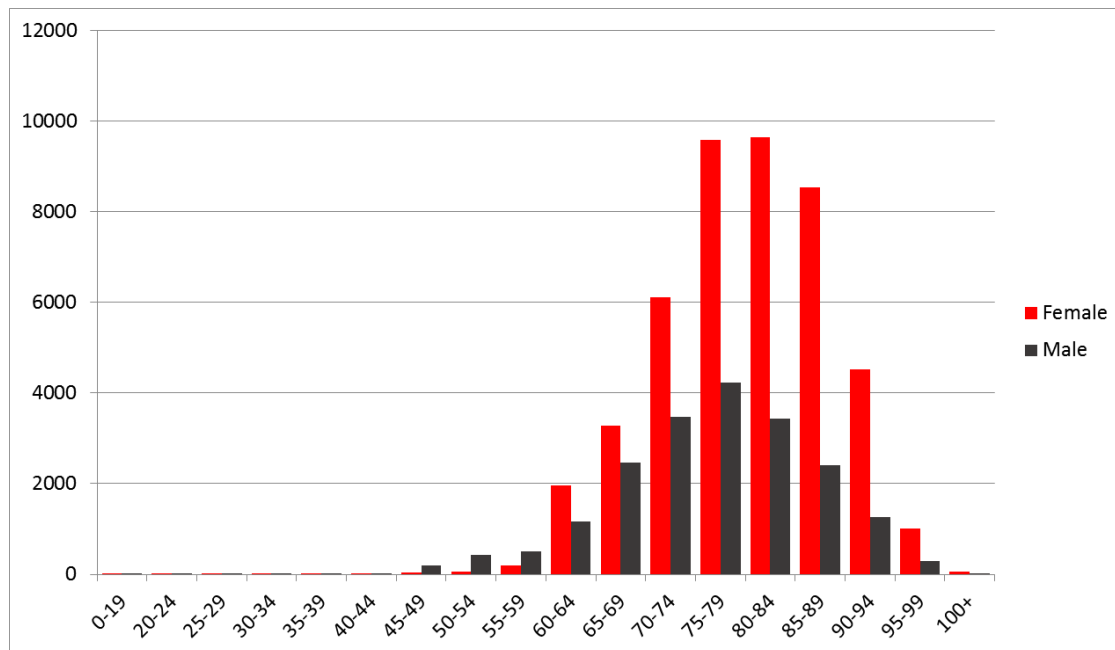


Figure 31. Age and gender profile of recipients of compensatory benefits in 2017

Over the last years, the number of recipients of victims’ state pensions has been steadily declining due to mortality of beneficiaries in old age.

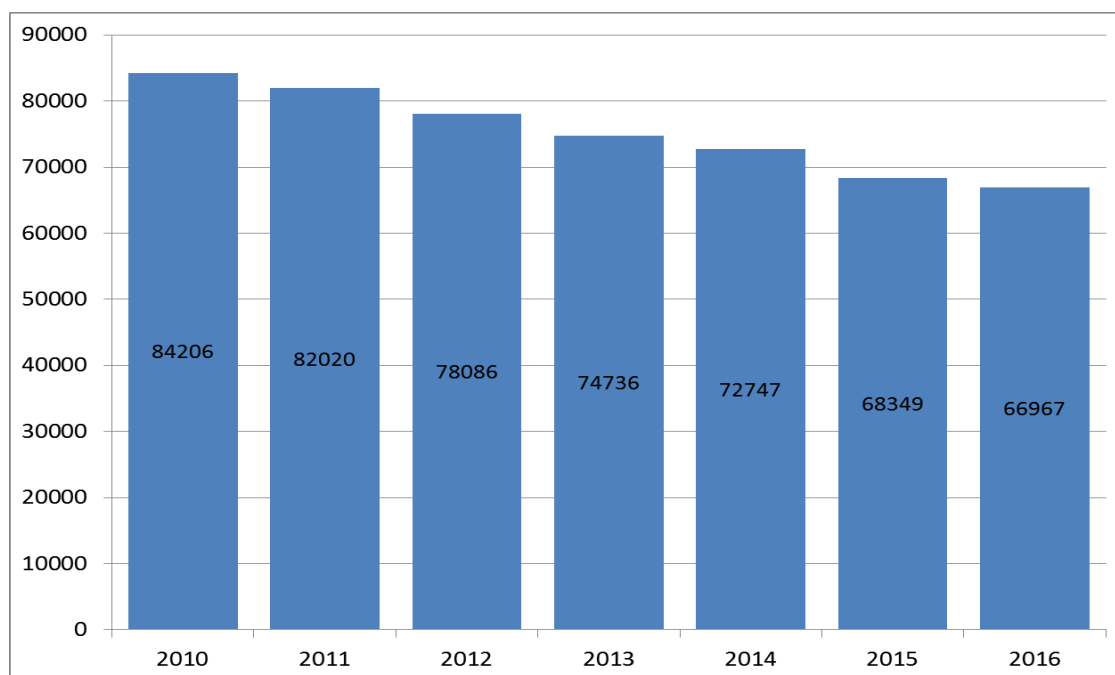


Figure 32. The number of beneficiaries of victims’ state pensions 2010-2016

The compensatory benefits for victims of repressions effectively constitute supplements to social insurance pensions, adding on average a supplement in the range of 15-20% to their social insurance pension.

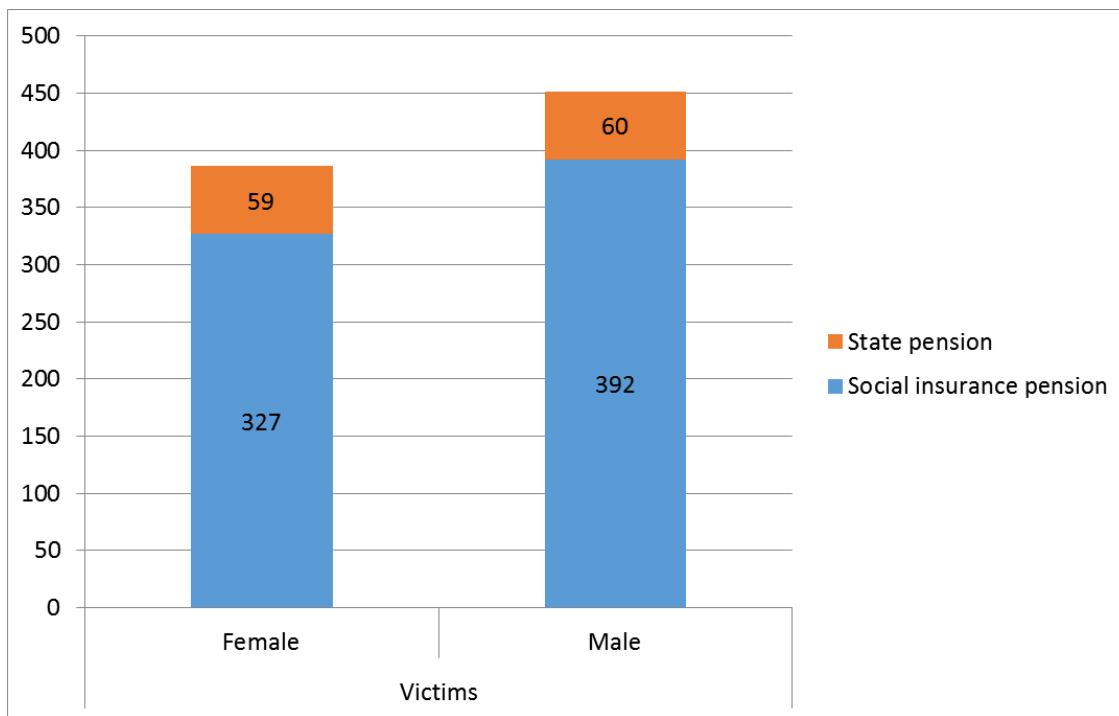


Figure 33. Average pension amounts of recipients of victims’ pensions (upon reaching pension age) in 2017

3. Projections

The number of beneficiaries of the state pensions for victims is projected to decline due to mortality, provided the personal scope of the scheme is not extended to other groups and no new categories of victims emerge. By 2040, around 11 thousand recipients of victims’ pensions are still alive.



Figure 34. Evolution of the number of beneficiaries of the compensatory state pension scheme for victims under the base scenario

In a similar vein, the costs of state pensions for victims will decline.

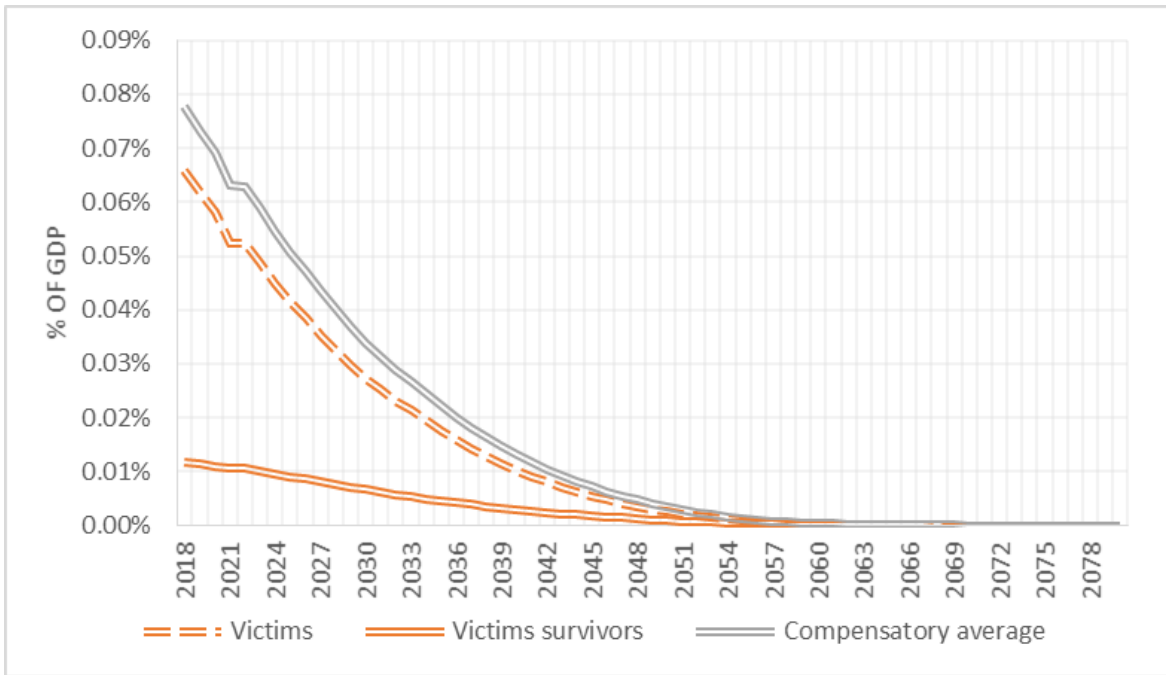


Figure 35. Evolution of expenditures of the compensatory pension scheme for victims under the base scenario (per cent of GDP)

4. Reform options

No reforms are suggested as to the personal and material scope of this scheme. Regular indexation of pensions in payment would be relevant to maintain their purchasing power.

Summary

The report analyses the schemes of state pensions in Lithuania from the perspective of their likely evolution in terms of the number of beneficiaries and expenditures, identifies key policy issues to be addressed by Lithuanian policy-makers and sets the main alternatives for policy reforms.

More specifically, the report includes an analytical description and comparative analysis of the categories and types of state pensions in Lithuania, a legal analysis of the constitutional law on occupational state pensions, a policy analysis of significant inconsistencies and inequities pertinent to the state pensions, projections of the number of beneficiaries and expenditures, identification of main reform options and their likely impact. The analysis is structured along three broad branches of benefits – occupational, merit-based and compensatory.

While falling under the same general legal label of ‘state pensions’, the types of benefits vary according to their core function (occupational, compensatory, merit-based). Furthermore, even within the same branch of occupational state pensions, the more specific actual roles vary by occupational groups. State pensions for judges carry the role of partial wage replacement (being calculated based on rather generous accrual rates), whereas compensations for professional stage art workers fulfil the role of ‘bridging pensions’ for the period before becoming eligible to state social insurance pension. On the other hand, the compensatory benefits for victims of repressions are essentially pension supplements which are not being designed to be the sole source of income. Hence the legal term of ‘state pensions’ is a misnomer, a term that is in common usage, but hardly serves as an overarching concept for the highly varied set of benefits. Nearly the only common denominator for the group of benefits called ‘state pensions’ is the fact that they all are financed from the state budget.

In 2016, the total number of beneficiaries of state pensions in Lithuania was 105790 persons. The same year the number of recipients of social insurance pensions paid by SoDra (Social Insurance Agency) was about 10 times higher, 1061195. A majority of state pensions are paid to persons who are in pension age or incapable to work. Hence these beneficiaries effectively receive two pensions – a social insurance pension and a state pension. For several categories of beneficiaries (e.g. victims, merit-based pensions, state pensions for scientists), a state pension is effectively a supplement to social insurance pension. However, there are also groups of beneficiaries (judges, former sportsmen) where the ‘supplement’ is actually higher than the social insurance pension, so that the state pension becomes the main pension whereas the social insurance pension serves as a supplement. On the other hand, there are also situations where state pensions are paid to persons before attaining pension age, who are not yet eligible to social insurance

pension. This is the case of state pensions for officials and servicemen and state pensions for stage artists, who qualify for the state pension on the basis of years of service with no applicable age criteria. In these cases a state pension is a sole pension at least for some period until qualifying for social insurance pension, while the person may earn wage income from some other work.

Figure 36 presents a summary view on the evolution of the number of beneficiaries across three categories of state pensions over the recent years.

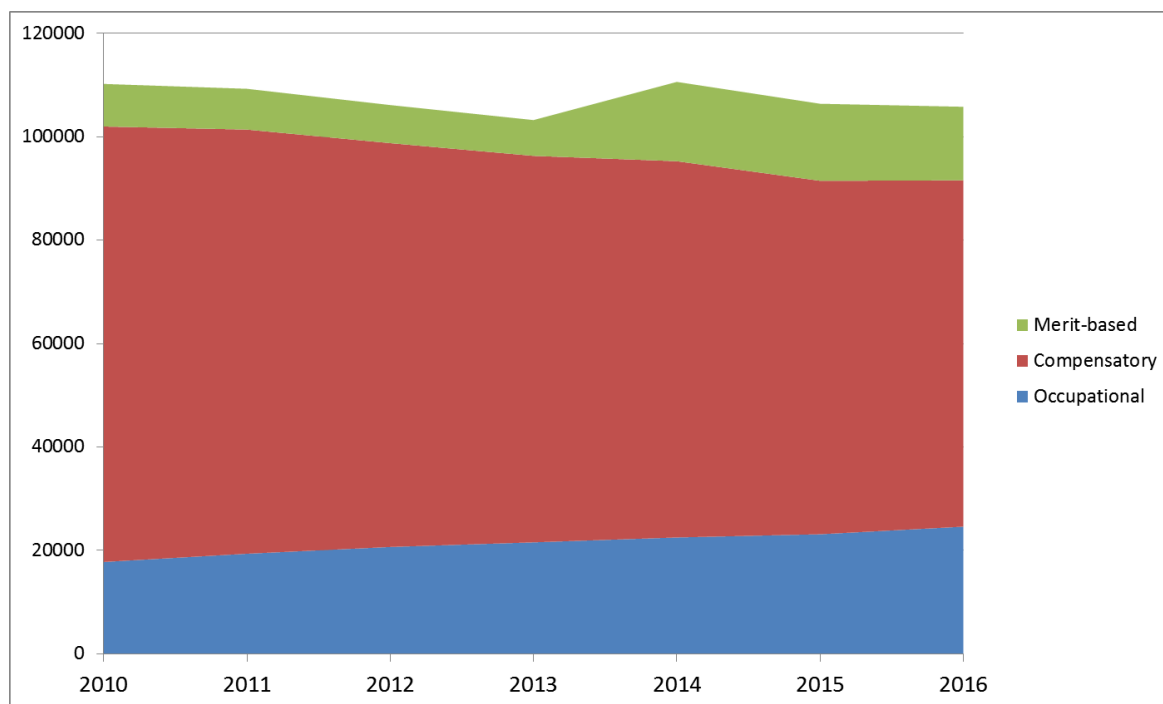


Figure 36. The number of beneficiaries of state pensions 2010–2016

Recipients of compensatory benefits (victims of repressions and their survivors) constitute the largest share, about 63% of the total number of recipients of state pensions, followed by the recipients of occupational pensions – 23% – and recipients of merit-based pensions – 14%.

The overall number of beneficiaries has had a declining trend. However, the dynamics in the evolution of the number of beneficiaries in different sub-schemes of state pensions are diverging. The number of recipients of compensatory benefits is declining due to mortality of beneficiaries in old age. The number of beneficiaries of merit-based pensions increased in 2014 as the personal scope of second degree state pensions was extended to mothers of 5 or more children (earlier mothers of 7 or more children were eligible), but after this one-off large increase the number of beneficiaries of merit-based pensions is again decreasing, related to the fact that the prevalence of large families in younger age cohorts is lower. At the same time, the number of recipients of occupational pensions is increasing.

The total expenditure on state pensions in 2016 amounted to 135 mln EUR. Compared to the total expenditure on social insurance pensions in the same year (2422 mln EUR), this was about 5,5%.

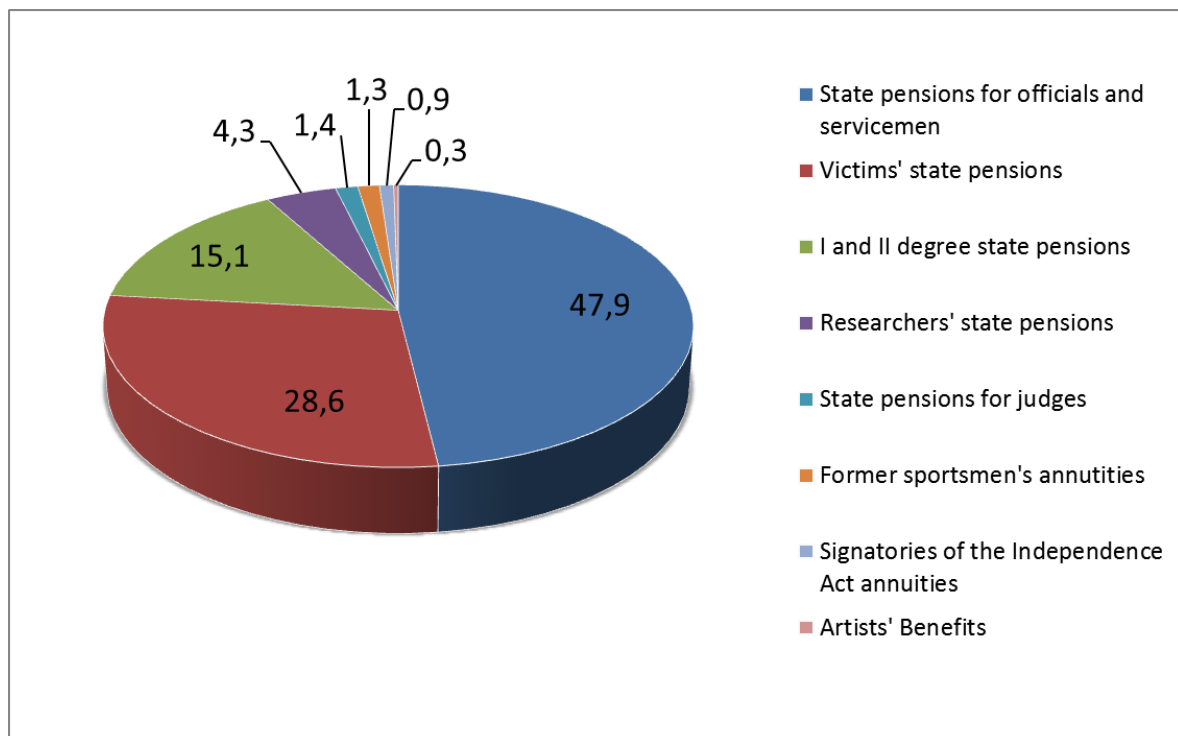


Figure 37. The share of expenditures on different types of state pensions (as % of the total) in 2016

Whereas the number of recipients is the highest on compensatory benefits for victims, the largest share of expenditures – nearly half of the total spending on state pensions – goes to finance state pensions for officials and servicemen. This artefact results from a combination of the number of beneficiaries and the payable rates of benefits.

For the time being the compensatory benefits for victims and their survivors concern the highest number of recipients of state pensions (about 65 thousand persons), while the expenditures constitute about 29% of all expenses on state pensions. On the other hand the amounts of these benefits are among the smallest compared to other types of state pensions. The age structure of beneficiaries (with about 85% of beneficiaries over the age of 70) implies a steady decline in the number of recipients and expenditures due to mortality.

In the branch of merit-based state pensions, the benefits for parents of 5 or more children constitute the largest subset. However, their number is declining due to mortality and lower prevalence of large families in younger age cohorts.

Occupational state pensions account for the highest share in terms of expenditures – about 54% of the total expenditures on state pensions. From the four occupational

groups covered by state pensions, the officials and servicemen are the largest subgroup and the number of beneficiaries of this sub-scheme is projected to grow substantially due to low effective retirement age leading to prolonged periods of benefit payment.

Figure 38 presents a summary view of projections on the number of beneficiaries and expenditures in discounted values (millions EUR) over a mid-term time horizon until 2040 under the base scenario.

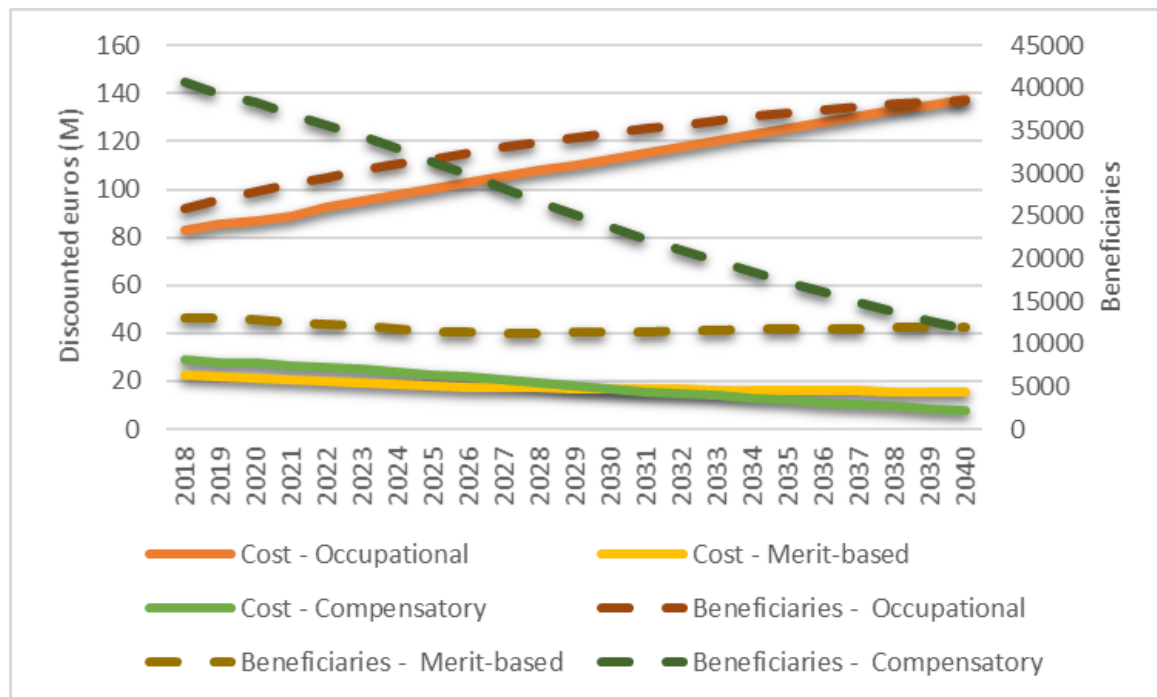


Figure 38. Projections of the number of beneficiaries and expenditures (millions EUR in discounted values) by three categories of state pensions

The main driver behind the overall increase is the increase in expenditures of the scheme for officials and servicemen. Increasing costs of the scheme for officials and servicemen are partly offset by declining expenditures of compensatory and merit-based pensions.

Figure 39 presents a summary view of the long-term projected evolution of total expenditures on state pensions by the three categories of benefits as a per cent of GDP comparing the base scenario with the policy alternative of indexation of all pensions with CPI.

We observe that under the base scenario the total expenditures on state pensions account for 0.3% of GDP. Expenditures on occupational state pensions are projected to increase whereas expenditures on merit-based pensions and compensatory benefits for victims will decline. However, if the benefits in payment were to be indexed with the CPI, the expenditure level would increase by nearly 1.5 times over the next 40 years.

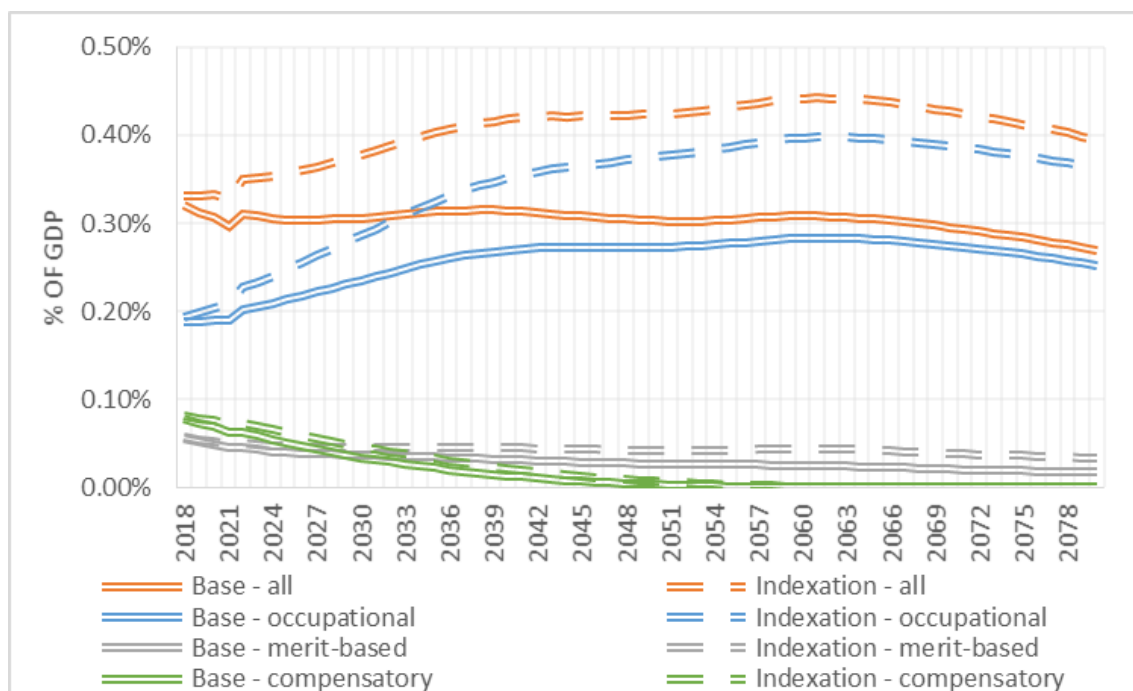


Figure 39. Projected expenditures (per cent of GDP) of the scheme for officials and servicemen if pensions are indexed with CPI compared to the base scenario

Reform strategies are to be tailored with consideration to existing differences between the three branches of state pensions.

As regards the compensatory-type benefits for victims and their survivors, no systematic reforms are suggested as the scheme will gradually diminish over time.

As regards merit-based pensions, the recognition of merits is at the discretion of the legislator. Nonetheless, some parametric reforms could be undertaken to harmonise the calculation bases and revalorisation rules of different types of merit-based pensions while maintaining justified differences in benefit amounts.

The occupational pension schemes call for the most significant reforms. The Lithuanian authorities may want to consider a combination of parametric reforms to be undertaken in a shorter term (e.g. introduction of an additional age criteria in schemes where it is currently missing to curtail unreasonably early retirement and elimination of groundless differences in treatment) with a more radical approach towards future special pension rights in a longer term.

Review of Constitutional Court rulings on state pensions

There have been 3 substantial rulings of the Constitutional Court directly addressing cases related to state pensions:

- 1) Ruling from 4 July 2003 on the state pensions of officials and servicemen (Case No. 46/2001-48/2001-50/2001-2/2002-6/2002-18/2002)
- 2) Ruling from 22 October 2007 on the state pensions of judges (Case No. 38/04-39/04)
- 3) Ruling from 29 June 2010 on the state pensions of judges (Case No. 06/2008-18/2008-24/2010)

Ruling from 4 July 2003 on the state pensions of officials and servicemen

On the specific matters of the merged cases examined by the Court, it ruled that:

- the legislative amendment of the Law on State Pensions of Officials and Servicemen adopted by the legislature in 2000 whereby the retired officials and servicemen who received so-called insured income (income subject to social insurance pension contributions) or social insurance sickness, maternity or unemployment benefits, could be paid only 30% part of their granted state pension of officials or servicemen, was in conflict with Article 23, Article 52 and Paragraph 1 of Article 48 of the Constitution; and
- the former provision whereby the granted state pension of officials and servicemen was no longer paid to persons convicted for intentional crimes was in conflict with Article 23, Paragraph 5 of Article 31 and Article 52 of the Constitution.

As to the first matter, the Court based its ruling on the argument that persons who satisfy the prescribed eligibility conditions for state pensions, acquire a right which is of a property nature: *“the fact that the law establishes the state pension of officials and servicemen means that the state undertakes an obligation to pay monetary payments of the established amount to persons for their service to the State of Lithuania, if these persons meet the requirements established by law (retirement from service, service record, age, etc.). Thus, a person, who meets these conditions, is entitled to demand that the state fulfil this obligation of property nature.”* On this basis, the Court held that *“when the person has fulfilled all conditions established by the law and when this pension has been granted and paid”,* the legal regulation whereby the pension is no longer paid or is reduced (partly suspended), violates the acquired property right of the person to the state pension which is to be guaranteed by the state, leading to simultaneous violation of

Articles 23 and 52 of the Constitution. The Court further noted that the legal regulation whereby the person who has been granted and paid the state pension of officials and servicemen must choose either to receive the full granted state pension, or to have some work income (so-called insured income) and to receive a part of the state pension, restricts the freedom to freely choose a job or business, thus violating Paragraph 1 of Article 48 of the Constitution.

As to the second issue, the Court noted that the provision of the Law on State Pensions of Officials and Servicemen whereby the granted state pension of officials and servicemen was terminated for persons convicted for an intentional crime was essentially *“a sanction of property nature, which, by its strictness, amounts to criminal punishment.”* Referring to the constitutional provision (Paragraph 5 of Article 31) whereby *“No one may be punished a second time for the same crime”*, the Court held that termination of payment of the state pension of officials and servicemen for a person convicted by court for an intentional crime amounts to criminal punishment of a second time for the same crime, and hence violates Paragraph 5 of Article 31.

However, beyond these specific rulings the Constitutional Court when setting its line of reasoning, essentially developed a framework of constitutional doctrine on state pensions, which has been further elaborated in the subsequent rulings.

Among others, the Court noted that *“under the Constitution, other pensions or social assistance than those specified in Article 52 of the Constitution may be established by law (the Constitutional Court’s rulings of 23 April 2002 and 25 November 2002). Pensions for certain service to the State of Lithuania may also be established by law. While establishing such a pension for service, the legislature is bound by the rules and principles of the Constitution, as well as the striving for an open, just and harmonious civil society and a state under the rule of law.”*

In other words, the Constitutional Court held that the state may introduce pensions other than those explicitly listed in the text of the Constitution (old-age and disability), including pensions for service to the state. The Court considered such pensions legitimate and constitutional.

The Court further noted that it derives from the Constitution that *“the grounds for pensionary maintenance, the persons who are granted and paid pensions, the conditions for the granting and payment of pensions, as well as the amounts of the pensions are established by law only.”*

However, the Court also indicated some restrictions the legislature is bound when establishing and regulating such pensions. Specifically, the Court noted that *“the legislature, while establishing which persons are granted and paid pensions for service, the grounds and conditions for the granting and payment of these pensions, as well as the amounts of this pension, is bound by the constitutional imperative of social harmony, the*

principles of justice, reasonableness and proportionality. If the legislature, while establishing the pension for service of officials and servicemen, did not take account of the specific character of the service of officials and servicemen, the nature of concrete duties and other important circumstances, the granting and payment of such a pension would become a privilege.”

In other words, the Court seemed to indicate that while establishing and regulating special pensions for service for specific groups, the legislature needs to address the specific circumstances of the covered profession striking a balance with consideration to the principles of justice, reasonableness and proportionality. Notable is the comment from the Court that without due regard to the specific circumstances of the covered service, such a pension would become a privilege. The Court went on to note that the principles of justice, reasonableness and proportionality could be violated if *“the person would be able to retire unreasonably early, or an unreasonably short time period of service or work required in order to receive such pension would be established, or the amount of the remuneration of the official or serviceman would not be taken into consideration while establishing the amount of the granted pension /.../”*

The Court also commented that the state pension of officials and servicemen differ in their nature and character from state social insurance pensions, including from the old age pensions.

At the same time, according to the Court, the phrase *“the State shall guarantee”* in the wording of Article 52 of the Constitution implies that *“the state is obligated to guarantee it [the pension] to the indicated persons on the grounds and by the amounts established by the law, while the persons who meet the conditions provided by the law, have the right to demand that the state grant and pay this pension to them.”*

The Court further discussed the options for possible later reforms of such pensions by noting that *“the constitutional protection of acquired rights and legitimate expectations does not mean that the system of pensionary maintenance established by law may not be reorganised. While reorganising this system, the Constitution must be observed in every case. The system of pensions may be reorganised only by law, only guaranteeing the old age and disability pensions provided for by the Constitution, as well as observing undertaken obligations by the state, which are not in conflict with Constitution, to pay corresponding payments to persons who meet the requirements established by the law. If, while reorganising the pensionary system, the pensions established by means of the laws which are not directly specified in Article 52 of the Constitution were eliminated, or the legal regulation of these pensions were amended in essence, the legislature would be obligated to establish a just mechanism for compensation of the existing losses to the persons who had been granted and paid such pensions.”*

Here, on one hand, the Court refers to the constitutional principles of protection of acquired rights and legitimate expectations. On the other hand, the Court accepts that the state pensions for service at least in principle may be eliminated, and state may guarantee only old-age and disability pension explicitly mentioned in the text of the Constitution. At the same time, the Court restricts the possibilities of elimination of such state pensions for service with a condition that the legislature establishes a *just compensation mechanism* to persons concerned for *'existing losses'*. However, it is not self-evident what would constitute a just mechanism to compensate for existing losses to persons who had been granted and paid such pensions.

Furthermore, the Court noted that under Article 23 of the Constitution (which protects the right to property) *"the persons who have been granted and paid the state pensions of officials and servicemen have the right to demand that the payments be paid further in the amounts which were granted and paid earlier."* In this regard, the Court indicates that any reductions would be possible only in extraordinary situations and even then only temporarily *"pensions granted and paid under the Constitution may be reduced only in the event of an extraordinary situation in the state when there is objective insufficiency of funds that are necessary to pay the pensions. In this case the granted and paid pensions may be reduced to the extent necessary to ensure vitally important interests of society, and to protect other constitutional values. It is also noteworthy that the reduced pensions may only be paid temporarily."* Notwithstanding those temporary and extraordinary reductions, the Court expressed that *"persons who have acquired certain rights according to the law, have the right to reasonably expect that these rights will be maintained and implemented for the established time period"*, and that under the principle of legitimate expectations *"the rights and legitimate expectations acquired by the person may not be denied by changes in legal regulation."*

Also, when analysing the compliance with Article 23 of the Constitution, the Court held: *"while implementing the reform of the pensionary system, some pensions may be abolished, the amounts of others may be reduced. In this case the legislature must establish a just mechanism of compensations for persons that have suffered some losses because of this amendment of the regulation. Otherwise, the legal regulation, according to which the payment of the granted and paid state pension of officials and servicemen is no longer paid or reduced, should be judged to be in violation of Paragraph 2 of Article 23 of the Constitution which provides that the rights of ownership shall be protected by law."*

The Court went on to argue that *"if one established the legal regulation according to which the payment of the granted and paid state pension of officials and servicemen is no longer paid or reduced, one would violate the provision of Article 52 of the Constitution that the state shall guarantee the pensions in cases provided by the law."*

Finally, as regards the possible reorganisation of the pension system the Court noted *"the legislature, while reorganising the system of pensions /.../ must provide for a sufficient*

transitional time period during which the persons who have a corresponding job or perform corresponding service which entitles them to a respective pension under the previous regulation, would be able to prepare for these changes.”

Ruling from 22 October 2007 on the state pensions of judges

On the merits of the cases analysed, the Court held that the provisions of the Law on the State Pensions of Judges whereby the state pension of judges was not granted and the granted pension not paid, if the person had insured income (upon which state social insurance pension contributions were paid) or were receiving social insurance benefits for sickness, maternity or unemployment, was in conflict with Articles 52 and 109, and Paragraph 1 of Article 48 of the Constitution.

In the argumentation of the case, the Court reiterated some of the arguments of ruling from 4 July 2003 on the state pensions of officials and servicemen, while elaborating the line of reasoning further. Among others the Court noted *“other pensions or social assistance than those expressis verbis specified in Article 52 of the Constitution may be established by law. The grounds for pensionary maintenance, the persons who are granted and paid pensions, the conditions for granting and payment of pensions, as well as the sizes of the pensions are established only by law (in the case of the old age pension, the law must establish the age upon reaching which a person has the right to receive the old age pension, the grounds for granting and payment of this pension, its conditions and sizes, while in the case of the disability pension—what should be regarded as disability, as well as the grounds for granting and payment of this pension, its conditions and sizes); it is not permissible to establish the conditions of appearance of the right of the person to the pension by means of a substatutory act, as well as to limit or expand (in comparison with that established by law) the extent of this right.”* Notably, the Court further clarifies here that pension rights may not be regulated by substatutory acts, nor limit or expand such rights compared to what is established by law.

As regards the regulation of special pensions for service to the state, the Court noted: *“the peculiarities of the constitutional institute of the state service determine, inter alia, the fact that the legislature has the constitutional powers by means of a law to establish the pensions and/or the kinds of social assistance which are granted only to the state servants or separate groups of state servants /.../”.*

Here, similarly to the case of state pensions for officials and servicemen, the Court effectively acknowledges that state pensions for judges are legitimate and constitutional. At the same time, the Court also emphasised the necessary means of legal protection of the legislated rights to pension: *“The provisions of Article 52 of the Constitution, which guarantee the right of the citizens to pensionary maintenance and social assistance, oblige the state to establish sufficient means for the implementation and legal protection of this right, thus, the law has not only to establish the types of pensions and social*

assistance which are specified in this article of the Constitution, but also to guarantee the appropriate implementation and legal protection of the right of a human being to receive a pension or social assistance.”

The Court goes on to justify the setting up of state pensions, while distinguishing the categories of those pensions in the following way: *“In some cases, state pensions (which, as it has been mentioned, are not directly named in the Constitution) are granted for a certain service, in other cases—for merits to the State of Lithuania or as compensation to victims. While establishing the persons who are granted and paid the state pension, the basis and conditions for granting and payment of the state pension, as well as the sizes of this pension, one must heed the constitutional imperative of social harmony and the principles of justice, reasonableness and proportionality; granting and payment of the state pension does not have to become a privilege.”* Against this background the Court essentially warns the legislature not to disregard the constitutional principles, which could be the case if the legislature: *“granted the state pensions to the persons who may not be granted such pensions, established groundlessly big or small sizes of such pensions or established groundless conditions of granting or payment of such pensions.”* Moreover, the Court also warns that an arbitrary regulation of state pensions may turn these into an unjust and unreasonable privilege. It is not clear though where the boundary between reasonable and unreasonable lies to distinguish a fair compensation from a privilege.

The Court further draws a line of separation between state pensions and social insurance pensions by stating that: *“state pensions differ in their nature and character from state social insurance pensions and are paid from the state budget”*. Based on this, the Court indicates that the legislature *“may establish by law the maximum size of such pensions /.../ may establish certain cases when the state pension is not granted to the person (under the conditions provided for in the law) /.../ also establish by law the cases when the granted state pension is no longer paid.”* In other words, the Constitutional Court accepts, at least in principle, the setting of maximum amounts of state pensions and allows non-granting and suspension of payment of state pensions in some legally defined and justified circumstances.

Ruling from 29 June 2010 on the state pensions of judges

On the merits of the examined cases, the Court ruled that:

- 1) the provisions of the Law on state pensions for judges (Article 6§§1-3), which stipulated the calculation rules of state pension for judges, and the limit on the amount of the state pension of judges paid in conjunction with state social insurance pensions and other state pensions (the total not to exceed 1.5 times the economy-wide national average wage) were violating Paragraph 2 of Article 109 of the Constitution;

- 2) the provision of the Law on state pensions (Article 3§3) whereby the total sum of the state pension and state social insurance pensions granted to the same person could not exceed 1.3 times the average monthly remuneration for work in the economy, was violating Paragraph 2 of Article 109 of the Constitution.

The Court justified these rulings by arguing that when legislating rules of calculation of judges pension the legislature had not taken into account the *“peculiarities of separate court systems”*. Notably by finding a violating of Paragraph 2 of Article 109 of the Constitution (which reads: *“While administering justice, the judge and courts shall be independent”*), the Court’s interpretation implies that restrictions on the total sum of state pensions and social insurance pensions for judges interfered with the principle of independence of judges.

As regards the formerly legislated calculation method of state pensions for judges, whereby the replacement rate (percent of reference wage) increased with the length of service in increments (and not continuously), the Court noted that these provisions: *“created preconditions to make totally equal sizes of the state pensions of the judges who have gained the work record as a judge of a considerably different duration and which, on the other hand, creates preconditions to grant the state pension of judges of a considerably different size to the judges the duration of whose work record as a judge differs insignificantly, is not in line with the constitutional concept of the state pension of judges as a social (material) guarantee of judges upon expiry of their powers”* thus violating the provisions of Paragraph 2 of Article 109 of the Constitution and the requirements of justice, proportionality, and reasonableness.

As regards the possible temporary and extraordinary reduction of state pensions in a situation of extreme economic and financial difficulties of the state, the Court noted that due to the different nature and character of state pensions as compared to state social insurance pensions: *“the legislator may reduce these [state] pensions to a greater extent than old age and disability pensions”*. The Court added that: *“the losses incurred due to the reduction of state pensions may be compensated to a smaller extent than the losses incurred due to the reduction of old age or disability pensions (Constitutional Court decision of 20 April 2010).”*

In summary, the argumentation delivered by the Constitutional Court effectively establishes a constitutional law framework on conditions governing the regulation of state pensions, as well as restrictions on possible later reforms of such pensions once established. The key points may be summarised as follows:

- The state pensions for service to the state are legitimate and constitutional;

- The personal scope, the conditions of granting and payment of such pensions shall be regulated by laws, and not by lower level acts;
- The regulation of state pensions for service shall take into account the specific circumstances of service, while the eligibility rules may not be too relaxed and the size of pensions shall not be unproportional for the pension not to become a 'privilege';
- Once state pensions are legislated they fall under the constitutional obligation of the state to guarantee their payment to the qualifying persons;
- The state may establish maximum amounts of state pensions;
- Following the principle of proportionality the state pension for service of considerably different durations shall not be equal;
- The system of state pensions may be reorganised and some types of pensions may be abolished, at least in principle, however in such cases the legal regulation shall establish 'a just mechanism for compensation of losses' to persons in receipt of such pensions, and there shall be a sufficiently long transition period to address the legitimate expectations of persons who have acquired service periods in covered occupations.

The argumentation developed by the Constitutional Court appears to make state pensions, which have already been granted and are in payment virtually irreversible, as following the line of reasoning of the Court the just mechanism for compensation of losses is hardly anything significantly less than the previously granted amount under a possibly different name and legal act. The available reform options then may concern persons who have not yet retired from the occupations where pension rights for service are acquired, but any reform shall provide for a sufficiently long transition period and shall not interfere with their legitimate expectations.

Analysis of international law on social rights as regards supplementary pensions

Beyond domestic legislation and case-law of the Constitutional Court, the legal framework conditioning the provision of and possible reform options for state pensions includes also relevant provisions of international law.

Lithuania has ratified Article 12§§1 and 3 of the Revised European Social Charter, thereby undertaking, *with a view to ensuring the effective exercise of the right to social security:*

1. *to establish or maintain a system of social security; and*
3. *to endeavour to raise progressively the system of social security to a higher level.*

The European Committee of Social Rights (which is the committee of experts monitoring the implementation of the European Social Charter) has on several cases assessed, whether abolition or reduction of some supplementary social security rights is compatible with the obligations of the state arising from Article 12§3 of the Charter.

In the Statement of Interpretation on Article 12 (p. 48), Conclusions XIV-1, the ECSR held that any modifications of the social security system "*should not undermine the effective social protection of all members of society against social and economic risks and should not transform the social security system into a basic social assistance system*".

In the Decision on the merits of Collective Complaint No. 43/2007 Sindicato dos Magistrados do Ministério Público (SMMP) v. Portugal, the European Committee of Social Rights (ECSR) considered a situation where a special scheme for members of the Public Prosecutor's Office was abolished, and persons protected were transferred to a general scheme applicable to all state officials.

The ECSR held: "*States enjoy a wide margin of discretion on how to organize their social security systems, including defining the personal scope of schemes providing health care benefits, as long as a significant percentage of population is covered and the benefits provided are sufficiently extensive. Setting up of any special schemes for selected professional groups to provide complementary coverage and benefits beyond those provided in the general schemes, remains at the discretion of the States. Justification of such schemes depends on a series of factors and criteria at national level, which do not fall within the Committee's competence as long as they are not manifestly ill founded.*"

Based on this, the ECSR considered that the reform undertaken by Portuguese authorities did not contradict the obligations arising from Article 12§3 of the Revised European Social Charter.

Notably, the ECSR referred to the margin of discretion of the States as regards establishing any special schemes for selected professional groups to provide complementary coverage and benefits which go beyond those provided in general schemes.

On the other hand, in the Decision on the merits of Collective Complaint No. 76/2012 Federation of employed pensioners of Greece (IKA-ETAM) v. Greece, the ECSR held that: *"any decisions made in respect of pension entitlements must respect the need to reconcile the general interest with individual rights, including any legitimate expectations that individuals may have in respect of the stability of the rules applicable to social security benefits"*

The ECSR also noted that *"the restrictive measures at stake, which appear to have the effect of depriving one segment of the population of a very substantial portion of their means of subsistence, have been introduced in a manner that does not respect the legitimate expectation of pensioners that adjustments to their social security entitlements will be implemented in a manner that takes due account of their vulnerability, settled financial expectations and ultimately their right to enjoy effect access to social protection and social security."*

To summarize, in compliance with the obligations arising from ratification of Article 12 of the Revised European Social Charter, the States are free to organise and reorganise their social security systems, including establishing or abolishing any special supplementary schemes for selected groups, insofar as the remaining protection is sufficiently extensive. However, while reforming the system the States must respect legitimate expectations of beneficiaries and shall take into account of vulnerability of specific groups of beneficiaries.

Lithuanian State Pension Model LitPen structure and assumptions

The LitPen (Lithuanian state pension) model developed as a part of this project is an Excel-based model and is aggregated by age and gender. Pensions are simulated until 2080. This model covers Lithuanian state pensions:

- 1) Occupational schemes:
 - a. Officials and servicemen
 - b. Judges
 - c. Scientists
 - d. Stage artists
- 2) Merit-based schemes:
 - a. I degree
 - b. II degree
 - c. Sportsmen
 - d. Signatories'
- 3) Compensatory scheme:
 - a. Victims and their survivors.

Data

The model is using the following datasets (Lithuanian data unless otherwise stated):

- Beneficiaries at 31.12.2017 by sub-schemes:
 - Average pension by age and gender;
 - Number of beneficiaries by age and gender.
- Current employees working in occupations covered by state pension rights:
 - Number of employees by age and gender;
 - Average length of service by age and gender (if necessary);
 - Average wage by age and gender (if necessary).
- Population data:
 - Population projection by Eurostat from 2018 to 2080 (data update 17.01.2018);
 - Fertility projection by Eurostat from 2015 to 2080 (data update 17.01.2018);
 - Mortality projection by Eurostat from 2017 to 2080 (data update 17.01.2018);

- Life expectancy projection by Eurostat from 2015 to 2080 (data update 17.01.2018);
- Estonian data about deaths by education (Eurostat; data update 25.04.2018)
- Estonian data about population by education (Eurostat; data update 27.02.2018).
- Macroeconomic forecast until 2070 by Ageing Working Group

Structure of the model

Data on current retirees and employees, as well as the population projection and macroeconomic forecast are taken as input data. These input data are used to simulate the yearly number of beneficiaries and average pension by sub-scheme, gender and age. Expenditures of the state pension system by sub-scheme are calculated by multiplying the number of beneficiaries and the average pension for each sub-scheme.

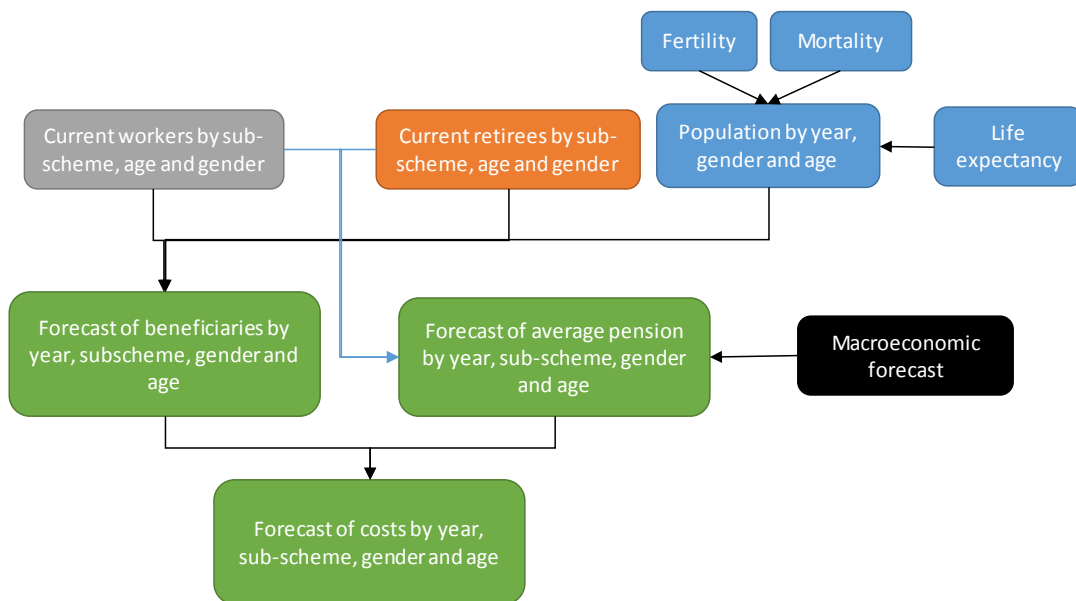


Figure 40. Structure of the LitPen model

Assumptions

General statutory pension age is used, if needed. As the model works year by year, the yearly pension age is used (see Figure 41).

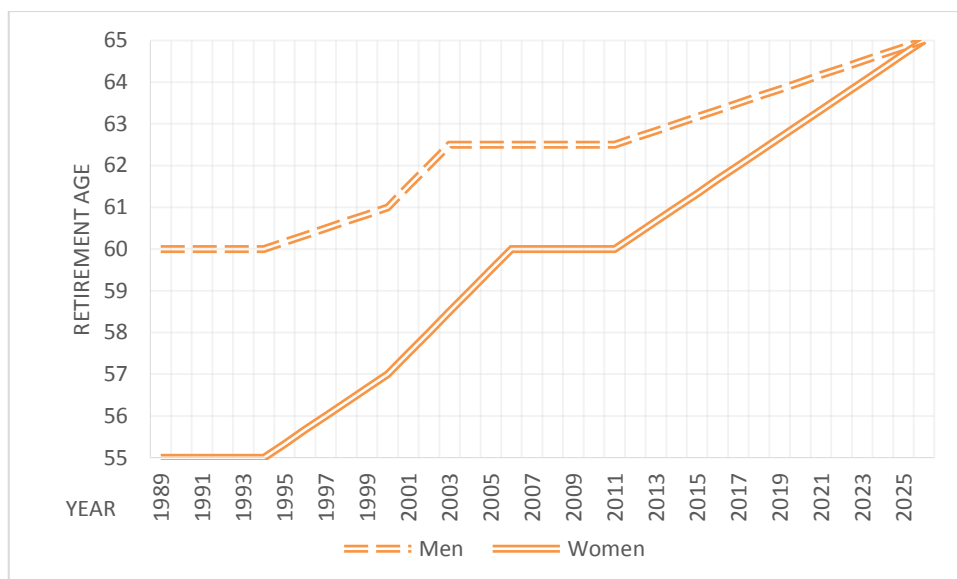


Figure 41. Statutory general pension age by gender and calendar year

The simulation approaches which are the same for all schemes:

- Women and men are simulated separately;
- No ceiling is used as in ordinary cases pensions do not reach the ceiling level.

The following scheme-specific assumptions are applied as schemes are too different to use the same assumptions for all.

Occupational schemes: Officials and servicemen

Simulation is made by the following sub-schemes:

- 1) Defence forces (military);
- 2) Special investigation service;
- 3) Prison department;
- 4) Interior affairs;
- 5) Customs;
- 6) Prosecutor’s office.

Average mortality rate is used in this scheme. Number of people, average length of service and average wage is simulated for every sub-scheme.

First, **the number of persons:**

- Actual data about current employees by gender and age is used as starting point at 2017;
- For the following years the average number of people from starting age (20 to 36 depending of the sub-scheme) is calculated and this is set to be the number of

entrants in the sub-scheme in the following years for the youngest age group. The number of entrants is corrected with age group size in simulation year and base year. For example, average number of female employees in military sub-scheme is 34 between age 20 to 44. However, the number of new entrants to the military sub-scheme in 2018 is not 34, but calculated as:

$$Entrants_{a,ss,y} = Entrants_{a,ss,y-1} \times \left(\frac{Pop_{a,y-1}}{Pop_{a,y}} \right)$$

where,

$Entrants_{a,ss,y}$ – the number of entrants at age a in sub-scheme ss in year y ;

$Pop_{a,y}$ – the number of people at age a in year y .

- Year, gender and age specific mortality rates are used to calculate the number of employees for the following age groups (see Table 13).

Age	2017	2018	2019
19	34 (calculated)	= 34 * (15825/14874)	= 32 * (14874/14349)
20	51	= 34 * (Mortality _{f,19,2017})	= 32 * (Mortality _{f,19,2018})
21	18	= 51 * (Mortality _{f,20,2017})	= 34 * (Mortality _{f,20,2018})
...

Table 13. An example of finding the number of female persons in military sub-scheme

- Between age of 40 to 50 (maximum number of current employees) the current employees start to retire with selected rate (changeable) – in base scenario this percentage is 14 (empirically calculated from current data). This means, 2/3 of employees will retire within 7 years ($1 - 0.86^7 = 65\%$) and 90% within 15 years. However, all must retire at age 65.
- Retirees of all sub-schemes are merged in one table and mortality rates until the age 100 are used. Mortality will be 1 at age 100, which is manually selected.

Second, **length of service**:

- The actual length of service by gender and age (2017 data) is used as the base;
- Each age group will earn one service year until first employees retire in the sub-scheme;
- Afterwards each age group will earn 0.9 (this is changeable) service years due to the fact that employees with more service years will retire in the first place. Therefore, once employees with more service years retire the average service years decrease, but those who continue to work on still earn one service year.

- Two ways to set maximum service years may be used in the model:
 - Minimum service years (20 or 25 years) + 2.5 years (empirically calculated) – right now this is used in the model;
 - Data provided by employers, for example 35+ years for those who just started to work, but this may be too optimistic.
- Minimum length of service requirement is raised by the law from 20 to 25 years. Therefore, the minimum length of service set by the law is used.

Third, **average wage**:

- The actual average wage by gender and age (2017 data) is used as the base;
- For future years the same wage proportions are used as in the base year and wages are multiplied with the growth of national average wage;

Reforms

Six reform scenarios are included in the model:

- 1) Defined-contribution (DC) scheme for new entrants to the scheme;
- 2) DC scheme for all from 2020, while employees who have already earned defined-benefit (DB) scheme rights receive those at retirement but do not earn new rights furthermore;
- 3) Closing DB scheme so that new entrants do not earn service years in DB scheme, but current employees earn until they work;
- 4) Closing DB scheme so that no new entrants and no current employees earn any more service years, but current employees receive DB pension if they retire at already earned service years level;
- 5) Minimum age of retirement is linked to general statutory age, e.g. five years before general pension age. The early retirement age (the number of years before to general pension age) is changeable in the model.
- 6) Maintaining pensions adequacy – pensions indexation with different indexes:
 - a. Consumer price index (CPI);
 - b. Growth of national average wage;
 - c. Selected index 1;
 - d. Selected index 2;
 - e. Selected index 3.

DC scheme assumptions

DC scheme uses three assumptions which all are changeable:

- 1) Contribution rate – set as 17%;
- 2) DC scheme yield during accumulation period – nominally 4%;
- 3) DC scheme annuity interest rate – nominally 1%.

To calculate the value of assets the current year contributions, previous year value of assets and yield is used.

$$Assets_{a,y} = Assets_{a-1,y-1} * (1 + yield) + C_{a,y} * (1 + \frac{yield}{2})$$

Where,

$Assets_{a,y}$ - Age group a assets in year y ;

$yield$ - DC scheme yield (4%);

$C_{a,y}$ - Age group a contributions in year y .

Excel function PMT is used to calculate annuity in DC scheme. Unisex life expectancy is used calculated from Eurostat population projection.

Occupational schemes: Judges

The same simulation method is used for judges as for officials and servicemen. However, lower mortality rates are applied as university education is required to be judge and highly educated persons have lower mortality. The average mortality is lowered by the difference of average and high educated people mortality rates by age. Estonian data is used due to fact that this information is not available for Lithuania in Eurostat database.

$$Mort_{a,g,y,judges} = Mort_{a,g,y,LIT} - (Mort_{a,g,EST} - Mort_{a,g,he,EST})$$

Where,

$Mort_{a,g,y,judges}$ - Age group a gender g mortality in year y for judges;

$Mort_{a,g,y,LIT}$ - Age group a gender g average mortality in year y in Lithuania;

$Mort_{a,g,EST}$ - Age group a gender g average mortality in Estonia;

$Mort_{a,g,he,EST}$ - Age group a gender g mortality rate for highly educated (he) in Estonia.

Occupational schemes: Scientists

Simulation is made by sub-schemes for:

- 1) Docents and professors;
- 2) Researchers.

The number of employees and retirees, and pension amounts are provided as input data. There is no wage information as scientists' pensions depend on the length of service.

Lower mortality rates for highly educated persons (as in the case of judges) are used. The steps to simulate future retirees and pension amounts:

- Length of service is calculated for current retirees who retired in the last 10 years. For women this is 24 years and for men 26 years;
- Scientists start to retire at general pension age and every year 50% (changeable) of eligible persons retire.

Occupational schemes: Stage artists

Simulation is made by sub-schemes for:

- 1) Ballet and circus artists – 18 years of minimum length of service;
- 2) Solo vocalists – 20 years of minimum length of service;
- 3) Wind instrument player – 25 years of minimum length of service;
- 4) Actors, choir artists, other musicians and conductors – 30 years of minimum length of service.

Maximum length of service is taken to be minimum length of service plus two years. Lower mortality rates for highly educated persons are used as being a stage artist in general requires a higher musical education. Before general pension age every year 50% of current artists retire if they have fulfilled the minimum length of service requirement. All will retire if the maximum length of service is fulfilled. Upon reaching the general statutory pension age 100% will retire.

Merit-based schemes: I degree

Simulation is made by sub-schemes for:

- 1) Armed resistance;
- 2) Winners of National Culture Prize and the highest state officials.

For armed resistance sub-scheme there are no new entrants who earn new rights. All will retire upon reaching the general pension age.

For winners of culture prize and the highest state officials the proportion in population is kept constant at age 56. All will retire upon reaching the general pension age.

The benefit is fixed – four times the state pension base.

Merit-based schemes: II degree

Simulation is made by sub-schemes for:

- 1) Mothers or fathers who have raised at least five children;
- 2) Donors.

The proportion of donors in population at age 53 is kept constant and will retire upon reaching the general pension age.

Rights for raising children are taken up by women in the first place. To account for women who die before reaching pension age, a proportion of rights is transferred to men in three years older age cohort. This means, if 10 women die at age 40 then 9 men at age 43 earn the right to receive II degree pension (not 10 as 89% of this cohort are still alive). Rights are transferred to three years older men because by marriage statistics men are on average three years older than women when they marry.

All will retire upon reaching the general pension age at the first opportunity. After general pension age the rights to second degree state pension for raising children are not transferred to fathers if the mother dies.

The benefit is fixed – two times the state pension base.

Reform scenario

One scenario is considered – extending the rights to parents with 4 children. For projections the number of children by age cohorts is needed. Eurostat fertility rates by age and year and the size of population by year and age is used for this purpose. For each age cohort the number of children is calculated. It is assumed that the current proportions of women who have 4+ and 5+ children are maintained – 5.4% with 4+ children and 2.2% with 5+ children. 2020 is taken as the reform start year.

Merit-based schemes: Former sportsmen

The proportion of sportsmen is kept constant (22 for women and 23 for men) and they will retire at age 35. The benefit is fixed – 1.5 times national average wage, changed annually.

Merit-based schemes: Signatories

There are no new beneficiaries. The benefit is fixed – 50% of the wage of the Member of the Parliament.

Compensatory schemes: Victims

There are no new entrants to victims' scheme. Actual data on pension amounts and the number of beneficiaries by gender and age (2017 data) is used as the base. Pensions are paid upon reaching the general statutory pension age. The benefit amount may vary from 0.8025 to 8.56 times of state pension base, but empirically the average multiplier is 1 for men and women and therefore all future beneficiaries receive one-time state pension base. Victims and victims' survivors are also simulated in this scheme. The proportion of victims' survivor pension to the state pension base is empirically calculated – this is 0.36 for women and 0.49 for men.

Only victims' spouses can receive victims' survivor's pension in the simulation. If a victim dies, then his or her rights are going to three years younger or older spouse (respectively for male and female victims) considering what share of this cohort is still alive.

Scheme	Before general pension (if possible)	Upon reaching general pension age
Officials and servicemen	14%	100%
Judges	-	50%
Scientists	-	50%
Stage artists	50%	100%
I degree	-	100%
II degree	-	100%
Sportsmen	100%	100%
Signatories	-	-
Victims	0%	100%

Table 14. The percentages of eligible employees with the minimum required length of service retiring before or upon reaching the general pension age by schemes