Finland

The two-tier pension system consists of a basic state pension, which is pension-income-tested, and a range of statutory earnings-related schemes, with very similar rules for different groups. The schemes for private-sector employees are partially pre-funded while the public-sector schemes are pay-as-you-go financed (with buffer funds to even out future increases in pension contributions).

Qualifying conditions

The national pension is subject to a residency test (but no contribution requirements), withdrawn against pension income from the earnings-related schemes. Both the national and the earnings-related pensions are payable from age 65. The full benefit is payable with 40 years residence as an adult, with *pro rata* adjustments for shorter periods of residence.

Benefit calculation

Earnings-related

From 2005, the accrual rate will be 1.5% of pensionable pay at ages 18-52, 1.9% at ages 53-62 and 4.5% at ages 63-67. Currently, the accrual rates are 1.5% at younger ages and 2.5% between ages 60 and 64. The modelling includes the effect of this reform. For a full-career worker working from age 20 until retirement at age 65, the total lifetime accrual will be 77.5% of pensionable earnings. Currently, there is a maximum replacement rate of 60% of pensionable earnings but this is abolished from 2005.

Currently, earnings are averaged over the last ten years of employment in a particular scheme. Years with exceptionally low earnings can be ignored (to a maximum of one third of total years of coverage). From 2005 onwards, pensionable pay will be based on average earnings of the whole career. Earlier years' earnings are re-valued in line with a mix of economy-wide earnings and prices. Currently, wage and price inflation are equally weighted but from 2005 onwards, wage growth will have an 80% weight and price inflation, 20%. At the baseline assumptions for prices and wages growth, this policy reduces the value of the pension to 91.5% compared with a policy of full earnings valorisation of earlier years' pay.

There is no contribution floor and no ceiling to contributions or pensionable earnings. Pensionable pay is defined as gross earnings less employees' pension contributions (which are described below). Note, however, that the replacement rates are shown relative to total gross earnings (for comparison with other countries) rather than this measure of pensionable pay.

After retirement, the earnings-related pension is uprated using a formula of 20% of earnings inflation and 80% of price inflation. Under current rules, pensions drawn early (before the age of 65) have a more generous indexation procedure: 50% of earnings inflation

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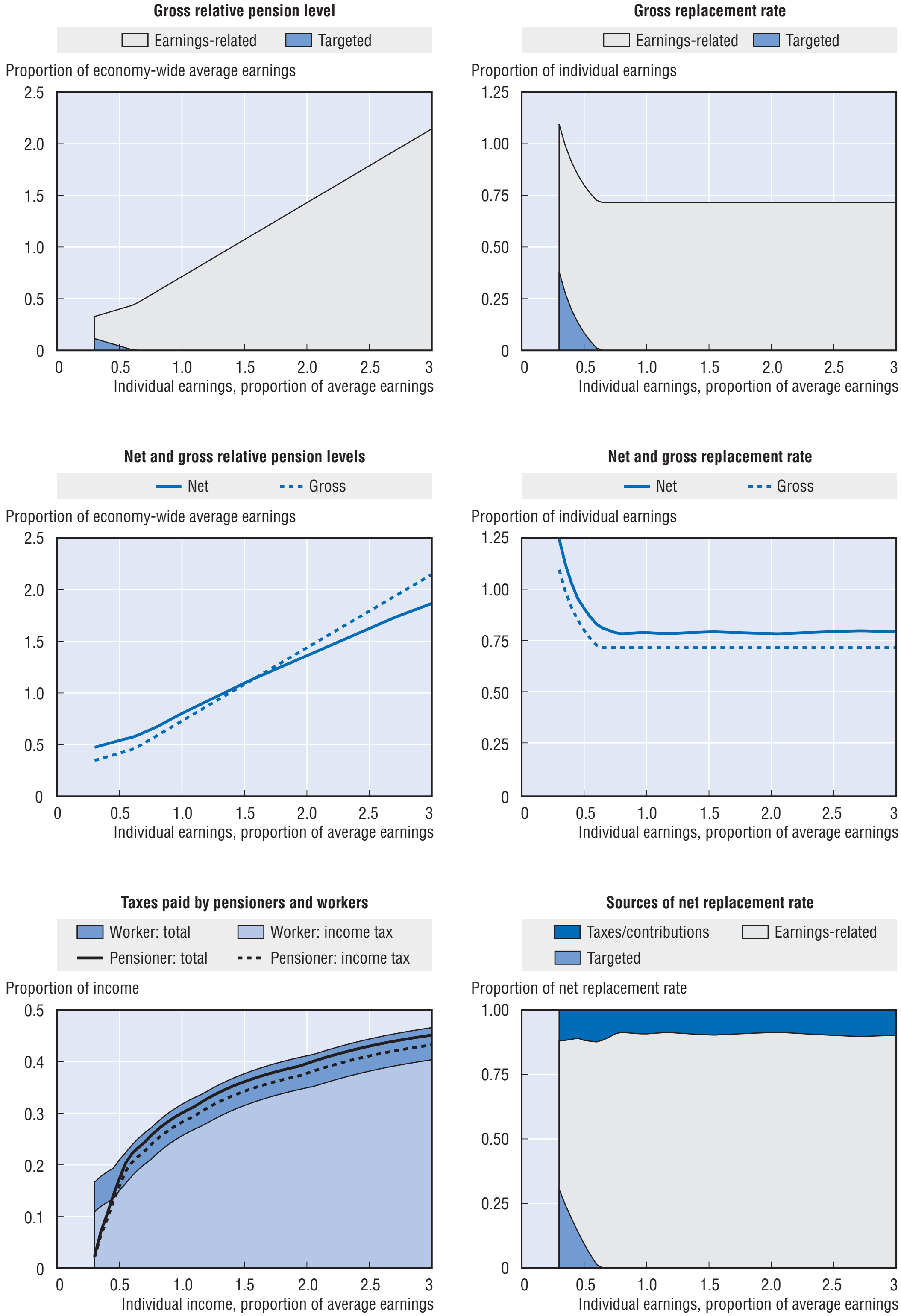
Pension modelling results: Finland



Source: OECD, based on information provided by the countries.

and 50% of price inflation. From 2005 onwards, however, 20% earnings and 80% prices will be used at all ages. The Finnish Centre for Pensions co-ordinates the schemes, resulting in a single pension payment even for people who have been members of different plans.

Targeted

The parameters of the system differ from one municipality to another to reflect regional differences in the cost of living. The basic monthly benefit for a single pensioner in 2002 was between EUR 467 and EUR 488 (around a fifth of average earnings). The national pension is reduced by 50% of the difference between other pension income and a small disregard of EUR 550 per year. No pension is payable once other pension income exceeds between EUR 958 and EUR 999 per month (depending on municipality).

The basic pension benefit and the parameters of the means test are uprated annually in line with prices.

Personal income tax and social security contributions

Taxation of pensioners

There are no special rules for the taxation of pensioners.

Taxation of pension income

Recipients of pension income can deduct an allowance from their income subject to municipal income tax. The amount of pension-income allowance in municipal taxation is based on the full national pension and the basic allowance for all individuals with low incomes. In 2002, the maximum allowance was EUR 6 540 for a single person and EUR 5 580 for each partner in a married couple. (There is separate taxation of couples.) The allowance is withdrawn at a rate of 70% of the amount by which the income subject to tax exceeds the full allowance. This means that there is no allowance once the income exceeds EUR 15 883 (single person) or EUR 13 552 (each partner in a couple). The pension-income allowance cannot exceed the amount of pension. The allowance is "wasteable": *i.e.*, the pension-income allowance cannot exceed the amount of pension income.

There is also a pension-income allowance in the central-government income tax. However, the allowance is currently exhausted before the income reaches the lowest income bracket of the central-government income tax. This allowance therefore has no practical effect.

Workers receive a deduction for work-related expenses, which is not available for pensioners.

Social security contributions paid by pensioners

There are no contributions on pension income for pension or unemployment insurance. However, the same sickness insurance contributions are levied on pensioners' incomes as on those of workers. In 2002, there was an additional 0.4% sickness insurance contribution on pension income (*i.e.*, the rate for pension income was 1.5% + 0.4%). In 2003, this additional sickness-insurance contribution on pension income was abolished. The sickness-insurance contribution is levied on taxable income as defined in municipal taxation.

Pension modelling results: Finland

Men	Individual earnings, multiple of average					
Women (where different)	0.5	0.75	1	1.5	2	2.5
Gross pension level	40.0	53.6	71.5	107.2	142.9	178.6
(% of average earnings)						
Net pension level	52.5	63.1	78.8	108.4	135.2	161.7
(% of average net earnings)						
Gross replacement rate	80.0	71.5	71.5	71.5	71.5	71.5
(% of individual earnings)						
Net replacement rate	90.7	78.8	78.8	79.2	78.3	79.3
(% of individual net earnings)						
Gross pension wealth	6.3	8.4	11.2	16.9	22.5	28.1
(multiple of average earnings)	*7.4*	*10.0*	*13.3*	*20.0*	*26.6*	*33.3*
Net pension wealth	8.2	9.9	12.4	17.0	21.3	25.4
(multiple of average net earnings)	*9.7*	*11.8*	*14.7*	*20.2*	*25.2*	*30.1*

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Table of Contents

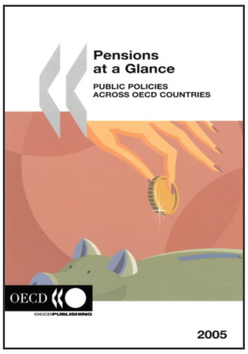
Part II

Country Studies

List of Box

List of Tables

List of Figures



From:

OECD Pensions at a Glance 2005

Public Policies across OECD Countries

Access the complete publication at:

https://doi.org/10.1787/pension_glance-2005-en

Please cite this chapter as:

OECD (2006), “Finland”, in *OECD Pensions at a Glance 2005: Public Policies across OECD Countries*, OECD Publishing, Paris.

DOI: https://doi.org/10.1787/pension_glance-2005-20-en

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