Bulgaria social briefing:
Pension System in Bulgaria

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Summary

The pension insurance system in Bulgaria is based on the development of the so-called three pillars:

- first pillar - mandatory state pension insurance as an element of the State social insurance;
- second pillar - additional mandatory pension insurance in pension funds managed by licensed pension insurance companies;
- third pillar - additional voluntary pension insurance in pension funds managed by licensed pension insurance companies.

The current Bulgarian pension system came into force with the Mandatory Social Insurance Code on 1 January 2000 (renamed the Social Insurance Code [SIC] in 2003). The main goal of the three-pillar pension model is to combine the advantages of the pay-as-you go and capital-based systems to ensure pension income that would substitute a significant part of the income before retirement.

The pension system in Bulgaria has undergone substantial structural reforms since the late 1990s when the Bulgarian government launched a process of preparation of a strategy for pension reform. The process of developing the strategy was coordinated by the World Bank. Its main strategic goals fit into the logic of consolidation the budget and stabilization of macroeconomic framework and policies required by the country international donors (WB and IMF). This brings the concept of pension reform known as ‘Chilean’ or ‘multi-pillar pension model’, which is developed by the World Bank in the early 1980s.

Finally in Bulgaria the traditional pay-as-you-go system was transformed into a three-pillar system through the introduction of compulsory and voluntary fully funded pillars.

For the first time voluntary private pensions were introduced in 1995. Other aspects of the pension reform include the separation of the State social insurance budget from the State budget, the establishment of specialized funds, and the introduction of the tripartite management of the State social insurance system. The current Bulgarian pension system came into force with the Mandatory Social Insurance Code on 1 January 2000 (renamed the Social Insurance Code [SIC] in 2003).
The main objectives of the reform were to stabilize the existing public insurance system (first pillar), and to allow the Bulgarian population to receive higher incomes after retirement through participation in second and third pillars of the pension system. From 2000 onwards, parametric reforms in the first pillar were implemented. The same year, a mandatory second pillar system for workers in hazardous occupations was implemented. It was followed in 2002 by a mandatory second pillar for all employees.

**The first pillar** is a pay-as-you-go public pension insurance system. Promoting the principle of mandatory participation and universality, the first pillar covers all economically active persons. It is financed through contributions from employers and employees, as well as through transfers from the State budget for covering all non-contributory pension benefits and some non-contributory periods, which are regarded as insurance periods. In the period 2009-2015 the State was participating as a “third insurer” and was paying contributions equal to 12 percent of the total insurance income of all insured persons. As of 2016 the State contribution was abolished. In addition, the State has the obligation to cover any remaining financial gaps and deficits of the public pension system.

The first pillar is administrated by the National Social Security Institute (NSSI), which is responsible for the entitlement and payment of pensions and other social insurance benefits in the event of one’s temporary incapacity to work, maternity and unemployment. The pension policy is formulated and implemented by the Ministry of Labour and Social Policy.

**The second pillar** is a supplementary mandatory pension insurance system. It is based on individual retirement savings accounts managed by private pension insurance companies. The second pillar is comprised of two types of pension funds: Universal Pension Funds and Professional Pension Funds.

The Universal Pension Funds (UPF) of Supplementary Mandatory pension insurance (second pillar) cover all persons insured through the public pension insurance born after 31 December 1959 and provide supplementary life-long old-age pensions as well as payments in case of death. They are still in accumulation phase and the first pensions are expected to be paid this year.

The Professional Pension Funds (PPF) of Supplementary Mandatory pension insurance (second pillar) are mandatory funds for early retirement intended to cover all persons working at hazardous environment (labour ‘at risk’).

**The third pillar** is a supplementary voluntary pension insurance system. It is a pension savings scheme based on voluntary contributions deposited in private pension funds that are maintained by licensed pension insurance companies. Currently, two types exist: the Voluntary Pension Funds and the Occupational Pension Funds. The latter are provided under occupational
schemes and are based on collective agreements. Contributions to the third pillar are paid by the members themselves or by their employers and they are tax-exempt up to a certain limit. Benefits can be paid in the form of life annuities, fixed-term annuities, lump sums or programmed withdrawals for survivors’ benefits.

The pre-reform system in Bulgaria was a pure Pay As You Go system, the design of which suffered from various problems. The retirement age of 55 for women and 60 for men was quite low. Employees in various occupations could retire even earlier, and early retirement was used as a means of cutting the workforce during the transition period. Evading social security contributions was a widespread practice, and the dramatic rise in unemployment led to a fall in the number of contributors. The link between contributions and benefits was weak, as pension benefits were based on the three best-earning years. To remedy the situation, the government developed a reform strategy that was implemented after 2000. Key measures included lowering the overall contribution rate and gradually increasing employee contributions.

The pensions system has undergone a number of reforms over the years. The changes are aimed at raising the retirement age and trying to ensure better pension provisions. On 28 July 2015, the National Assembly adopted important changes to the Social Security Code.

The first change was a 2 percentage point increase in social security contributions - 1 point from the beginning of 2017 and 1 point from the beginning of 2018. Such a mild increase was recommended in a 2013 report by the World Bank. There is no new increase of the social insurance contribution for pensions since the beginning of 2019.

The second change in the amended Social Security Code consists of raising the retirement age. In 2015, the retirement age for men in Bulgaria was 63 years and 10 months; for women it was 60 years and 10 months. In 2017, it was raised gradually for both men and women to finally reach the target of 65 years by 2029 for men and by 2037 for women. For men, the retirement age began to increase by 2 months in 2017 and by 1 month in every subsequent year. For women, the retirement age began to increase at a faster pace – by 2 months each year from 2017 until 2029 and by 3 months each year from 2030 to 2037. The required length of service / contribution period (which was in 2015 38 years and 2 months for men and 35 years and 2 months for women) began also to increase gradually for both genders, by 2 months each year staring from 2017 until it reaches 37 years for women and 40 years for men.

At the same time, there are many employees, who can retire earlier, even with shorter periods of service, on the base of the quality of their working conditions (for example, miners, part of workers in metallurgy, employees in the civil aviation etc.). This early retirement applies also to employees in military services, police, security services, supervisors in prisons and others.
Finally, a third important change and the most controversial one consists of the possibility for people who have insurance contributions, based both on the first and the second pillar of the pension system, to make multiple shifts between their savings. Those who have paid insurance contributions for the second pillar in a private pension fund can choose to transfer their pension savings from that fund to the national pension fund (which is state-owned) and continue to pay the amount of the two contributions into the national pension fund. It is also possible to shift funds back.

**In conclusion** we have to say that the pay-as-you go system is based on the principles of solidarity between generations. This means that the working generation of today, through their social security contributions, provides the payment of pensions to the pensioners. At the same time the deterioration of the demographic structure means that the number of working persons is decreasing and that poses major challenges to the state social security system in paying adequate pensions in the future.

Currently, the Bulgarian pension system is facing serious demographic challenges. In 2021, pension expenditures are expected to reach 9.9% of GDP. Between 2025 and 2034, the share of pension expenditures in GDP is expected to remain at a relatively constant level of around 10.0%. According to the Ministry of Finance, in the period from 2035 to 2060, as a result of the aging process and the expected higher life expectancy, the fiscal pressure on the state pension system will increase and the cost of pensions as a share of GDP will start to grow, reaching its highest value of 12.5% in 2060.