BETTER FINANCE
The European Federation of Investors and Financial Services Users
Fédération Européenne des Épargnants et Usagers des Services Financiers

PRESS RELEASE

Dismantling the Estonian Pension System is not the Answer

27 October 2020 – On Tuesday, 20 October 2020, the Supreme Court of Estonia ruled that the current government's hotly contested pensions "reform" is not unconstitutional. The reform is set to dismantle the foundation of the second (occupational) pillar of the Estonian pension system. It is worth noting that many of the Judges who ruled in its favour, did admit that although the law is likely to have an overall negative effect on second pillar pensions and does violate some property rights, it does not breach the Constitution.

Indeed, the new law in Estonia will allow people to stop contributing to the - until now mandatory - second pillar pension and to dip into their accumulated pension savings at any age, as is the case in other EU Member States that are authorising early withdrawals in response to the economic fallout from the Covid-19 crisis.

The government argues that the new law will also give people more freedom and choice on how to invest their savings than is currently the case. However, surveys conducted by Kantar Emor show that most of the people who, given the opportunity, intend to liquidate their current pension fund savings, would use the money to cover running costs, such as home renovations or paying back loans, rather than investing for retirement.

Pensions poverty

People who cash in on their second pillar savings without reinvesting, are likely destined for old-age poverty, since the first pillar is not currently intended to provide an adequate retirement income by itself. The average first pillar pension payments in Estonia are well below the national minimum wage.

The potential exit of a significant number of current savers from the system over a short time period could also have a negative effect on the returns on savings of those who stick with the second pillar, due to potentially higher fee percentages because of lower amounts of assets under management, and because pension funds may potentially have to either liquidate assets at the wrong time due to mass withdrawals or keep much larger portions of assets in cash deposits to mitigate this withdrawal risk. This was the argument at the heart of the Supreme Court case.

BETTER FINANCE call not to sacrifice the long-term and pension adequacy

BETTER FINANCE calls to reverse this decision before it is too late. While we agree that the pension system needs improving to ensure higher real returns for pension products and better income-replacement rates upon retirement, the newly promulgated law is a shift in the wrong direction.

There are better ways of giving savers more and better options of investing their second pillar pension savings, including removing bureaucratic impediments to investing second pillar saving into Pan-European Pension Products (PEPP).

The Estonian mandatory pension funds market has seen many improvements in the last few years and we encourage the government to build on these rather than break the system completely and subject hundreds of thousands to old-age poverty in the future.

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