# Latvia

## Data Overview

### Macroeconomic and Demographic Data

<table>
<thead>
<tr>
<th>Year</th>
<th>Nominal GDP (millions of national currency)</th>
<th>GDP per capita (US $)</th>
<th>Total Labour Force (thousands)</th>
<th>Employment rate</th>
<th>% population over 65</th>
<th>Dependency Ratio</th>
<th>Life expectancy at birth</th>
<th>Fertility rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>5,219</td>
<td>3,492</td>
<td>1,106</td>
<td>87.03</td>
<td>15.30</td>
<td>32.63</td>
<td>ND</td>
<td>1.21</td>
</tr>
<tr>
<td>2002</td>
<td>5,758</td>
<td>3,929</td>
<td>1,124</td>
<td>88.03</td>
<td>15.53</td>
<td>32.38</td>
<td>ND</td>
<td>1.23</td>
</tr>
<tr>
<td>2003</td>
<td>6,393</td>
<td>4,744</td>
<td>1,126</td>
<td>89.42</td>
<td>15.86</td>
<td>32.82</td>
<td>ND</td>
<td>ND</td>
</tr>
<tr>
<td>2004</td>
<td>7,434</td>
<td>5,865</td>
<td>1,136</td>
<td>89.56</td>
<td>16.19</td>
<td>33.04</td>
<td>ND</td>
<td>ND</td>
</tr>
<tr>
<td>2005</td>
<td>9,059</td>
<td>6,608</td>
<td>1,135</td>
<td>91.27</td>
<td>16.52</td>
<td>33.59</td>
<td>ND</td>
<td>ND</td>
</tr>
<tr>
<td>2006</td>
<td>11,265</td>
<td>8,781</td>
<td>ND</td>
<td>ND</td>
<td>16.80</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
</tr>
</tbody>
</table>

### Assets

<table>
<thead>
<tr>
<th>Year</th>
<th>Total investments (National currency millions)</th>
<th>Total investments, as a % of GDP</th>
<th>Of which Assets overseas, as a % of Total investment</th>
<th>% Issued by entities located abroad</th>
<th>% Issued in foreign currencies</th>
<th>% Issued by entities located abroad</th>
<th>% Issued in foreign currencies</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>13</td>
<td>0.24</td>
<td>8.00</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
</tr>
<tr>
<td>2002</td>
<td>26</td>
<td>0.45</td>
<td>5.00</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
</tr>
<tr>
<td>2003</td>
<td>45</td>
<td>0.71</td>
<td>13.00</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
</tr>
<tr>
<td>2004</td>
<td>74</td>
<td>0.99</td>
<td>16.00</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
</tr>
<tr>
<td>2005</td>
<td>119</td>
<td>1.31</td>
<td>32.00</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
</tr>
<tr>
<td>2006</td>
<td>179</td>
<td>1.59</td>
<td>32.00</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
</tr>
</tbody>
</table>

### By pension fund type (as a % of Total investments)

- **Pension funds (autonomous)**
  - 100.00
- **Book reserves (non autonomous)**
- **Pension insurance contracts**
- **Other financing vehicle**

### By pension plan type

- **Occupational assets**
  - 10
- **% of DB assets**
  - 100.00
- **% of DC (protected and unprotected) assets**
- **Personal assets**
  - 3

### Structure of Assets (as a % of Total investments)

<table>
<thead>
<tr>
<th>Category</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash and Deposits</td>
<td>33.00</td>
<td>29.86</td>
<td>28.29</td>
<td>34.65</td>
<td>28.59</td>
<td>28.58</td>
</tr>
<tr>
<td>Fixed Income</td>
<td>62.44</td>
<td>65.28</td>
<td>66.42</td>
<td>51.90</td>
<td>47.21</td>
<td>49.94</td>
</tr>
<tr>
<td>Of which:</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bills and Bonds issued by the public and private sector</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
</tr>
<tr>
<td>Loans</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
</tr>
<tr>
<td>Shares</td>
<td>3.04</td>
<td>3.24</td>
<td>2.15</td>
<td>2.10</td>
<td>2.48</td>
<td>1.16</td>
</tr>
<tr>
<td>Land and Buildings</td>
<td>ND</td>
<td>ND</td>
<td>1.14</td>
<td>2.60</td>
<td>4.14</td>
<td>3.55</td>
</tr>
<tr>
<td>Other Investments</td>
<td>1.52</td>
<td>1.62</td>
<td>2.00</td>
<td>8.75</td>
<td>17.58</td>
<td>16.77</td>
</tr>
</tbody>
</table>

### Contributions and Benefits (as a % of GDP)

- **Total Contributions**, as a % of GDP
  - 0.13
- **Employer Contributions**, as a % of Total contributions
  - 99.00
- **Employee Contributions**, as a % of Total contributions
  - 1.00

### Total Benefits, as a % of GDP

- **% of benefits paid as a Lump sum**
- **% of benefits paid as a Pension**
- **% of benefits paid as an Insurance premium payable for allocated insurance contracts**

### Membership (in thousands of persons)

<table>
<thead>
<tr>
<th>Category</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total members</td>
<td>292</td>
<td>356</td>
<td>522.00</td>
<td>673</td>
<td>841</td>
<td>1,000</td>
</tr>
<tr>
<td>% of Total active members</td>
<td>ND</td>
<td>ND</td>
<td>80.00</td>
<td>85.00</td>
<td>70.00</td>
<td>80.00</td>
</tr>
<tr>
<td>% of Total passive members</td>
<td>ND</td>
<td>ND</td>
<td>15.00</td>
<td>13.00</td>
<td>23.00</td>
<td>11.00</td>
</tr>
<tr>
<td>% of Total deferred members</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
<td>ND</td>
</tr>
<tr>
<td>% of Other beneficiaries</td>
<td>ND</td>
<td>ND</td>
<td>5.00</td>
<td>7.00</td>
<td>7.00</td>
<td>9.00</td>
</tr>
</tbody>
</table>

### Number of Pension Funds/Plans

<table>
<thead>
<tr>
<th>Category</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total number of funds</td>
<td>4</td>
<td>4</td>
<td>5</td>
<td>5</td>
<td>6</td>
<td>6</td>
</tr>
<tr>
<td>Total number of plans</td>
<td>15</td>
<td>19</td>
<td>31</td>
<td>35</td>
<td>41</td>
<td></td>
</tr>
</tbody>
</table>

Source: OECD, Global Pension Statistics

ND = data not available
NA = data not applicable
II. Pension system
The Latvian pension system consists of a state pension scheme composed of an earnings-related pension financed on a pay-as-you-go basis through notional individual accounts (NDC PAYG); a fully funded, defined contribution, mandatory pension scheme; and private voluntary occupational and individual pension arrangements.

Public pension system
The NDC PAYG system has been in operation since 1996 and covers those aged 50 and over at the time of introduction in 1996. Those between 30 and 49 could choose whether to operate under the NDC system or to join the funded pension system, while those under 30 had to join the funded system (see below). Pensions are calculated according to a pension formula\(^1\) that is based on social insurance contributions. Participants are eligible to receive pension benefits after at least 10 years of insurance and upon reaching the statutory minimum retirement age, which will reach 62 for men and women by 2009.

Employees contribute 9% of gross monthly earnings. Employers pay 24.09% of employees’ gross salaries, of which 16% is attributed to the PAYG system and 4% to the funded mandatory individual account system. The remaining contributions (4.09%) finance other social insurance benefits. The percentage of contributions that is directed towards the funded mandatory individual account system will rise to 10% in 2010. The total contribution amount will however remain the same, as the amount of contributions towards the NDC scheme will decrease correspondingly.

Social insurance benefits are adjusted in line with the CPI in April, and in line with the CPI and changes in average contributory earnings in October of each year.

Since 1997, benefits paid under the state pension scheme are subject to income tax. However, old age pensions attributed before January 1996, when the new law came into force, are not subject to taxation. A state social security benefit is paid to those who do not qualify for old-age pension benefits (LVL45 in 2006).

Funded Pension System
Mandatory

Coverage
The state mandatory funded pension scheme (SFPF) has been in operation since 2001, participation in the scheme is mandatory for new labour entrants and those who were younger than 30 when the reform came into force. Early 2007, some 900,000 people participated in the mandatory funded pension scheme. It was estimated that as of 2006 78% of the active population was covered.

 Contributions
The contribution rate paid from the employees’ gross salary is 4% (2007) and will gradually increase to 8% in 2008, 9% in 2009 and 10% from 2010 onwards. Contributions to the state pension system will decrease from 16% in 2007 to 10% in 2010.

 Benefits
Retirees can purchase an annuity from an insurance company or choose the “refunding” option: i.e. moving their capital to the NDC pension scheme and receiving a payout calculated following a slightly modified

\[ P = \frac{K}{G} \]

where \( P \) is annual pension under the NDC pension scheme, \( K \) is accumulated life-time notional pension capital for insured person that is recorded in the individual notional account; \( G \) is expected years for pension payout, based on estimation of unisex life expectancy of the work’s age cohort.

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\(^1\)
NDC pension formula. Lump sum payments are not allowed. Detailed provisions on the payout phase have not yet been elaborated as the first pension benefits will be paid out in 2014.

Taxation
Contributions are income tax deductible. Pension benefits are taxed at the ordinary income tax rate of 25% when they exceed LVL 1,200 for the year. Pensions are not subject to social security contributions. Investment income is exempt from tax.

Asset management companies
The main entities involved in the administration of the SFPS are the State Social Insurance Agency, investment management companies and custodian banks. Participants may change their asset manager once a year and change investment plan under the same manager twice a year free of charge. Members are free to make a choice of investment plan and can choose a conservative investment plan, a balanced investment plan or an active investment plan. The investment policy of these investment plans varies mostly by the weight of equities in their portfolio (could be 0% - 50% according to legislation) The State Treasury manages the default fund (conservative). The State Treasury has completed the activities in management of SFPS assets as per November 2007 and the assets of State Treasury investment plan has been distributed between conservative investment plans of private asset managers according to special decision of Cabinet of Ministers.

Investment legislation sets both quantitative and qualitative restrictions. Private asset managers may invest in government and municipal securities; corporate debt and equity securities; open-ended investment funds; bank deposits and derivatives. There is no maximum limit to investments abroad, provided they are listed on the official list of stock exchanges registered in a Baltic, EU or EFTA countries. The law does however stipulate a 70% currency matching rule (except investments in EUR where there are no limits). Assets may not be invested in real estate (except investments through investment funds) or financial instruments issued by the asset manager of the investment plan (except investment funds managed by the asset manager if there are no commissions charged for buy/sell of investment fund certificates), nor are managers permitted to take loans with the assets. Investments in risk capital markets are also limited to 5% of the investment plan assets.

Fees
Entry or exit fees may not be charged. Administration fees may be charged but are capped at 2.5% of total annual contributions. Custodian fees, asset management fees or other fees are not regulated, but should be identified in the prospectuses of investment plans.

Market
According to IPE, in 2006, Latvia’s pension assets in the mandatory pension system totalled almost LVL127m (€180m). As of the end of 2006, SFPF assets were managed by nine investment management companies, with these companies and the State Treasury offering a total of 26 investment plans to participants. Current estimates project, assuming a 4% annual real gross return on capital (net of administrative expenses), that the SFPS assets should attain around LVL 1.3bn (€1.9 bn) by 2014.

Replacement rate
OECD estimates the gross replacement rate for an average worker from mandatory pensions to be 58.2% (81.8% net).

\[ P = \frac{(K_n + K_f)}{G} \]

where \( P \) is annual pension under the NDC pension scheme, \( K_n \) is notional pension capital accrued under the NDC pension scheme, \( K_f \) is financial capital accrued under the SFPS and \( G \) is expected years for pension payout.

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2 \( P = \frac{(K_n + K_f)}{G} \), where where \( P \) is annual pension under the NDC pension scheme, \( K_n \) is notional pension capital accrued under the NDC pension scheme, \( K_f \) is financial capital accrued under the SFPS and \( G \) is expected years for pension payout.
Voluntary Personal Coverage
Voluntary pension funds may be closed or open and they may offer one or more pension plans. Plans can be DB or DC in nature, or hybrid (DC with a guaranteed investment return or cover against biometrical risks). Pension plan participants may participate directly or with the involvement of their employer.

Contributions
No contribution rates are prescribed in the law. Employers typically contribute between 5-10% of the employee’s salary, while employees contribute around 5%.

Benefits
Pension plan participants can receive benefits from age 55 or continue participating and receive capital in parts. Benefits are paid out as an annuity, a phased withdrawal or a lump sum.

Taxation
Employee and employer contributions are tax exempt up to 10% of the employee’s annual employment income. Benefits are tax exempt, while investment income is taxed.

Management companies
According to the law private pension funds are not allowed to manage assets of pension plans themselves but should contract out the asset management of the pension plans to the external asset managers. According to the law credit institutions, insurance joint stock companies, investment brokerage companies and investment management companies which are allowed to provide services in Latvia can be contracted as the asset managers of pension plans. Investment rules are largely the same for DB and DC schemes, though some minor differences exist. There are no restrictions on switching funds: a written application sent to the pension fund one month in advance suffices.

Fees
Fees are unregulated and their level is laid down in the pension plan. Private pension funds charge their fee for administration of pension plans. There are also fees to asset managers and custodian banks and may be charged other fees, too.

Market
According to IPE, in 2006, Latvia’s voluntary pension assets totalled LVL 51 m (€73 million). There are currently six voluntary pension funds operating in Latvia, among them five are open and one is closed. Only about 5% of Latvian companies offer voluntary private occupational arrangements to their employees. A total of 99 596 members participated in voluntary pension arrangements at the end of 2006.

Proposed reforms
It is expected that government will concentrate on the following issues in the near future: further strengthening of the regulatory and monitoring framework of private pension arrangements; improving the financial literacy of participants; deregulating investment regulations in the state mandatory retirement income system; encouraging voluntary pension savings.

Legislation and supervision
The Law on State Funded Pensions regulates the mandatory pension system, while the Law on Private Pension Funds regulates voluntary pension arrangements. Supervision of both systems is carried out by the Finance and Capital Market Commission: [http://www.fktk.lv/eng](http://www.fktk.lv/eng).
The Ministry of Welfare is charged with the development of policy in the social security system, including the pension system: www.lm.gov.lv.