IOPS COUNTRY PROFILE: PERU

DEMOGRAPHICS AND MACROECONOMICS

Nominal GDP (USD bn)	**226.8**
GDP per capita (USD)	**6 978**
Population (000s)	**32 510**
Labour force (000s)	**19 356**
Employment rate	**75.1**
Population over 65 (%)	**8.4**
Dependency ratio[1]	**12.6**

Data from 2019.
1. Ratio of over 65-year-olds the labour force.
Source: World Bank, various sources.

PERU: COUNTRY PENSION DESIGN

STRUCTURE OF THE PENSION SYSTEM

Public pensions

- The social assistance programme, providing minimum benefits.
- The public social insurance programme.

Private pensions: personal (mandatory)

- It covers employees both in public and private sectors. However, self-employees and those in the informal sector are not covered.
- New entrants need to choose between this pillar and the public pension as above.
- It is a funded DC scheme.

Private pensions: personal (voluntary)

- The legal framework of this pillar is basically the same as the mandatory one.
- Balance in this pillar is allowed to be transfered to the mandatory one.

Source: OECD Global Pension Statistic.

PERU: THE PENSION SYSTEM'S KEY CHARACTERISTICS

PUBLIC PENSION

The public pension provision is made up of at least two different programs. The first program provides assistance and minimum benefits for low-income individuals. By the end of 2019, the minimum pension was 500 soles per month (US$151). The government also provides the same amount of benefits for all members of the private pension system who, at retirement, have not accumulated enough funds in their personal accounts to finance a pension of an amount equal to or greater than the minimum pension, and who fulfill certain requirements as specified by law - including having contributed for at least 20 years.

The second program is the public Social Insurance system. It is a contributory, defined-benefit, pay-as- you-go system. Contrary to other pension reforms, which phased out the old public system, the public pension scheme competes with the private pension scheme. New entrants to the labor force have to decide whether to join the Private Pension Fund Administration System (SPP) or the public social insurance system (SNP) within a period of 10 days. If the worker does not make this choice, the employer will automatically affiliate the worker to the private system. Workers affiliated to the public system can remain there or switch to the private system at any time. However, workers in the private system are not allowed to switch back to the public system.

Under the SNP system, the employees contribute 13% of their taxable income for old age, survivor and disability coverage. It provides earning related benefits for those workers with 20 years of contributions who reach age 65 (for both men and women). Old-age benefits range from 30% to 45% of average earnings during the last 5 years of employment, plus 2% for each additional year of contributions exceeding 20, up to a maximum of 100%. Disability benefits are set at 50% of the reference salary, plus 1.5% for each year of contributions exceeding 3 years. Survivorship benefits are set at similar levels.

PERSONAL MANDATORY

Coverage

Private and public employees who entered the labor market are required to choose between the public social insurance system (SNP) and the mandatory private pension system (SPP). Participation is not mandatory for the self-employed, the unemployed, those in the informal sector or those who were covered by the old system. By December 2019, the number of members in the mandatory private pension system was 7.4 million.

Contributions

All workers who opted out of the Social Insurance scheme contribute 10% of their taxable income to their private investment funds. Workers must contribute another 1.35% of gross earnings to cover term survivor and disability insurance plus a fee determined by each AFP, which is:

- A percentage of monthly salary: this fee should be applied by AFP equally to all members.

- Fee on Assets Under Management (AUM). As a process of transition a mixed fee (monthly salary: 0.31 per cent – December 2019, plus AUM: 1.13 per cent – December 2019) is being implemented. The process will finish in 2023. This mixed fee is mandatory for new entrants, from 2013.

- There are not maximum earnings for contribution purpose. Employers are not required to contribute.

Benefits

The system is defined contribution in nature. The value of the old-age pension varies according to the member's contributions to the individual account plus accrued earnings, minus administrative fees.

Retirement benefits are available at age 65 for both women and men. Retirees may choose between five benefits options: programmed withdrawal from their individual accounts; two-tier annuities; life annuities; and deferred annuity with temporary programmed withdrawals. Since May 2016, members at age of retirement are able to withdraw the lump sum of their individual account (95.5% of the total amount), and the remaining 4.5% are paid to the National Health Insurance System (Essalud) in order to grant the retiree a health insurance policy for life, regardless of the amount withdrawn.

The Private Pension System also offers the following early retirement options:

Early retirement: Affiliates may retire at 55 years of age for men and 50 years of age for women, provided that their pension equals to at least 40 per cent of their indexed average monthly salary in the last 120 months and that they have contributed for at least 72 months within the last 120 months.

Early retirement for the unemployed: a new special regime (REJA 30939) was established in May 2019 for affiliates who:

- Are over 55 years of age for men and 50 years of age for women in order to apply for the benefit;
- Have been unemployed for at least the last (12) twelve months;
- Meet the requirements to prove their unemployment, which vary depending on the nature of their work (dependent or independent).

The state guarantees a minimum pension (S/. 500 Soles at the time of this writing) for retirees aged (65) sixty-five or more whose benefit does not exceed the minimum pension and who have contributed for at least 20 years to the Public Pension System and/or the Private Pension System.

Terminal Illness or Cancer: Members who have been diagnosed with a Terminal Illness or Cancer that reduces their life expectancy (validated by a medical commission) and are unable to access a Disability Pension may opt to retire early. This early retirement option allows the member to withdraw up to 50% of their pension capital if they had no beneficiaries.

Early retirement for risk labour: Affiliates who work in risky occupations, such as mining, metallurgy, iron and steel or civil construction activities (administrative jobs in aforementioned fields do not qualify as risk labour), may choose early retirement. There are two regimes:

- Generic regime: Supplementary contributions are co-financed with the employer. In mining, an additional contribution of 4% is shared equally between the employee and employer, and the retirement age can be advanced by two years for every 36 months of contributions. For those working in civil construction, additional contributions are 2% shared equally between the employee and employer, and the retirement age can be advanced by one year for every 36 months of contributions. If the employee switched from the SNP to the SPP before 2003 there is an additional bonus provided;

- Extraordinary regime: The Government provides a supplemental bonus to increase the pension to the level that would have been obtained in the SNP's Mining Retirement Scheme. To qualify for this regime, workers must comply with years of risk exposure, minimum predominant work period, and have at least 20 years of contributions to the pension system. Depending on the type and duration of the occupation, they can then retire from age 40 to 50.

Employees who have accrued rights under the Public Pension System and have decided to switch to the Private Pension System receive recognition bonds in return for their accrued rights. These recognition bonds are credited to their individual accounts but only become effective when the member retires.

Disability benefit is payable to members under retirement age where work capacity is reduced by at least 50 per cent: Partial disability is defined as a reduction in earnings capacity of between 50 per cent and 66.6 per cent. Total disability is then defined as a reduction in earnings capacity exceeding 66.6 per cent.

The reduction in the degree of work capacity must be certified by the Medical Committee of the AFP (COMAFP) and the commission evaluates whether the condition may be temporary or permanent. The Committee will issue a decision which can be appealed to the SBS's Medical Committee (COMEC).

Private Pension System also grants Survivorship benefits if the deceased was an active member or a retiree. Eligible survivors are the spouse or cohabitee, orphans under age 18 or older as long as they pursue basic or higher levels of education in a continuous and satisfactory manner (no age limit if disabled) and parents who are unable to work due to disability or who are older than age 60 for fathers and 55 for mothers.

Deceased and disabled active members are covered by the disability and survivorship insurance within the first (2) two months of membership after the first contribution to the Private Pension System or if they had four months of contributions within the last (8) eight months before the date of death. If they are not covered by the survivorship insurance, benefits are financed only with the accumulated capital in the individual account. It is worth noting that, in order to be eligible for insurance coverage, the sinister must not have cause for exclusion such as suicide or injury during wartime, radioactive exposure, risk labour (must be covered by a different mandatory insurance), among others.

Tax

Mandatory contributions are taxed. Investment incomes and benefits are tax exempt.

Fees

AFPs are allowed to charge members a variable commission as a percentage of contributions for the administration of pension funds. Each AFP is free to set these commissions; however, they are still required to charge the same fee to all of their affiliates. By December 2019, the average fund administration commission was 1.58%.

However, a mixed fee (salary plus AUM) is being implemented as a process of transition. The process will finish in 2023. This mixed fee is mandatory for new entrants from 2013. For older members they had the opportunity to choose between fee based on salary or based on AUM. By December of 2020, the average fee was 0.31% for the salary component and 1.13% for the AUM component. The average premium for the disability and survivorship insurance was 1.35% on the salary.

Personal Voluntary

Coverage

Both, employees and self-employed who are enroll in the SPP may contribute voluntarily to the mandatory individual account. Member who chose the public system are not allowed to make voluntary contributions.

Benefits

Voluntary contributions are transferred to the mandatory individual account of each member, in order to increase the amount of their pension. Retirement benefits provided by voluntary contributions are available only when they retire. Early withdrawals before retirement are not allowed.

Tax

The investments income from voluntary contributions with non-pension purposes is taxed.

Market information

Personal mandatory

Pension funds under the private scheme are managed by specialized private pension fund managing companies (AFPs). These companies are in charge of managing participants savings deposited in individual retirement accounts. AFPs are not allowed to do any other business than pension fund management. They have to be set up as joint-stock companies. The net worth of the AFP is independent of that of the pension fund, and the AFPs must keep the accounts of the pension fund net worth separately. AFPs are licensed, regulated and supervised by a specialized agency, the Superintendence of Banking, Insurance and Private Pension Funds Administrators (SBS). Currently there are 4 AFPs operating in the market.

Initially, AFPs could only offer one tightly regulated pension fund to their affiliates, with the allocation of assets limited by law. However, under a new regulation passed in the second half of 2003 and the regulations approved by the end of 2004 and the regulations approved in the second half of 2012, AFPs are now allowed to offer four types de pension funds, each with its own level of risk and investment limits established in the regulations. The four fund types are differentiated by the proportion of their portfolio invested in equities and fixed income securities. Thus, the more conservative fund (fund type 0) is allowed to invest up to 0% in equities, the second conservative fund (type 1) is allowed to invest up to 10%, the balanced fund up to 45% (type 2), whereas the more aggressive fund can invest up to 80% (type 3). Initially, only the fund type 2 existed, later the funds type 1 and 3 started to operate by the end of 2005, and the last fund (type 0) started to operate by the beginning of 2016. Pension funds administrators have accumulated assets equivalent to 52,793 million dollars as of December 2019 or 22.8% of GDP. The annual average rate of return of the pension system (excluding administration fees) was around 11.1% between December 1992 and December 2019. By mid of 2019, 25.7% of total assets were invested in government bonds, 10.8% in securities issued by domestic financial institutions, while investment in domestic corporate bonds represented around 7%. Local equities and mutual funds represented 8.2% and 1% respectively, whilst foreign securities have increase to around 42.27%.

The private scheme set up a minimum profitability guarantee in order to protect affiliates from strong fluctuations in the returns of the funds. If an AFP underperformed, the shortfall had to be made up from the mandatory reserve. Thus, the minimum return is calculated as follows:

Fund Type 0: This fund doesn't have an established minimum performance, this fund has a stable performance over time because, as stated above, it can only invest in short term instruments like cash deposits.

Fund Type 1: The minimum performance may not be lower than:

- Average annualized real return for last (36) thirty-six months of Type 1 fund minus (2) two percentage points; or
- (50%) fifty percent of average annualized real return for last (36) thirty-six months of Type 1 fund.

Fund Type 2: The minimum performance may not be lower than:

- Average annualized real return for last (36) thirty-six months of Type 2 fund minus (3) three percentage points; or
- (35%) thirty-five percent of average annualized real return for last (36) thirty-six months of Type 2 fund.

Fund Type 3: The minimum performance may not be lower than:

- Average annualized real return for last (36) thirty-six months of Type 3 fund minus (4) four percentage points; or
- (25%) twenty-five percent of average annualized real return for last (36) thirty-six months of Type 3 fund.

Personal voluntary

Voluntary contributions are managed by the AFPs. The regulatory framework for managing voluntary contributions is basically the same as for the mandatory contributions.

Voluntary personal schemes in Peru are not very attractive because there are not tax incentives for voluntary contribution and there are not maximum earnings for mandatory contribution.

POTENTIAL REFORM

Through Law 30939, published in May 3, 2019, the Peruvian Congress created a Council to evaluate the current situation of the public and private pension systems, with the following functions: a) Carry out an evaluation of the conditions of access, costs and benefits of the early retirement regimes in the Private Pension System, which includes the identification of stakeholders and groups of interests that could directly or indirectly be beneficiaries or harmed by such regimes; and b) Evaluate the main conditions of the public and private pension system in Peru, including aspects such as fiscal sustainability, the adequacy of pensions (minimum pension), demography and universal coverage of the population, and issue recommendations.

The Council was made up of a representative of the Ministry of Economy and Finance, the Superintendency of Banking, Insurance and Private Pension Fund Administrators, the Ministry of Labor and Employment Promotion, and the Oficina de Normalización Previsional (ONP).

The Council presented the guidelines for a proposal to reform the Pension System, establishing as the main objective to guarantee income for the elderly, prevent poverty and reduce inequality in old age, based on three axes:
- Increasing pension coverage.
- Redesigning and integrating pension systems to promote inclusion and equal opportunities for pension purposes.
- Improving the quality of pensions.

The indicated axes are intended to:
i) Redesign the Peruvian pension system towards an integrated scheme;
ii) Improve coverage and pension savings;
iii) Improve efficiency and cost reduction;
iv) Improve the pension fund investment regime;
v) Improve the benefits in order to mitigate the risk of poverty in old age.

The proposal presented by the Council considered the following items, still in discussion:
a) Create a multi-pillar pension system integrating the non-contributory component and the second contributory systems (pillar 0, pillar 1, pillar 2 and pillar 3).
b) Implement measures to improve operative processes such as the centralization of some operative process.
c) Reevaluate the withdrawal of 95.5% and other forms of lump sum withdrawals, in order to preserve the purpose of the pension system.
d) Introduce complementary measures to improve the funded system: improve competition, improve transparency and access to information on pension systems.
e) Promote measures to improve the profitability of pension funds, portfolio management, portfolios of reference, etc.
f) Strengthen voluntary savings.
g) Promote financial literacy a considering short, medium and long-term strategies.
h) Evaluate periodically the parametric variables (contribution rate, retirement age, mortality table, employer contributions, etc.)
i) Reevaluate the early retirement regimes in the SPP, since they distort the pension fund purpose, which is to protect the affiliates at the old age.

REFERENCE INFORMATION

KEY LEGISLATION

- Law Decree 25,897 of 1992. It established the system of private pension schemes.
- Supreme Decree 054-97-EF. It provides the regulatory framework for the licensing, regulation and supervision of the AFPs.

KEY REGULATORY AND SUPERVISORY AUTHORITIES

- Superintendency of Banking, Insurance and Private Pension Funds Administrators (SBS)