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Pension Reform and the Development of Pension Systems: An Evaluation of World Bank Assistance

Background Paper
South Korea Country Study

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Acronyms and Abbreviations

ASEM	Asia Europe Meeting
DB	Defined Benefit
DC	Defined Contribution
EET	Exempt-Exempt-Tax (treatment of contributions, returns and benefits)
ERL	Economic Reconstruction Loan
EU	European Union
FSS	Financial Supervisory Service
GDP	Gross Domestic Product
IEG	Independent Evaluation Group (formerly OED)
IMF	International Monetary Fund
INPRS	International Network of Pensions Regulators and Supervisors
ISSA	International Social Security Association
KCTU	Korean Council of Trade Unions
KEF	Korean Employers Federation
KIHASA	Korean Institute for Health and Social Affairs
NPRB	National Pension Review Board
NPS	National Pension System
OECD	Organization for Economic Cooperation and Development
OED	Operations Evaluations Department (changed its name to IEG in December 2005)
PAYG	Pay As You Go
PRTF	Pension Reform Task Force
SAL	Structural Adjustment Loan

Contents

Tables

Preface

This paper belongs to series of 19 country and regional case studies commissioned as background research for the World Bank's Independent Evaluation Group (IEG) report "Pension Reform and the Development of Pension Systems." The findings are based on consultant missions to the country or region, interviews with government, Bank, donor, and private sector representatives involved in the pension reform, and analysis of relevant Bank and external documents.

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Executive Summary

1. Korea is a high-income economy, with a 'young' but rapidly aging population and immature and somewhat poorly designed pension policies. Consideration of, and actual, reforms to Korean pensions have been ongoing since the early 1990s.

2. In 1997, the World Bank became involved in Korean pension reforms in the context of structural adjustment lending in the wake of the Asian financial crisis. Korea had graduated from Bank assistance in the early 1990s and the Bank involvement in Korea had wound down. However, over the tenure of the renewed Bank assistance, the developments were considerable and included:

- The introduction of a zero pillar (a non-contributory age pension).
- An improvement in the management of all public pension schemes and a greater awareness of the importance of long-term financial stability, including the introduction of five-yearly actuarial projections for all public pension schemes, the phasing-out of mandatory investment of NPS reserves in public sector assets and parametric reforms.
- The introduction of financial instruments to encourage pre-funding of retirement allowances.
- The introduction of EET taxation for all forms of retirement saving.
- The facilitation of high level Korean pension expertise among personnel in government, academia and interest groups and the production of a stock of policy-related pension research.

3. The overall impact of the Bank assistance has been to fast-track structural reforms to components of the pension system and to greatly increase the probability of systemic reform and the capacity of Koreans to successfully implement such reform.

1. Introduction

1.1 Korea is a high-income economy, with a 'young' but rapidly aging population. At the end of 2003, Korea's population totaled around 48 million of which 6.1 percent were over the age of 64. However, due to a combination of a dramatic drop in the birth rate (from six in 1960 to around 1.2 in 2003) and an increase in life expectancy (from 61 years at birth in the early 1970s to 74 years at birth in 2003), the population will age at a dramatic rate. The old age dependency ratio is estimated to increase from 11.6 percent in 2003, to 21.3 percent in 2020 and 62.5 percent in 2050 (see Table 1).

Table 1: Population Projections (% population)

	1996	***2003***	***2010***	***2020***	***2030***	***2040***	***2050***
Age 65 and over	6.1	7.7	10.7	15.1	23.1	30.1	34.4
Age 15 to 64	71.0	71.4	72.1	71.0	64.6	58.4	55.1
Under age 15	22.9	20.3	17.2	13.9	12.4	11.5	10.5
Old age dependency ratio	8.6	11.6	14.8	21.3	35.7	51.6	62.5

Source: Korea National Statistical Office, web site www.nso.go.kr

1.2 Korea's current pension policies are summarized in Table 2. Despite an apparently comprehensive system of retirement income provision, the policies are immature, have incomplete coverage and are generally poorly designed. Korean pension experts have been concerned about the adequacy of the Korean pension policies since the early 1990s and proposals to reform and actual reforms have been ongoing since that time.

Table 2: Pension Policies in Korea, 2004

Safety Net	Basic livelihood security (non-contributory old age pension)*		
Mandatory Public	National Pension Scheme (NPS)		Special public pension schemes
Mandatory Private	Mandatory retirement allowance	Na	Na
Voluntary	Personal pensions		
Segment of labor force	Private sector employees** (35% labor force)	All self-employed, farmers, fishermen (58% labor force)	Government employees, the military, private school teachers (7% labor force)

Notes: * Funded from general revenue; ** Except private school teachers, who are covered by a special public pension scheme.

1.3 This evaluation focuses on the pension reform activities of the World Bank in Korea over the period 1997 to 2001. The evaluation was undertaken in the first half of 2004 and included careful consideration of Bank documents (see Annex B) supplemented by interviews and follow-up correspondence with a wide range of Korean pension experts (see Annex C). The evaluation is set out as follows. Section 2 provides background in terms of the structure and performance of the Korean pension system before World Bank involvement. It also details the reforms achieved during the tenure of the Bank and discusses the preliminary results. Section 3 describes the evolution of World Bank assistance to Korea on pensions in the 1990s. The basic Bank strategy is discussed and the instruments of Bank assistance are outlined and partially evaluated. The impact of the World Bank assistance is detailed in Section 4. Following the OED framework, the Bank assistance to Korea on pension reform is assessed in terms of outcomes, institutional development impact and sustainability. Attribution of results in terms of the performance of the Bank and the borrower are discussed in Section 5. Section 6 concludes.

2. Background

The Korean Pension System in the 1990s, before World Bank Involvement

Structure of the Korean pension system in the mid 1990s

2.1 In the mid 1990s the Korean pension system included public pensions, retirement allowances (severance payments) and private pensions. Formal provision for retirement dates back to 1953 with the introduction of voluntary retirement allowances. At this time Korea had no public welfare programs so the retirement allowances were designed to provide for unemployment, saving for housing, and retirement. In 1961, retirement allowances became mandatory for large firms (with at least 30 employees), and since 1990, they have been mandatory for workplaces with at least 5 employees. The retirement allowance is equal to at least one month of salary for each year of employment (equivalent to a contribution rate of 8.3 percent), and is paid by employers in the form of a lump sum whenever a worker leaves his/her job.

2.2 The main platform of Korean retirement income provision is public pensions. These include the National Pension Scheme (NPS), introduced in 1988, and a number of special public pension schemes for government employees (introduced in 1960), the military (1963) and private school teachers (1975). Employees covered by the special public pension schemes are not covered by either the NPS or the retirement allowance scheme.

2.3 The NPS was to commence in 1974, but its introduction was deferred indefinitely following the 1973 oil price shock. When finally introduced in 1988 the NPS covered all employees (aged 18 – 60) in workplaces with 10 or more employees. The total contribution rate was three percent and around 30 percent of the labor force was covered. In 1992, the NPS was expanded to include employees in firms with 5-9 employees, and then in 1995, to farmers, fishermen and the rural self-employed. By 1996, the NPS covered around 37 percent of the labor force.

2.4 In the mid 1990s, the NPS was a partially funded DB system with a total contribution rate of six percent[1] and a target replacement rate of 70 percent of lifetime average income for average income workers with 40 years of contributions. The benefit formula was progressive (with flat-rate and earnings-related components), with higher target replacement rates for workers with below average earnings. The minimum retirement age was 60, and a minimum of 15 years of contributions was required to receive benefits. Old age pension benefits were paid in the form of price-indexed pensions. The scheme also provided for disability and survivor benefits.

2.5 For the special public pension schemes, the benefit level was set even higher at 76 percent of final income for workers with 33 years of contributions. Like the NPS,

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[1] This comprised two percent from employees and four percent from employers (including two percent from the retirement allowance reserve). The contribution rate for the self-employed was also 6 percent.

special public pensions were partially funded DB schemes, although a higher mandatory contribution rate of 13 percent applied.[2] Retirement was available at age 50 or after 20 years of contributions, and benefits were provided in the form of wage-indexed pensions. There was no portability between the NPS and the special public pensions, which covered around six percent of the labor force.

2.6 The final component of the Korean pension system of the mid-1990s consisted of the newly introduced voluntary private pensions. Since 1994, Koreans aged 18-60 had been permitted to contribute up to 12 million won each year to private pension plans. Tax concessions applied where the savings were preserved for at least 10 years and benefits could be accessed from age 55 in the form of an annuity of at least five years duration.

2.7 However, in the mid-1990s, few elderly Koreans received public or private pensions: all public pension schemes were immature, retirement allowances had only partial coverage and were rarely used for retirement purposes, there were no occupational pensions and voluntary private pensions had just commenced. In 1996, out of nearly three million Koreans over age 60, less than five percent received public pensions. Public assistance for the elderly poor was minimal, as well. Elderly Koreans generally relied on their own earnings and family support.

2.8 The structure of the Korean pension system in 1996 (and its comparison with 2003) is summarized in Annex A.

Performance of the Korean Pension System in the mid-1990s

2.9 Assessed against criteria relevant to both individual retirees and the economy as a whole, the Korean pension system of the mid-1990s performed poorly. Findings are summarized in Table 3.

2.10 For individual retirees, who are concerned about: pension coverage, adequacy, insurance against inflation and longevity, and benefit security, the pension system at that time was inadequate. In 1996, less than five percent of the elderly in Korea received any public pension and only around 170,000 persons over the age of 65 received cash or in-kind assistance through the livelihood protection program (which paid an amount of around six percent of the average wage). While around 30 percent of the labor force was covered by the retirement allowance system, these payments tended to be used to cover periods of unemployment or to start a business, rather than for retirement purposes. Further, the voluntary component of retirement income provision, personal pensions, was new, and with a minimum saving period of 10 years, it would be unable to assist with retirement provision for at least a decade. Most elderly Koreans relied upon their own income or family support. Therefore, for retirees in the mid-1990s, pension coverage was minimal, pension adequacy was low and the insurance attributes and security of pension benefits were irrelevant.

[2] This comprised a 6.5 percent employee contribution and a 6.5 percent government contribution for the government employees and military schemes and a 6.5 percent employee contribution, a four percent employer contribution and a 2.5 percent government contribution for the private school teacher’s scheme.

2.11 For future retirees, the performance of the pension system was more favorable, but still problematic. Coverage was incomplete. Even when fully mature, the public pension schemes of the mid-1990s did not cover employees in small firms (fewer than five employees) or the urban self-employed. In total, more than 50 percent of the labor force was excluded. As noted earlier, only around 30 percent of employees had access to the retirement allowance scheme.

2.12 For those covered by public pensions in the mid-1990s, retirement income would be adequate for workers with long contribution periods, as the target replacement rate for the NPS was 70 percent after 40 years of contributions, and 76 percent after 33 years for the special public pension schemes. As well, some private sector workers would also receive retirement allowances and/or may contribute to voluntary private pensions.[3] However, as few workers would really be expected to participate for 40 years, actual replacement rates would be much lower. Phang (2004) suggests that actual labor force participation is less than 30 years, due to late entry into the labor market (due to years in education and mandatory military service of 1-3 years for men) and early retirement (particularly involuntary retirement at ages 45-55).

2.13 Similarly, those covered by public pensions would be insured against inflation and longevity by the lifetime, indexed pensions provided by each of the schemes (price indexed in the case of the NPS and wage indexed for the special public pension schemes). However, with an almost universal reliance on (financially unstable) public pensions and little pre-funding of the retirement allowances, the security of future benefits could be questioned.

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[3] Moon (2001) estimates that 30 years of contributions to the retirement allowance system converts to a replacement rate of around 20 percent.

Table 3: Performance of the Korean Pension System in the mid 1990s

For Individual Retirees		
	Current retirees	***Future retirees***
Coverage	Poor	Fair, but incomplete
Adequacy	Poor, even for those covered	Adequate, for those covered
Longevity and inflation insurance	n.a	Yes, for those covered
Benefit security	n.a.	Poor
Economy-wide issues		
Inter generational equity	Poor: all public pensions financially unstable, likelihood of increased contribution rates and reduced benefits for future generations	
Intra generational equity	Poor: incomplete coverage, differential coverage within a given cohort	
Efficiency	Poor: differential (and possibly increasing) contribution rates for workers and employers, no portability between public pension schemes, early access of retirement allowances	
Capital markets	Poor: little role for the private sector, very limited private sector management of assets	

2.14 In assessing the economy-wide performance of the Korean pension system in the mid 1990s, the following criteria are considered: inter generational equity, intra generational equity, efficiency issues and capital market implications.

2.15 The financial instability associated with all the public pension schemes raised questions of *intergenerational equity*. Because the NPS had commenced in 1988, it was immature and at a phase in which contributions were growing fast and benefits were minimal. In 1996, the NPS received 4,944 billion won in contributions (1.1 percent GDP), but paid out only 1,118 billion won in benefits (0.2 percent GDP). But, due to poor design (including a mismatch between contributions and benefits and questionable fund investment practices) and a rapidly aging population, the NPS reserve fund was faced with deficit by the mid 2000s (see Table 4). Under the mid 1990s design, contribution rates would need to more than triple to maintain benefits for future generations. The special public pension schemes were in a worse financial position, with the military scheme bankrupt (since 1997) and the government employee's scheme close to bankruptcy.

2.16 The Korean pension system of the mid 1990s also performed poorly in an *intra generational* sense. As noted above, less than 50 percent of the labor force was covered by public pensions. For those covered, there were substantial differences in target replacement rates within a given cohort. Workers in small firms, the urban self-employed and those outside the formal labor force were not covered by either public pensions or retirement allowances. Workers in large firms had access to the NPS with a target replacement rate of 70 percent and possibly retirement allowances. Public sector workers and teachers participated in separate public pension schemes with a target replacement rate of 76 percent.

2.17 The Korean pension system of the mid-1990s raised a number of *efficiency* issues. Employees and employers faced differential and potentially increasing contribution rates, while labor market flexibility was hindered by the lack of portability among public pension schemes and the design of retirement allowances as a severance payment.

2.18 Finally, the impact of the pension system on the development of Korean *capital markets* was poor. The role of the private sector was minimal due to the predominance of public pensions, little pre-funding of retirement allowances, the immaturity of private pensions, the absence of a system of occupational pensions, and the directed investment of NPS reserves in public sector assets. In 1996, nearly 70 percent of NPS reserves were held in public sector assets (see Table 5), while private pension assets accounted were only 1.4 percent of GDP.

Table 4: National Pension Fund (bill won)

Year	*Contributions*	*Investment returns*	*Total revenue*	*Benefits paid*	*Accumulated Reserves*
1988	507	21	528	0.3	528
1996	4,944	1,925	6,869	1,118	21,671
2002	13,466	6,067	19,513	2,106	92,798
2010p	27,739	22,341	50,080	10,921	328,694
2020p	50,174	58,899	109,073	34,701	908,028
2047p	139,326	0	139,326	472,333	-96,159

Source: National Pension Research Center (2003), Annual Report in National Pension Fund Management. Projections from the Actuarial Estimates of the National Pension System (2003), National Pension Development Committee.

Table 5: National Pension Fund, Asset Allocation, %

Year	*Public sector*	*Welfare sector*	*Financial sector*			
			Bonds	*Cash*	*Outsourcing*	*Stock*
1988	54.6	0	11.2	34.2	0	0
1996	67.7	3.2	12.2	11.9	0	4.9
2002	32.6	0.6	60.8	0.9	1.9	3.2
2003	14.0	0.5				85.5

Source: National Pension Research Center (2002).

Korean Pension Reforms (1997-2004)

Description of major reform attempts

2.19 Consideration of, and actual reforms to, Korean pensions has been ongoing since the mid 1990s.[4] The main reforms (and attempts to reform) are summarized in Table 6. This period is characterized by parametric reforms initiated by the Korean Government and the influence of the World Bank in policy development from late 1997 to late 2000.

2.20 Since the early 1990s, Korean pension experts had been drawing attention to the structural weaknesses and financial instability of all public pension schemes (Kim and Lee 2003).[5] Similar concerns among public policymakers led to the establishment in 1997 of the National Pension Review Board (NPRB) to consider the long-term financial stability of the NPS and its relationship with the special public pension schemes. Initially the World Bank had no role in the outcome of this review as Korea had graduated from World Bank lending in 1994 and had ceased to be involved with Korean policy development. However, following Korea's request for World Bank/IMF intervention in the wake of the Asian financial crisis, the final pension reforms did reflect World Bank views. The focus of the NPRB was the long-term fiscal sustainability of the NPS.

2.21 In December 1997 the NPRB presented three proposals covering not only parametric changes, but also canvassing systemic reform. However, following public discussion, the reforms passed by the National Assembly were parametric and included: a reduction in the target replacement rate from 70 percent to 60 percent; an increase in the pensionable age from 60 to 65 (by 2033); and a reduction in the minimum contribution period from 15 to 10 years. Coverage was expanded to the urban self-employed and workers in small firms. While an increase in the contribution rate was not legislated, five-yearly actuarial projections for the NPS were mandated, with appropriate contribution rates to be considered at each review.

2.22 From 1997-2000, in the context of structural adjustment lending, the World Bank was involved in pension reform in Korea. Reforms introduced over this period included:

- Creation of a single financial regulator/supervisor (in 1997).
- Introduction of a non-contributory old age pension (in 1999).
- A phasing-out of directed investment of NPS reserves in government assets, with mandatory appropriations capped at 65 percent in 1999, 40 percent in 2000 and fully phased-out by 2001.

[4] For greater detail and commentary of recent pension reforms and proposals see Moon (2001), Sin and MacArthur (2001), Shin (2001), Yang (2001), Kim and Lee (2003), Phang (2004) and Takayama (2004).
[5] As noted in Kim and Lee (2003), a research team from the Korea Institute for Health and Social Affairs (KIHASA) published research questioning the financial viability of the public pension schemes. They estimated that the NPS would run deficits from 2028 and be bankrupt by 2039. Other papers included Min and Choi (1991) and Min and Puschra (1991).

- Establishment of a Wage Guarantee Fund, to enhance the security of retirement allowances and the introduction of retirement insurance to encourage funding of retirement allowances.
- Parametric reforms to the special public pension schemes.
- Income tax reforms to provide uniform EET taxation of retirement saving from all sources.

Table 6: Pension Reforms (and attempts to reform), 1997-2004

Year	*Reforms*
1997/98 National Pension Review Board	Parametric reforms to the NPS: reduction of target replacement rate, increase in pensionable age, reduction in the minimum contribution period, expansion in coverage to urban self-employed and workers in small firms.
1997 Financial regulation	Creation of a single financial regulator/supervisor.
1998 NPS reserves	Automatic channeling of NPS reserves to the Central Government phased-out from 1999.
1998 Retirement allowance scheme	Introduction of a Wage Guarantee Fund to improve the security of retirement allowances.
1999 Social assistance to the aged	Introduction of non-contributory old age pension benefit (the elderly pension).
1998-2000 Pension Reform Task Force	Prepared a White Paper on public and private pension reform. Overall recommendations included parametric and systemic (multi-pillar) reforms. None of the recommendations were implemented.
2000 Special public pension schemes	Parametric reforms to the special public pension schemes: increase in the contribution rate, increase in the minimum retirement age, price rather than wage indexation of benefits.
2000 Income tax reforms	Introduction of uniform EET taxation of all retirement saving, both publicly and privately provided.
2000 Retirement allowance scheme	Retirement Insurance and associated tax concessions introduced to encourage funding of retirement allowances.
2003/2004 National Pension Scheme Development Committee	Parametric reform proposals of the NPS (reduction in target replacement rate and increase in contribution rate) submitted to the National Assembly in 2003, but consideration delayed by April 2004 General Election.
2003/2004 Retirement allowance scheme	Policy proposal to convert retirement allowances into funded corporate pensions announced by Minister of Labor in 2003 and included in Minister's 2004 priorities.

2.23 Further, as a requirement of the structural adjustment lending, the Korean government established a Pension Reform Task Force (PRTF) to draft a White Paper on pension reform. The White Paper, released in August 2000, included proposals for parametric reforms to public and private pensions and systemic reform. However, its release coincided with the Korean government's final redemption of IMF/World Bank loan repayments, which reduced the influence of the World Bank on Korean policy. The Korean government never officially considered the recommendations of the White Paper.

2.24 In the post World Bank era, Korea has continued along the path of pension reform. However, reforms have fallen short of the systemic (multi-pillar) reforms advocated by the Bank and in the Korean proposals recommended in the 2000 White Paper.

2.25 In March 2002 the Ministry of Health and Welfare (the Ministry responsible for the NPS) established the National Pension Scheme Development Committee to prepare five-yearly actuarial estimates of the NPS (as required under the 1998 reforms) and consider options for reform. The actuarial projections showed that if the current NPS format were kept unchanged, the scheme would run into deficit from 2036 and be depleted in 2047 (see Table 4). To ensure financial stability the contribution rate would need to be raised to 39.1 percent by 2070 (Yun 2004). However, systemic reform was ruled out and the final proposal submitted to the National Assembly in October 2003 involved a reduction of the target replacement rate from 60 percent to 50 percent and a gradual increase in the contribution rate from 9 percent to 15.9 percent. Consideration of these proposals by the National Assembly is pending having been delayed by the general election in April 2004.[6]

2.26 Further, in September 2003, the Ministry of Labor released a proposal for the conversion of the retirement allowance scheme into a corporate pension scheme. Proposed features include voluntary conversion of retirement allowances to funded corporate pensions, an increase in coverage to all employees and the self-employed and accrued benefits to be fully portable and paid as annuities from age 55. The policies are included in the 2004 Labor Policies of the Minister of Labor and will be considered by the National Assembly in 2004.[7]

2.27 Therefore, it is likely that 2004 will see parametric reforms to the NPS and possibly the creation of a second pillar with the conversion of retirement allowances to corporate pensions. Further reforms of public and private pensions are still on the policy agenda with government committees considering a range of reform issues including professional funds management of the NPS reserves, universal coverage of the NPS, portability between all public pension schemes, and systemic reform towards multi-pillar pension arrangements.

Support and reaction of the public, interest groups, politicians and others

2.28 Support for the parametric reforms introduced over the period 1997-2004 has been mixed. The general public are confused by the policy debates and do not really understand the issues associated with alternative policy design or the concepts such as 'funding', multi-pillar' or similar language (Kim and Lee 2003). Public information has been influenced by the mass media that have emphasized the financial problems of the NPS and the reduction in target benefits.

2.29 Among the interest groups, the labor organizations are most critical of current pension policy design and the parametric reforms that increase contributions but reduce

[6] For details of proposals put forward see Kim and Lee (2003), Phang (2004) and Yun (2004).
[7] See Hur (2003), Kim Dae Hwan (2004) and Phang (2004).

benefits. They are concerned that current policies do not adequately cover the poor and advocate greater, rather than less, public provision of pensions. They favor a two-tier NPS, with a basic pension for all aged persons and an earning-related component for contributors and suggest that the future financing problems of the NPS could be addressed by higher contributions from high-income earners. The labor organizations do not consider retirement allowances as a retirement income pillar, but a reward for service to be used in times of unemployment, and do not support their conversion to privately managed funded corporate pensions.[8]

2.30 On the other hand, the employer groups accept the parametric reforms to reduce target benefits, but are concerned about the impact of increased NPS contribution rates on labor costs. They would prefer that the NPS contribution rate remained at nine percent rather than be increased to 15.9 percent as envisaged by the current reform proposals. Similarly they are concerned about the impact on labor costs of the proposed conversion of retirement allowances to funded corporate pensions.[9]

2.31 Consumer groups are particularly concerned about the welfare of the poor and are prepared to accept lower target replacement rates provided pension policies cover the poor. They have expressed concern about the costs and complexity of private pensions based on their experience of insurance products.[10]

2.32 Academics and researchers have been supportive of both the actual parametric reforms (and the multi-pillar reforms canvassed) and have participated in the public debate with detailed policy proposals (see, for example, Moon 2001, Kim and Lee 2003, Phang 2004).

2.33 Support of politicians and their Ministries has been mixed. Since responsibility for pension policies covers several ministries, there has been politics at play. In particular, the Ministry of Health and Welfare, the ministry responsible for the NPS, has historically opposed systemic reforms, which would reduce the role of the NPS. However, with the increased profile given to multi-pillar pension provision following the involvement of the World Bank in 1997-2000 and the broad based participation in the Pension Reform Task Force, systemic reform is now gaining wider acceptance from politicians and their policy advisers.[11]

Preliminary results of the reforms

2.34 The pension reforms over the period 1997-2003 included parametric reforms to the NPS and the special public pensions, the introduction of a non-contributory old age pension, improved management of NPS reserves through the elimination of directed public-sector investments, some funding of retirement allowances, the establishment of a

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[8] Based on discussions with the Korean Council of Trade Unions (KCTU).

[9] In discussions with the Korean Employers Federation (KEF), concerns included the extension of coverage to small employers and the pre funding required for corporate pensions.

[10] Based on discussions with the Consumers Union of Korea.

[11] As suggested in discussions with officials from the Ministry of Health and Welfare, the Ministry of Finance and Economy and the Ministry of Planning and Budget.

single financial regulator and the consistent taxation of retirement incomes. Systemic reform has not yet been achieved, but nor has it been unequivocally rejected.

2.35 For current retirees, the main impact is the introduction of non-contributory age pension (the elderly pension). This is paid to elderly Koreans subject to an income threshold of 523,000 won per month and a property threshold of 50 million won. In 2003, nearly 16 percent of Koreans over the age of 65 received the elderly pension, at an average amount of 346,000 won. Current retirees or those near to retirement benefit from the reduction in the minimum contribution period of the NPS from 15 to 10 years. For future retirees, the performance of the pension system is still problematic. Coverage of public pensions has increased from around 45 percent to over 80 percent of the labor force – due to the extension of the public pension system to the urban self-employed and workers in small companies - but is still short of universal. The unemployed and persons not in the labor force remain outside the public pension system.

2.36 Despite a reduction in the target replacement rate under the NPS from 70 percent to 60 percent, adequacy remains satisfactory for those with sufficiently long contribution periods. However, few Koreans are expected to contribute for the maximum period. As noted earlier, Phang (2004) suggests that actual contribution periods are closer to 30 years. Even if workers have access to retirement allowances, it is unlikely that they will be used for retirement purposes.[12] Benefit security is still compromised by heavy reliance on (financially unstable) public pensions and largely unfunded retirement allowances. While these problems would be alleviated if the National Assembly passed the current NPS and retirement allowance reforms, the uneven reliance on public provision for retirement would remain.

2.37 The performance of the retirement income system in terms of the economy as a whole also remains poor. Intergenerational inequity remains due to the financial instability of all public pension schemes. The government employee’s pension scheme went into deficit in 2001, while the teacher’s pension scheme is projected to go into deficit in 2012 and be depleted by 2018. Projections from the National Pension Corporation indicate that if the NPS scheme remains unchanged it will move into deficit in 2036 and be bankrupt by 2070. The current policy proposals to address the financial problems of the NPS advocate a further increase in the contribution rate to 15.9 percent (from three percent in 1988, six percent in 1993 and ninc percent in 1998). Intra-generational equity issues remain while coverage is less than universal, non-compliance is rife and differing schemes continue to apply across different segments of the labor force. (It is estimated that up to 50 percent of the self-employed under-report their incomes and a substantial number do not comply at all). Efficiency issues remain due to high and increasing contribution rates for employees and employers (from three percent in 1998 to a proposed 15.9 percent), and labor market inflexibility remains due to an

[12] A survey of unemployed persons conducted by the Korean Labor Institute indicates those for those in receipt of the retirement allowance, 44 percent use it for living expenses, 11 percent for children related expenses (education and marriage), 6.6 percent for housing and 5.7 percent for business (Phang 2002).

absence of portability among public pension schemes and the availability of retirement allowances as severance payments not contingent on retirement.[13]

2.38 There have, however, been some developments in the role of the private sector in Korean pensions. The elimination of mandatory public sector investment of NPS reserves, has led to an increase in private sector assets held by the NPS from 30 percent in 1996 to nearly 86 percent in 2003 across a range of bonds, stocks and international assets. As well, there has been a four-fold increase in private pension assets since 1996 to 206.3 billion won (or 3.8 percent of GDP), while retirement insurance, introduced in 2000 as a means of funding retirement allowances, now totals 2.4 percent of GDP. Further benefits would be expected if and when the proposals are passed to convert retirement allowances to funded privately managed corporate pensions.[14] However, while public pensions remain the centerpiece of Korean pension policy, concerns about the growing size of the NPS reserves (projected to reach 50 percent of GDP at its peak, Kim Youngha 2004) on Korean capital markets remain.

[13] Although this latter issue would be addressed had the Minister of Labor's proposals to convert retirement allowances into funded corporate pensions been passed by the National Assembly.
[14] Around 40 percent of retirement allowances are unfunded or under funded (Phang 2002).

3. Evolution of World Bank Assistance to Korea in the 1990s

Genesis of World Bank Involvement

3.1 By 1990, Korea's per capita income had passed the World Bank guidelines for graduation from Bank lending, and in 1991, Korea and the World Bank agreed on a four-year graduation plan. Over this period, World Bank funding was limited to small projects in areas of mutual interest.[15] In 1994, Korea graduated from Bank lending, and the World Bank office in Seoul closed.

3.2 However, in 1997, a financial crisis spread across Asia, and by late 1997, the Korean economy faced severe difficulties. The exchange rate had depreciated by 50 percent against the US dollar, real interest rates rose to around 30 percent, and the government was having difficulties financing an external debt of US$120 billion, of which around 50 percent was short term debt and US$20 billion was due by the end of that year. In November 1997, the Korean Government formally asked the IMF/World Bank for assistance.

3.3 At that time, the World Bank no longer had an office in Seoul and was not conducting economic and sector work on Korea, as would have been the case had Korea been an active borrower. However, using existing World Bank staff expertise on Korea, their prior knowledge of the Korean economy, and the experience of other countries affected by the East Asian Financial Crisis, an Economic Reconstruction Loan was developed in the short period between the initial request for Bank assistance on 17 November 1997 and the loan approval on 23 December 1997. This was both the largest and fastest loan made in the history of the Bank. It was broadly agreed that Korea's economic problems did not stem from poor macroeconomic fundamentals, but from structural deficiencies in the financial and corporate sectors.

3.4 The World Bank agreed to recommence lending to Korea with up to US$10 billion to support structural reforms. This led to Bank assistance in the area of pension reform as part of three structural adjustments loans (one in 1997 and two in 1998), as well as technical assistance (funded by the ASEM trust fund) and policy advice (in the form of an analytical pension reform paper prepared by the World Bank).

3.5 World Bank assistance was both demand and supply driven. It was demand driven in the sense that the Korean government had made the initial request for assistance, and supply driven to the extent that the specific pension reforms required were developed by Bank (in conjunction with the Korean government). It is emphasized, however, that pension reform was only a small part of the structural reforms required under the structural adjustment loans.

[15] This included a US$100 million loan to provide technical assistance to the Korean government and the Bank of Korea to develop a program of structural reform in the financial sector.

3.6 An overview of the required pension reforms and the recommended policy measures (see World Bank 2000) indicates some influence of *Averting the Old Age Crisis* (1994). Both support consideration of multi-pillar approach based on a balance of public and private pensions.

3.7 Since the assistance took the form of large structural adjustment loans, the counterparts were at the highest level (Head of Government and Ministerial Heads), and this continued throughout.

Description of World Bank Assistance

3.8 The basic strategy towards pension reform was as a component of broader structural reforms. As noted earlier, it was agreed that Korea's macroeconomic and financial problems resulted from structural deficiencies in the financial and corporate sector and in relation to labor markets and the social safety net. As a result, the focus of the pension reforms was long-term structural change. However, the structural adjustment lending also recognized the immediate impact of the Asian financial crisis on the current aged.

The Instruments of World Bank Assistance

3.9 The World Bank assistance included three structural adjustment loans, technical assistance funded from an ASEM grant and an analytical pension policy reform paper (see Table 7). The analytical paper was officially released after the third structural adjustment loan had closed, but the analytical work of earlier drafts had been used to design the pension components of the reforms required as part of the structural adjustment lending.

3.10 The main structural adjustment loan relevant to pension reforms was Structural Adjustment Loan 2 (SAL 2). This included a detailed policy matrix but few conditional reforms. World Bank documents are listed in Annex B.

Economic Reconstruction Loan

3.11 A US$3 billion Economic Reconstruction Loan (ERL), approved on December 23 1997, was the first phase of the renewed World Bank assistance to Korea. The objectives of the ERL were to provide emergency liquidity to restore confidence in the Korean economy and to develop a framework for medium term structural reform that would serve as a basis for a program of structural adjustment lending. The agreed agenda of structural reforms included financial sector restructuring, corporate governance, competition policy and labor markets and social safety nets (including pensions), to be funded by subsequent Structural Adjustment Loans of up to US$7 billion. Two further structural adjustment loans were made, SAL 1 and SAL 2. A final structural adjustment loan had been planned for 2000, but was not implemented.

3.12 The most significant result in the short term was enabling Korea to avoid default of debt repayments. However, progress was also made on the financial sector reforms including the merging four separate supervisory agencies into a single agency – the

Financial Supervisory Service (FSS) - independent of both the Bank of Korea and the Ministry of Finance and Economy. In terms of specific pension reforms, the main achievement was the commitment to introduce a non-contributory means-tested social pension for the elderly (65 and over)

Structural Adjustment Loan 1

3.13 A subsequent structural adjustment loan (SAL 1) was approved on March 26 1998, to provide for US$2 billion of lending for immediate foreign exchange assistance and longer term financial sector restructuring and development, corporate sector reform, labor market reform and strengthening of social safety nets. Pension policy measures required under SAL 1 included the introduction of a non-contributory pension for the elderly and longer-term reforms including wider pension coverage of the NPS and improved fund management of NPS reserves. However, the second Structural Adjustment Loan (SAL 2) was far more comprehensive in relation to pension reforms.

Structural Adjustment Loan 2

3.14 A Second Structural Adjustment loan (SAL 2) was approved on October 22 1998. This comprised US$2 billion in two tranches. The first US$1billion was released on October, 23 1998 and second (released on May 11 1999) was conditional upon satisfactory implementation of the reform process. The aim of SAL 2 was to build upon the progress made in SAL 1, by deepening reforms in three key areas: (i) financial sector restructuring, including the resolution of weak financial institutions, improvement of prudential regulation and supervision and capital market development. (ii) corporate sector reform, including corporate debt restructuring, improvements in corporate governance and competition policies, and reform and privatization of state-owned corporations, and (iii) enhancement of labor market flexibility and strengthening of social safety nets. In relation to pension reform, the SAL 2 policy matrix included detailed objectives and policy measures. Of these, the objective to 'achieve a more efficient allocation of National Pension Fund assets' was one of 12 conditional policy measures for the release of the second tranche.

3.15 The main short-term impact of SAL 2 was considered to be the averting of a possible secondary macro/financial crisis and the resulting economic recovery that was far stronger than market expectations. For the longer term, the structural reforms supported by SAL 2 addressed key structural and institutional deficiencies in the Korean economy. In relation to safety nets and pensions, the main accomplishment was considered to be the establishment of a reform process to achieve a modern welfare state within a Korean context.

Table 7: Instruments of World Bank Assistance

Instrument	***Timing***	***Main objectives***	***Ratings****
Economic Reconstruction Loan (ERL) US$3 billion	Approved December 23, 1997 Closed February 28, 1998	To provide emergency liquidity to restore confidence in the Korean economy and develop a framework for medium term structural reform to serve as a basis for a program of structural adjustment lending	Satisfactory
Structural Adjustment Loan 1 (SAL 1) US$2 billion	Approved March 26, 1998 Closed August 31, 1998	Immediate foreign exchange assistance and establish conditionality for areas of the ERL covering: financial sector restructuring, corporate governance, competition, labor markets and safety nets and institutional reform in economic policy management. Pension policy measures under SAL 1 included the introduction of a non-contributory pension for persons aged 65 and over and longer-term reforms including wider pension coverage and improved fund management of the NPS fund.	Satisfactory
Structural Adjustment Loan 2 (SAL 2) US$2 billion	Approved October 22, 1998 and released in two tranches: US$1 bill on October 23, 1998 and US$1 bill on May 11, 1999 Closed June 30, 1999	To deepen structural reforms in the financial sector, corporate sector, labor market and social safety nets. The pension reform objectives included to: mitigate the impact of the financial crisis on the living standards of the elderly; improve the transparency and governance of all public pension schemes; develop an integrated pension reform proposal; and achieve a more efficient allocation of National Pension Fund assets.	Satisfactory
ASEM Grant for Social Protection of the Elderly (Project ID No PP064185) US$870,000	Approved July 1998 Closed June 30, 2001	To provide technical assistance to help with implementation of SAL 2 including supporting the ongoing work of the Pension Reform Task Force, and improving the fund management capacity of the National Pension Corporation.	Satisfactory
Policy advice paper 'Republic of Korea: The Korean Pension System at the Crossroads' (World Bank 2000)	Final version, May 2000	To provide analytically sound pension policy recommendations to be used to formulate the pension component of the SAL 2 policy matrix and provide background analysis for the Pension Reform Task Force (required under SAL 2).	N.A.

3.16 The specific pension policy measures required under SAL 2 and the subsequent outcomes shows that success was mixed. The impact of the financial crisis on the living standards of the aged was addressed with the introduction of a non-contributory age pension in 1999. However, the objective to improve the transparency and governance of all public pension schemes through the creation of an office of the actuary and subsequent actuarial projections of all public pension schemes was only partially achieved. The position of government actuary was not created, although five–yearly actuarial projections are now required for the NPS and the special public pension schemes.[16] While the conditional policy objective to achieve a more efficient allocation of NPS reserves through a phasing-out of mandatory appropriations to the public sector was achieved, the additional measure to improve the management and governance of the National Pension Fund (through professional asset management) is still under consideration.

3.17 Finally, the objective to 'develop an integrated pension reform proposal' was only partially achieved to the extent that proposals were developed, but not implemented. A government task force was established and it did produce the required White Paper on pension reform. However, this White Paper was completed nearly 12 months behind schedule and its release coincided with the withdrawal of the World Bank from Korea (and therefore the influence of the Bank on Korean pension policy).

Technical Assistance

3.18 The ASEM Grant for Social Protection of the Elderly was a technical assistance grant (of US$870,000) designed to provide ongoing support for the Pension Reform Task Force (established under SAL 2) and to improve the fund management capacity of the National Pension Corporation (a conditional policy measure under SAL 2). This was one of a number of grants funded from the ASEM-EU Asian Financial Crisis response Fund. Other grants were used to fund poverty alleviation projects in China, Indonesia, Malaysia, Thailand, the Philippines and Vietnam. The World Bank managed the ASEM grant and the activities it funded are summarized in Table 8.

Table 8: ASEM Grant for Social Protection of the Elderly

Objectives	***Activities***
• Ongoing support for Pension Reform Task Force (which was required under SAL 2 to produce a White Paper). • Improvement in the fund management capacity of the National Pension Corporation.	• 1 week workshop, training on World Bank pension modeling software, PROST (Seoul, October 1999). • 2 day workshop sponsored by the World Bank and the FSS, International Workshop on Private Pension Design and Supervision. Private pension regulators from several OECD countries and Hong Kong presented their supervisory strategy and interacted with Korean regulators. (Seoul, December 1999). • Workshop on public pension fund governance, (Cheju Island, October 2000). • Workshop on private pensions, (Hong Kong, March 2001). • Funded background studies, training programs (including study tours) and workshops, to assist the Pension Reform Task Force.

Source: ASEM Trust Fund.

3.19 The ASEM grant achieved its objectives by fostering an appreciation of international best practice among government officials and Korean pension analysts and

[16] The NPS projections are carried out by the National Pension Research Corporation, with the assistance of academics.

facilitating the production of concrete proposals for reform of both private and public pensions. While, with limited exceptions, the government has not adopted the proposals, the technical assistance has contributed to the development of a core group of Korean experts engaged in a long-term policy dialogue about pension reform. The overall rating of the technical assistance provided under the ASEM grant was satisfactory (see ASEM Trust Fund Implementation Completion Report).

Policy Advice Paper

3.20 The final assistance provided to Korea was via an analytical policy advice paper (World Bank 2000). The context of this paper was to inform the pension reform components of the SAL 2 policy matrix and to provide an analytical background for the Korean Government's Pension Reform Task Force (required under SAL 2 to produce a White Paper on pension reform). While the final version of this paper was released in May 2000, associated background analysis was used in policy development in 1998 and 1999. The pension reform recommendations developed in this paper are summarized in Table 9.

3.21 The policy recommendations include both parametric and systemic pension reforms. The aim of the parametric reforms were to address the financial instability of all public pension schemes and to promote the development of Korean capital markets through improved management of the NPS fund and the restructuring of the retirement allowance scheme. However, the focus was systemic reform to multi-pillar pension provision. It was argued that this could be achieved by merging all public pension schemes, reducing the target replacement rate from public pensions and expanding pension coverage, converting retirement allowances to fully funded private pensions, and encouraging personal pensions through improved regulation and supervision. The recommendations envisaged a multi-pillar framework for retirement provision comprising: an earnings-related (but redistributive) public pension, mandatory externally funded DC corporate pensions and voluntary personal pensions, as well as a non-contributory public pension financed from general revenues for the elderly poor (see World Bank 2000).

3.22 In advocating systemic reform, the World Bank argued that it would address risk diversification (and therefore benefit security) by spreading risk across public and private sectors (as new entrants would receive roughly half of their retirement benefits from the NPS and half from private pensions). Intra generational inequity would be addressed through the greater uniformity of target replacement rates (to around 60 percent in total) and intergenerational equity would be enhanced (and the burden on future generations reduced) by the improved financial sustainability of all public pensions. Finally, the combination of the recommended measures would alleviate pressure on payroll taxes and assist the development of a private pension industry.

3.23 While systemic pension reform was not achieved during the tenure of the Bank in Korea (1997-2000) or since, the analysis and recommendations for reform developed in the Bank's policy advice paper played a major role in informing the deliberations and output of the Pension Reform Task Force and have continued to influence the Korean policy debate.

Table 9: Recommendations for Reform, World Bank Policy Advice Paper*

Recommendations	***Results***
<u>Parametric reforms</u>	
Safety net: Expand the livelihood protection scheme for the current elderly	Achieved. An elderly pension (funded from general revenues) was introduced in 1999 for the old aged with low income who are excluded from the NPS.
Retirement allowances: Convert the retirement allowance scheme into a modern private pension system with external private fund management and strong regulatory oversight.	Partially achieved. Policy proposals to convert retirement allowances to corporate pensions on a voluntary basis announced by Minister of Labor in 2003. To be considered by the National Assembly in 2004.
National Pension Scheme: Reconsider benefit targets and improve the management and governance of the National Pension Scheme Reserves.	Partly achieved. Policy proposals announced in 2003 include an increase in the contribution rate and a reduction in the target replacement rate. Consideration by the National Assembly delayed by April 2004 election. Government committees are currently considering professional management of NPs reserves, and the expansion of coverage.
Special public pensions. Parametric reform of the special public pension schemes with the aim of achieving financial balance.	Partially achieved. Parametric reforms to the special public pension schemes in 2000 included an increase in the contribution rate, an increase in the pensionable age and price rather than wage indexation of benefits. However the long-term financial imbalance was not addressed. Portability between all public pension schemes is under consideration by a government committee.
Contractual savings. Strengthen the regulation and supervision of contractual savings' including licensing criteria for pension fund managers, increased monitoring and enforcement, development of asset allocation and risk concentration parameters, strengthening of public financial disclosure and a review of the tax treatment of contractual savings.	Some policy developments. Uniform (EET) taxation of all retirement saving introduced in 2000.
<u>Systemic reforms</u>	
Create a multi-pillar framework for retirement provision (with a unified public pension, mandatory externally funded DC private pensions and voluntary personal pensions) by: merging all public pension schemes and reducing target benefits and contributions; converting the retirement allowance scheme to a broad coverage DC private pension scheme; and encouraging private pensions through improved regulation and supervision.	Not achieved.

Notes: * For detail, see World Bank (2000).

4. Assessment of the Impact of World Bank Assistance

4.1 Following the OED framework, the Bank assistance to Korea on pension reforms is assessed in terms of outcomes (relevance and efficacy), institutional development impact and sustainability and in terms of Bank and borrower performance. Ratings for each are summarized in Table 10.

Outcomes

Relevance

4.2 Relevance refers to the extent to which the objectives of the overall assistance and the individual projects were consistent with the country's initial conditions, needs and development priorities.

4.3 The objectives of the overall pension reform assistance to Korea, provided through the structural adjustment lending, technical assistance and policy advice were three-fold:

- To address the immediate problem of poverty among the aged;
- To address structural problems evident in the public pension schemes; and
- To facilitate systemic reform of the pension system to a multi-pillar arrangement, to be driven by the Koreans but supported by the Bank through technical assistance and policy advice.

4.4 At that time, Korea was a high-income developed economy but had been severely affected by the Asian financial crisis and was unable to service its short-term debt. It was agreed that Korea's fundamental economic problems related to structural deficiencies and were best addressed through structural adjustment lending. The pension system was immature, poorly designed with undue emphasis on public provision, and provided little coverage to the current elderly. In this context the pension reform objectives were well designed and relevant. Poverty among the elderly due to the financial crisis was addressed first, followed by structural problems in the public pension schemes, with consideration of systemic reform left to last. This was appropriate in both design and sequencing. Pension coverage of current retirees was particularly low (with less than five percent of persons over the age of 60 in receipt of public pensions or social assistance) and this cohort had been particularly hard hit by the Asian financial crisis. Further, the structural problems of the NPS, which involved mandatory investment in public sector assets and the lack of any independent actuarial estimates, could be addressed fairly quickly.

4.5 All components of the pension system were considered, whether directly through policy reforms required under the structural adjustment loans, or indirectly via the Korean Pension Reform Task Force, or the supplementary policy advice provided by the Bank (as detailed in World Bank 2000).

4.6 Reforms of both the zero and first pillars were addressed in the policy matrix developed for the structural adjustment lending (specifically SAL 2) through the introduction of a non-contributory pension for the current elderly and reforms to improve the financial stability of the various public pension schemes and to ensure a more efficient asset allocation of National Pension Fund reserves.

4.7 While structural reforms to other components of the pension system and systemic reform were not specifically addressed, the policy matrix (developed for SAL 2) required them to be reviewed. Here the Bank's approach was to facilitate and support Korean driven reform. The Korean government was required to establish a Pension Reform Task Force, with broad membership (including representatives from government ministries, public pension corporations, research institutes, labor unions and employer groups), to produce a White Paper on public and private pension reform. The Bank then supported the Task Force through technical assistance provided under an ASEM grant and policy reform analysis and recommendations via a policy advice paper (World Bank 2000). The technical assistance included conferences, workshops and background studies (see Table 9) all of which exposed Korean pension experts to international best practice and provided training in the latest analytical techniques.

4.8 The design of this strategy for assistance suggests that the Bank had an open attitude and took into account the initial situation in Korea as well as Korea's specific needs. The structure of the SAL 2 policy matrix and the recommendations of the policy advice paper (World Bank 2000) suggest that the broad idea to move towards multi-pillar pension arrangements had been informed by *Averting the Old Age Crisis*. However, the Bank played the role of educating and advising the Koreans, rather than prescribing the future policy direction. Importantly, this ensured that the Koreans had ownership of any subsequent reforms. And, if and when systemic reform was achieved, it would do so with support of Korean policymakers, interest groups and the general public.

4.9 The quality of the analytical advice underpinning the World Bank projects was mixed. When the Korean government requested emergency intervention by the World Bank in late 1997, Korea had graduated from Bank lending and the World Bank no longer had an office in Seoul nor had been undertaking analytical work on Korea. However, the time constraints of the structural adjustment loans meant that a policy matrix had to be developed quickly. The Bank overcame these challenges in a number of ways. First, the Bank assembled a team with prior experience of the Korean economy and of other countries affected by the Asian financial crisis. Second, the Bank left the detail of the required pension reforms until SAL 2, by which time some analytical work had been carried out. Finally, the Bank provided guidelines and guidance, but leaving the exact design of any systemic reform to the Korean Pension Reform Task Force.

4.10 The Bank supported the Pension Reform Task Force through technical assistance and policy advice. The Bank's policy recommendations as published in the policy advice paper 'Republic of Korea: The Korean Pension System at the Crossroads' are summarized in Table 10. As with the structural adjustment lending, the approach was not to prescribe systemic reform. Instead, the Bank paper presented a sequence of structural reforms, which could be coordinated into a multi-pillar framework.

4.11 The overall quality of the reforms recommended in this paper was good, and the policy advice was well researched and supported by PROST modeling. The recommendations included structural reforms to all components of the retirement income system: the zero pillar in the form of increased social assistance to the existing elderly poor; the first (public pillar) by merging all public pension schemes and reducing contribution rates (to 4.5 percent) and target benefits (to 30 percent); the second (private mandatory) pillar through conversion of existing retirement allowance to DC corporate pensions (funded by an eight percent contribution) and increasing coverage to the entire labor force; and the third (voluntary) pillar by improving the coverage, safety and security of personal pensions. These reforms would combine to create multi-pillar pension provision, providing an overall target replacement rate of 60 percent. Redistribution would be enhanced through the proposed improvements in coverage of the public pensions (and redesign of the benefit formula to include a basic pension for all). Efficiency would be enhanced through the changes to the asset management and governance of the NPS (such as eliminating mandatory public sector investments), the reduction of the size of the NPS fund, portability between public pension schemes and redesign of the retirement allowance system away from a severance payment to funded corporate pensions.

4.12 In terms of the specific reforms recommended in this paper, the PAYG reforms were not overly ambitious, as the NPS was immature and in the fortunate position of having many contributors but few pensioners. While the special public pension schemes were already bankrupt or close to bankruptcy, they covered only six percent of the labor force. The Bank's actuarial projections showed a bringing forward of the deficit of the NPS due to lower contributions, but a large reduction in the fiscal imbalance facing future generations. Therefore, transition would be fairly uncomplicated. The Bank's analytical paper also provided advice on the management of the NPS reserves, drawing on its own analysis and international experience. The suggested second pillar reforms, which involved converting the current largely unfunded retirement allowance system to funded DC corporate pensions, were supported by analysis and discussion of international experience. Some guidance for sequencing of the necessary policy reforms for both the second pillar and possible expansion of the third pillar was also presented.[17]

4.13 In conclusion, the objectives of the overall assistance and the individual projects were consistent with the initial conditions, needs and development priorities of Korea. They were well structured and sequenced to facilitate well-informed Korean proposals for pension reform. ***The overall rating for relevance is high***, that is, most of the objectives were highly relevant.

[17] As noted earlier, the World Bank withdrew from Korea (a second time) in 2000. However, in 2003 the Minister for Labor released a policy involving the conversion of the retirement allowance schemes to a system of funded corporate pensions. While this was a Korean initiative, it draws on the design proposed by the World Bank in the 2000 policy advice paper, and the recommendations of the 1999-2001 Korean Pension Reform Task Force.

Efficacy

4.14 The issue here is the extent to which the objectives of the Bank assistance were achieved. The broad objectives of the overall pension reform assistance were to: address the immediate problem of poverty among the aged; address structural problems evident in the public pension schemes; and facilitate systemic reform of the pension system to a multi-pillar arrangement, to be driven by the Koreans but supported by the Bank through technical assistance and policy advice. Many of the pension reform objectives of the Bank were achieved, some were partially achieved and others were not achieved, either during or since the duration of the Bank's assistance.

4.15 To address poverty among the aged, a non-contributory pension was introduced for the current elderly poor in 1999. In the mid 1990s, less than five percent of Koreans age 65 and over received a public pension, and only six percent received cash or in-kind assistance through the livelihood protection program. In 2003 nearly 16 percent of elderly Koreans received the non-contributory pension at an average rate of 346,000 won per month. At the same time, however, the NPS has matured. In 2003, 1,171 million Koreans received a pension from the NPS.

4.16 The objective to address structural problems evident in the public pension schemes had two components: first, to improve the transparency and governance of all public pension schemes; and second, to achieve a more efficient allocation of NPS reserves. Both objectives were partially achieved. Five-yearly actuarial projections are now conducted for all public pension schemes, most recently for the NPS in 2003 and for the special public pensions in 2000. However, the office of a government actuary was not established. Instead, the relevant pension fund corporations carry out the actuarial projections, with the assistance of academics. The phased reduction of mandatory investment of NPS reserves in public-sector assets was a conditional policy reform under SAL 2, and was achieved over the period 1999 to 2002. Since 1996, the proportion of NPS reserves invested in public assets has fallen from 70 percent to 14.5 percent in 2003 (see Table 5). Other policy requirements under SAL 2 involved moving to professional external asset management of the public pension funds. This has not been implemented, but is under consideration by a government committee.

4.17 Finally, the objective to develop an integrated pension reform proposal 'that fully recognizes and rationalizes the mandatory public and private components of the existing system' was partially achieved. A Korean Pension Reform Task Force was established and produced the required White Paper on integrated pension reform in late 2001. However, the timing was such that its release coincided with Korea's final repayment of the structural adjustment loans and therefore the withdrawal of the World Bank from Korea, so the proposals were not acted upon at that time. However, the Korean pension expertise built up throughout the period of World Bank involvement (1997-2000) has been instrumental in framing recent pension reforms and proposals and gaining support for systemic pension reform.

4.18 For example, during the tenure of the World Bank in Korea (1997-2000), a number of pension reforms were implemented that had not been specifically included as requirements for the structural adjustment lending. These included parametric reforms to the NPS and the special public pensions, the introduction of retirement insurance to encourage funding of retirement allowances, and income tax reforms to provide uniform EET taxation of all retirement savings.

4.19 Moreover, consideration and debate of pension reform proposals has been ongoing since that time within the bureaucracy, and among academics and interest groups. In 2003, proposals were announced by the Minister for Health and Welfare for parametric reforms of the NPS and by the Minister for Labor for structural reforms to convert the retirement allowance system to funded corporate pensions. Both are expected to be considered by the National Assembly in 2004. Government committees are currently investigating a range of issues including management of NPS reserves, restructuring the NPS to ensure universal coverage, portability among all public pension schemes and the introduction of multi-pillar pension provision. Many policymakers and academics now support systemic pension reforms, although there is less support from employer organizations and little support from labor unions.

4.20 The overall impact of reforms introduced either directly or indirectly as a result of World Bank influence has been positive. In terms of individuals, public pension coverage has almost doubled to 80 percent since the mid 1990s, and as a result of parametric reforms the financial stability of all public pension schemes has improved. However, compliance is still a problem amongst the self-employed with close to 50 percent either exempt or under-reporting their income for NPS purposes (Phang 2004). Retirement income adequacy will be improved further if the National Assembly passes the proposals to convert retirement allowances to funded corporate pensions (and expand coverage to the entire labor force).

4.21 Benefit security has been enhanced by structural reforms to all public pension schemes, particularly the requirement for frequent actuarial reviews, the discontinuation of mandatory investment in public sector assets, and the overall reforms to improve the regulation and supervision of the financial sector. However, the retirement allowance scheme is still largely unfunded. The efficiency of the NPS will be improved further if it moves to professional asset management (currently under consideration by government).

4.22 In terms of the economy as a whole, the World Bank involvement has had a number of positive results including: some improvement in inter-generational equity and the financial stability of public pensions (with the higher contribution rates and reduced target replacement rates); and some improvement in intra-generational equity (with the increased coverage of the NPS and the introduction of a non-contributory elderly pension). However, the pension reforms introduced as a direct result of World Bank assistance have had only a minor impact on the private pensions industry. Voluntary private pensions were introduced in Korea in 1996 (before the re-entry of the Bank) and a funded second pillar has not yet been introduced. World Bank related pension initiatives that have impacted the private sector include the introduction of a uniform EET tax treatment of retirement saving, the introduction of retirement insurance to encourage funding of retirement allowances, and the increase in private sector assets held by the National Pension Fund. Private pension and externally funded retirement allowance assets increased from 1.4 percent of GDP in 1996 to 6.2 percent of GDP in 2003. A further impact would be expected if the current proposal to convert the retirement allowance scheme to fully funded corporate pensions materializes. However, as a whole the pension system still suffers from over-reliance on public pensions, which compromises the security of Korean retirement benefits and has limited the impact of the pension system on the development of Korean capital markets.

4.23 ***The overall rating for efficacy is substantial***. The major objectives were met, or were expected to be met, with only minor shortcomings. The immediate objective of alleviating poverty amongst the elderly was achieved with the introduction of a non-contributory age pension, and the short-term objective of structural change to the NPS was partially achieved with the introduction of actuarial projections, the phase-out of directed investment in the public sector and parametric reforms. During the tenure of the Bank, parametric reforms were made to the other public pension schemes, a mechanism for pre funding was introduced for retirement allowances and EET taxation was introduced for all retirement saving. The shortcoming was that White Paper outlining multi-pillar recommendations had no immediate policy impact. However, this is mitigated by the increased Korean expertise in pension reform, through broadly based participation in the Pension Reform Task Force and access to the technical assistance provided under the ASEM grant. The ideas canvassed in the World Bank initiated pension reform proposals continue to be considered in policy debates.

4.24 ***The overall rating for outcome is satisfactory*** – that is, high for relevance and substantial for efficacy.

Institutional Development Impact

4.25 The institutional development impact of the Bank assistance is considered next. The issue here is the extent to which the Bank assistance facilitated the build up of institutional capacity in the pension area.

4.26 The largest impact of the World Bank assistance to Korea has been to improve greatly the capacity of Koreans to formulate their own pension policies and to manage their public pension schemes. Most important was the requirement under SAL 2 to establish a Pension Reform Task Force with broad representation across government ministries, public pension corporations, research institutes, labor unions and employer organizations, with technical assistance provided by the ASEM grant. This exposed a cross-section of Korean pension experts to international best practice and provided training in modern analytical techniques. The success of this strategy is evidenced by continued analytical review of pension policies by academics (e.g. Kim and Lee 2003) research institutes (e.g. Phang 2004), public pension corporations (e.g. Yun 2004) and interest groups such as labor unions[18] and employer groups (see KEF 2004). Further indications include the well-developed reform proposals put forward in 2003 for the NPS (by the Ministry for Health and Welfare) and the retirement allowance scheme (by the

[18] The KCTU included social protection issues in their policy proposals for the 2004 general election.

Ministry of Labor). Korean pension experts have been sharing their experience internationally through participation in international workshops and conferences.[19]

4.27 As a result of the Bank assistance, Korean pension experts are more aware of the issues associated with the governance, management and financial stability of their public pension schemes. While Korea fell short of creating the position of a Government Actuary (as was required under SAL 2), the Bank assistance has resulted in a more careful consideration of financial stability and five-yearly reviews are now required for all public pension schemes. Management and governance has improved through the phasing-out of mandatory public sector investments, and a government committee is considering professional asset management. The Bank contributed to the build-up of capacity in this area through technical assistance provided from an ASEM grant, which funded a workshop providing training on PROST (the World Bank pension modeling software) and an international workshop on public pension fund governance.

4.28 As noted earlier, the final reforms supported by the Bank fell short of systemic reform and the introduction of a funded private pillar, so the institutional development impact in terms of the regulatory and supervisory framework for private pension funds has been minimal. Nevertheless, through participation in the Pension Reform Task Force and the associated workshops and conferences (specifically a workshop co-sponsored with the new Korean financial services regulator, the FSS, to consider private pension design and supervision) and exposure to the World Bank analysis via the Bank's policy advice paper (World Bank 2000), there are now a number of pension experts in Korea who are aware of the issues associated with the introduction, regulation and supervision of a private pension fund industry. This expertise has been instrumental in the development of detailed policy proposals for the conversion of the retirement allowance scheme to funded corporate pensions, released by the Minister of Labor in 2003. As well, Korean experience with the creation of a single financial regulator (in 1997) and other structural reforms in the financial sector (required under the structural adjustment lending) will assist with any future design and implementation of private pensions.

4.29 Overall, the broadly based Korean participation in the Pension Reform Task Force, the training and research support provided under the ASEM grant and the exposure to World Bank pension analysis, has provided Korea with a large pool of expertise and a body of policy-related research with which to develop their own pension reform proposals.[20] *The overall rating for the institutional development impact is high.*

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[19] See, for example Yun, presented to a regional conference of the ISSA (Yun 2004), and Han presented to a World Bank conference on public pension fund management (Han 2003). As well, in October 2002, Korea hosted an OECD/INPRS conference on private pensions in Asia.

[20] This view was confirmed following discussions with Professor Kim Sang Kyun, the former Chairman of the Pension Reform Task Force and Professor Chung Kyung Bae, former President of KIHASA, the research institute responsible for managing the Pension Reform Task Force.

Sustainability

4.30 The question is the extent to which the positive outcomes of the World Bank's assistance are likely to be sustained over time. To recall, the positive outcomes of the Bank assistance to Korea were:

- The creation of a zero pillar (of a non-contributory age pension).
- An improvement in the management of all public pension schemes and a greater awareness of the importance of long-term financial stability. Achievements included the requirement for five-yearly actuarial projections for all public pension schemes, the phasing-out mandatory investment of NPS reserves in public sector assets and parametric reforms.
- Some funding of retirement allowances.
- Consistent EET taxation of retirement saving.
- Creation of a number of Korean pension experts spread across government, academia and interest groups and a stock of policy-related pension research.

All of these outcomes have been maintained or extended.

4.31 Support for the pension reforms actually made was generally positive. The main detractors were the labor unions, who were concerned about parametric reforms to the NPS that lowered target replacement rates, and the employer groups who were concerned about the impact of higher NPS contribution rates on labor costs. Overall however, there is now greater understanding of, and support for, systemic pension reforms.

4.32 In relation to the public pension schemes, the Bank assistance did not lead to large-scale reforms with full or partial conversion to funded private pensions. Instead, the assistance required that Korea address the financial stability, management and governance of their public pension schemes. Korea now conducts regular actuarial reviews of all public pension schemes on a five-yearly basis, with the view to consider parametric reforms where necessary. The latest analysis was undertaken in 2003 and proposals for parametric reforms of the NPS to improve its long-term stability will be presented to the National Assembly in 2004. If passed, these would involve a reduction in the target replacement rate to 50 percent (from 60 percent) and an increase in the contribution rate to 15.9 percent (from 9 percent). These reforms would address the long-term financial stability of the NPS (but not the imbalance in public/private pensions or other outstanding pension policy issues). As well as completing the required phase-out of the mandatory investment of NPS reserves in public sector assets, a government committee is currently considering external management of the NPS fund.

4.33 The 2000 reforms to encourage funding of retirement allowances through the introduction of retirement insurance have been strengthened and expanded with the 2003 proposals from the Ministry of Labor to convert the largely unfunded retirement allowances to funded corporate pensions.

4.34 A major component of the Bank assistance in relation to both the structural and systemic reforms was to facilitate Korean development and ownership of the reform proposals. This was done by giving Koreans the responsibility of developing pension reform proposals as part of the Pension Reform Task Force and by providing training and exposure to international best practice through technical assistance. Therefore, the main investment was in human capital, and as discussed above, the development of human capital continues as pension reform issues are continually researched and discussed by government policymakers, academics and interest groups. With the withdrawal of the Bank from Korea in 2000, this has continued independent of Bank assistance.

4.35 In summary, the positive outcomes of Bank assistance are likely to be sustained. All of the structural reforms introduced have been maintained and the investment in human capital is being extended as researchers and policymakers continue to debate and develop policies and interact with international researchers and institutions. ***The overall rating for sustainability is highly likely***. That is, Bank assistance will continue to generate positive outcomes.

5. Attribution of Results

5.1 The results of the World Bank assistance can be attributed in terms of the performance of the Bank (at entry and during supervision) and performance of the borrower (in relation to preparation, implementation and compliance). It is noted that the period of Bank assistance was limited to the time between the request for emergency assistance in November 1997 to the closure of the ASEM grant in June 2001. From the World Bank documents provided and the interviews conducted, it appears that the World Bank was the sole international agency involved in pension reforms in Korea over this period.

Bank Performance

5.2 The issue for Bank performance is the extent to which the services provided by the Bank ensured quality at entry and supported implementation through appropriate supervision. The Bank faced difficult circumstances at entry: Korea had graduated from Bank assistance in 1994, the Bank office in Seoul had closed and the Bank was no longer conducting analysis on Korea. The context of the pension assistance as part of emergency structural adjustment lending meant that a plan had to be developed very quickly and the Bank was likely to be in Korea for only a short time. Potentially very difficult circumstances were mitigated by the Bank's use of high quality pension experts and the sequencing of the assistance, which addressed the immediate problems (and those requiring the least analytical advice), and allowing time for analysis and collaboration with Korean pension experts for the more difficult reforms. In spite of the initial difficulties, the quality of the analytical work on Korean pensions was good, the overall design of the assistance was sympathetic to Korean circumstances and a broad cross-section of Koreans became involved in the pension reform proposals. ***The quality at entry is rated satisfactory***.

5.3 The initial problems were further addressed once Bank personnel became reacquainted with Korea and made links with the already established Korean pension research community. The sequencing of the assistance gave the Bank time to research, investigate and produce (drafts of) their analytical Korean pension reform paper (subsequently published in May 2000). The Bank's performance during implementation was characterized by close collaboration with Koreans and well-targeted technical assistance through the ASEM grant to assist with reforms to the management of NPS reserves and the deliberations of the Pension Reform Task Force. The Bank's approach was to facilitate Korean-driven reforms, rather than impose pro forma systemic reform. The assessment by Bank staff was good and the appropriateness of proposed solutions was excellent. The performance of the Bank during implementation has increased the likelihood of systemic pension reform in Korea. Overall, the Bank assistance reflected appropriate priorities and was well constructed. ***The quality at supervision is rated highly satisfactory.***

5.4 ***Therefore, the overall rating for Bank performance is satisfactory*** –satisfactory at entry and highly satisfactory at supervision.

Borrower Performance

5.5 The issue for borrower performance is the extent to which the borrower assumed ownership and responsibility to ensure quality of preparation and implementation, and complied with covenants and agreements towards the achievement of development objectives and sustainability.

5.6 In terms of preparation, the context of the pension assistance as part of emergency structural adjustment lending meant that the government of Korea at the highest levels collaborated with the Bank to design the initial ERL and the subsequent structural adjustment loans. The government was very supportive, having just been re-elected on a platform of structural reform. ***The rating for preparation is highly satisfactory***.

5.7 In terms of implementation, the issue is the extent to which the government performance supported the policies required under the structural adjustment lending, and for pension reforms, particularly the policy matrix as specified in SAL 2. The government was fairly cooperative. It implemented the immediate reforms and some of the structural reforms to the NPS quickly, but did not establish an Office of the Actuary. Instead a process was established for five-yearly actuarial projections for each of the public pension schemes. It implemented the phasing-out of the mandatory investment of NPS reserves in public sector assets but did not make any other improvements to the management of NPS fund assets. While it did implement the requirement to set up a Pension Reform Task Force, the process was slow and the required White Paper on Pension Reform was delivered over 12 months late. ***Borrower implementation is rated satisfactory***.

5.8 Finally, in relation to compliance, the context considered is that of compliance with the policy reforms required under the structural adjustment lending, particularly the policy matrix specified in SAL 2. All requirements were at least partially complied with, including the conditional reform to the phase-out public sector investments of NPS reserves. However, despite the overall government support for Bank assistance, there was reluctance within parts of the bureaucracy to comply. In particular, the Ministry of Health and Welfare (the Ministry with responsibility for the NPS) were uncooperative during some Bank missions and had to be removed as task managers of the ASEM grant. As well, compliance can be questioned with the delays in the establishment of the Pension Reform Task Force and the production of a White Paper. ***The rating for compliance is satisfactory***. That is, the borrower generally met or exceeded all major commitments, with only minor shortcomings.

5.9 Therefore, ***the overall rating for borrower compliance is satisfactory*** – highly satisfactory for preparation, and satisfactory for implementation and compliance. The ratings assessing World Bank assistance in Korea are summarized in Table 10.

Table 10: Assessment of Bank Assistance - Summary

Criteria	***Rating***
Outcomes	
Relevance	High
Efficacy	Substantial
Overall outcomes	Satisfactory
Institutional Development Impact	High
Sustainability	Highly likely
Attribution of Results	
Bank performance	
Quality at entry	Satisfactory
Quality at supervision	Highly satisfactory
Overall Bank performance	Satisfactory
Borrower performance	
Preparation	Highly satisfactory
Implementation	Satisfactory
Compliance	Satisfactory
Overall borrower performance	Satisfactory

What would have happened if the Bank had not been present?

5.10 Even before the World Bank re-engaged with Korea in 1997 (after withdrawing in 1994), Korean pension experts and policymakers had been questioning Korea's pension provision arrangements. This became more widespread as academics and other pension experts became exposed to the ideas for systemic pension reform presented in publications such as *Averting the Old Age Crisis.* In 1997 the Bank, the Korean Ministry of Finance had established the National Pension Review Board to consider the financial stability of the NPS. Its initial recommendations, released in December 1997, just before the re-entry of the World Bank, set out parametric reforms but also canvassed 'Chilean-style' reforms. Consideration of pension reform has continued following the departure of the Bank from Korea (again) in 2000.

5.11 In the absence of the Bank assistance in 1997-2000, it is likely that there would have been reforms to the Korean retirement income system, but these would have been parametric in nature and would probably have taken place at a slower pace. The impact of the Bank assistance has been to fast-track structural reforms to components of the pension system – safety nets, public pensions and retirement allowances. The Bank assistance has greatly increased the probability that multi-pillar reforms will eventuate, by educating a broadly-based group of Korean policymakers, academics and interest group representatives on pension reform issues and exposing them to international best practice in analysis, design and implementation.

6. Lessons Learned and Agenda for Future Action

6.1 Lessons learned and the agenda for future action must be put into the context of the short period of Bank assistance and the vehicle of emergency structural adjustment lending. Initially, the Bank was faced with many problems when it re-engaged Korea due to its limited knowledge base. It is therefore important that the Bank continue monitoring countries once they have graduated from Bank assistance.

6.2 The success of the Bank's assistance on pension reform was largely due to its use of high quality pension experts from within the Bank and the sensible sequencing of reforms. The Bank knew that it would be involved with Korea for only a short time, yet rather than rush into systemic reforms, it concentrated on setting up a framework to enable the Koreans to design and implement their own reforms.

6.3 The impact of this approach was increased through the Bank's collaboration with a cross-section of pension experts from government ministries, public pension corporations, academia, research institutes and interest groups, rather than a single government department. This allowed a broad variety of pension experts to be involved in the deliberations of the Pension Reform Task Force and access the workshops and courses funded by the ASEM grant. The growing body of policy-related pension research and the reasonably sophisticated understanding of pension issues by Korean policymakers, researchers and interest groups is evidence of the success of this approach.

6.4 Overall, the Bank assistance has greatly increased the likelihood of systemic pension reform in Korea, designed and driven by Koreans. For the future, the Bank should maintain involvement with Korea and build upon the good relationships formed with the Korean pension research community during the short period of renewed Bank assistance. This will enable the Korean pension experts to keep their knowledge and skills up-to-date and facilitate the continued development of high quality pension reform advice and implementation in Korea.

Annex A: Data Annex

Annex Table 1: The Korean Pension System

	1996	*2003*
Coverage and maturity of the pension system		
Population		
Total	45,525,681	47,925,318
Age 65 and over	2,794,822 (6.1%)	3,969,036 (7.7%)
Age 15 to 65	32,326,522 (71.0%)	34,237,549 (71.4%)
Under age 15	10,403,277 (22.9%)	9,718,733 (20.3%)
Labor Force	21,288,000	22,916,000
Employment	20,853,000	22,139,000
Affiliates (registered workers)		
National Pension Scheme	7.829 mill	17.182 mill
Other public pension schemes		
Government employees	982,000 (1997)	930,000 (2002)
Private School teachers	207,664 (1999)	220,000 (2002)
Military personnel	Na	2,000 (2002)
Retirement Allowance	6.168 mill (1995)	6.584 mill (2002)
Active Contributors		
National Pension Scheme	Na	9.828 mill
Other public pension schemes	Na	Na
Beneficiaries		
National Pension Scheme	109,449	1.171 mill
Other public pension schemes		
Government employees	63,693	181,726
Private School teachers	4,618	17,900
Military personnel	Na	15,000 (2002)
Old age		
National Pension Scheme	58,099	934,819
Other public pension schemes		
Government employees	58,248	165,483
Private School teachers	4,226	16,553
Military personnel	Na	Na
Disability		
National Pension Scheme	8,670	38,995
Other public pension schemes		
Government employees	5,055	14,871
Private School teachers	382	1,319
Military personnel	Na	Na
Survivors		
National Pension Scheme	42,680	197,220
Other public pension schemes		
Government employees	390	1,372
Private School teachers	10	39
Military personnel	Na	Na

Annex Table 1 *(continued)*

	1996	*2003*
Key Indicators		
Old age dependency ratio (Age 65 and over/Age 15 to 65)	8.6%	11.6%
System dependency ratio (beneficiaries/contributors)		
National Pension Scheme	1.4%	6.8%
Other public pension schemes		
Government employees	7.4% (1997)	18.2% (2002)
Private School teachers	9.7% (1999)	7.3% (2002)
Military personnel	Na	750% (2002)
Coverage of contributors (% labor force)		
National Pension Scheme	36.8%	75.0%
Other public pension schemes		
Government employees	4.5% (1997)	4.1% (2002)
Private School teachers	1.0% (1999)	1.0% (2002)
Military personnel	Na	0.01% (2002)
Retirement Allowance	Na	28.8% (2002)
Coverage of contributors (% employed)		
National Pension Scheme	37.5%	77.6%
Other public pension schemes		
Government employees	4.6% (1997)	4.2% (2002)
Private School teachers	1.0% (1999)	1.0% (2002)
Military personnel	Na	0.01% (2002)
Retirement Allowance	Na	46.4% (in 2002)
Coverage of old age population (beneficiaries/pop age 65 & over)		
National Pension Scheme	3.9%	29.5%
Other public pension schemes	3.0%	5.4%
Basic Parameters		
Contribution rates (total)		
National Pension Scheme	6%	9% (7% self empl)
Other public pension schemes		
Government employees	13%	17%
Private School teachers	13%	17%
Military personnel	13%	17%
Retirement Allowance	8.3%	8.3%
Contribution rates (employer)		
National Pension Scheme	4% (a)	4.5%
Other public pension schemes		
Government employees	6.5%	8.5%
Private School teachers	4% (b)	5% (b)
Military personnel	6.5%	8.5%
Retirement Allowance	8.3%	8.3%

Annex Table 1 *(continued)*

	1996	*2003*
Contribution rates (employee)		
National Pension Scheme	2%	4.5%
Other public pension schemes		
Government employees	6.5%	8.5%
Private School teachers	6.5%	8.5%
Military personnel	6.5%	8.5%
Retirement Allowance	0%	0%
Contribution rates (self-employed)		
National Pension Scheme	6%	7% (9% by 2009)
Retirement Allowance	Na	Na
Retirement Age		
National Pension Scheme	60	60 (65 by 2033)
Other public pension schemes	age 50 or 20 yrs of contributions	60
Retirement Allowance	No minimum age	No minimum age
Minimum Years of service/ contribution		
National Pension Scheme		
Other public pension schemes	15	10
	20	0 minimum retirement age of 60
Retirement Allowance	1	1
Target replacement ratios for full career workers		
National Pension Scheme	70% lifetime earnings for the average income earner	60% lifetime earnings for the average income earner
	76% final salary after 33 years	76% final salary after 33 years
Other public pension schemes	paid as lump sum	paid as lump sum
Retirement Allowance		
Level and Structure of Benefits		
Average pension/average wage		
National Pension Scheme	7.6%	7.9%
Other public pension schemes		
Government employees	232%	91.8%
Private School teachers	87.6%	75.7%
Military personnel	Na	Na
Old age pension/average wage		
National Pension Scheme	7.1%	7.1%
Other public pension schemes		
Government employees	235%	94.1%
Private School teachers	90.1%	77.5%
Military personnel	Na	Na

Annex Table 1 *(continued)*

	1996	*2003*
Level and Structure of Benefits (cont)		
Disability		
National Pension Scheme	11.9%	15.6%
Other public pension schemes		
Government employees	161%	57.1%
Private School teachers	60.8%	53.0%
Military personnel	Na	Na
Survivors		
National Pension Scheme	7.4%	7.8%
Other public pension schemes		
Government employees	344%	137.9%
Private School teachers	65.2%	54.9%
Military personnel	Na	Na
Finances of public pensions		
Contribution revenues (%GDP)		
National Pension Scheme	1.1%	1.96% (2002)
Other public pension schemes		
Government employees	0.4% [c]	0.4% (2000)
Private School teachers	0.1%	Na
Military personnel	0.1% (1998)	Na
Pension expenditures (% GDP)		
National Pension Scheme	0.2%	0.3%
Other public pension schemes		
Government employees	0.5%	0.6%
Private School teachers	0.01%	0.05%
Military personnel	0.2% (1998)	Na
Other		
Tax Base (% GDP)	19.7%	22.3%
Labor income	Na	420.8 trill won
Wage bill	214.5 trill won	294.4 trill won

Annex Table 1 *(continued)*

	1996	*2003*
Capital Market Indicators		
Assets of pension funds (% GDP)		
National Pension Scheme	4.8%	15.6%
Other public pension schemes	2.0%	1.0%
Retirement allowances	Na	2.4% [d]
Private pensions	1.4%	3.8%
Composition of pension fund portfolios		
National Pension Scheme		
Public sector		
Welfare sector	67.8%	14%
Financial sector (cash, bonds, stock)	3.2%	0.5%
	29%	85.5%
Returns on pension fund assets		
National Pension Scheme	10.8%	6.4% (2002)
Administrative costs of pension funds (% assets)		
National Pension Scheme	0.3%	0.6% (2002)

Notes:

a. 2% employer contribution plus 2% from retirement allowance reserve.
b. Plus 2.5% government contribution in 1996 and 3.5% government contribution in 2003.
c. Employee and government contributions.
d. Amount of retirement insurance

Sources:

Demographic, labor market, national accounts, public finance data: Korea National Statistical Office (www.nso.go.kr) and World Bank Development Indicators (www.worldbank.org).

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Annex B: World Bank Documents

Economic Reconstruction Loan (ERL)	
October 2, 1998 Report No. PID6892	Economic Reconstruction Loan
1998: Structural Adjustment Loan (SAL 1)	
September 25, 1998 Report No. PID6882	Report on the Structural Adjustment Loan
1998: Structural Adjustment Loan (SAL 2)	
24 September, 1998	Letter of Development Policy: MOFE Korea to the President of the World Bank
April 19, 1999	QAE (Quality at Entry) Assessment, SAL 2
ASEM grant	
April 24, 2002	ASEM Trust Fund Implementation Completion Report
Policy advice paper	
May 10, 2000 Report no. 20404-KO	Republic of Korea: The Korean Pension System at a Crossroads

Annex C: Korean Officials Interviewed*

Ministry of Health and Welfare

Mr. Chan Hyoung Park	Director, Pension Policy Division

Ministry of Finance and Economy

Mr. Ki-Sang Yoon	Director, Welfare Policy Coordination Division
Mr. In Woong Hwang	Deputy Director, Welfare Policy Coordination Division

Ministry of Planning and Budget

Mr. Tae-Sung Lee	Director, Social Funds Division

Korea Institute for Health and Social Affairs (KIHASA)

Dr. Soon-il Bark	President
Dr. Byungsik Yoon	Senior Fellow, previously Executive Secretary of the Pension Reform Task Force
Dr. Hwajong Baek	Senior Research Fellow
Dr. Byongho Choi	Senior Research Fellow

National Pension Research Centre (NPRC)

Dr. Inchul Noh	Director
Dr. Sukmyung Yun	Senior Research Fellow

Korea Labor Institute (KLI)

Dr. Hanam Phang	Research Fellow

Academics

Dr. Kyungbae Chung	President of the Socio-Economic Society, Chairman of the Public Hearing on Pension Reform and Fund Management, Former President of KIHASA
Professor Sang-Kyun Kim	Department of Social Welfare, Seoul National University
Professor Yongha Kim	Department of Finance and Insurance, Soonchunhyang University, Director of the Korean Institute for Social Insurance
Professor Wonshik Kim	Department of Economics, Konkuk University

Korean Council of Trade Unions (KCTU)

Dr. Keon-Ho Oh	Research Fellow

Consumers Union of Korea

Ms. Jung-Hwa Kang	Secretary General

Korea Employers Federation

Mr. Ho-Sung Lee	Head, Economic Research
Mr. Woo-Young Jang	

Samsung Insurance

Dr. Keechul Shin	Vice President, Samsung Insurance, previously Director, Korean Financial Supervisory Institute

The World Bank

Mr. Robert Palacios

* All officials (with the exception of Robert Palacios and Dr Keelchul Shin) were interviewed face-to-face over the period April 5-9, 2004.

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