Executive summary

Since July 1995 volcanic activity has brought challenges and uncertainty to the people of Montserrat. With almost two-thirds of the population having migrated by 1998, and 60% of the island uninhabitable, Montserrat continues to be in a state of flux. At the time of writing this report, scientists indicate that although damage to the present “safe zone” remains unlikely, continued volcanic activity for many years is a real possibility.

Like all other aspects of the Montserrat’s economy and society, activity at the Soufriere Hills Volcano has greatly affected the Montserrat Social Security Scheme. While benefit expenditure continued to increase each year, contribution income in 1998 was just over one half of the amount collected in 1996.

Much is, therefore, dependent on the future state of the volcano, the stability or growth of the population and the health of the economy. The main projections presented in this review assume that a complete evacuation of the island will not be required. Population projections presented in this report suggest that over the next 50 years, the population may stabilize at between 6,000 and 8,000 persons. For Social Security, the larger the population and the greater real economic growth are, the better positioned the scheme will be to meet its future obligations.

Projections of Social Security long-term benefits up to 2050, using a simplistic but plausible scenario of the future, have also been performed. While the ongoing uncertainty may cast doubt on results of such an extended period, the nature of social security benefits and the way they are funded require long-term forecasts. Ironically, it turns out that it is the short-term projections of Social Security finances that reveal the need for important decisions to be made.

Although there have been recent positive signs of growth in contributions, the surpluses that Social Security has experienced each year since inception may be short-lived. Results of projections presented later in this report suggest that, if no changes are made to contribution provisions, total expenditure may exceed total income for the first time in 2006. This will occur mainly due to the relatively low contribution rate of 7.5%, but has been accelerated by recent declines in contribution income.

In a partially funded system, such as Montserrat Social Security, the contribution rate is below the rate required to cover the full cost of all the benefits being promised. This system of funding calls for part of the costs of one generation to be met by later generations. With ageing populations resulting in fewer contributors for each pensioner, the intergenerational transfer will place greater burdens on future contributors.

Other than an across-the-board increase in pensions in 2002 and annual adjustments to the ceiling and pensions in line with inflation, the projections assume that no changes are made to contribution and benefit provisions. These projections reveal that:

1. The reserves of the LTB Branch are projected to grow from $9 million at the end of 1999 to just over $11 million in 2006. Thereafter, they will steadily decrease until being exhausted in 2015.

2. If the contribution rate is not increased until the reserves are completely exhausted, a contribution rate of 11.3% in 2015 will be required. The scheme will enter what is usually termed a “pay-as-you-go” state where current contribution income will be expected to meet current benefit and administrative expenditure. This rate will increase gradually to almost 30% in 2050.

3. Alternatively, to secure positive reserves throughout the projection period and a reserve of twice-annual expenditure in 2050, one reasonable schedule of contribution rates is shown below.
<table>
<thead>
<tr>
<th>Year</th>
<th>Total Contribution Rate</th>
<th>Year</th>
<th>Total Contribution Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Up to 2002</td>
<td>7.5%</td>
<td>2025 – 2029</td>
<td>17.0%</td>
</tr>
<tr>
<td>2003 – 2009</td>
<td>9.0%</td>
<td>2030 – 2034</td>
<td>19.0%</td>
</tr>
<tr>
<td>2010 – 2014</td>
<td>11.0%</td>
<td>2035 – 2039</td>
<td>21.0%</td>
</tr>
<tr>
<td>2015 – 2019</td>
<td>13.0%</td>
<td>2040 – 2050</td>
<td>23.0%</td>
</tr>
<tr>
<td>2020 – 2024</td>
<td>15.0%</td>
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</tbody>
</table>

4. The average cost of projected long-term benefits payable between 2000 and 2050 is 13.2%. Given that 3% of insurable earnings is allocated to cover short-term and employment injury benefits, a level total contribution rate of 16.2% of insurable earnings would be required from 2000 until 2050 to maintain the present level of funding.

5. The number of active contributors for each pensioner will fall from 7.4 in 2000 to 1.4 in 2050. Given the partial funding system for benefits, where current contributors are expected to meet a portion of the cost of pension payments, future generations of contributors will be required to contribute significantly more than the present rate of 7.5% of insurable earnings.

6. Should a full evacuation be required, there will be insufficient funds to meet all accrued obligations. With an estimated 2000 year-end reserve of 10 times 2000’s expenditure, and half of the assets invested locally, the Social Security Fund will only be able to continue making benefits payments for fewer than 10 years. (For partially funded social security schemes, having enough funds on hand to meet all earned entitlements is never an objective.)

The Short-term and Employment Injury Benefits Branches are adequately funded and the present allocation rates for contributions are sufficient for the foreseeable future. In fact, transfers of reserves out of both branches to the Long-term Benefits Branch, and reductions in the proportion of contribution income allocated to the Employment Injury Benefits Branch, are being recommended.

Other than an increase in the contribution rate within the next three years, drastic measures aimed at extending the life of the Social Security Fund are not required immediately. However, planning for the inevitable increases in contribution rates, or the reform of benefits, should begin by raising the public’s awareness of the scheme’s future financial challenges.

Several recommendations are made in this report. For issues on which further discussion and review by the Board and stakeholders are considered necessary, comments and ideas are provided but no specific recommendations made. It is anticipated that the government and its social partners will closely consider each issue to ensure that Social Security provisions best meet the ever-changing socio-economic environment in Montserrat with which they are most familiar.

The specific recommendations made throughout this report are:

(a) Transfer $1.8 million from the Short-term Benefits Branch to the Long-term Benefits Branch.

(b) Transfer $1.8 million from the Employment Injury Benefits Branch to the Long-term Benefits Branch.

(c) Reduce the percentage of contribution income allocated to the Employment Injury Benefits Branch from 1.5% to 0.75% of insurable earnings.
(d) Increase the proportion of contribution income allocated to the Long-term Benefits Branch from 4.5% to 5.25% of insurable earnings.

(e) Increase the ceiling on insurable earnings from its current level of $600 per week, $2,600 per month. The amount to which the ceiling will be increased should be decided after considering the effects such an increase may have on the economy and the pending integration of public servants into Social Security. At a minimum, the revised ceiling should be set at $800 per week.

(f) Develop short, medium and long-term funding objectives such as the desire to have a reserve-expenditure ratio of 7 in 2005, 5 in 2025 and 2 in 2050. This will assist in the long-range planning for contribution rate increases.

(g) At a minimum, the contribution rate should be increased from 7.5% to 9% within the next three years. This will prevent Social Security from incurring its first deficit in 2006.

(h) Increase the amounts payable to all pensioners whose pension was awarded prior to 2001. Most of these persons have not had their pensions adjusted and thus the purchasing power of that pension has been reduced due to the effects of inflation. The actual amount of the increase will depend on the desired objective of the increase and the effect the increase will have on the Fund. If granted, the adjustments should vary depending on the time elapsed since the pension was awarded.

(i) Increase the minimum pension to at least $60 per week or $260 per month. Consideration may be given to increasing it to $300 per month, the amount now paid by the Welfare Act to the elderly, the disabled and others who are deemed in need.

(j) Amend the payment duration for Maternity Allowance so that payment need not stop 6 weeks after confinement. Instead, the maximum duration of 12 weeks should be maintained, but will begin from the first day the Allowance is actually payable.

(k) Amend the necessary regulations to require contributions from those under 16 and over 59 towards Employment Injury benefits only.

(l) Proceed with plans to integrate established civil servants into Social Security so that all workers in Montserrat have universal and portable social protection. In revising the Pensions Act, the Government of Montserrat must ensure that various classes of civil servants continue to qualify for adequate and equitable pensions, with few anomalies.

(m) Put in place a system of regular verification of pensioners, especially those overseas, so that the pensions are paid only to those who remain eligible.

(n) Amend either or both of the Employment and Social Security Ordinances so that employers may be able to reduce wages during periods when the employee is in receipt of Sickness or Maternity benefits. This would ensure that the worker does not receive more income when off from work by receiving Social Security benefits in addition to regular wages.

(o) Create Financial & Accounting Regulations that, among other things, stipulate the method of allocating income and expenditure items to the three benefit branches.

(p) Calculate the accumulated value of contributions and interest for former National Provident Fund members so that the total amount due these persons can be established. Once determined, funds that are now part of the National Provident Fund in excess of the amount due should be transferred to the Long-term Benefits Branch.

(q) Make Social Security’s financial operations and the results of this and future actuarial reviews public through annual reports, booklets, discussion forums and other effective
means. This will ensure that public understanding and appreciation of the Board’s affairs are increased and that all residents are aware of the challenges that lie ahead.

(r) Prepare an Investment Policy Statement for the purpose of creating specific policies, guidelines and a general framework within which the assets of the Social Security Fund will be invested and managed.

(s) Gradually change the asset mix of the SSF by increasing the proportion held in long-term securities and decreasing the amount held in fixed deposits. The long-term goal should be to increase the returns of the investment portfolio and to hold assets that better match the scheme’s liabilities.

Consideration should also be given to:

(a) Placing in Social Security Regulations the timing and magnitude of adjustments to the ceiling on insurable earnings, grants, minimum pensions, and all pensions in payment. Such provisions could provide for annual increases in line with changes in price and wage inflation.

(b) Negotiating a reciprocal arrangement with the United Kingdom.

(c) Allowing National Provident Fund balances to be used for payment towards current mortgages or down payment on new mortgages.

Key to a meaningful social security programme for future generations is the development and expansion of Montserrat’s economy. Favourable volcanic and socio-economic conditions that facilitate a growing population, with increased employment and escalating incomes, will serve to enhance the island’s prosperity and in turn Social Security benefits.

Future increases in the contribution rate are inevitable. To reduce the magnitude of contribution rate increases, the first of several rate increases should occur soon. Reforms to benefit provisions should also be considered sooner rather than later. To eliminate the element of surprise and resistance from future contributors, the results of this and future actuarial reviews should be shared with all residents. With the continued monitoring of scheme experience, sound planning, frank discussion with stakeholders, and the timely implementation of reforms, the Social Security Board will be better prepared to meet the challenges that lie ahead.