

04/2017

FINNISH CENTRE FOR PENSIONS, STUDIES

## SUMMARY

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### The economic welfare of disability pensioners' in the 2000s

The Finnish earnings-related pension system is designed to ensure that a person's usual and customary income level is reasonably maintained in the event of old age, disability or the family provider's death. The national pension system is intended to guarantee a minimum pension for all pensioners residing in the country. In this study, we review how the economic welfare of disability pensioners has developed in the 2000s. The numbers concerned are substantial: in 2016 there were 211,000 disability pensioners in Finland, representing 6 per cent of the working age population. In addition, this study was motivated by an earlier observation that disability pensioners have been falling behind old-age pensioners in terms of income development.

Our focus is to explore the recent changes in disability pension legislation and in the sociodemographic characteristics of disability pensioners. Income is examined in terms of overall pension and disposable money income, and an international comparative perspective is included. This is the first broad overview of its kind into the financial position of disability pension recipients in Finland.

Our main data sources are the 2000–2016 statistical register on Finnish pension recipients compiled jointly by the Finnish Centre for Pensions and the Social Insurance Institution; a 10 per cent sample of the 2000–2012 household population residing in Finland built around Total statistics on income distribution by Statistics Finland and international statistics such as Eurostat's income and living conditions database.

## Minor changes to the determination of disability pensions in the 2000s

There has been a succession of reforms affecting the level of disability pensions under the earnings-related pension scheme since the mid-1990s. Following the economic recession, the decision was made to deduct the employee's earnings-related pension contribution from their wages, which was the basis for their pension determination. At the same time, projected pension accrual rates were lowered. Further changes were made in connection with the 2005 pension reform, which among other things saw the introduction of a life expectancy coefficient. Disability pensions in payment were linked to a pension index, replacing the halfway index that was more closely tied with the development of wages. This, however, was offset by a one-off increase to the pensions of young disability pension recipients, and furthermore by improvements made in 2010 to the determination of the projected part of the pension. Overall the changes made to earnings-related pensions since the 1990s have contributed to lower the level of disability pensions.

The negative changes made to the benefits under the earnings-related pension scheme have been offset by a number of step increases to the minimum pension during the 2000s. In addition, the decision to do away with the classification of municipalities increased the national pensions of people living in the lower cost-of-living category. The guarantee pension was introduced in 2011. Since the 1990s pensioners' tax rates have also been reduced. The lowered tax burden served to offset the effects of withdrawing the basic amount of earnings-related pension recipients' national pension.

The individual early retirement pension for older workers with long employment histories was discontinued in connection with the 2005 pension reform, after a short transitional period. However, under the new rules a disability pension can be awarded on more lenient criteria in the case of persons aged 60 or over, and from 2018 onwards as a years-of-service pension. Rehabilitation has gained increasing importance since the rehabilitation reform in the 1990s, when the fixed-term disability pension was renamed as the rehabilitation subsidy to underscore the role of rehabilitation in reducing the incidence of permanent disability pensions. The role of the partial disability pension and of working part-time while drawing the pension have been emphasized.

## Disability pensioners are fewer in number and younger than earlier

The number of disability pensioners and their share of the working age population increased somewhat in the early 2000s, but since 2008 the figures have fallen sharply. In 2000, the number of disability pension recipients was one-fifth higher than today, and their proportion of the working age population was one percentage point higher. This has its background in accelerating baby boomer retirement and particularly in the clearly reduced disability risk in the older age groups. In younger age groups the changes have been less pronounced, and among those under 35 the risk of disability retirement has in fact increased somewhat. Overall, disability pensioners are somewhat younger than before.

The younger average age of disability pensioners has been reflected in the division of labour between the earnings-related and the national pension schemes. Today, there are increasing

numbers of disability pension recipients who have no other income than a national pension. This is opposite to the trend seen among old-age pension recipients, where there has been a steady decrease in the proportion of those receiving only a national pension.

Another structural change has seen the individual early retirement pension 'replaced' by the partial disability pension. In 2000, the proportion of individual early retirement pension recipients of all disability pension recipients was 12 per cent, and the share of partial disability pension recipients was 4 per cent. In 2016, the number of individual early retirement pension recipients was down to zero, while the proportion of partial disability pension recipients was 11 per cent. The vast majority, 89 per cent of all disability pension recipients were on a full disability pension.

### Changing age structure lies behind disability pensioners' modest income development

In 2016, the overall pension income of disability pensioners averaged 1,118 euros a month. Compared with the year 2000, this marked a decrease in real terms of around 6 per cent. However, the fall is explained almost entirely by the removal of pensioners' housing and care allowances of pension income statistics. Overall pensions have nonetheless shown modest development and the gap to old-age pension recipients has clearly widened. Today the average overall pension of disability pension recipients is around one-third lower than the pension of old-age pension recipients, while in 2000 they were still more or less on a par with each other.

Disability pensioners' overall pension income increases across age groups. In 2016, the pension in the age group 60–64 was 50 per cent higher than in the youngest age group of 16–34. A long employment career increases the earnings-related pension and thereby the overall pension level. The age group differences have narrowed somewhat during the 2000s. The introduction of the guarantee pension in 2011 improved the position of younger disability pension recipients in particular. The gender gap has also been reduced by four percentage points in the 2000s. In 2016 women disability pensioners' overall pension was 87 per cent of the corresponding pension for men.

The modest development of disability pensions is largely explained by the changing age structure of the disability pension recipients, as there are increasing numbers of young disability pensioners today and fewer people who are approaching old-age retirement age. The discontinuation of high individual early retirement pensions in the early 2000s and the increasing take-up of partial disability pensions during the current decade have also played some role in this respect.

Disability pensioners have nonetheless seen an improvement in their pension security while in retirement. During the period under review, pensions in payment have increased in real terms due to indexations (earnings-related pension index 7% and national pension index, including step increases, 11%). As for people whose disability pension started in 2002, overall pensions in this group increased in real terms by 20 per cent through to 2016. An examination

of the pension security of disability pensioners during old-age retirement showed that their income gap to other old-age pension recipients remains unchanged during old-age retirement.

### Rise in number of single-living people has increased the low income rate

A more positive picture emerges of the economic welfare of disability pensioners when it is measured using total household disposable money income. In 2012, the average equivalent income of disability pensioners was 22,300 euros, or some 1,860 euros a month (in 2016 money). From 2000, disability pensioners' income increased in real terms by 14 per cent. However, the income gap to old-age pensioners widened. In 2012 disability pensioners' income was 90 per cent of old-age pensioners' income, while in 2000 the two groups still had the same income level.

Other family members' income has great importance for disability pensioners' economic welfare. In 2012 these incomes accounted on average for 42 per cent of the gross income of disability pensioners. The pension recipient's earnings-related pension and other own income transfers such as national pension and guarantee pension accounted for just under half of the total. Compared with old-age pensioners' income structure, own earnings-related pension accounted for a smaller share of disability pension recipients' income, but the share of other family members' earned income in particular was higher. The role of the family was also apparent when examining income gaps between disability pension recipients in that the biggest differences were found between those living alone and those with a family. Age and gender were less significant factors. Among the different types of disability pension, one group that stood apart was those receiving a partial disability pension, with an annual income of around 30,000 euros.

In 2012 one in four recipients of a full disability pension was at risk of poverty when using the 60 per cent of median income threshold. The poverty risk was highest among people living alone and those under 45, with almost half and around one-third, respectively, at risk of poverty. The most significant change during the period under study has been the growth of the at-risk-of-poverty rate among people living alone, which has risen by 17 percentage points. As the proportion of single-living people of all disability pension recipients has increased, this goes some way towards explaining why the at-risk-of-poverty rate among disability pensioners has remained high since 2008, while among old-age pension recipients it has fallen.

### Share of young disability pensioners has increased in almost all countries under comparison

In a comparison with Sweden, Norway, Denmark, the Netherlands and Germany, Finnish disability pensioners' economic welfare is around or just below the average. Gross disability benefits are slightly lower than average, but when the income concept is expanded to include total household income per capita, the income of Finnish disability pensioners is around the average. When measured at purchasing power parity, the economic welfare of Finnish disability pensioners is comparable to the international average.

The position of disability pensioners was strongest in Norway, where their disposable income and purchasing power were clearly higher than in the other countries under comparison. The position of disability pensioners was by far the weakest in Germany, where there was also widespread risk of poverty. From 2005 to 2013 the position of disability pensioners vis-à-vis old-age pensioners deteriorated the most in Sweden. In Finland, too, the relative position of disability pension recipients has deteriorated.

The development of the economic welfare of disability pensioners reflects the changes made to the disability pension schemes in the countries under comparison. In Germany, for instance, the reforms in the early 2000s have resulted in declining economic welfare and an increased risk of poverty towards the end of the decade. In Sweden, on the other hand, the number of disability pension recipients has clearly declined following reforms in 2003 and 2008. However there has been a significant rise in the number of young pension recipients, and therefore young people's lower than average pensions have a stronger downward effect on the total averages. Indeed, a common feature across all the countries concerned has been the growing share of young disability pensioners.

**The Publication is available only in Finnish:**

Työkyvyttömyyseläkkeensaajien eläketurva ja toimeentulo 2000-luvulla. Eläketurvakeskuksen tutkimuksia 04/2017.

**Ordering of publication:**

[www.etk.fi](http://www.etk.fi) > Publications > Studies > The economic welfare of disability pensioners' in the 2000s  
or [aineistotilaukset@etk.fi](mailto:aineistotilaukset@etk.fi)

ISBN 978-951-691-267-0 (s-b)

ISBN 978-951-691-269-4 (PDF)

ISSN 1236-3049 (printed)

ISSN 1798-7482 (online)

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