



European Commission's Green paper "Towards adequate, sustainable and safe European pension systems" [SEC(2010)8]

CEC European Managers Position
15 November 2010

Preface

CEC:

- welcomes the integrated approach of the Green paper. CEC agrees that a broad analysis is needed that goes beyond isolated elements of the member states' pensions system and includes all types of retirement provisions,
- agrees with the analytical framework that focuses on adequacy, sustainability and safety as key criteria for *all* pillars of the member states' pensions scheme.
- welcomes the Commission's recognition of the member states' as well as the social partners' prerogative in developing and reforming their respective pension systems at national level,
- welcomes the Green paper's apparent preference for measures aimed at reducing investment risks in funded schemes, particularly close to and in the pay-out phase. The financial crisis has shown that not only public PAYG systems have systemic risks (due to demographic change) in terms of sustainability. Many funded schemes also have deficits in terms of adequacy and safety that have not been adequately addressed in all member states.
- calls on the Commission to adequately take into account the huge diversity among the member states' pensions systems. Due to the intricate interdependencies between the pillars of each system, identical measures of harmonisation can potentially lead to very different outcomes in each member states, sometimes with desirable, but sometimes also with unwanted outcomes. This has to be taken in account particularly in all cross-border related policy measures, particularly with regard to portability and vesting periods.
- calls on the Commission to adequately take into account the systemic, legal and fiscal differences between second pillar pension schemes (IORPs) and private pension schemes, especially when it comes to regulatory issues such as Solvency. Furthermore the role of Social partners in shaping IORPs, a key criterion that distinguishes second from third pillar systems, should also adequately be taken into consideration.

(Q1) How can the EU support Member States' efforts to strengthen the adequacy of pension systems? Should the EU seek to define better what an adequate retirement income might entail?

- In principle, CEC welcomes the EU's initiative to set the goal of adequate (and sustainable) pensions for all member states.
- However, from CEC's viewpoint the responsibility for ensuring adequate pensions (and for reducing/avoiding old-age poverty) should not be limited to the first pillar systems (public pension schemes) only. Within the EU, the differences with regard to the individual weight of each pillar are very big. Accordingly, universal recommendations that apply to only one of these pillars are hardly conceivable.

- CEC prefers a rather global definition of adequate retirement incomes that leaves the member states enough flexibility to find individual solutions for each of the pillars role in securing adequate pensions. Forcing member states to leave historically deep-rooted development paths in their pension policies would not be desirable.

(Q2) Is the existing pension framework at the EU level sufficient to ensure sustainable public finances?

- Considering the experiences with the current economic and financial crisis it is indisputable that the EU should play its role in monitoring the member states fiscal policies, in a more effective manner - especially with regards to the stability pact.
- Discussions on what lessons to draw are already underway. In principle, the CEC is open to a more integrated approach with regard to the public finances of the member states. Under the viewpoint of subsidiarity however, an economic governance, i.e. a stringent and effective system of coordination, would be preferable over an economic government, i.e. new structures or new bodies with own decision-making powers on the EU-level.

(Q3) How can higher effective retirement ages best be achieved and how could increases in pensionable ages contribute? Should automatic adjustment mechanisms related to demographic changes be introduced in pension systems in order to balance the time spent in work and in retirement? What role could the EU level play in this regard?

- Automatic adjustment mechanisms (for instance linking retirement age to the growth of the average life expectancy) could be an answer to the demographic changes and the associated financial problems.
- The necessary increase in the retirement age should go hand in hand with a more flexible labor market and a greater focus on senior policy in companies.
- However, even considering the experiences of the past years in which encouraging progresses have been made in many member states, it is hard to conceive that working periods grow at a similar pace like the life-expectancy. An automatic adjustment of retirement ages to the increase of life-expectancy would therefore go to the sole disadvantage to employees and not fulfil the criterion of a fair risk-sharing.
- Ultimately, it goes without saying that the responsibility for adjusting retirement ages, should continue to lie within the sole responsibility of the member states.

(Q4) How can the implementation of the Europe 2020 strategy be used to promote longer employment, its benefits to business and to address age discrimination in the labour market?

- In the past 10 years labour market participation of older employees (age group 55 to 64) has increased in many member states. From CEC perspective it is plausible that the predecessor of "Europe 2020", the Lisbon strategy, has contributed to this positive development. Therefore, it would be desirable that the issue of labour market participation of older employees remains a key goal under the new the Europe 2020 strategy as well.
- As far as age discrimination is concerned, CEC believes that the existing EU and national regulation is sufficient at least for the time being. The latest directives have come into effect only a few years ago, often surrounded by severe controversies and by opposition of many employers and even by some employees. Today, there are early signs for a

change of (positive) mentality in the fields of recruiting, employee retention and human resources development with regards to older employees.

- Generally, CEC believes that the decision on whether new legislation is needed should be based on a thorough analysis of the effects of the past reforms. Given the short time that has passed since the directives on equal treatment have come into effect, a temporary “reform pause” might be advisable.

(Q5) In which way should the IORP Directive be amended to improve the conditions for cross-border activity?

- From CEC’s perspective, the calls for the removal of barriers for cross-border activities of pensions’ funds have been closely linked to the idea of an EU-wide harmonisation of pension systems in general and of occupational pension systems in particular. For CEC, such a harmonisation is not desirable.
- The relatively low occurrence of foreign-based pension providers in most CEC member states is, in CEC’s eyes, not so much the result of obstacles for the freedom of services or the freedom of establishment. Rather, it is more plausible to attribute this fact to the institutional diversity in the field of occupational pension schemes within the EU. Simply put, the more individually a national model is shaped, the less likely it is that a foreign-based pension provider can offer an own model that fits the need of employees in this respective country.
- CEC expects that when a discussion takes place on strategies to facilitate cross-border activities of pension providers, the benefits and risks for employees receive the same attention as the pension providers’ economic interests in opening new markets for their products.

(Q6) What should be the scope of [occupational pension] schemes covered by EU level action on removing obstacles for mobility?

- In the past years CEC has criticised the Commission’s proposals on facilitating the portability of pension rights for being too rigid and for not respecting the historically grown diversity of pension systems in the member states. This argument applies in particular to book reserves whose role as an internal source of financing makes it impossible to treat them in the same way as externally funded systems when it comes to the issue of mobility or portability.
- Nevertheless, with the exception of book reserve schemes, most externally funded schemes can legitimately be the subject of new regulation that aim at a better mobility of employees.

(Q7) Should the EU look again at the issue of transfers or would minimum standards on acquisition and preservation plus a tracking service for all types of pension rights be a better solution?

- Besides the (above-mentioned) issue of mobility CEC has also in the past criticised the EU’s proposals for directives for being too “insensitive” to the different roles that occupational pension schemes can play in the different member states. There are member states or companies in which the funding of occupational pension schemes is more or less just one element of compensation. In other member states or companies, however, occupational pensions tend to be used as a human resources instrument, particularly with the goal to retain employees and to reward “loyalty” to the company. To a

certain degree these motives are still legitimate today, providing that vesting periods are not excessively long and provided that both the employer and the employee agree on not maximizing flexibility in their employment relationship.

- In sum, CEC is open to reasonable minimum standards. Maximum vesting periods should still be long enough for *employer-financed* pension schemes to be used as an HR instrument. In other words, CEC would prefer a “corridor” of maximum vesting periods that can be higher in one EU member state and lower in another, over a uniform standard.
- Beyond that, it goes without saying that any national legislation on issues such as minimum ages for the acquisition of rights or on vesting periods rights must comply with the existing EU regulation on age discrimination. In this field many national regulations that (today) still exist are currently being examined by courts. Some of these regulations might in the near future be found to be incompatible with EU legislation. This fact alone should in the long run also lead to more convergence as far as the acquisition and preservation of pension rights is concerned.

(Q8) Does current EU legislation need reviewing to ensure a consistent regulation and supervision of funded (i.e. backed by a fund of assets) pension schemes and products? If so, which elements?

- From CEC perspective, consistency in regulating funded schemes primarily means that regulation and supervision has to address the specific features and the specific systemic risks of each features.
- With differences from one member state to the other, occupational pension schemes share many similarities with private, non employment-related pension schemes on the one hand. On the other hand there are also considerable differences in many member states as a result of specific regulation for occupational pensions in the fields of labour and fiscal law. These differences are adequately reflected in the recent decision to develop specific solvency requirements for IORPs rather than applying the Solvency II standards that were primarily designed for non-employment-related insurance schemes. Accordingly, CEC expects that even under the new supervisory structure with one joint supervisory authority (European Insurance and Occupational Pensions Authority) sector-specific differences are adequately taken into account.

(Q9) How could European regulation or a code of good practice help Member States achieve a better balance for pension savers and pension providers between risks, security and affordability?

- To begin with, the member-states prerogative for shaping and reforming their member states’ pensions’ systems precludes any uniform EU-wide standards, with regard to investment risks or security. Not only would this contradict the subsidiarity principle. It also has to be taken into account that the acceptance and acceptability of investment risks vary from member state to member state.
- Nevertheless, CEC would welcome general policy recommendations aimed at reducing the investment risks for employees and individual investors in funded schemes. This would increase these systems’ sustainability, ensure their contribution to avoiding old-age poverty and indirectly contribute to financial stability: The more generously member states contribute to pension savings through tax reliefs or tax exemptions, the higher their interest in a reliable taxable income throughout the retirement period.
- To reach this goal, various instruments are conceivable, ranging from security-oriented investment strategies (life-cycle-investment), or provisions on minimum return over the

entire accumulation phase, to formal guarantees. Here, of course, the cost of any guarantees (such as lower returns) must be addressed.

Furthermore policy recommendations should also include a general recommendation for a sufficient portion of private and occupational pensions to be paid out as a life-long annuity. Lump-sum payments or temporary annuities should however remain a possibility provided that an overall income level above the poverty-level is ensured.

(Q10) What should an equivalent solvency regime for pension funds look like?

- The question touches on the issue whether or not, or rather: to what extent occupational pension systems should be the subject of the solvency requirements of the Solvency II directive.
- CEC objects to the notion that occupational pension systems and private pension funds (financed through private savings with no link to an employment relationship) are more or less identical as far as risks for an employee's pension rights are concerned. Accordingly, CEC does not support calls for the creation of one "level playing field" on which, indiscriminately, occupational and non-occupational pension funds should act under the same conditions.
- Rather, a solvency regime for occupational pension funds should take into account the specific legal features that exist in many countries such as a legal obligation of the employer to assume a pension funds liabilities in case of underfunding. Wherever such provisions exist that (verifiably) increase the protection of an employee's pension rights there is no need to apply the same strict solvency requirements that have been created for life-insurances or other pension funds without an employers' involvement.

(Q11) Should the protection provided by EU legislation in the case of the insolvency of pension sponsoring employers be enhanced and if so how?

- From CEC perspective, the legal requirements of the insolvency directive 80/987/EEC of 20 October 1980 and the level of protection that it provides to employees are relatively low for today's standards. Therefore more stringent rules on the EU level are conceivable at least in principle.
- However, here again, CEC calls on the Commission to respect the grown diversity of systems as long as they fulfil their role to protect employees' pension rights successfully. For CEC, a "blue-print" for a uniform European model on insolvency protection is not needed at this moment.
- Beyond that, CEC awaits the results of the study that has been launched by the Commission on the effectiveness of insolvency protection in defined-benefit systems and in book reserves schemes.

(Q12) Is there a case for modernising the current minimum information disclosure requirements for pension products (e.g. in terms of comparability, standardisation and clarity)?

- CEC supports the goal of improving the clarity and reliability of information on individual pension rights. However, in dealing with projections, one must bear in mind conflicts of interest. On the one hand, there is the individual's natural wish to plan ahead for his/her retirement. On the other hand, one must bear in mind the costs of compiling the information and also the question of liability for the employer or the pension provider. Information that solely projects the expected pension without any guarantee is of limited

value for the employee. On the other hand, the formal guarantee of a certain return limits the investment possibilities and increases the risk for the employer to be held liable in case of underfunding in later years.

- It might therefore be useful to define the conditions under which an employee can ask for a projection of his future retirement benefits (“legitimate interest”) and the frequency of such requests.
- Depending on the type of system (defined benefit, defined contribution with or without guarantees) and depending on the type of investment, the amount of information to which an individual is entitled will have to vary.
- Comparability is a legitimate goal in principle, but should not serve as a pretext for an EU-wide harmonisation of occupational pension systems.
- Beyond that, “clarity” and “comparability” are of course important goals. Another important issue that might be reviewed by the Commission, but which is not approached in this question, is the costs and fees of the investment, most importantly their disclosure before and after the conclusion of a contract.

(Q13) Should the EU develop a common approach for default options about participation and investment choice?

- CEC would welcome it if the EU encouraged member states to allow for more default options, in the sense that an individual (employee) could choose between a limited number of investment strategies involving different risks (for example by using some of the instruments mentioned in the answer to question 9).
- Nevertheless, given that one of the key features and strengths of occupational pension systems are collectively defined conditions for access, acquisition of rights and investment strategies. Therefore individualisation of investment choices should not reach too far.

(Q14) Should the policy coordination framework at EU level be strengthened? If so, which elements need strengthening in order to improve the design and implementation of pension policy through an integrated approach? Would the creation of a platform for monitoring all aspects of pension policy in an integrated manner be part of the way forward?

- CEC generally approves of soft law elements such as policy coordination through reporting and benchmarking systems. CEC has traditionally favoured these instruments over direct regulation.
- The existing processes of policy coordination have been both modified („streamlined“) and strengthened repeatedly in the past years. For example, the Open Method of Coordination in the field of socially policy has been confirmed by its formal introduction into new Lisbon Treaty (TFEU).
- For the time being, a further strengthening of this instrument is not necessary from CEC’s viewpoint.