JOHAN BARNARD
Head of International Public Affairs, APG

WILFRIED MULDER
Strategic Policy Advisor, APG

European Pension Plans

The initiative from the European Commission for the development of a Pan-European Personal Pension Plan (PEPP) aims at to many goals to be realized at the same time, using only one policy instrument. The focus should be on filling existing pension gaps, starting with the most important ones. More attention is needed for incentives and distribution, which may call for somewhat different approaches in different member states. Therefore the implementation of a phased and multifaceted approach should be considered.

Introduction

In its action plan[1] on building a Capital Markets Union, the European Commission announced that it "will assess the case for a policy framework to establish a successful European market for simple, efficient and competitive personal pensions, and determine whether EU legislation is required to underpin this market." In a "first status report" on the CMU[2] the Commission also announces a public consultation of its own, after having received requested advice from EIOPA in May 2016. Key idea of the Commission is to encourage more pension savings in order to increase pension adequacy in specific member states and/or for specific vulnerable groups,[3] and to channel these savings towards long term investing to help establish a Capital Markets Union. Although no decisions have been taken, both EIOPA (taking into account its recent consultation of a personal pension product)[4] and the Commission seem to consider a "2nd regime" for a third pillar pension product. An analogy often mentioned is UCITS.

Important to note as well, is that part of the justification for an eventual proposal may also be a need to enhance the internal market, both for pension providers as well as for beneficiaries and members. In some markets in some member states competition may be limited, and certainly European solutions would help achieve economies of scale. Workers making use of their Treaty rights by pursuing an international career are now faced with at least considerable complexity in catering for good pensions because of the existing differences in member state pension regimes.

Tinbergen rule

Dutch economics Nobel Prize winner Jan Tinbergen (1968) formulated a rule that in any systemic and coherent model of the economy, one needs at least an equal number of policy instruments to reach a given set of policy aims. Although politics, and also politics of European integration, often follow their own logics, this Tinbergen rule should make us pause to consider what the real aims for a Personal Pensions Plan could be. Mentioned are:

1. Enhance pension savings in the EU
2. Fill pension gaps in Member States without adequate pillar 1 and/or 2 systems
3. Encourage more long term investments
4. Encourage pension providers to provide services and/or establish across borders
5. Solve problems for workers with an international career in several Member States

All these policy aims are important, but to achieve them one may consider some prioritization and also adding further policy instruments.

Pension narrative?

The Commission announced its initiative to work on personal pensions in the context of the Action plan on building a Capital Markets Union, and therefore mainly as a source of savings that could be turned into needed long term investments. The risk of this framing is that one loses sight of the underlying ageing and pension adequacy problem, as is described in the Commission's 2012 White paper on Pensions[5] and in the 2015 Pension Adequacy Report. At the same time this context can also be read as an indication of ambition. Substantial extra long term investments need substantial extra savings. Therefore priority should be given to the largest pension adequacy problems. These do not relate to the relatively low percentage of international workers within the EU, but instead to large groups in the working population of several member states that either have no access to satisfactory pension products, or, for whatever reason, do not make use of these products. Starting from these groups and an analysis of their problems, appropriate (set of) policy instruments should be found. A third pillar European Personal Pension Plan can be one of those instruments, but the analysis should be broadened. In this respect a first step should be to further investigate the reasons of these inadequacies at national levels and to explain the differences between member states.

Distribution

At the present, still preliminary, phase of discussion, one gets the impression that a well defined European Personal Pension Plan, that can be provided by institutions of different kinds throughout the internal market, and that should be portable for those who take it, will sell itself to large numbers of workers. And this will certainly be the case if a solution is found to ensure that existing tax incentives at the national level, will apply to European Personal Pension Plans as well.

Unfortunately this may be too optimistic. By far the majority of workers in the EU do not work across borders, and in quite a few member states decent third pillar pensions are already on offer, so it is not immediately clear what the introduction of European Pension Plans would change. Apart from the availability of adequate pension products, a big issue is that consumers in general consider pensions to be complicated and not very attractive subjects to look into, which easily leads to postponing or not taking any decision on how to provide for one's old age. Traditionally this has been one of the reasons for the introduction of compulsory second pillar pension schemes in several member states (often by social partners). More recently behavioral economics have increased our knowledge and has led to initiatives to build better pension schemes by making use of 'nudging'. One of the most interesting, and at first sight successful, developments in this area being auto enrollment in the UK.

Cultural elements may play a role as well. The Netherlands for instance has both a well developed 2nd pillar and a decent market for 3d pillar products.[6] Nevertheless also in the Netherlands one can find pension adequacy difficulties, in particular relating to the growing number of self-employed without personnel. This group provides the Dutch labour market and economy with a lot of flexibility, but many do not sufficiently save for their pension. Several providers amongst which APG insurance subsidiary Loyalis, have created specific and very flexible products for this group, but demand has remained lower than expected.[7] Within a wider political debate on the future of Dutch pensions, one of the issues is pensions for the self-employed and the question whether an obligation, or a compulsory auto-enrollment system should be introduced. In parallel APG has set up a research project with the Erasmus and Harvard universities to study possible "nudges", that could lead to a better absorption(?) .

In order to effectively increase pension savings more attention is therefore needed to issues of distribution.

In terms of instruments attention also has to be given to 2nd pillar pension plans. The fact that at the European level no legal base may exist to legislate, should not lead to the immediate exclusion of this type of instrument, but rather to opening a dialogue with member states, for instance in the context of the European Semester, in which peer review between member states could lead to better economic policies at the national level. In addition the possible introduction of a High Level Group of experts to enhance occupational retirement provision in the member states, as mentioned in the recitals of the current proposal for a revision of the IORP-Directive (IORP II)[8] could be considered. And of course this IORP II could, thanks to the proposed reinforcements in the field of governance, risk management and the provision of information can play an important role in the further development of 2nd pillar pension plans.

Gresham's law?

In economics, Gresham's law is a monetary principle stating that "bad money drives out good".[9] In the pension's world some may hesitate about the introduction of a Pan-European Personal Pension Plan (PEPP), from the perspective that perhaps also "less sophisticated pensions, drive out better developed pensions". One of the main ideas behind a PEPP is to fill existing gaps where people do not have adequate pensions. The introduction of a PEPP should not inadvertently harmonize downwards well functioning existing pension schemes in member states with less pension adequacy problems (for example as a result of PEPP's replacing existing pension schemes), nor should it lead to a 'one-size-fits-all approach' in submitting different types of institutions to equal rules without taking due account of the differences between these institutions. It may be worthwhile to think a bit longer about this. More Europe, but less pension is not a good outcome.

Tax and other difficulties

As with other financial services, tax is very important. Many member states operate tax incentives to encourage pensions saving. Unfortunately they operate different systems, and tax harmonization requires unanimity under

the Treaty. It is obvious that European Pension Plans in order to be successful should be at least as tax efficient as existing national pension regimes. In other words: a discriminatory tax treatment of a European Pension Plan vis-à-vis similar national pension products should be avoided. Early engagement with tax policy makers at the national level will be crucial. Success will also depend on taking into account legitimate tax considerations. For example many member states operate a tax system where premiums and capital gains in the accumulation phase are tax exempt, but pension income in the decumulation phase is taxed.[10] In judging the design of a European Personal Pension Plan, tax policy makers may consider it instrumental that effective taxation in the decumulation phase takes place, irrespective of the question in which member state a pension is drawn. And certainly tax policy makers will worry about possibilities for tax arbitrage, for example in the form of tax deductibility of paid premiums in one member states and a tax exemption of the resulting pension benefits. These are legitimate concerns of national tax authorities that will have to be addressed, in particular if one aims for between member states portable European

Pension Plans. Wishing these problems away, or just arguing about the internal market, implicitly mounts up to asking the member states to give up taxing rights and therefore future government income. Solutions to these problems will however take time and may have consequences for the design of such a product.[11]

Similar difficulties may arise around issues like duty of care, labour law and contract law.

How to continue: a phased and multifaceted approach?

Taking into consideration the aforementioned Tinbergen-rule, it is perhaps possible to think of a phased approach in which not all problems will have to be solved with just one policy instrument, in one go.

The first work stream of such phased approach should be encouragement of more pensions' savings throughout the EU. The laudable initiative of Commissioner Lord Hill and his services could in this respect be reinforced by closely associating Employment Commissioner Marianne Thyssen and her services with this project. Perhaps it is possible to draft a core for a European Pension Plan in such a way that distribution is possible both as a personal as well as a collective Plan and therefore both in a 2nd and a 3d pillar context. The Commission should engage with member states to encourage them to do what is necessary at the national level to increase an uptake of more pensions by workers, be it national pensions or a new European pension scheme. In this context attention should also be paid to the question which institutions should provide pensions, and/or should be involved. Is this something one can leave to the market? Or could for instance social partners play a role as well?

The second work stream, which may take longer but could start at the same time, could look for a tax solution that is acceptable for all member states, also in a cross border context, and could be legislated in a tax directive. Advantage of starting in time with this would be that first results could then already l be taken account of in the design of a European Pension Plan, even before full unanimity is reached.[12]

In parallel other difficulties like duty of care, labour law and contract law will have to be identified and preferably solved. In order to alleviate difficulties of cross border workers, a first step could be a vigilant control by the Commission that existing Treaty rights, in particular non-discrimination, are scrupulously respected by the Member States. Furthermore the TTYPE-project ("Track and Trace Your Pensions in Europe"),[13] that seeks to establish a European tracking and tracing system that should allow all European cross border workers easy access to their pension situation in all relevant member states in an integrated way, could contribute considerably to the pension situation of cross border workers.

A third workstream could be to look at fundamental solutions for cross border pensions. These however may have wait until the moment the Member states are at least ready to agree to tax incentives that work across borders as well, if one does not want to run the risk of getting a very European outcome at the price of much less attractive pensions. (No incentives for anybody would go a long way to solve portability, but would not really help convince savers to buy these products ...)

1. Action Plan on Building a Capital Markets Union, COM(2015) 468 final, 30.09.2015
2. Brussels 25-4-2016, SWD (2016) 147 final.
3. Compare: The 2015 Pension Adequacy Report: current and future income adequacy in old age in the EU, joint report by the Social Protection Committee (SPC) and the European Commission (DG EMPL)
4. Consultation Paper on EIOPA's advice on the development of an EU Single Market for personal pension products (PPP), 1 February 2016
5. White Paper, An Agenda for Adequate, Safe and Sustainable pensions, European Commission, Brussels, 16 February 2012
6. In its recent 'Consultation paper on EIOPA's advice on the development of an EU Single Market for personal pension products', EIOPA-CP-16/001, 1 February 2016, EIOPA acknowledges this and mentions a particularly stark concentration of asset values in NL, UK and Be (page 9).
7. Figures are mentioned in a recent newspaper article: http://www.nrc.nl/nieuws/2016/04/27/zzper-en-pensioen-lastige-combinatie-1612548
8. Proposal for a Directive of the European Parliament and of the Council on the activities and supervision of institutions for occupational retirement provision (recast), Recital 9a
9. https://en.m.wikipedia.org/wiki/Gresham%27s_law has a nice explanation.
10. EET = exempt, exempt, taxed
11. Excluding the decumulation phase and maximizing flexibility for the consumer, almost automatically complicates finding tax solutions, while for instance a compulsory annuity for pension draw down would be easier to handle, under any EET scheme.
12. End result could be two legal instruments, one directive decided by the ordinary legislative procedure and therefore with qualitative majority voting in the Council and codecision with the European Parliament, and a parallel tax directive decided by unanimity in the Council.
13. See www.TTYPE.eu