SUPPLEMENTARY PENSIONS IN THE EUROPEAN UNION

DEVELOPMENT, TRENDS AND OUTSTANDING ISSUES

Report by the European Commission's Network of Experts
on Supplementary Pensions

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This report was produced by independent experts and should not be taken to represent the views of the European Commission.

List of Members of the Experts' Network on Supplementary Pensions

Mr. Giovanni Tamburi (Coordinator)	(Italy)
Prof. Carla Angela	Italy
Mr. Chris Daykin	United Kingdom
Prof. Vicente Gonzales Catala	Spain
Prof. Coriolano Albino Ferreira	Portugal
Prof. Erik Lutjens	Netherlands
Mr. Gerry Mangan	Ireland
Mr. Finn Østrup	Denmark
Prof. Pierre Pestieau	Belgium
Ms Hélène Petridou	Greece
Mr. Emmanuel Reynaud	France
Mr. G. Schroeder	Luxembourg
Prof. Heinz-Dietrich Steinmeyer	Germany

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INTRODUCTION

Purpose and Scope

In 1992 the European Commission decided to establish an Experts' Network on supplementary pension schemes, bringing together 12 independent national experts (one from each Member State) and a coordinator.

The Network's main task is to review and to analyse the different facets of the current development in Member States of schemes and arrangements, whether private or public, whose aim is to enable individuals to obtain at retirement a cash benefit over and above an individual's entitlement under mandatory state social security legislation. A specific topic in the Network's terms of reference is to relate the development of the 'second tier' of pension protection to issues relevant to the process of European integration.

In the course of 1993 each national expert contributed a report describing the main features of supplementary pensions in his/her own country and examining policy issues relevant to the national European debate in this area. The information contained and the opinions expressed in the national contributions have been summarised and joined together in the present consolidated report. In doing this, the Coordinator has - whenever necessary - inserted additional analysis in order to enhance the discussion of questions of particular relevance.

Following an initial clarification of terminology and definitions, this report is structured in chapters dealing respectively with:

- the origins and role of supplementary pension provision, with its social, financial and political implications (Chapter 1);
- an analysis of the link between supplementary provision and social security in terms of retirement income expectations and experience (Chapter 2);
- a sketch of the overall structure of the first and second tier of retirement provision in each Member State (Chapter 3);
- a full account of the supplementary pension schemes which have been made compulsory by way of national legislation (Chapter 4);
- a detailed description of the main features of voluntary and private supplementary pension arrangements (Chapter 5);
- a review and a summary of statistical data concerning the economic and financial implications of funding pension liabilities (Chapter 6);
- an overview of existing and/or proposed European legislation dealing with different aspects of supplementary pension rights (Chapter 7);
- an analysis of the European issue relating to cross-border labour mobility and pension rights (Chapter 8);
- an agenda for the future (Chapter 9).

The present report is aimed at a broad audience: those who seek an explanation of the origin, the role and the salient features of supplementary pensions as well as those specialists who have a professional interest in obtaining detailed national information. Naturally, the report is also addressed to readers who follow Community policies on pensions.

Terminology used and conventional definitions

The first tier of pension protection is constituted by public retirement income provision, that is the mandatory social insurance or social security programmes or schemes which are found in each Member State, albeit shaped differently according to national legislation. In the present report the first-tier will be referred to in short as 'social security'.

The terms of reference of the Experts' Network indicate that the present report should deal with the 'second-tier' of pension provision. Two questions, however, arise. The first relates to terminology. The term 'supplementary pension provision' is usually used in this report to describe the scope of the 'second tier', recognising that (i) in certain countries alternative terms are used, such as 'occupational pensions' (in the United Kingdom and Ireland), and that in French the relevant concept is expressed by using the adjective 'complementary' (*complémentaire*) rather than 'supplementary'. The second question, more importantly, relates to the definition of the scope of the 'second tier', an issue of great importance when comparisons are made between EC countries.

One is concerned not so much with a possible overlap between first and second tier but rather with establishing criteria that will allow the second tier to be separated logically from the third. Difficulties arise because of the similarities between the two tiers, such as their ultimate object (supplementary provision for retirement), the fact that the state encourages both (both may enjoy favourable tax treatment) and the fact that individual initiative is not necessarily an exclusive feature of the third tier.

A satisfactory demarcation line between the second and third tiers could not be achieved by opposing the concept of collective to that of individual arrangements, or by contrasting public with private provision, or by using the terms compulsory and voluntary alone. There are obvious second-tier supplementary arrangements that cut across such dichotomies (as will be shown later).

The distinction becomes easier if one recognises that, unlike the third tier, the second normally requires an additional element which is past or present membership in the workforce of an enterprise, or membership in a profession. It must be accepted that borderline cases do exist and that it would be pointless to ignore them, pretending that perfect, indisputable definitions can be given.

This report takes a pragmatic approach, treating borderline cases on their merits and taking account of their importance, while accepting that, as a general rule, the second tier of supplementary pension provision discussed here includes arrangements having the following characteristics.

(i) The benefits are intended to ensure that the person covered (member) acquires an entitlement to a cash benefit in the event of retirement (and, if the case may be, in the event of disability and death), representing income which would be additional (i.e. supplementary) to that due to the said person for the same contingency by the public retirement income system (social security).

(ii) Coverage is collective, i.e. plans and schemes are established for the benefit of a *group* of people (such as the employees of one or more companies, the members of an association, a given category of self-employed). Exceptions to the collective coverage criteria have, however, been made in order to cover cases where individual coverage or individual choice is a legally acceptable alternative for opting out of or opting in to a collective retirement arrangement. 'Legally acceptable' means here that the option exercised by the individual is specifically foreseen (permitted) by the regulatory framework of supplementary pension provision.

(iii) Coverage may be compulsory[1] or voluntary. For the purpose of this report, 'compulsory schemes' are meant to be those which impose on the employer a legal obligation to affiliate its employees either to a statutory scheme purposely established to provide pensions which are supplementary to social security or to a contractual supplementary scheme previously established by agreement between the social partners. Such a legal obligation may be directed not only to employers but, collectively, to self-employed persons. The usual definition adopted means that in this report 'compulsory schemes' do not include those based exclusively on a contractual obligation. Furthermore, the fact that an employee may be obliged to join his employer's scheme (if there is one), is not a criterion that defines the scheme as 'compulsory' in the context of the present report. The conventional definition includes among the compulsory arrangements those made by the state, through specific legislation, to provide supplementary retirement benefit to its employees.

CHAPTER 1
AN OVERVIEW OF THE ORIGIN OF AND THE RATIONALE FOR SUPPLEMENTARY PENSIONS

The development and the relevance of supplementary pensions are not the same throughout all the countries of the European Union. Their contribution to social protection or their impact on labour and capital markets varies considerably from one country to another. Public perception of the subject is not uniform either. It seems therefore important to begin the analysis of the present situation by clarifying an initial question: why do supplementary pensions present such dissimilarities within the EU?

All the countries of the European Union started early in the 20th century to adopt legislation and to organise institutions which were to ensure retirement income to large categories of wage earners and salaried employees in the private and public sectors. In Germany social insurance legislation dates back to 1891.

Old age pensions paid by social insurance were not necessarily generous. In the first half of the century they would hardly have enabled workers to maintain their previous standard of living, although certain occupational groups (i.e. public servants, miners) fared better than others.

Historically, a turning point was reached in the late 1940's when the influence of new and more ambitious social and political doctrines was increasingly felt, and when the guarantee of a decent income after retirement became a basic social and economic right to be granted to all citizens. A new approach to social security[2] with an increasing acceptance of welfare state policies, led all European countries to review and to reform the earlier state old-age and retirement systems.

During the 1950's and early 1960's, more and more categories of citizens were brought within the scope of compulsory pension insurance, reaching in some countries (the United Kingdom, Denmark and the Netherlands) the entire resident population. At the same time, old-age benefit levels were gradually improved. In spite of the pursuit of such common policies it became clear, however, that European countries were taking different paths as regards the role that public provision should play within an overall national pension strategy.

Countries in the northern part of Europe had strong traditions of government-sponsored non-contributory benefits and means-tested old-age pensions. It was natural for them to build a consensus around policies which, under the state scheme, would guarantee for the elderly modest pensions, often near subsistence level. The understanding was that private provision would fill the gap for those who wished for higher benefits and who could pay for them.

The development of social security in the United Kingdom is a good illustration of this approach. The reform of National Insurance (1948) along the lines recommended by Lord Beveridge (a modest flat-rate old-age pension for all) clearly spelled out the vitally important role assigned in future years to private pension provision.

In fact, company pension arrangements were already well established in the UK and no attempt was made by the government to restrict their development. Only in 1959 (when increasing prosperity created pressure for better pensions) was a graduated pension scheme introduced for employees, under which earnings-related retirement benefits became payable on the basis of earnings-related contributions. It was too late, however, to reverse public acceptance of, and public support for, occupational pensions already provided, at the time, to over 8 million employees. Consequently, the 1959 National Insurance Act permitted employers to 'contract-out' from the earnings-related retirement benefit if their employees enjoyed rights under an occupational scheme at least as generous as those available under the state scheme. This policy was enhanced by the 1975 Social Security Pensions Act which improved on the earnings-related pension entitlements (henceforth called *SERPS*) but maintained the 'contracting-out' option.

These developments revealed a deliberate governmental choice to seek a partnership between public and private provision, rather than trying to assert the primacy or priority of state benefit schemes.

Another example is Denmark. The present system for the state 'social pension', which comprises a basic flat-rate universal benefit, was introduced in 1957. Being a modest amount, the basic social pension left ample opportunities for additional provision outside the state scheme. During the 1960s and 70s, there was discussion over whether to improve the coverage of public pensions through the introduction of a supplementary pension scheme covering all employees or all residents. One result of these discussions was the establishment of the compulsory supplementary labour market pension (*ATP*), enabling wage earners to save for retirement with the financial contribution of their employers. The benefits under the *ATP*, however, turned out to be not very attractive. This led trade unions and individuals to seek better pension protection through additional private provision, and a number of pension schemes, covering employees belonging to a profession or to an economic sector, were negotiated between the labour market partners in the 1960s and early 70s. The wage negotiations which took place in 1989-93 extended supplementary pension schemes to cover the large majority of Danish employees.

It is interesting to recall that deliberate public policies aimed at creating opportunities for private pension provision were not exclusive to Anglo-Saxon or Nordic countries. In France, post-war legislation (1945) opted for earnings-related state old-age pensions well above subsistence level, but public policy clearly recognised and then encouraged a second tier of occupational pensions based on collective agreements freely negotiated by the social partners.

In Germany, the partnership between public and private provision may not have been as obvious as in other countries, but the outcome has not been very different. In this country, compulsory pension insurance was extended gradually, after the end of World War II, to various categories of citizens until 1972, when almost universal coverage was reached. Pension levels were gradually improved but, at the same time, supplementary pension arrangements, which had a long tradition in large enterprises, continued to expand and develop. No attempt was made by successive governments to limit them; on the contrary, fiscal policies clearly encouraged enterprises to earmark resources for private pension provision.

A different pattern emerged in the countries of southern Europe, and to some extent in Luxembourg and Belgium. Successive governments seem to have interpreted the post-war welfare state doctrines as requiring the state to meet all the retirement income needs of the labour force directly through state schemes. Compulsory pension insurance legislation set, from the start, generous income replacement levels for old-age benefits. The intention was clearly that private provision was to remain marginal or confined to highly paid employees.

Taking a broad view of all the EU countries, it can be said that alternative developments to public and private pension provision were, without significant exception, spurred on by a wide political consensus. Various political parties under different economic conditions all tended to move in the same direction, with the result that a substantial 'market' for supplementary pensions was opened in Denmark, the Netherlands, the United Kingdom, Ireland, Germany and, under different assumptions, in France and in Greece.

In the other European countries such an 'opening' was not encouraged and the debate remained dormant until the 'second wave' of pension reforms which reached Europe in the 1980's for reasons which are all too well known: social and demographic change, the maturing of pension programmes and the effect of liberal benefit provisions in a context of economic slowdown have all resulted in the escalation of the cost of providing public pensions and in increasing difficulties in finding the necessary additional financing. During the subsequent process of reviewing pension strategies, still outstanding in some European countries, governments have begun to look to private supplementary pensions as a means of providing retirement income, without, it is hoped, having to raise taxes and compulsory contributions in future years.

Contrary to what happened forty years ago when the State was confidently distributing the roles, private retirement provision seems to have now become desirable mainly as a 'remedy' for the difficulties encountered by the state in sustaining the growing cost of social security. This new perception is not without significance because it has reopened a debate, which some thought had been closed half a century ago, on the virtues, or otherwise, of relying on the individual initiative of workers and employers to enhance economic security in retirement.

A gradual shift of public policy is taking place in several countries. Spain (in 1987) and Italy (in 1993) have adopted comprehensive new legislation to encourage and to regulate private pension provision. The constitution of Portugal (1976) specifically assigned to private provision fundamental social security objectives. Between 1989 and 1992 this constitutional principle was implemented by way of specific legislation dealing with supplementary pensions.

In France, legislation has, since 1972, established that the *'régimes complémentaires'* managed by the social partners were to become compulsory for the large majority of private sector employees. Notwithstanding renewed government commitment not to deviate from the principles of *'répartition'* and solidarity between generations, on which such *'régimes'* rest, a change of emphasis in the government's plans for the future is noticeable in some of the statements included in the 1991 White Paper *(Livre Blanc sur les Retraites).*

Among the measures which, according to this White Paper, deserve closer scrutiny, mention was made of promoting the constitution of collective savings funds in various occupational sectors covering, for instance, all the workers of a given enterprise or occupational group. Established by the social partners, such supplementary pension funds would be financed according to the pre-funding technique (*'capitalisation'*).

The point is that renewed interest in the virtues of private provision is presented to the public with the help of considerations which go beyond the traditional argument according to which pensions (whether basic or supplementary) are a response to social goals and needs. The argument is that a shift towards more private provision would be beneficial because of financial, rather than social, considerations.

In Italy, for instance, the 1993 legislation regulating the growth of supplementary pension funds was a response to the government's declared aim of increasing savings and capital accumulation within the economy, of supporting and enlarging the domestic financial market, and of creating the capacity to absorb the huge amount of assets to be put on the market during the process of privatisation of public enterprises.

It should be added that financial objectives linked to the role of pension funds in capital markets are not new in Europe. However, they now acquire more weight and new exposure in the current political debate on pensions in those countries which have not had a long tradition of funded private pension arrangements.

The financial aspect of the rationale of supplementary pensions will be developed in Chapter 6. A few general explanations are, however, in order here because of the growing interest in the subject, and the fact that the European Commission has been developing specific new directives in this field.[3]

Old-age pensions paid and guaranteed by the state are, of necessity, financed through a pay-as-you go system, meaning that the pension costs of each year are covered by the taxes and contributions collected during roughly the same period. No reserves are accumulated, except as contingency provisions.

Private pensions, on the contrary, are often (not always) funded ('pre-funded'), meaning that future liabilities are matched by assets accumulated in advance through appropriate contributions. The funding technique (in French *'capitalisation'*) is standard practice in group-life insurance transactions and is also common practice in a large number of private pension funds (*'institutions for retirement provision'*, to use the EU jargon).

In the EU, many employers and workers participating in pension plans rely on group-life insurance contracts or similar insurance policies. Considerable reserves are accumulated by the relevant institutions.

As an alternative to insurance contracts, the sponsors of private provision have established pension funds, welfare institutions, pension trusts and similar financial vehicles which also pre-fund their liabilities according to actuarial standards. They do so either of their own free will or because the regulatory framework makes *'capitalisation'* (i.e. funding) a condition for obtaining preferential tax treatment on contributions or on investment yield (in Ireland, Italy, Spain, etc.).

Pre-funding private or occupational pension liabilities has generated large scale capital accumulation in countries such as the United Kingdom, the Netherlands, and Ireland. In the rest of the EU the volume of pension assets may be less striking but, on the domestic scene, it is not of negligible importance (see Chapter 6).

In Germany and in Luxembourg the use of tax deductible balance-sheet provisions (*'book-reserves'*) to back the employer's pension promises in a large number of enterprises, does not explicitly lead to the accumulation of segregated assets available for investment on the capital market. However, this technique does have an important economic and financial dimension because it has provided a welcome and substantial source of self-financing for the enterprise.

It is, however, fair to point out that in Europe there are many examples of private pension arrangements financed on a pay-as-you-go basis (apart from the special case of the *'régimes complémentaires par répartition'* in France). Public servants or civil servants funds in the United Kingdom, in Ireland, in Spain or elsewhere are relevant examples.

Economists have been arguing over whether or not the expansion of funded pension arrangements increases the rate of national savings. No consensus has emerged, which, in political terms, does not have much importance. What is certain, and is visible, is that pension funds as well as insurance companies managing pension assets, have become important and respected institutional investors in a number of countries such as the United Kingdom, the Netherlands and Ireland, to mention the most obvious markets in the EU. In a modern economy, with the increasing internationalisation of financial markets, the institutional investor wields considerable power and may have an influence on major corporate decisions.

From passive investors, fund managers have begun to take an active interest in company management, as well as in their finance. This reality, coupled with the fact that all EU governments have granted preferential tax treatment to the savings channelled through institutions for supplementary pension provision, justifies and explains the keen interest that finance ministries show for retirement income policies involving the private sector and which imply the funding of future liabilities.

Turning now to another issue, it will be recalled that the link with the labour market is often discussed as part of the rationale of supplementary pensions. It has been argued that the growth of employer-sponsored pensions may have an effect on labour mobility, on retirement choices, on labour productivity, on wage adjustment, etc.[4] The theoretical treatment of these subjects is not always supported by reliable empirical evidence, at least in Europe, although one does not deny that labour market issues do arise in this context and that they may be important.

In the present report attention will be focused only on the possible impact of supplementary pension provision on labour mobility because the subject is of particular interest for the European Union, which has among its fundamental aims the freedom of movement of persons within the Single Market. The European Commission is naturally concerned that cross-border labour mobility, in particular, should not be hampered by the ways in which membership and entitlement of workers to supplementary pensions is organised in various Member States. Chapter 8 will explain and develop this important issue.

In concluding, it could be said that historical factors[5] influencing the alternative choices made by Member States as regards the role of public pensions help to explain the dissimilarities now observed in the scope of supplementary pension provision. But even when 'first tier' policies were similar or convergent the supplementary pension scene took different paths, because of the preference given to a specific technique for financing the pension commitment in each Member State, a subject which will be fully illustrated in the following chapters of this report.

The differences in the outcome could also be related to the role played in this context by the trade unions: from an active and sustained role in certain countries (Denmark, France, Netherlands) to minor involvement in others (the United Kingdom).

CHAPTER 2
THE LINK BETWEEN SUPPLEMENTARY PENSIONS AND SOCIAL SECURITY

Assessing expectations from State pensions

For an individual, the desire to belong to a supplementary pension arrangement, or the preference given to subscribing to a retirement saving plan, springs essentially from the actual or the presumed inadequacy of the pension that the individual expects from social security. His perception is that more may have to be done to maintain the living standards enjoyed while at work.

For an employer, the incentive to sponsor a supplementary pension arrangement for his employees is more subtle. Several factors play a role: the desire to attract the best staff and to retain them, the need to match the behaviour of competitors, a sincere wish to care for staff welfare, and the importance of bargaining for pensions in overall industrial relation practices. Employers' motivation, as it is well known, is also strongly driven by available opportunities to reduce the company's tax burden through contributions to a staff pension plan. It has often been said that supplementary pensions are essentially 'tax driven'. The actual or the presumed inadequacy of the social security benefits at retirement does, however, also play a role in shaping employers' willingness to sponsor employees' pension plans[6].

Given the fact that acquiring entitlements to an old-age or retirement benefit is a long term process that may well span over 40 years (or more) in the life of an individual, and recognising that over such a long period social security legislation is likely to change more than once, the individual's perception of the actual or the presumed inadequacy of the expected social security benefit depends inevitably on assumptions.

Assumptions may derive from the observation of the amount of social security pensions currently received by people who have retired, at least by those in a comparable socio-professional environment and discounting personal factors. Assumptions may also be made with reference to available information on average expected benefits under current legislation. What proportion of final earnings (income) would be replaced by the social security pension at the time of retirement?

A general (not individual) answer to the question is provided by statisticians who simulate, through appropriate calculations based on a given set of assumptions, the so-called 'replacement rate' at retirement for a particular social security pension scheme.

This exercise is, as will be explained later, full of hurdles and traps due to the complexity and the volatility of some of the basic assumptions. Notwithstanding the difficulties, replacement rates are estimated, circulated and quoted frequently in technical reports and in press articles throughout Europe. Comparisons among EU countries are made and conclusions, often hurried, are drawn.

The EUROSTAT income replacement rates: highlights and interpretation

A very valuable recent source of information is an analytical study carried out by the Statistical Office of the European Communities, EUROSTAT, containing data on the relationship between retirement income and final pre-retirement earnings[7]. Data refers to 1989 earnings and to pensions claimed on 1.1.1990.

Two sets of figures are presented. One relates to gross pension and gross earnings at the point of retirement, another compares net pension with net earnings, that is deducting direct taxes and compulsory social security contributions. The results obtained reflect various hypothetical profiles as to marital status, length of insurance career and average level of earnings. The object of the analysis here is the first tier of pension protection. However, for countries with nationwide compulsory second-tier schemes these benefits are also included.

A general impression given by the EUROSTAT results is that social security benefits in many countries replace a very high proportion of pre-retirement earnings, in particular for average or lower income groups and for comparisons made on a *net* basis. This confirms the common perception that higher incomes attract relatively less from state schemes and that taxation tends to be less heavy for pensioners than for active persons.

Table 1:

Typical replacement rates for countries with high social security coverage, assuming a full insurance career

Country:	Gross rate (%)	Net rate (%)
Greece	87	96
Italy	70	79
Portugal	82	98
Spain	90	98

Assumptions: - male employee with spouse
- average wage at retirement
- first tier of compulsory coverage.

Remark: High coverage is taken to be that of a scheme offering rates above 70% on a gross basis.

A few key results of the EUROSTAT study are shown in a series of tables as an illustration of the prevailing trends; they are followed by a number of observations intended to put the results into perspective.

The picture looks different if one looks at the replacement rates corresponding to an average length of insurance career of 20 years (instead of 35-40 as in Table 1). A similar drop in the expected level of social security benefits for shorter careers at retirement can be observed in the other countries where replacement rates for a full career ranged between 40% and 70% (for the typical worker reflected in these tables).

The important point here is that social insurance records show that women, for instance, seldom reach a 'full' career. Long-term unemployment and extended periods of education and training may also reduce the number of years taken into account in the final pension calculation for both men and women. Migration is another factor, notwithstanding the compensating effect of the coordination of pension legislation achieved by the EU Regulations. The increasing frequency of early retirement also tends to reduce the length of insurance careers.

Table 2:

Typical replacement rates for countries with high social security coverage assuming an insurance career of 20 years

Country:	Gross Rate (%)	Net Rate (%)
Greece	61	67
Italy	40	51
Portugal	48	58
Spain	63	73

Assumptions: see Table 1.

There is a feeling, moreover, that the EUROSTAT replacement rates may tend to overstate the adequacy of social security pensions for another reason. Taking countries where old-age benefits are earnings-related (the majority in the EU), legislation prescribes that retirement pensions are calculated on the basis of the earnings of the covered person over a prescribed period before retirement (5, 10, 15 or more years). The trend now is to extend gradually this period and, in some countries, to reach the average of all the career's earnings (e.g. the recent reform in Italy). Unless the earnings in earlier years are effectively revalued when the pension is calculated, the benefit amount would accordingly suffer because the average would be negatively affected by inflation, wage trends, etc. The methodology followed by EUROSTAT in calculating replacement rates assumes that past earnings revaluation is thorough and complete in all cases, an assumption which could be challenged for countries such as Spain, Portugal or Italy. A recent study in France has shown that the technique used in the general scheme for employees to revalue past earnings may have the result of depressing the theoretical replacement rate for a full career at the earnings ceiling[8].

Table 3:

Typical replacement rates for countries with average or modest social security coverage, assuming a full or a reduced length of insurance career.

Country	Full career		20 years' cover	
%	Gross rate	Net rate	Gross rate	Net rate
France	45-69	54-83	24-38	29-46
Germany	53	69	23	31
Ireland	48	62	48	62
Netherlands	48	67	48	67
United Kingdom	35-46	45-59	16-27	21-34

Assumptions:
- male employee with spouse
- average wage at retirement
- first tier of compulsory coverage.

Remarks:

France: - the second figure in each column represents the rate including the compulsory *régimes complémentaires.*

United Kingdom: - the second figure in each column represents the rate including the earnings-related benefit component (*SERPS*).

Another point to be kept in mind is that the level of retirement income provided to an individual by social security at the date of retirement could be significantly eroded, in terms of living standards or purchasing power, unless the benefit is frequently adjusted upwards to take account of inflation, currency depreciations and trends in real wages. The replacement rates normally calculated and published, including those of EUROSTAT, only reflect the situation at the time of pension award. The effect - good or bad - of subsequent adjustment by various indexation techniques cannot be appreciated[9]. Recent experience has shown that, pressed by cost escalation and other unfavourable circumstances, governments tend now to be less generous than in the past, particularly when it comes to legislating on periodic adjustments of pensions in payment.

Pressure for supplementary pension provision has been more strong in a national environment where social security pensions (first tier) are not meant to replace a very significant portion of pre-retirement earnings, even on a net basis. A few examples, drawn from the EUROSTAT study, illustrate this point. The countries included in Table 3 are in effect those where the second tier of pension provision is well developed, as will be shown in following chapters.

Traditionally, employees in the higher wage bracket have been the first to benefit from supplementary, mostly private, pension arrangements. For them social security benefits tend to be much less adequate for maintaining the habitual standard of living.

The main reasons are twofold. In earnings-related pension schemes contributions and benefits are subject to an earnings ceiling and, in some schemes, a maximum pension amount is laid down. In flat-rate pension schemes, the flat-rate component is, by definition, degressive in adequacy (as incomes rise).

The level of the earnings ceilings observed in 1993 in EU countries, with reference to the general scheme for private employees are shown in Table 4, in local currency and in ECU. Apart from the impact of the earnings ceiling (Table 4) the pensions of higher income employees may be limited by upper limits applied by national legislation to benefit levels. First, we consider benefits when flat-rate benefits are given (Table 5). Secondly, we turn to the situation where legislation sets a specific maximum for the level of earnings-related retirement benefit (Table 6).

Table 4:

Earnings ceilings in social security pension schemes, 1993 (annual earnings)

Country:	Local currency	ECU's
Belgium	BF 1,330,000	32,500
France	FR 149,820	22,658
Germany, West	DM 86,400	44,055
Germany, East	DM 63,600	32,430
Greece	DR 5,299,000	19,841
Luxembourg	LF 2,372,892	58,886
Spain	PTA 4,057,560	27,076

Remarks: ECU rates as at 1 July 1993
Belgium: the ceiling applies only to the calculation of pensions (and not for assessing contributions).

Table 5:

Maximum annual benefit amount for a couple

Country:	National currency	ECU
Denmark	92,616	12,282
Ireland	5,668	7,048
Netherlands	25,114	11,417
United Kingdom	4,670	6,070

In Belgium, the earnings ceiling for contribution purposes has been abolished, but a ceiling is still applied to earnings on which the retirement pension is calculated, at present (1993) equal to BF 1,330,000, that is 32,500 ECU. A couple whose breadwinner worked 45 years would earn the maximum retirement pension of 25,125 ECU.

Table 6: Maximum annual benefit prescribed		
Country:	National currency	ECU
Greece	5,299,000	19,842
Luxembourg	1,923,446	47,732
Spain	3,437,644	22,939

Table 7:

Comparison between the limits imposed to pension entitlements and the income of non-manual workers
Recent estimates (ECU)

Country:	Earnings ceiling	Benefit ceiling	Average earnings, non-manual workers in industry
Belgium	32,500	25,125	26,148
Denmark	-	12,282	29,172
France	22,658	-	24,468
Germany, West	44,055	-	31,620
Greece	19,841	19,842	11,340
Ireland	-	7,048	23,352
Luxembourg	58,886	47,732	31,944
Netherlands	-	11,417	23,616
Portugal	-	-	8,172
Spain	27,076	22,939	19,320
United Kingdom	-	6,070	26,556

Remarks: For data in the first two columns refer to footnotes and explanations concerning Tables 4 and 5. Data in the third column are from: EUROSTAT, *Earnings in Industry and Services*, 1992, page 154. Figures are either last quarter 1991 or first quarter 1992, except for Luxembourg and the Netherlands (1990 data).
Italy: there is no earnings ceiling in the general scheme (*INPS*). In the pension scheme for executives and managers the earnings ceiling was 122,200 ECU per year in 1992.

In Italy, better paid employees with executive and management functions are affiliated to a special scheme which enables them to have higher benefits than those normally paid by the general scheme for wage and salary earners (*INPS*). The ceiling for this special group has been set at a relatively high level, 195 million lire per year in 1992, which was approximately

122,200 ECU. In the other five countries there are no specific benefit limits, except those resulting from the benefit formula.

The above information acquires more meaning when compared to the average earnings of potential beneficiaries (see Table 7). Confirmation that higher paid employees have lower expectations from social security is given by the results of the EUROSTAT study, looking at replacement rates for insured persons earning twice the average national wage (Table 8).

Table 8:

Typical replacement rates for employees earning twice the average wage in manufacturing

Country:	Full career		20 years' cover	
	Gross rate (%)	Net rate (%)	Gross rate (%)	Net rate (%)
Belgium	43	62	24	38
Denmark	29	46	29	46
France	31	40	17	21
Germany	39	55	18	24
Greece	78	89	45	59
Ireland	24	35	24	35
Italy	69	79	39	49
Luxembourg	54	65	30	39
Netherlands	24	37	24	37
Portugal	79	103	45	59
Spain	90	97	63	71
United Kingdom	17	24	8	11

Assumptions: - male employee with spouse
- first tier compulsory coverage

Since 1990, the year of measurement of the EUROSTAT replacement rates, the trend is towards downward benefit revisions, austerity measures and similar restrictions on future entitlements.

An example is the 1992/93 Italian pension legislation. A new pension formula will henceforth be applied to new entrants in the general scheme for employees, resulting in a drastic reduction of future replacement rates. The current generation is also - to a lesser degree - affected.

Similar measures have been taken in Greece: as from 1993 old-age benefits for new entrants will be far less generous than in the past (higher age, lower pensions).

A recent reform in Portugal (Law No.329 of 25 September 1993) introduced stricter entitlement conditions. The retirement age for women will be raised gradually from age 62 to 65, the minimum qualifying period of contributions for retirement benefits has increased from 10 to 15 years, the accrual rate has been lowered from 2.2% per year to 2.0% and the reference pensionable salary has been re-defined as the average of the gross salary over the best 10 years out of the last 15 (instead of the best 5 out of the last 10).

The suggestion that great care should be taken in handling the subject of replacement rates is confirmed by the following information, from national sources, illustrating pension levels from an angle which is different from that adopted by EUROSTAT.

Income replacement rates estimates from other sources

DENMARK

The level of the state universal social pension is fixed annually and is calculated with reference to the index for the average earnings of an industrial worker. There is no official goal as regards the income level provided through the social pension as compared with the average income of wage earners.

Average earnings of a male worker (1993) (estimate)	225,000 DKR
Income tax	101,800 DKR
Disposable income	123,200 DKR
Social pension for single person without supplements (for housing, heating, family circumstances)	58,200 DKR

The net replacement ratio provided through the social pension is relatively high, taking into consideration that pensioners receive a tax allowance which is the double that granted to working persons. A comparison of the disposable income of the average wage earner and of a single person receiving the old-age social pension is given by the following calculation, which does not take into account the various supplementary benefits that a pensioner may receive.

With the introduction of new tax rules from 1994, the double tax allowance for pensioners will be abolished but at the same time there will be a considerable increase in the social pension. The end result of the tax reform entering into force from 1994 should be an improvement of the relative income situation of pensioners.

In addition to the social pension, Denmark has instituted a second-tier compulsory retirement scheme, the Supplementary Labour Market Pension (*ATP*) (see Chapter 4). A person who has been a full-time wage earner since the establishment of the *ATP* in 1964 currently receives an amount of 9,600 DKR annually (which is subject to ordinary income tax). This represents a relatively modest amount compared to the benefits provided under the social pension.

FRANCE

A sample survey was carried out in 1988 in order to obtain reliable estimates of net replacement rates for employees with a full career. A full career is 37.5 years, according to the standard set by the general social security schemes for employees. The old-age pension after 37.5 years of service should be equal to 50% of average revalued earnings of the best 10 years. A contribution ceiling is traditionally applied in old-age pension insurance - it was Fr. 12,010 per month in 1992). The results of the survey are shown in Table 9.

In France, however, a second tier of pension provision which was initially organised voluntarily by the social partners was made compulsory for all wage earners and salaried employees in the private sector (see Chapter 4).

Consequently, social security replacement rates in France often include the effect of the compulsory membership of workers to the supplementary schemes (essentially *AGIRC, ARRCO*) which levy contributions on incomes below *and* above the social security ceiling.

Traditionally, public policy in France was that the desirable income replacement target including basic and supplementary mandatory schemes should be in line with the standard used for the civil service retirement scheme: 75% of the last gross remuneration for a full career. The trade unions continue to support this target.

Table 9:
France: Net replacement rate for selected levels of earnings under the first and second tier of compulsory pension coverage

Full career, year of birth 1922, year of observation 1988.

	only first tier		first and second tier	
Last monthly net earnings (Fr. Francs)	Males (%)	Females (%)	Males (%)	Females (%)
Less than 5,000	86	72	113	95
5,000 - 6,000	75	60	102	79
6,000 - 8,000	63	57	93	79
8,000 - 10,000	52	49	84	75
10,000 - 12,000	43	41	83	74
12,000 - 16,000	34	34	77	69
16,000 or more	20	n.a.	66	n.a.

The theoretical target of 75% seems to have been largely met for employees having a full insurance career thanks to, in particular, the effect of income tax schedules which favour retirement income and to a very substantial extent 'second pensions'. Many French pensioners, however, did not have a full career and received lower old-age pensions and the minimum pension.

For the self-employed different social security schemes operate both at the first and the second tier. The income replacement rates are uneven: they tend to be low for the self-employed in handicrafts, trade and commerce and high for liberal professionals.

GERMANY

The main national pension insurance scheme covers broadly wage earners and salaried employees (excluding civil servants) as well as self-employed persons who apply for mandatory coverage. It is administered by the Federal Insurance Office as regards salaried employees and by regional pension insurance institutions as regards wage earners, (see also Chapter 3, Germany).

The level of benefit depends on the number of years a person has been insured and his average earnings during these years in relation to the average income of all employees. There is an income limit for the assessment of contributions which is also relevant to benefit levels (see Table 4). Benefits are adjusted every year in accordance with the net wages of people in employment.

Pension insurance is aimed at guaranteeing an adequate standard of living in old age, understood as 70% of the last net earnings in employment after a full employment career of 45 years. This level is now set out in section 68, subsection 3, of the Social Code, sixth book (Public Pension Insurance). The net replacement rate in 1991 would be 68.3% for West Germany and

68.8% for East Germany in case of a full employment career of 45 years. For a career of 40 years the replacement rate would be 60.7% for West Germany and 61.1% for East Germany.

In 1990 the average number of years of insurance (earned or credited) of those applying for benefits was 37.3 years for men and 23.4 years for women in West Germany whereas the same numbers for East Germany are 47.1 years for men and 36.2 years for women. This means that for an average employment career the theoretical replacement rate aimed at by the legislation would not be achieved.

Social security benefits are only taxable in part. This part is in theory the revenue of contributions paid in the past (*Ertragsanteil*). The Income Tax Act (*Einkommensteuergesetz*) contains a table which shows the taxable percentage depending on the age of the pensioner at the beginning of payments of benefits. This percentage is 24% at age 65, 26% at age 63 and 29% at age 60.

Such percentages are very likely to be increased with effect from 1 January 1994. The percentage for age 65 then will be 27% and for age 60 it will be 32%. The recent reform of the pension insurance system (*Rentenreform 1992*) links the indexation of benefits to the variation of net wages and net benefits.

GREECE

The estimates made by EUROSTAT were based on legislation in force in 1990.The reform of social security effective 1 January 1993 has changed the conditions for entitlement to a retirement pension under the general scheme (*IKA*) reducing the expectations to benefit. Apart from the fact that pensionable age is to be gradually raised to 65, new entrants into the scheme with a full insurance career of 35 years cannot earn a pension representing more than 60% of gross pensionable earnings (revalued earnings of the last 5 years).

IRELAND

An analysis of the percentage of a male industrial worker's income replaced by the old age contributory pension, since it was introduced in 1961 is contained in two Irish studies (Hughes: 1985; Hughes: 1994)[10]. The analysis deals with net replacement rates, as earnings are subject to income tax and social insurance contributions, whereas a social insurance pension is exempt from taxation, if it is the only source of income. In 1961 approximately 20 per cent of the single male industrial worker's average gross earnings was replaced by the basic old age contributory pension. The replacement rate was around 23 per cent, when account was taken of deductions of income tax and social insurance contributions.

The gross replacement rate in 1982 for a single adult was over 29 per cent of average earnings and the net replacement rate was 42 per cent. Hughes points out that the much larger increase in the net replacement rate was due to the increase in the burden of income tax and social insurance contributions on the average industrial worker during that period.

In 1992, the gross replacement rate for a single person was 24 per cent of the average earnings of a male industrial workers and the net replacement rate was 37 per cent.

The net replacement rate for a married couple increased from about 36 per cent of male average industrial earnings in 1961 to over 62 per cent in 1982. In 1992 the net replacement rate was 51 per cent (where one spouse is under age 66), and 53 per cent, where both spouses are over age 66.

The replacement rates would be higher if account were taken, where appropriate, of the various allowances ('household', 'living alone' and 'over 80').

ITALY

Stricter entitlement conditions, lower accrual rates and a significant raising of state pensionable age have been introduced with the 1992 pension reform. The effect of such changes on the benefit level promised by the general scheme for employees (*INPS*) has been estimated as follows. For a future full career (40 years) of an employee the average gross replacement rate might be around 56 to 60% of final earnings, down from the present promise which varies between 70% and 80% gross, according to income. At present in Italy a large number of *INPS* pensions are awarded on the basis of fairly short insurance careers.

LUXEMBOURG

Pensions calculated on the basis of a full career, that is 40 years of contributory social security coverage, would represent on a gross basis 76% of the earnings level of active workers in non-agricultural employment. There would be a higher replacement rate for workers in agriculture.

The corresponding rate on a half-net basis (that is deducting compulsory social insurance contributions from the earnings of active persons) would rise to 85%.

PORTUGAL

The general social security scheme for employees and self-employed persons promises old-age pensions at the rate of 2.2% of the reference salary for each year of contribution, with a minimum of 30% and a maximum of 80%. The reference salary is the gross amount of monthly earnings averaged over the best five out of the last ten years of contribution. Pensions are paid in 14 payments over the year (one payment every month, plus at Christmas and Easter). There are no earnings ceilings.

Theoretically, with a full career of 37 years a worker should reach a gross replacement rate of 80% at retirement (it was only 70% between 1965 and 1982).

In practice, replacement rates are lower because:

- monthly earnings averaged for the purpose of pension calculations are not revalued for inflation or changes in salary scales;
- pensionable earnings do not include miscellaneous items of compensation (bonuses, allowances);
- average contribution careers fall short of 37 years;
- there are delays in indexation in the year of award.

Neglecting the effect of inflation is a serious shortcoming in pension calculations because in Portugal the consumer price annual index increased between 9% and 13% during the last six years (higher rates were recorded in previous years).

The average length of an insurance career was - in 1991 - less than 15 years for 68% of the pensioners retiring in that year. Only 7% of pensioners could claim on the basis of a full career. As a consequence 61% of pensioners were drawing only the minimum pension (52.10% of the minimum wage). The average pension was only 22% higher than the minimum.

A favourable circumstance for the pensioner is that pensions are subject to lower personal income tax rates than earnings. Moreover, the threshold of taxable income is such that it is estimated that about 97.7% of pensioners virtually pay no income tax.

In theory, a single person retiring in 1992 on the basis of a pensionable salary averaged over the period 1987-1991 and with a full career (37 years), would reach in 1992 and 1993 a replacement rate of 68.9% gross and of 85.1% net.

The above empirical rates appear to be lower than the comparable estimates shown in the EUROSTAT study.

SPAIN

Old-age pensions under the General Scheme for Employees are paid at age 65 subject to a minimum period of contribution, at present 15 years. The pension rate is 50%, of average relevant earnings, for the first 10 years of contribution, plus 2% per additional year, reaching 100% after 35 years of contribution. A minimum pension is guaranteed from age 65 to a beneficiary with a dependent spouse: in 1993 the minimum annual amount was Ps. 780,150.

The average annual amount of all the new pensions awarded in 1992 was Ps. 1,171,380. This amount, compared with average insured earnings (Ps. 1,684,464), shows an average replacement rate of 69.5%. This gross rate is influenced by the actuarial reduction applied to early retirement pensions (8% per year between age 60 and 65) because the group of the 1992 new pensioners retired on average at age 62.4. Another factor to be taken into account is that average revalued earnings are calculated on the basis of annual earnings over the last 8 years, of which only 6 are revalued to neutralise the effects of inflation.

UNITED KINGDOM

The amount of the flat-rate National Insurance old-age pension payable to residents at 65 (men) and 60 (women) corresponded in 1992 to approximately 18 per cent of national average earnings. For the lowest paid workers whose earnings are around £3,000 per year the flat-rate pension for a person with a complete contribution record would yield a replacement rate of 100%; but as earnings increase this rate falls.

In addition to the flat-rate old-age pension, earnings-related pensions are payable from state pensionable age to those who have contributed as employed persons. The earnings-related scheme was only introduced in 1978, and thus has not yet matured. Persons reaching state pension age in 1993-94 can receive an additional pension of around 18% of revalued career average earnings in the band between the lower and upper earnings limit. This proportion will rise to 25% for those reaching state pension age in 1998, before falling gradually to 20% for those reaching state pension age in 2001 and later.

Table 10:
UK: Replacement ratios for different generations at different earnings levels. Total basic pension and additional pension as percentage of earnings

Earnings as percentage of all persons average earnings

Year of award	25%	50%	100%	200%	300%
1993	76	48	33	20	14
1998	75	50	37	23	15
2003	70	47	35	21	14
2008	66	44	33	20	13
2013	63	42	31	18	12

Notes: Additional pension is calculated on the basis of constant earnings in each year at specified level in terms of all persons average earnings, excluding absence.
It is assumed that full contributions are paid in each year of working life.
Basic pension and additional pension in the year are shown as a percentage of average earnings in April of that year.
Actual earnings are taken into account to 1991/92; assumptions for 1992/93 and 1993/94 are:

Upratings	5%
Earnings	6.575%

For the long term it is assumed that upratings of pensions will be in line with a cost of living of 5% per year and an earnings increase in real terms of 1.5% per year.

An estimate was made of the maximum possible replacement rates for a few selected generations at different earnings levels, including both the flat-rate and the earnings-related components of the old-age social security pensions.

Contrasting expectations with present conditions

The information obtained from national sources should help to put the results of studies, such as the study by EUROSTAT, into perspective. While the replacement rates give a measure of the potential coverage under current social security legislation, figures on the amount of pensions in payment at present, particularly those emerging from earnings related schemes reflect the past history of insured persons during times when wages were lower and periods of insurance coverage shorter, particularly in schemes which have not yet reached maturity. Benefits in course of payment also reflect the number - considerable in some countries - of pensions which were awarded in the past at minimum rates.

Statistically it would not be very significant to compare current average pensions with average earnings of the working population. The average hides the situation of individual groups in the respective distributions. On the other hand, a full statistical analysis of the relationship between salary distribution and the relative position of different categories of pensioners is beyond the scope of the present report.

A comparison in national currency could be attempted for the countries paying flat-rate old-age pensions, which are not based on averages but are universal uniform entitlements.

Country	Flat rate pension	Average earnings salaried employees (industry)
Denmark	DKr 92,616 (1993)	DKr 231,500 (1992)
Ireland	Ir£ 5,668 (1992)	Ir£ 17,900 (1991)
Netherlands	HFI 25,114 (1993)	HFI 54,860 (1990)
United Kingdom	£ 4,670 (1993)	£ 18,780 (1992)

The differences in the years for which data are available are regretted; nevertheless the order of magnitude of the relationship between the two series can still be appreciated.

For other countries, the following information may help to throw some additional light on the present level of social security pensions for various groups.

In Italy the average annual amount of pensions in payment at the end of 1991 was as follows:

General scheme for employees	Lire 10,625,000
social pension*	" 4,649,000
self-employed	" 6,348,000
special schemes: - banks - transport, telephone, etc - mines, gas, etc.	 28,797,000 21,807,000 19,182,000
*paid at age 65 to citizens without pension insurance entitlements (means-tested)	

In France the overall average retirement pension paid under the general scheme for employees at 31.12.1990 was Fr. 30,109 per year, an amount considerably higher than the average pension in payment for other categories such as agricultural labourers (Fr. 13,440), artisans (Fr. 18,794) or farmers (Fr. 17,315). It was, however, much lower than the average pension enjoyed by lawyers (Fr. 54,800).

In Germany, data for 1992 show that old-age pensions in payment (net of health insurance contributions) for employees retiring at 65 were significantly lower (DM 1,325 per year) than those of employees who had retired at 63 (DM 2,273).

In Luxembourg a special survey was carried out to assess the retirement pension actually paid to insured persons who retired in 1990 and in 1991. Out of the 5,000 new pensioners only about 900 had a full insurance career. For the latter group the relationship between the pension and last earnings gave replacement rates very close to those shown in the EUROSTAT study (full career).

In Spain the average annual pension currently in payment by the general scheme in 1992 was PTA 1,070,426 while for coal miners it was 1,677,830 and for agricultural labour 669,088.

These few examples underline the concern of pension analysts to acquire a fair perception of the actual and potential level of income security guaranteed by the social security retirement benefits in order to plan for a second tier of protection. One should not forget that at present social security pensions do represent the most important means of financial support for millions of pensioners, as illustrated by the examples presented in Table 11.

Table 11:
Sources of income of pensioners:
Available estimates for EC countries

% of total income received from each source

Country:	State pension	Supplementary pension	Employment	Investments, property	Other
France (1984)	85.2		6.0	8.8	-
Germany (1986)	78.0	15.0	2.0	4.0	1.0
Ireland (1983)	55.2	38.4	1.9	4.3	0.2
Netherlands (1989)	76.0	15.0	1.0	4.0	4.0
United Kingdom (1988)	51.0	23.0	8.0	17.0	1.0

Remarks:
France: Former employees (*salariés*) aged over 60 and not employed full-time.
Germany: excluding civil servants
Ireland: recent pensioners
Netherlands: data refer only to persons in receipt of a basic pension, with total annual income in the range of: HFL 22,000 to 26,000 per year.

A study made in Belgium about the sources of income of persons aged 54 or more showed that in 1988 the social security pension represented 85.2% of the total for persons in the lowest income quartile but only 28.4% in the highest quartile.

The data for Greece, admittedly not representative of all categories of pensioners, does nevertheless indicate that 88.5% of income after retirement was attributable to pensions from compulsory schemes.

Table 11 also confirms the greater role occupied by occupational pensions in overall retirement income in countries such as Ireland and the United Kingdom whose social security legislation provides universal retirement pensions at a modest rate.

To conclude this section, it is interesting to show the results of a sample survey carried out among retired people between 20 April and 18 May 1992 under the auspices of Directorate-General V of the European Commission. Retired people were asked whether the pension income they received at the time of the survey from the state and from supplementary arrangements was, in their opinion, adequate.

The answers are summarised as follows in the relevant publication[11]:

"Three groups of countries can be observed. A first group comprises Denmark, Germany (including this time the former GDR), Luxembourg, the Netherlands and (to a lesser extent) Belgium; here vast majorities of older people declare themselves as satisfied (many 'completely') about the adequacy of their pensions. Smaller, but still significant majorities in these countries also feel that, taking into account the contributions made during their working life, the pension they receive allows them to lead the life they would like to live. A second group comprises Spain, France, Ireland, Italy and the UK; here opinion is more divided between adequacy and inadequacy and the balance contribution/pension received is considered as not very favourable. The pension systems of these countries do not quite seem to pass the 'contentment' test. The third group comprises Greece and Portugal, where dissatisfaction is the substantial majority view, on both counts: a significant amount needs to be done by these countries to meet the pension aspirations of their citizens. It is interesting to note that, at aggregate EU level, women tend to be less satisfied than men: only 48% as opposed to 59% men consider the pension they receive as (completely/just about) adequate and only 33% as opposed to 42% of men think that they receive (definitely/probably) a decent pension considered the contributions they made. As we have already noted, pension systems, in penalising career interruptions, have an unfavourable indirect bias against women"

Similar questions were asked of a sample of non-retired persons. The pattern of their responses was rather similar to that of the retired.

The pursuit of global pension objectives

Social security and supplementary pensions are two facets of the same retirement income coin but are they linked to social security by common deliberate objectives or are the two tiers of protection developing fairly independently? This question, briefly touched upon in Chapter 1, deserves further development because the answer is not the same for all countries of the EU, as shown by the following examples.

In France, the general social security pension scheme for employees has developed since the 1950's in full awareness that the social partners were taking responsibility for the organisation of a supplementary pension that would eventually reach the same categories of the population. The social security earnings ceiling for pensions has been deliberately maintained at reasonable levels in order to allow room for the supplementary schemes. A coherent policy has been followed in relation to pensionable age. Trade unions and employers have negotiated on the understanding that for workers with a full career (37.5 years or more) an income replacement rate of 75% of last gross earnings was the desirable objective for the sum total of the state plus supplementary pension. The confirmation that public policy endorsed such a package came when the largest supplementary schemes were extended and made compulsory.

In Germany a different attitude seems to have prevailed so far. The state views the old-age benefits of its social security system for both private and public employees as providing adequate retirement income: sufficient, in principle, to maintain the pre-retirement standard of living. The role of supplementary provision seems to be appreciated by the state for what it is: a voluntary and private initiative, undoubtedly useful since it is encouraged through preferential fiscal treatment. On the other hand, the social partners are not necessarily convinced that the state pension is adequate in all cases and have shown considerable interest in the development of a private second tier. Trade unions, in particular, have sometimes argued that company pensions are part of the global remuneration package. Employers, who are predominantly financing the second tier, tend to worry about public interference (notably from the Federal Labour Court) rather than pressing for a coherent joint public policy between compulsory and private provision.

The perception of the link with social security in Ireland is quite specific. The main priority of public policy on pensions has been to ensure that all residents in Ireland will have a minimally adequate income in the event of retirement/old age, permanent incapacity for work and, for surviving dependants, in the event of death. The state social security pensions system was designed to achieve this objective through both flat-rate pensions under social insurance and social assistance.

Based on the recommendations of a Commission on Social Welfare, the Government position is that the introduction of an earnings-related second-tier pension is not a priority. The main objective is to use limited resources to improve the income position of all categories of people in need (not only the elderly). The deliberate policy is therefore to rely on occupational schemes and private pension arrangements to provide supplementary pension cover, in particular, for those on higher than average earnings.

Occupational pension schemes have been established for virtually all public employees and employees of semi-state bodies, of both a commercial and non commercial nature. The state promotes the establishment of occupational and private pension arrangements in the private sector through the favourable tax treatment accorded to contributions to these schemes and to returns on investment of scheme assets, and by providing for a regulatory system under the Pensions Act 1990 to safeguard pension rights, including the rights of early leavers. The Pensions Act also prohibits discrimination between men and women. Benefit targets in private arrangements are not a matter of public policy, except that there are upper benefit limits for the purposes of the tax treatment accorded to such arrangements.

The view of the Netherlands government and the policy so far pursued is that the state is responsible for ensuring an adequate but *basic* income to all citizens and that it has fulfilled this responsibility through the universal *AOW* social security scheme.

According to this view, responsibility for supplementary pension arrangements rests with the social partners. The legislature has only a limited twofold task with regard to supplementary pension arrangements. In the first place it has the task of creating a suitable regulatory framework. To this end, the legislature has, for example, introduced tax facilities relating to supplementary pensions, and has established rules making certain industry pension funds compulsory.

Secondly, the state acknowledges its responsibility (with regard to supplementary pension schemes) to deal with matters of public interest, for example, combating discrimination (such as discrimination between men and women), and protecting early leavers' rights in supplementary pension schemes.

In the United Kingdom public policy for more than a decade has been to restrict the growth of public provision for retirement and to encourage the growth of private provision. The basic pension is intended to provide a low level of guaranteed retirement income for the majority of members of the population, financed according to ability to pay by earnings-related contributions (subject to a ceiling).

In the government's view, the second tier of retirement income should ideally be provided by occupational pensions or personal pensions. In recognition of the fact that the coverage of such arrangements is not universal and is unlikely to become so in the foreseeable future, an additional earnings-related pension facility (*SERPS*) was introduced in the state system. This is clearly envisaged as a back-up, or safety net, and every encouragement is provided to employers and to individuals to replace this additional level of social security by occupational or personal pension provision. Social security incorporates incentives to encourage private provision. Tax incentives are given to encourage both occupational and personal pensions. The self-employed are covered by the basic pension and are encouraged to make further provision through tax-efficient personal pensions.

The five countries taken as examples are a fair illustration of the trend toward adopting a global policy approach in respect of the respective roles of basic and supplementary retirement provision. In other EU countries the degree of deliberate integration of the two components into a global strategy is not as clear, particularly where the second tier still performs a marginal role. However, the rationale for supplementary pensions is a pervasive one: it contains social and financial considerations which inevitably fall into each country's political debate and, sooner or later, filter through government policy, even where, traditionally, a global pension strategy was not systematically pursued.

CHAPTER 3: THE STRUCTURE OF NATIONAL TWO-TIER PENSION PROVISION

1st Tier: **Social Security**
2nd Tier: **Supplementary Pensions**

Remark:

The following country tables have to be read in conjunction with Chapters 4 and 5, where the terminology used is fully explained and where the scope and nature of the various *second tier* schemes and arrangements, which are part of the national structure for pension provision, are described in some detail.

<table>
<tr><th colspan="4">BELGIUM

First and Second Tier of Pension Provision
OVERALL STRUCTURE</th></tr>
<tr><td>1st tier Social Security</td><td colspan="3">- General scheme for employees in the private sector
- Pension scheme for the self-employed
- Civil service pension scheme</td></tr>
<tr><td rowspan="5">2nd tier supplementary pensions</td><td colspan="3">VOLUNTARY:</td></tr>
<tr><td rowspan="4">Private Sector Employees (mainly white-collar)</td><td rowspan="2">Insurance</td><td>Group contracts</td></tr>
<tr><td>Deposit administration</td></tr>
<tr><td rowspan="2">Non-profit institutions</td><td>Pension funds ASBL/VZW</td></tr>
<tr><td>Mutual associations</td></tr>
</table>

<table>
<tr><th colspan="3">DENMARK

First and Second Tier of Pension Provision
OVERALL STRUCTURE</th></tr>
<tr><td>1st tier Social Security</td><td colspan="2">Universal Social Pension</td></tr>
<tr><td rowspan="8">2nd tier supplementary pensions</td><td colspan="2">COMPULSORY:</td></tr>
<tr><td>Private sector employees</td><td rowspan="2">Supplementary Labour Market Pension (ATP)</td></tr>
<tr><td>Public sector employees</td></tr>
<tr><td colspan="2">VOLUNTARY:*</td></tr>
<tr><td rowspan="2">Private sector employees</td><td>Company schemes administered by life assurance companies or company pension funds</td></tr>
<tr><td rowspan="2">Schemes covering specific occupations or economic sectors administered by life assurance companies or industry-wide pension funds</td></tr>
<tr><td rowspan="2">Public sector employees</td></tr>
<tr><td>Special schemes**</td></tr>
<tr><td colspan="3">* Excluding personal plans with banks/insurance companies. An employee taking a job in a company where a pension scheme has been established by a collective agreement is obliged to join the scheme.
** Pensions are paid through the state budget to public employees with the status of 'public official' (tjenestemand).</td></tr>
</table>

<table>
<tr><th colspan="3">FRANCE

First and Second Tier of Pension Provision
OVERALL STRUCTURE: I. EMPLOYEES</th></tr>
<tr><td>1st tier Social Security</td><td colspan="2">General social security scheme for employees in industry, trade and services.
Agricultural employees' social security scheme.
Special schemes for public servants and for miners, seafarers, notary clerks.</td></tr>
<tr><td rowspan="8">2nd tier supplementary pensions</td><td colspan="2">COMPULSORY:</td></tr>
<tr><td colspan="2">Private sector employees: ARRCO and AGIRC schemes OR:</td></tr>
<tr><td colspan="2">Other compulsory schemes (for employees in social security*, civil aviation, agricultural services, savings institutions)</td></tr>
<tr><td colspan="2">Scheme for public sector employees without civil servant status (IRCANTEC)</td></tr>
<tr><td colspan="2">VOLUNTARY:</td></tr>
<tr><td>Private sector employees</td><td>Employers can add:
- additional contributions to AGIRC scheme
- top hat arrangements
- savings plans</td></tr>
<tr><td>Public servants, non-classified public employees</td><td>PREFON or CREF schemes</td></tr>
<tr><td colspan="2"></td></tr>
<tr><td colspan="3">* Since 1.1.1994 has joined the federations AGIRC and ARRCO</td></tr>
</table>

FRANCE OVERALL STRUCTURE: II. SELF-EMPLOYED		
Category of self-employed:	1st tier Social Security:	2nd tier supplementary pensions:
Farmers	Social insurance scheme (*MSA*)	Voluntary, *COREVA*
Industry and commerce	Special fund, *ORGANIC*	Compulsory survivors benefit + optional coverage
Handicraft	Special fund, *CANCAVA*	Compulsory + optional coverage
Liberal professions	Special fund, *CNAVPL*	Compulsory + optional coverage, depending on profession
Lawyers	Special fund, *CNBF*	Compulsory
Church Ministers	Special fund, *CAMAVIC*	none

<table>
<tr><th colspan="3">GERMANY

First and Second Tier of Pension Provision
OVERALL STRUCTURE</th></tr>
<tr><td>1st tier Social Security</td><td colspan="2">- General pension insurance for wage earners, salaried employees and non-established public sector employees*
- Civil service pension scheme
- Miners' pension scheme
- Self-employed farmers' pension scheme</td></tr>
<tr><td rowspan="8">2nd tier supplementary pensions</td><td colspan="2">COMPULSORY:</td></tr>
<tr><td>Public sector employees</td><td>Supplementary Civil Service Pension Scheme</td></tr>
<tr><td colspan="2">VOLUNTARY:</td></tr>
<tr><td rowspan="4">Private sector employees</td><td>Direct commitment (Direktzusage) by employer; book reserve with insolvency insurance (Pensionssicherungs-verein, PSV)</td></tr>
<tr><td>Group insurance contracts (Direktversicherung)</td></tr>
<tr><td>Pension funds (Pensionskassen)</td></tr>
<tr><td>Support funds (Unterstützungskassen), with insolvency insurance (PSV)</td></tr>
<tr></tr>
<tr><td colspan="3">Certain categories of self-employed are also covered (teachers, craftsmen, artists, etc.). There is a separate compulsory scheme for construction workers.</td></tr>
</table>

GREECE **First and Second Tier of Pension Provision** **OVERALL STRUCTURE**	
1st tier Social Security	- General scheme for employees and urban self-employed, *IKA* - General scheme for the rural sector, *OGA* - Special schemes (civil servants, etc.)
2nd tier supplementary pensions	COMPULSORY:
	IKA/TEAM, private sector employees in industry commerce, services
	NAT, seamen
	IKA/ETEAM, public sector employees, including bank employees
	Auxiliary funds, employees or self-employed
	OGA, agricultural employees and self-employed
	Civil servants' funds
	Provident funds (lump sums only)
	VOLUNTARY
	Mutual associations (under the Civil Code)
	Single employer group insurance contracts

<table>
<tr><th colspan="3">IRELAND

First and Second Tier of Pension Provision
OVERALL STRUCTURE</th></tr>
<tr><td>1st tier Social Security</td><td colspan="2">- Universal non-contributory pensions for all residents (means-tested)
- Social insurance (contributory) pensions for employees and the self-employed (non means-tested)
- Occupational pensions (earnings related) for certain public sector employees who are exempt from social insurance pension cover</td></tr>
<tr><td rowspan="5">2nd tier supplementary pensions</td><td colspan="2">VOLUNTARY:</td></tr>
<tr><td rowspan="2">Employees in private sector and commercial public sector</td><td>Self-administered pension funds</td></tr>
<tr><td>Group insurance contracts</td></tr>
<tr><td>Employees in non-commercial public sector</td><td>Public sector superannuation schemes (pay-as-you-go)</td></tr>
<tr><td>Self-employed</td><td>Personal pensions</td></tr>
</table>

<table>
<tr><th colspan="3">ITALY

First and Second Tier of Pension Provision
OVERALL STRUCTURE</th></tr>
<tr><td rowspan="3">1st tier Social Security[1]</td><td>Private sector employees</td><td>General scheme (FPLD) managed by INPS and 8 special schemes including the industrial managers' pension scheme (Dirigenti)</td></tr>
<tr><td>Public sector employees</td><td>Special schemes: central government, local government</td></tr>
<tr><td>Self-employed</td><td>14 special schemes</td></tr>
<tr><td rowspan="6">2nd tier supplementary pensions</td><td colspan="2">VOLUNTARY
(Situation before Decree-Law 124/1993)</td></tr>
<tr><td>Private sector employees</td><td>Single employer funds, industry-wide funds, sectoral funds[2]</td></tr>
<tr><td colspan="2">VOLUNTARY
(Situation after Decree-Law 124/1993)</td></tr>
<tr><td rowspan="3">Employees and self-employed</td><td>Funds in operation before D-L 124/1993</td></tr>
<tr><td>Closed pension funds, post-1993</td></tr>
<tr><td>Open pension funds, post-1993</td></tr>
<tr><td colspan="3">Notes:
1 From 1.1.1993 private and public sector pension insurance legislation has been harmonised and unified, subject to maintaining separate management and accounting for the existing schemes.
2 Pre-1993 funds were either pay-as-you-go, funded, book-reserve or directly provided by the employer. Public employees' supplementary pensions would fall under compulsory provisions.</td></tr>
</table>

LUXEMBOURG

First and Second Tier of Pension Provision
OVERALL STRUCTURE

<table>
<tr><td>1st tier Social Security</td><td colspan="2">- General schemes for employees (2 schemes) and self-employed (2 schemes)
- Public employees' pension schemes
- Railway employees' pension fund</td></tr>
<tr><td rowspan="4">2nd tier supplementary pensions</td><td colspan="2">VOLUNTARY</td></tr>
<tr><td rowspan="3">Private sector employees</td><td>Direct commitment by employer with or without book-reserve</td></tr>
<tr><td>Group insurance contracts</td></tr>
<tr><td>Pension funds</td></tr>
</table>

<table>
<tr><th colspan="3">NETHERLANDS

First and Second Tier of Pension Provision
OVERALL STRUCTURE</th></tr>
<tr><td>1st tier Social Security</td><td colspan="2">Universal schemes for all persons resident in the Netherlands:
- Old-age pension (AOW)
- Widows'/widowers' pension (AWB)
- Disability pension (AAW)</td></tr>
<tr><td rowspan="8">2nd tier supplementary pensions</td><td colspan="2">COMPULSORY:</td></tr>
<tr><td>Private sector employees</td><td>Industry-wide funds</td></tr>
<tr><td rowspan="2">Public servants</td><td>Civil service pension fund (ABP)</td></tr>
<tr><td>Railway employees' fund</td></tr>
<tr><td colspan="2">VOLUNTARY:</td></tr>
<tr><td rowspan="3">Private sector employees</td><td>Single employer funds</td></tr>
<tr><td>Industry-wide funds</td></tr>
<tr><td>Group insurance contracts</td></tr>
</table>

PORTUGAL **First and Second Tier of Pension Provision** **OVERALL STRUCTURE**		
1st tier Social Security	- Universal non-contributory pensions - General social security scheme for employees and self-employed - Special scheme for agricultural workers - Special schemes for selected categories of employees - Civil service pension scheme	
2nd tier supplementary pensions	VOLUNTARY	
	Private sector employees	Closed pension funds
		Opened pension funds
		Mutual benefit associations
		Insurance contracts, book-reserves*
* not qualifying for tax advantages		

<table>
<tr><th colspan="4">SPAIN

First and Second Tier of Pension Provision
OVERALL STRUCTURE</th></tr>
<tr><td>1st tier Social Security</td><td colspan="3">- Universal non-contributory pensions
- General social security scheme for employees in industry, trade and services
- Special schemes for self-employed
- Special scheme for public employees
- Special schemes for selected categories of employees</td></tr>
<tr><td rowspan="5">2nd tier supplementary pensions</td><td colspan="3">VOLUNTARY</td></tr>
<tr><td rowspan="4">Employees in the private sector and in the nationalised industries</td><td colspan="2">Qualified pension funds</td></tr>
<tr><td colspan="2">Mutuals for retirement benefits</td></tr>
<tr><td rowspan="2">Non-qualified Pension Plans</td><td>insured</td></tr>
<tr><td>non-insured</td></tr>
</table>

UNITED KINGDOM **First and Second Tier of Pension Provision** **OVERALL STRUCTURE**		
1st tier Social Security	Universal contributory old-age pension (National Insurance)	
2nd tier supplementary pensions	COMPULSORY:	
	Private and public sector employees	State earnings-related pension scheme (*SERPS*) OR:
		Guaranteed minimum pension under a contracted-out occupational pension scheme* OR:
		Minimum contributions to an approved personal pension (contracted out)
	VOLUNTARY:	
	Private sector employees and self-employed	Occupational pension scheme
		Group insurance contracts
		Personal pensions
		Additional voluntary contributions (AVC)
* Public sector employees are covered by a Civil Service Superannuation Scheme and by separate schemes for employees of public corporations and Local Authorities.		

CHAPTER 4
SUPPLEMENTARY PENSIONS: COMPULSORY PROVISION

Policy overview

The gradual development and extension of social protection in some European countries has included the policy option of making compulsory the provision of supplementary pensions. Legislation enacted ensures that, over and above the first tier of pension protection many employees would be able to benefit from a second pension.

It should be recalled, first of all, that the meaning of the term 'compulsory' in the present report has been described and explained in the Introduction. Compulsion is an essential ingredient of any public policy aiming at ensuring economic security in old age to the population at large. It may, however, be difficult to apply compulsion in all situations without obstructing private initiatives which may be more generous, disturbing conditions of employment or adding to public expenditure. Some countries substitute compulsory provisions with incentives such as tax exemptions.

The underlying justifications for choosing the compulsory option are common to European countries that have followed this path. Differences concern the strategy or the technique applied in order to attain the stated objectives.

In countries where the post-war social security consensus gave priority to establishing universal flat-rate pensions (examples are Denmark, the United Kingdom and the Netherlands) subsequent economic growth and increased prosperity fully justified an enhancement of retirement incomes so that the elderly could also share the improvements in the living standards of the working population. Middle and higher income groups, in particular, could not be satisfied with contemplating retirement on the flat-rate pension alone. The earnings-related benefit offered the desired alternative.

Governments could, at that point, have relied on voluntary private provision, including contractual arrangements freely negotiated by employers and the trade unions, in order to foster and to promote earnings-related retirement benefits. Such an option seemed particularly attractive in countries where private provision was already well developed (United Kingdom, Netherlands).

However, governments expressed a legitimate concern that a strictly voluntary approach could become too selective, favouring the better paid employees or those in large enterprises to the detriment of lower income workers, or women in less stable jobs, or white and blue collar workers in small private sector firms, and more generally to vulnerable groups in the labour market. A broad-based compulsory second tier was considered politically more advantageous, at least from the point of view of equity, and also because it was not at all meant to exclude parallel private provision.

The option had an additional appeal. By institutionalising the second tier (even within limits) labour mobility would be enhanced because the difficulties in accruing adequate pension rights often encountered by members of company pension plans who change jobs could be avoided. It is not a negligible advantage for an employee to remain in the same supplementary pension scheme when moving from job to job during active life.

Denmark and the United Kingdom opted for a new general supplementary pension scheme for large groups of the working population. In the UK a new scheme, *SERPS*, was actually 'grafted' on top of the flat-rate national insurance pension, while in Denmark the *ATP* scheme (see below) took the shape of a clearly separate institution entrusted to the social partners for its management.

Because of this choice *SERPS* was financed on a pay-as-you-go basis like the basic national insurance scheme. In Denmark, on the contrary, *ATP* was conceived as a contribution defined arrangement, much like a provident fund where employer and employee contributions are set aside year after year, accumulated, invested and returned to the worker at retirement in the form of a pension.

France and the Netherlands chose another approach: building compulsory coverage by cementing the contractual relationship that the social partners had previously freely established. Broad-based supplementary pension schemes were achieved by making it compulsory for employers in particular industrial or economic sectors, or, as in France, to all private sector employers, to belong to a contractual supplementary pension network organised and managed by the social partners.

The policy yielded the desired results in both the Netherlands, where the schemes made compulsory by the state were, and remained, fully funded (*capitalisation*), and in France, where for historical and social reasons, the complementary pension plans made compulsory were and remained pay-as-you-go (*répartition*). Furthermore, while in the Netherlands the basic universal pension was, and still is, flat-rate, the French social security pension was, and still is, wage-related. The above shows that the value of relying for the second tier on broad contractual arrangements, having an element of solidarity, is independent from the choice as to the method of financing or to the type of pension formula applied by social security.

Naturally, the approach adopted was not devoid of political implications. In the UK, *SERPS* is planned, administered and controlled directly by a government department (*Department of Social Security, DSS*). When the 1986 Social Security Act scaled down the retirement benefits in order to contain overall social security expenditure in the longer term, the measure caused concern about the future adequacy of the supplementary state pension.

In the other three countries with wide-spread compulsory supplementary pension provision the guidance and management of compulsory schemes are entrusted to the representatives of the social partners. It is true that the public authority retains a distant benevolent role of supervision and that it follows with political interest the development of institutions which, although private, are, in fact, part and parcel of social policy.

Greece offers yet another pattern of state intervention in establishing compulsory supplementary pensions. The pattern developed from traditions and conditions which date back several decades. In 1951, when social security was reviewed and reformed, the state opted for a social insurance pension of a modest amount, although it was not flat-rate. Insured earnings were low and average contribution careers short. In fact, the pension scheme was originally intended to cater mainly for low paid workers.

With the assent of the government, a number of private enterprises voluntarily organised supplementary retirement benefit schemes referred to as 'auxiliary funds'. State benefits improved later but the need for a network of supplementary arrangements was still felt. In 1979, the state enacted Law 997, creating the Employees' Supplementary Social Security Fund (*TEAM*). The aim was to provide, through a new compulsory scheme, supplementary pensions to all private sector employees who were not already covered by an auxiliary fund. Earlier auxiliary funds whose benefits were lower than those mandated under *TEAM* were gradually taken over. Employees of public enterprises were also affiliated under special arrangements.

TEAM became, de-facto, a major part of the state's compulsory provision for retirement. In August 1983 it was formally attached to the state social security institution (*IKA*), albeit maintaining separate management and accounts.

In 1987 a special supplementary pension fund was organised for the rural population. Self-employed persons remained outside the mandatory funds. They were, however, allowed (since 1979) to organise their supplementary coverage and to make it compulsory on a sectoral or occupational basis.

The recent social security reform has not challenged the fundamental choices made earlier, including a compulsory second tier of pension provision where benefit levels are put into common lines and solidarity among occupational groups is maintained.

Compulsory and voluntary pension provision can run parallel

In each one of the five countries reviewed above, the decision of the state to introduce a strong element of compulsion within the second tier of pension provision did not dissuade employers, workers or trade unions to continue to make private and voluntary arrangements capable of enhancing retirement incomes. The parallel development of compulsory and voluntary supplementary pension has, however, a different connotation in each Member State, because the impact or the performance of the compulsory element is not necessarily the same.

The case of the United Kingdom stands out as unique, insofar as legislation permits 'contracting out', that is workers are allowed to opt out of the compulsory scheme (*SERPS*), provided that employers and workers meet certain conditions of equivalence in coverage through company plans or personal arrangements.

In Denmark the low benefit expectations emerging from membership in the compulsory *ATP* created pressure in recent years to develop a wide new network of supplementary pension plans. It is characteristic of the Danish approach that the voluntary supplementary pension arrangements have mostly resulted from wage negotiations concerning entire groups of employees in a specific economic branch or occupation, while single employer company pensions have found less appeal.

In France, on the contrary, the weight and the considerable extension of supplementary protection, which is virtually and effectively compulsory, has definitely discouraged parallel private initiative. Another reason for the lack of private initiative is that in the compulsory schemes (*AGIRC, ARRCO*) the employer has a choice of plan, that is he has the freedom to increase benefit expectation through higher contributions. Marginal private and voluntary arrangements (top-hat schemes, etc.) for individuals or senior employees do exist.

In the Netherlands the obligation to belong to industry-wide pension funds dates back to 1949 and is widespread, but it has not crowded out other forms of pension provision. Out of about 2.7 million members of supplementary pension funds in the private sector (in 1991) about 530,000 were *not* in industry-wide funds.

In Greece, the state took a leading role in the promotion and development of compulsory provision. However, the trade union movement also took significant initiatives in the organisation of mutual insurance funds and mutual benefit societies, some of which are still in operation. The trade union freedoms embodied in the constitution and special legislation dating back to 1976 have provided the legal foundation for the inclusion of pension commitments in a number of collective agreements. Moreover, large companies have made additional voluntary arrangements for their employees either directly, or through insurance contracts.

The broad-brush picture presented above for the five countries concerned is further clarified and enriched by the following detailed information set out separately for each country. The information on compulsory second-tier schemes may be better understood by making reference to the overall structure of pension provision presented in the tables in Chapter 3.

Detailed Country Information

DENMARK

In 1964, the law on the *Arbeijdsmarkedets Tillaegspension* established a new compulsory supplementary labour market pension, *ATP*. Participation in *ATP* is obligatory for employees from age 16 to age 66, provided they are employed (for at least 10 hours a week) in Denmark, or are employed abroad by a Danish public or private employer or are on Danish ships. Citizens from other EC or Nordic countries employed in Denmark are also affiliated to *ATP*. Contributions to *ATP* are paid by employers and workers. In 1992 the monthly amount of contributions was DKr 65 (worker) and DKr 130 (employer).

At the age of 67 the accumulated balance of each member's cumulated contributions with interest is paid in the form of a life annuity (pension). In addition to the old-age pension, in case of a contributor's death, a survivor's pension is paid to the widow and to children under 18 years.

Self-employed workers are excluded from *ATP* membership; it is, however, possible for them to retain membership acquired while working as employees before becoming self-employed (minimum of 3 years' participation is required).

The basic data concerning *ATP* are summarised below:

	Total number of contributors in the year	Total number of members with a contribution balance at the end of the year	Number of pensioners
1986	3,300,000	2,550,000	371,000
1992	3,400,000	2,600,000	478,000

The value of accumulated contributions after deduction of the amount paid out in benefits has grown from 30.7 billion DKr at the end of 1983 to 97.8 billion DKr at the end of 1992.

FRANCE

The development of contractual supplementary pension schemes, having become compulsory, has reached significant proportions in France. For reasons of space and balance with other country profiles shown in this chapter, the following description focuses almost exclusively on the two largest schemes for wage earners and salaried employees, i.e. the *AGIRC* and *ARRCO* federations. Only brief mention will be made of the other compulsory schemes listed in the overall structure.

Origin of AGIRC and *ARRCO*

The first *régime complémentaire*, as well as the most significant since it more or less served as the model for subsequent schemes, was formed as a result of the national collective agreement of 14 March 1947 setting up a *repartition* (pay-as-you-go) pension scheme for engineers and managerial staff (*cadres*) of industrial and commercial enterprises. A multi-institutional basis was retained, but participating institutions had to be approved and become members of the *Association générale des institutions de retraite des cadres* (*AGIRC*).

The unique feature of this arrangement was that all employers belonging to the *Conseil National du Patronat Français (CNPF)*, the national employers' association, were obliged to affiliate their own *cadres* to one of the funds federated under *AGIRC*.

The example of *AGIRC* was followed in other collective agreements. In 1957 the social partners decided to coordinate and rationalise the whole network of *répartition* pension schemes; first, the agreement of 19 May 1957 instituted the *Union nationale des institutions de retraite des salariés (UNIRS)*, then the agreement of 8 December 1961 formed the *Association des régimes de retraite complémentaires (ARRCO)*. Under the latter agreement it became compulsory to affiliate non-cadres employees of enterprises belonging to the *CNPF* to an institution administering a complementary pension scheme operating on a pay-as-you-go basis and authorised by the Ministry of Social Affairs. Contractual commitments were turned into wider obligation by an 'extension procedure' whereby the supervising ministry, having noted the consensus of the organisations signing the agreement, extended such commitments to all employers in the branch of activity concerned, whether or not they belonged to an employer's organisation member of *CNPF*. Coverage was further widened in 1972.

The *AGIRC* agreement of 1947, as well as the *ARRCO* agreement of 1961, was extended by law to all employees belonging to the state pension scheme, even if their employer did not belong to a branch of activity covered by *CNPF*. Few exceptions were made in respect of some employees affiliated to other complementary schemes.

In 1973 the social partners agreed to make it compulsory for *AGIRC* members to contribute also to *ARRCO*, in respect of that part of their salary under the social security ceiling. By that time supplementary pension provision for private employees (blue and white collar workers) had become complete.

Coverage and financing (AGIRC *and* ARRCO*)*

Both *AGIRC* and *ARRCO* are federations of supplementary pension funds (*Caisses*). As of November 1993 *AGIRC* federated 54 funds, all implementing the same contribution and benefit plan. *ARRCO* federated 111 funds, which overall implemented 46 different type of plans.

The funds federated by *AGIRC* deal exclusively with the so-called *cadres*, a term which covers senior executives, technicians and more generally employees ranking above a given level in the company's hierarchy. Funds federated by *ARRCO* cater for all employees whether they are cadres or not and also receive contributions from *AGIRC* membership (see above) earning pension rights.

Contributions are closely linked to the social security earnings ceiling which is established every year by the general social security pension scheme for employees (*régime général, CNAVTS*). Non-cadres members of *ARRCO* pay contributions related to earnings up to three times the social security ceiling. Members of *AGIRC* pay contributions related to earnings up to eight times the said ceiling; provided their contributions on earnings up to the social security ceiling are paid into *ARRCO* (not *AGIRC*).

The relevant figures for the first quarter of 1993 were:

Social security ceiling	Fr. 12,360 per month
Social security ceiling x 3	Fr. 37,080 per month
Social security ceiling x 8	Fr. 98,880 per month

Each of the two federation operates a full pooling of risks among their own affiliated funds; costs are shared independently of the demographic or economic condition of a member enterprise or an affiliated fund.

Contribution rates vary both within *AGIRC* and *ARRCO*. All members have to respect the minimum standard contribution rate on covered earnings: 4% in *ARRCO* and 12% in *AGIRC*. Above the minimum, each member may choose a higher rate, either through a collective agreement or by a joint employer/employee decision.

Restrictions on the freedom of paying higher optional contribution rates have recently been imposed by *ARRCO* (the maximum allowed being 6% instead of 8%), moreover a single rate of 6% is to be introduced in 1999. *AGIRC* affiliates still have a choice between 12% (the minimum), 14% or 16%.

The benefit model (AGIRC *and* ARRCO*)*

In *ARRCO* and *AGIRC* the originality of the financing technique and of the benefit scheme taken together is that they constitute a pooled 'contribution defined' set of plans which aims at paying inflation proof benefits at and after retirement. This aim is achieved by introducing a 'notional unit' for contributions and for benefits, called the 'point', hence the term 'point system' often used in this context.

A worker acquires every year a given number of points proportional to the amount of contributions actually paid. Points accumulate from year to year in the worker's individual account, irrespective of the enterprise where he or she works (within all the enterprises belonging to the funds of each federation). At retirement the total number of points acquired is transformed into a pension, proportional to the number and to the current value of a point.

The value of the point is calculated each year by the governing body of each federation. It determines the value of newly awarded pensions and that of all pensions in payment, whose amount is re-calculated each year. Up to the end of 1970, the progression of the yearly value of the point has outpaced the level of the consumer price index. In recent years the pace of progression follows more or less price inflation.

Because the system is contribution-defined, it is understandable that employees wish to belong to a higher contribution plan. In fact, it is the employer who, in any case, pays the largest share of the joint contribution.

The normal pensionable age was originally 65 but because from 1983 the state scheme paid full pensions from the age of 60 to employees in the general scheme with 37.5 years' contribution, the *AGIRC* and *ARRCO* funds had to be adjusted. Pensions are now awarded from the age of 60 to employees with 37.5 years' contribution, without the actuarial reduction which normally applied for pensions claimed before age 65. The ensuing financial imbalance for the two federations has been offset by a joint financial effort by the government, employers and employees (called *Association pour la gestion de la structure financière, ASF*).

A distinctive feature is that *AGIRC* and *ARRCO* also credit pension points to workers during spells of unemployment or absence due to sickness, maternity or injury. For the unemployed, the unemployment insurance agency (*UNEDIC*) pays the contributions to the federations.

It is worth recalling that when the *répartition* schemes were launched, past service liabilities were taken on by the respective funds without a counterpart in terms of past service contributions. Substantial pensions could be paid from the start to late entrants. This was not a negligible social achievement, but it did obviously have a cost. Accordingly, French schemes are close to maturity as demonstrated by the fact that the average number of pension points awarded per claim varies little over time:

***AGIRC*: average number of points per new pension award**	
1954	29,670
1964	26,437
1974	26,600
1984	29,200
1990	30,600

On the other hand the number of pensions in payment shows a steady increase. In the case of *AGIRC*, the figures are as follows:

***AGIRC*: number of pensions in payment**		
Year	Old-age	Survivors
1980	344,010	212,391
1989	712,857	328,283

Similar trends are observed in *ARRCO*.

The French *répartition* system allocates the contribution income received in the year to cover the cost of pensions in payment in the same year and it aims at the full maintenance of the pensions' purchasing power.

As expenditure rises systematically from one year to another (see above), the system can keep its promises without excessive increases in contributions, provided that the growth of membership matches the increasing costs and provided that the members' average insured wage keeps pace at least with inflation. Experience shows that in past years the latter was easier to achieve than the former because of slow economic growth and high rates of unemployment. The ageing of the population is also likely to negatively affect the financial equilibrium of the schemes described. Membership and pensions at the beginning of 1990 in the two federations were reported as follows:

1990	Number of members	Number of pensioners (all categories)
ARRCO	16,675,000	7,289,000
AGIRC	2,634,000	1,041,000

Other compulsory schemes

Independently of the federations *ARRCO* and *AGIRC*, certain groups of employees are affiliated to compulsory supplementary pension schemes. The largest of these is the scheme covering public sector employees without civil servant status (*IRCANTEC*) with 1,850,000 members and 1,047,000 pensioners. It was established by legislation rather than as a result of collective bargaining. Many members do not spend years in the scheme as they move up to established jobs in the public sector or away to other occupations. Pension rights accrued are, on average, consequently much lower than in other supplementary schemes.

The fund for employees of social security institutions (*CPPOSS*) was initiated under collective agreements. The number of employees was 187,000 in 1990 and pensioners totalled 75,000. Unlike *IRCANTEC* which operates a benefit point system, *CPPOSS*'s benefits are linked to final salary and are integrated with state social security. From 1 January 1994, *CPPOSS* joined the Federations *AGIRC* and *ARRCO* in order to strengthen its financial position.

Mention should also be made of some smaller funds which are either totally or partially independent from *AGIRC* and *ARRCO*. They cover civil aviation, banks and credit institutions, services in agriculture. Joint employer/employee management is a common characteristic of all the supplementary schemes described.

A different situation has developed with regard to the self-employed. Those in handicraft joined a supplementary pension fund (*CANCAVA*) in 1979. Past service liabilities were not fully validated and the scheme's pension costs are rising more gradually than in the corresponding arrangements for salaried employees. Moreover, *CANCAVA* has been accumulating substantial reserve funds (16.8 billion francs at the end of 1991).

The self-employed in trade and industry only have supplementary provision for survivors. Other benefits, such as retirement pensions, are optional and generally modest.

Liberal professionals had to organise substantial supplementary provision because the first tier only granted them minimum coverage. Within this group, lawyers and barristers decided in 1954 to make their own separate arrangements. Data on membership was as follows in 1990:

France: the self-employed	
Self-employed in trade and industry	652,000
Handicraft	542,000
Liberal professions	390,000
Lawyers, barristers	19,000

GREECE

According to a pattern which also prevails within the first tier of social security, compulsory supplementary pension schemes have been established in Greece according to occupational criteria. Overall membership is of the order of 3,360,000 persons.

The general scheme is *IKA/TEAM*, founded in 1980. It has gradually absorbed a number of occupational funds which could not guarantee the minimum benefits provided by the general scheme. At the end of 1991 *IKA/TEAM* covered about 895,000 employees in industry, commerce and services. It had an annual income of 74,853 million Drachmas (ECU 280.3 million) and an expenditure of 44,000 million Drachmas (ECU 164.0 million).

TEAM is a non-profit organisation attached to the main Greek social security institution, *IKA*, but enjoying separate legal status. It is financed by a contribution of 6% of payroll up to the *IKA* social security ceiling, shared equally between the employer and the employee. It has been estimated that an employee whose earnings are below the *IKA* ceiling would, at retirement, obtain a supplementary *TEAM* pension of approximately 20% of final earnings (when the scheme is fully matured).

The second largest complementary pension fund is *OGA* which had in 1991 a membership of 1,170,000 agricultural workers and farmers. Income was Dr. 35,650 million (ECU 33.5 million) and expenditure Dr. 23,000 million (ECU 86.1 million). Apart from *IKA/TEAM*, *OGA* and *IKA/ETEAM*, there were 57 occupational 'auxiliary' funds (of which 44 autonomous funds) which reached a broad section of the economically active population.

As a general rule, the auxiliary funds are financed by employer/employee contributions or, as regards the liberal professions and the self-employed, by the members themselves. The method of financing is pay-as-you-go. State subsidies (including resources obtained from earmarked taxes) have been granted to some funds in order to cover any shortfall of income. Since 1992, however, such subsidies have been frozen at 1992 levels and they are now channelled through a new 'solidarity fund' (*L.A.F.K.A.*) whose aim is financial support to the weaker auxiliary funds.

The network of provident funds is a separate component of compulsory coverage. They number 95, of which 50 cater for the legal profession. They pay, on retirement from the occupation, a lump-sum benefit only. Provident funds reach about 17% of the labour force, including liberal professions, bank employees, public enterprise employees and civil servants, i.e. occupational groups which are simultaneously affiliated for pension entitlements to the above-mentioned auxiliary funds.

The large, as well as the small, compulsory auxiliary funds are supervised by the Ministry of Health and Social Security. Exceptions are the complementary scheme for seamen (Ministry of the Merchant Navy) and a few funds for some civil and military personnel (Ministry of Finance, Ministry of Defense).

NETHERLANDS

Private sector

On the basis of an act adopted in 1949, relating to compulsory participation in supplementary industry pension funds, the Minister of Social Affairs and Employment has the power, at the request of a delegation from the branch of industry, to make participation in an existing industry pension fund compulsory for all staff employed in that branch of industry.

The employee is not free to opt out from a compulsory industry pension fund. Exemption of employers from participation in a compulsory industry pension fund, however, is possible in two ways. First, the industry pension fund itself has the power to exempt an employer if the latter has set up an alternative staff pension scheme providing at least equivalent entitlements. Secondly, the Minister of Social Affairs and Employment has the power to grant exemptions from compulsory participation in special individual cases. The Minister exercises this power, for example in respect of foreign workers on temporary secondment in the Netherlands.

The Minister of Social Affairs and Employment may make compulsory the participation of a self-employed person in the pension fund which has been established for his particular professional category. Most of the industry-wide pension funds have become compulsory.

Industry-wide pension funds in the Netherlands		
Year:	1985	1991
Total number of industry-wide funds	77	81
- of which compulsory	63	65
Total number of members	1,499,077	2,203,977

In the Netherlands, the following arguments have been advanced in support of making industry pension funds compulsory:

- the principle of solidarity can be applied and risks are pooled. Contribution rates do not depend on the employee's age or health status;
- labour mobility is enhanced within the industry. A change of employer does not result in the need to change pension fund membership;
- employees' membership of supplementary pension funds is extended considerably;
- competition among employers is restrained, as far as employment and pension conditions are concerned.

On the other hand, the policy of compulsory membership in industry-wide funds has been criticized in the Netherlands on the following grounds:

- it may lead to the creation of undesirable monopolies;
- it restricts the freedom of employers about plan design or the choice of a plan administrators;
- it may run contrary to the policy of integrating pension and compensation practice for firms with several subsidiaries in different branches of economic activity;
- it may restrict the freedom of individual employees to choose how best to make contributions or to save for retirement provision.

Public sector

There is special statutory supplementary pension legislation for employees in the public sector: the 'General Civil Pensions Act' (*ABP*), in which are laid down the entitlements for civil servants, and the 'Railway Pensions Act', which applies to railway personnel. As of January 1994 the railway pension fund is privatised and has since then been set up as an industry-wide fund. Membership of the *ABP* fund is compulsory (employees do not have the individual right to opt out). The benefit target for the maximum period of participation (40 years' service) is a pension which, including social security, amounts to 70% of the last gross wage received. Pension liabilities of the *ABP* fund are fully funded. The board of management of the fund consists of an equal number of staff and management representatives, plus a chairman. The total assets under management by the civil service pension fund (*ABP*), which covers about 1 million public servants, was estimated as follows:

Assets of the *ABP* pension fund in million Dfl.	
1985	126,600
1988	149,800
1992	177,044

This makes *ABP* one of the largest pension funds in Europe. The 1992 asset figures were equivalent to about 82 billion ECU. A recent estimate of the assets held by the railway employees' fund shows a figure of about 10 billion Dfl (4.7 billion ECU).

UNITED KINGDOM

In the United Kingdom all employed and self-employed workers earning more than a low threshold income pay contributions to the national social security scheme to earn entitlement to a basic pension. The amount of the basic pension depends on the individual's contribution record and not on the level of their earnings.

Since 1978, a second tier of provision has been available to all employees through the social security earnings-related additional pension (*SERPS*). The scheme is compulsory but it is possible to contract out of this part of social security through membership in a suitable occupational pension scheme or by means of an appropriate personal pension plan.

Earnings-related pensions (*SERPS*) are payable from state pension age to those who have contributed as employed persons. Earnings-related widows' pensions are also available. The main benefit is an additional pension which was planned to build up over the first 20 years of the scheme to 25% of average earnings in the range between the lower and the upper earnings limits, revalued to the level appropriate at the time of retirement. This additional pension does not accrue in respect of periods of self-employment.

The lower earnings limit corresponds fairly closely to the amount of the basic pension (about 18% of national average earnings). The upper earnings limit is 7.5 times the lower earnings limit, currently 135% of national average earnings. Following the 1988 changes, the proportion of revalued earnings which will be paid as benefits to those who retire will fall after 1988, until a long-term figure of 20% of average revalued career earnings is achieved. Revaluation of relevant career earnings is in line with the general movement of earnings over the period. The upper and lower earnings limits are revalued in line with the basic state pension, i.e. usually in line with the retail price index.

Employers are permitted to contract out, from the additional earnings-related pension, employees who are members of an adequate defined benefit occupational pension scheme. The scheme must undertake to provide members and their surviving spouses with guaranteed minimum pensions, which are broadly equivalent, although not identical, to the earnings-related additional pension to which they would have been entitled if they had not been contracted-out.

Those who are contracted-out are entitled to a rebate in their National Insurance contributions in respect of earnings between the lower and the upper earnings limit. The effect of this form of contracting-out is to substitute earnings-related benefits provided by occupational pension schemes, on a fully funded basis, for the earnings-related benefits which would otherwise have been payable through the social security scheme on a pay-as-you-go basis. Almost half the work force is contracted-out through membership of such defined benefit occupational pension schemes.

In 1987 the possibility of contracting-out was extended to those with appropriate personal pension arrangements. The minimum contribution, which was initially set at the level of the contribution rebate for contracted-out defined benefit occupational pension schemes, is paid directly into the personal pension arrangement by the Department of Social Security. There are certain restrictions on the form in which the benefit may be paid.

For an initial period, up to March 1993, a further incentive payment of 2% of earnings in the relevant band was payable in respect of newly contracted-out arrangements, including all personal pensions. This incentive payment is no longer payable, but an incentive payment of 1% of earnings in the relevant band became payable from April 1993 in respect of all those over the age of 30 who have an appropriate personal pension.

Since the minimum contribution is the same for all, regardless of age and sex, but the cost of providing a given level of benefit increases with age, contracting-out by means of personal pension is particularly attractive to younger employed persons. About a quarter of the employed workforce, nearly 5 million people, is now contracted-out on the basis of appropriate personal pensions.

Contracting out is now also possible for employers with money purchase (defined contribution) schemes *(Contracted-Out Money Purchase schemes, COMPs)*. Their obligation extends only to paying the minimum contribution into the scheme and no guaranteed minimum pensions have to be provided. Additional contributions may be made by the employer and by the employees. About 300,000 employees are now thought to be members of *COMPs*.

An individual who has been contracted-out may still receive an earnings-related additional pension from the state social security scheme. The amounts of any guaranteed minimum pensions payable from occupational pension schemes are simply deducted from the total entitlement to additional pension which there would have been if the individual had not been contracted-out, and the balance is payable from the social security scheme.

SERPS is financed on a pay-as-you-go basis, with the contribution rates for employees, employers and the self-employed set for each year so as to cover the expected outgoings on benefit expenditure and administration costs, taking into account any proposed Treasury grant from general tax revenue. Earnings-related pensions will become more and more significant, and in future years most of these will be paid as occupational and personal pensions under the contracting-out arrangements. The residual amount of earnings-related pensions paid through the social security scheme is projected to grow until it constitutes almost one-third of the total cost of social security pensions by 2030-31.

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One of the main policy objectives of a compulsory system of supplementary pensions is to guarantee access to a second pension to a very wide group of citizens. The following figures seem to support the view that the objective has been broadly attained. In the Netherlands a very extended voluntary pension system compensates for the low percentage covered by schemes which have been made compulsory (see Chapter 5). Moreover, if the compulsory *ABP* scheme was included, the coverage percentage shown in Table 12 would rise to around 50 per cent.

Table 12:
Estimated number of persons covered by compulsory supplementary pension schemes (absolute and relative figures)

Country:	Year	No. of persons covered (1)	Labour force (2)	(1)/(2) (%)
Denmark	1990	2,600,000	2,898,000	89.7
France	1990	17,988,000	24,133,000	74.5
Greece	1991	3,360,186	3,935,000	85.3
Netherlands	1990	2,203,977	6,801,000	32.4
United Kingdom	1990/91	22,700,000	28,658,000	79.2

Remarks:

Column (1):
Denmark: Number of contributors to *ATP*
France: Membership of *ARCCO*, *AGIRC* and other schemes
Greece: Compulsory schemes supervised by the Ministry of Health and Social Security
Netherlands: Membership of industry-wide pension funds
United Kingdom: Membership of *SERPS*
Column (2): Source: EUROSTAT Labour Force Survey

CHAPTER 5
SUPPLEMENTARY PENSIONS: THE VOLUNTARY OPTION

Introduction and scope

For over a century private and public employers have used their discretion to create arrangements with the object of providing their employees with pensions or lump-sum payments on retirement, disability or death. For example, large industrial undertakings in Germany introduced retirement benefits for their personnel well before 1891, when the first state pension insurance scheme was created. In Denmark similar initiatives were taken at the turn of the century, although their development gathered pace only after 1919. A similar situation was observed in the United Kingdom. With the introduction and extension of social insurance and social security, voluntary provision of retirement benefits by enterprises concentrated on ensuring supplementary rather than basic coverage.

The rationale for this shift in emphasis and in aims has already been discussed in Chapter 1. In the present chapter, the intention is to describe and to analyse how, in practice, voluntary pension provision is shaped, organised and implemented in Member States. In order to deal in an orderly manner with such a vast field of contemporary practice, the substantive issues will be covered under the following headings:

- establishment of voluntary pension commitments, the actors and the institutions involved;
- coverage, in terms of membership and persons protected by voluntary arrangements;
- contributions and benefits contemplated in prevailing national practice, including conditions for eligibility and maintenance of rights in cases of withdrawal from membership;
- tax treatment;
- protection of members' rights.

Establishment procedures and institutions involved

The whole process leading to the voluntary establishment of supplementary pensions can be broken down into four distinct parts. The first is related to the actors who participate in sponsoring the pension arrangement - the employers, trade unions, and representatives of the categories or professions concerned. The role that each plays in exercising their discretion is a matter which Member States have viewed from different angles.

The second aspect deals with the degree of freedom enjoyed by the sponsoring parties in the context of setting up a pension arrangement. In every country a regulatory framework imposes constraints that, as a rule, are readily accepted by employers and employees since they bring fiscal rewards.

The third aspect arises because ultimately pension promises or pension commitments voluntarily undertaken necessitate the establishment of an appropriate institution to assume responsibility for their management. More than one type of institution (including the sponsoring employer) may be compatible with the requirements laid down by the national regulatory framework.

Fourthly, institutions are in the hands of responsible individuals, representing the interests of the partners in the pension commitments (employers, members, beneficiaries). The relative weight of the representation granted to each group is a matter of great practical importance, and upon which there are diverging views among Member States.

Taken together, these four aspects constitute the 'institutional profile' of voluntary supplementary pensions. This profile has considerable national specificity, although paradoxically a common feature of the profile is that it will normally differ from one undertaking, profession and, generally speaking, professional and social status to another.

National institutional profiles and the traditions they preserve represent a peculiar reality that European and national legislators should thoroughly understand and respect when dealing with schemes and arrangements that are, within limits, voluntary. It is the freedom of choice at this level which is fundamental to the concepts, motivations and attitudes underlying private provision.

A short and factual description, as far as the information was available, of each country profile is given in the following section.

BELGIUM

Individual employers, in particular large enterprises, take the initiative to sponsor supplementary benefits (paid either as pensions or as lump sums). Less frequently, retirement benefit arrangements are the result of collective agreements covering all employers in a specific sector. In firms employing more than 20 workers, representatives of the personnel have to be consulted by employers designing a voluntary retirement scheme.

The applicable regulatory framework is essentially laid down in:

- legislation on private pension funds (Act of 9 July 1975, Royal Decree of 14/15 May 1985) and subsequent enactments;
- legislation regulating the functioning of insurance companies;
- applicable provisions of commercial or civil law.

Employers are free to choose the institution implementing the pension commitment. The most common choice is between an autonomous pension fund and an insurance contract. A pension fund may consist of a private and independent legal entity: a non-profit association (*Association sans but lucratif, ASBL*), or a non-profit mutual insurance company.

The statutes of an *ASBL* are drawn up by a general meeting of the association which consists of employers' representatives. The presence of employees is not required. The general meeting appoints a board of directors which must always include at least one representative of the employees, except when the fund is contributory, in which case employers and employees must have equal representation.

Employers choosing the 'insurance solution' take out group insurance providing retirement benefits. The life insurance companies involved are not allowed to carry out non-life activities. Such companies are administered by a board of directors (not less than three) appointed by the shareholders' meeting. Their renewable term of office may not exceed six years. The group insurance contract has a separate legal status with the insurance company.

A third option available to employers is to entrust an insurance company with the management of the employer pension plan, through a so-called 'deposit administration contract', which does not have a separate legal status within the company.

Mention should also be made of individual pension plans, which were formerly entrusted to the *Office National des Pensions* or to the *Caisse Générale d'Epargne et Retraite*, and which are now managed by a number of private institutions, mainly large insurance companies.

All the institutions described above must, according to law, be legally and financially separated from the sponsoring enterprise.

DENMARK

Employers, employees and the self-employed have taken the initiative to organise a voluntary second-tier of pension protection.

The first two of the above groups have achieved this jointly through collective bargaining and wage negotiations. Only in a few cases has the initiative for establishing a supplementary pension scheme come from the employer alone.

The administration of the pension schemes has been entrusted either to pension funds or to life assurance companies. In several cases life assurance companies have been set up specifically with the purpose of administering pension schemes. In other cases pension schemes, mostly company schemes, are administered by ordinary life assurance companies.

There are two forms of pension funds: those which cover employees either belonging to the same branch of economic activity or having a common occupation (industry-wide pension funds), and those which cover the employees of a single firm (company pension funds). Company pension funds play only a limited role compared with the industry-wide pension funds and have been in decline. This is because wage earners have recognised the obstacles to labour mobility which may arise from membership of company funds.

The regulatory framework includes:

- fiscal legislation ('Pension Taxation Act');
- bank and insurance legislation (i.e. the 'Act on Insurance Businesses' regulates the functioning of industry-wide pension funds);
- pension fund legislation (i.e. the 'Act on the Supervision of Pension Funds' regulates the functioning of company pension funds).

According to the provisions laid down in pension legislation, pension funds are established as separate legal entities, independent from the sponsoring employer. The management board of industry-wide pension funds is elected directly by members, or is chosen by the relevant trade union.

Insurance companies involved in supplementary pension provision are joint-stock companies. Management decisions are taken by a board whose majority is elected by the shareholders.

GERMANY

Pension schemes may be established by individual or group contracts between employer and employees, or by agreements between the employer and the workers' council (*Betriebsvereinbarung*), or indeed by collective agreement between employers or associations of employers and trade unions (*Tarifverträge*). In practice, pension agreements negotiated between employers and employees cover employees who, due to their grade and degree of skill, are in a position to negotiate over their employment conditions.

Collective agreements (*Tarifverträge*) with the trade unions are only found in public service, in the construction industry, in part of the food industry and for journalists. In some of the above-mentioned industries and sectors, enterprises tend to be small and consequently employers are not likely to set up a pension arrangement unilaterally. They therefore deal with the relevant trade union. The sectoral (multi-employer) approach can be an effective vehicle in sectors with high labour mobility, such as the construction industry.

Pension arrangements provided for by collective agreement are binding on employers and union members belonging to a specific branch of activity. However, not all employees in a given branch may be members of the relevant trade union. In this case the pension agreement will not apply in practice to all the workforce in that branch of activity, unless the contracting parties request a special declaration of general applicability from the Federal Ministry of Labour and Social Order. This differs from the situation in public service, where provisions of collective pension agreements also apply to non-union members.

Collective agreements with works councils are, as a rule, made in order to restructure existing schemes (or to establish new schemes in the case of German subsidiaries of foreign companies). Works councils enjoy co-determination rights which include some aspects of pensions administration as well as regarding benefits. Trade unions do not have similar advantages. The employer's discretion, however, remains unchallenged when it comes to deciding on the amount of his contributions to the pension arrangement or on the financial vehicle chosen to implement it.

Four main solutions are available. The first is for the employer to handle the pension promise himself without establishing a separate institution and without actually segregating funds. This option, called 'direct commitment' (*Direktzusage*) implies the constitution of a 'book reserve' in the company's balance sheet and the purchase of insolvency insurance with the approved body (*Pensionssicherungsverein, PSV*). The majority of German enterprises have made such 'direct commitments'.

The second option is to establish a separate pension fund, as an independent legal institution, organised and managed as a mutual, non-profit insurance institution (*Pensionskasse*). Large enterprises are in a position to choose this option.

The third is to establish an independent body having separate legal status in the form of a 'support fund' (*Unterstützungskasse*). This is not organised as a mutual insurance company since it leaves some discretion to the employer as to the manner of providing benefits.

The fourth option is for the employer to insure the benefits directly through a contract with an established life-insurance company (*Direktversicherung*). Disability and death benefits are very often insured directly. Conventional group-life or individual life policies are found among this option.

The regulatory framework for the above is mainly to be found in the 1975 'Act on the Improvement of Occupational Pensions' (*Gesetz zur Verbesserung der betrieblichen Altersversorgung*). This act does not include all legal provisions regulating pensions, but it does lay down a number of principles and the substance of previous labour court rulings, which have occasionally prescribed less stringent conditions on employees (for instance on vesting).

In addition, binding provisions for supplementary pensions are found in labour legislation, fiscal legislation or company law. Labour legislation is particularly important because it regulates the contract of employment which determines the employers' liability to honour the pension promise.

The representation of different parties in the management of supplementary pensions depends on the option selected by the employer:

Book reserves: Since the relevant institution is the company, all management decisions concerning pensions are made by the company's managers, who normally employ external actuarial or benefit consultants. Employees' representatives may be consulted, although in certain cases they must be consulted, where provisions of the 'Works Council Constitution Act' so prescribe.

Pension funds: Decisions are taken by the board of management of the fund. There are legal requirements as to the board's composition. If the fund is a mutual society, its general meeting appoints the board members. If the fund is a limited company, the members of the pension board are chosen by the company's general assembly, or in accordance with specific rules laid down in the fund's statutes. In any event, the board must include at least two persons. They are appointed by the employer unless, as is most common, the statutes provide for equal representation (employer/employee). Workers' councils appoint board members who represent employees.

Support funds: A board of management is appointed according to company law. The difference between the rules here and those for pension funds is that in support funds the board always consists of employer and employee representatives.

Insured contracts: The composition of insurance company boards is laid down by legislation, which does not provide for the policy holder's (i.e. employer) representation, unless it is a mutual insurance society.

IRELAND

Pension schemes are usually established by individual employers for all their employees, or for certain categories of their employees. In many cases, they are established following negotiations with trade unions or other representatives of employees. These negotiations normally determine the eligibility conditions for membership, benefit levels, whether members are required to make contributions and the rate of contributions. It is then left to the employer to make arrangements for the establishment of a scheme on a formal basis.

A single pension scheme may be established in respect of the employees in a group of related companies. There are also a small number of industry-wide schemes, most notably for employees in the construction industry.

Schemes in the public sector, which operate on a pay-as-you-go basis, are normally established under legislation enacted by Parliament, with the detailed rules of the scheme being set down in regulations. Schemes in the commercial public sector are established in the same way as schemes in the private sector (see below). The Minister for Finance has overall responsibility for approving public sector schemes, with a view to standardising the rules and the range of benefits provided. When a scheme is established in either the private or the public sector, membership can be made a condition of employment and this is normally the case.

Schemes in the private sector and the commercial public sector, with few exceptions, are financed on a pre-funded basis. They are mainly set up as irrevocable trusts, as this is a requirement to qualify for the tax privileges for which these schemes are eligible.

A trust is an arrangement under which a person or group of persons hold and look after property on behalf of others. The persons who hold and look after the property are called trustees, the property is called a trust fund, and the people on whose behalf the trust fund is held are called beneficiaries.

In the case of an occupational pension scheme set up as a trust, the trustees hold and look after the assets for the benefit of members and their dependants. The terms of the trust under which a pension scheme is set up are set out in a legal document called the trust deed and rules. Trust funds are fully separate from the funds of the employer who sets up and is associated with the scheme.

Trustees are normally appointed by the employers sponsoring the scheme, with the procedures for appointment and replacement being set out in the trust deed. The trusteeship arrangements can vary from scheme to scheme, but there are three main types of arrangement.

(a) Individual trusteeship, where all the trustees are drawn from management and/or outside professionals (such as lawyers, accountants, or bank managers) and in some schemes from the representatives of employees.
(b) Corporate trusteeship: (i) where the employer, as a corporate body, acts as trustee (this is fairly common in small insured schemes); (ii) where a corporate body other than the employer acts as trustee (e.g. a specialist firm providing trusteeship services, or the trustee department of a commercial bank - this is very common in Ireland); (iii) where a separate trustee company is set up in lieu of individual trustees.
(c) A combination of individual and corporate trustees acting together, with individual trustees who may or may not include employee representatives.

At present only a minority of schemes have representatives of members as trustees. However, from 1 January 1994 most members of funded schemes will have a right under the Pensions Act to participate in the selection of trustees. It is envisaged that arrangements for member participation will normally be made by agreement between the employer and representatives of members. This will cover such matters as the overall number of trustees and the arrangements for the nomination and election of a number of trustees by the members. At a minimum, members will have a right to select for appointment two trustees, or half the total number of ordinary trustees, whichever is the greater, with the remaining trustees being appointed by the employer. The trustees appointed will then agree either on one of their number, with a casting vote, or on the appointment of a fifth trustee to act as chairperson. If there is no agreement, the chairperson is to be nominated by the employer.

These arrangements apply to schemes which have 50 or more members, or 12 or more members, if a directly invested scheme. For this purpose, a directly invested scheme is one which holds any segregated assets (other than cash), as opposed to only participating in a unit trust or trusts, or in a unit-linked fund or funds managed by an institution, or investing in an insurance policy. It is estimated that over 200,000 scheme members (including pensioner members) will have a right to participate in the selection of trustees from 1 January 1994.

Schemes in the non-commercial public sector which operate on a pay-as-you-go basis are not established as trusts. They are administered directly by the public sector organisation where the scheme members are or have been employed or by the government department which has overall responsibility for the organisation concerned. They are administered in much the same way as the payment of salaries and wages. No provision is made to enable representatives of scheme members to participate in the management of the schemes, and in fact such participation does not appear to be an issue with scheme members. This is mainly due to the fact that scheme rules normally have a legislative basis and there is state guaranteed financing.

The administration and operation of occupational pension schemes established as trusts are subject to a regulatory framework based on trust law and the Pensions Act 1990, in relation to the protection of pension rights, and on the Finance Act 1972, in relation to the approval for tax purposes. The Pensions Act 1990 and the Finance Act 1972 also have a limited application to unfunded public sector schemes. This regulatory framework is described below in the sections on *Tax Treatment* and on *Protection of Pension Rights.*

Trustees normally appoint other persons to administer the scheme on their behalf, while retaining overall responsibility for the administration. The administration of larger schemes is usually carried out by staff within the company. However, the trustees of such schemes will usually appoint external managers to manage the scheme's investments, and they may appoint more than one manager. Other services which can be purchased from pension consultants and/or life assurance companies include:

- actuarial services, in the case of defined benefit schemes;
- advice on benefit levels and investment performance;
- insurance of death in-service benefits (a common practice in Ireland);
- administration of scheme records and associated benefit calculations.

These services may be purchased separately, but many smaller schemes purchase a package of services from a life assurance company, covering a full range of services.

The Pensions Board in its Annual Report for 1992 gave statistics on the number of registration/fee contacts i.e. scheme administrators responsible for arranging scheme registration and payment of fees to the Pensions Board, in the case of schemes (including all public sector schemes) with more than one member.

Registration/Fee Contacts	Number	Number of Schemes	Number of Members
Life Assurance Companies	16	5,228	55,183
Brokers/Consultants	27	976	92,707
Individual Schemes	283	283	265,858
Total	326	6,487	413,748

There were in addition 24,259 one-member schemes, virtually all of which are administered by life assurance companies.

It can be concluded that in Ireland small schemes (less than 50 members) are administered mainly by life assurance companies. Consultants provide administration services for medium sized schemes - 50 to 500 members on average - while the larger schemes with more than 500 members are mainly administered by staff within the company.

ITALY

Establishment of a pension fund (according to the legislation of April 1993)

Supplementary pension provision may be established:

(a) by collective agreements, at the level of the undertaking or in a wider occupational context, as well as through agreements drawn up by employees themselves under sponsorship by national trade union organisations;

(b) by agreements drawn up by organisations of self-employed persons, sponsored by suitable professional unions;

(c) at the initiative of employers, in the absence of the agreements mentioned above;

(d) by special arrangements suited to public employment conditions.

The supplementary pension commitment shall be effected by establishing a pension fund. The rules for membership in a pension fund shall be agreed by its sponsors. However, individual freedom of membership shall be guaranteed.

The pension fund must have independent legal status, separate from that of its sponsors. Pension funds can take different juridical profiles, such as: (i) non-profit associations; (ii) private foundations or welfare institutions; (iii) welfare funds operated by incorporated companies, provided that their management accounts and controls are fully segregated from the company.

Fund establishment must be authorised by the Ministry of Labour and Social Security, subject to submission and approval by the competent supervisory body of the fund's statutes and, in particular, of proof of the independence of the fund's management (vis-à-vis the sponsoring employer) and of details regarding the competence and reliability of the members of the governing body of the fund. A register of authorised pension funds is to be established.

Employers and employees shall have equal representation in the governing body of the fund provided that both parties are under obligation to pay contributions. Funds financed solely by employees do not require employers' representation.

Public bodies administering state pension programmes (such as *INPS*) are empowered to establish open pension funds. These are funds set up to offer protection to those individual employees or self-employed persons who either do not have the opportunity to join a company or a similar collective fund, or who have left one of them (opting out, termination, transfer).

The right to establish an open pension fund is also granted to life insurance companies and banking institutions, including equity investment funds (*Fondi Comuni di Investimento Mobiliare*) authorised to operate in Italy (on the basis of the 1983 legislation).

Situation prior to the legislation of April 1993

Pension plans and funds had been established before April 1993 either on the basis of collective agreements, or unilaterally by employers. The main pattern was (i) book-reserves, (ii) pension funds or welfare funds (*Cassa*) with segregated assets and an autonomous legal status, and (iii) group insurance contracts.

LUXEMBOURG

Voluntary provision is not widespread. Social security retirement benefits are satisfactory except for employees earning above the social security ceiling (these numbered 16,000 out of 180,000 insured persons in 1991), almost all white-collar workers.

The initiative to establish supplementary pensions rests solely with the employer. The employer has a choice between:

- direct pension promises, backed by a 'book reserve' which may be totally or partly externally insured;
- discretionary pension promises, without reserve back-up.

In both cases no specific institution is created for implementing the commitment.

Further choices, involving an institutional framework, are:

- establishing a pension fund as an autonomous separate legal entity. In 1993 only one bank had followed this approach;
- buying a group-life insurance contract with a company established in Luxembourg.

There is no specific regulatory framework for voluntary pension provision, except the rules dictated by the fiscal authority with regard to the (favourable) tax treatment granted to the different ways of implementing pension promises.

NETHERLANDS

For employees in the private sector a supplementary pension scheme can be established on the basis of:

- either a pension promise made by the employer; or

- compulsory participation in an industry-wide pension fund (called hereafter industry funds).

A pension promise forms part of the conditions of employment as between employees and employers. There are different ways in which a pension promise may apply to the employee: it may be included in an individual's contract of employment, or it may made be separately in writing (a 'pension document').

A pension promise is often part of a collective labour agreement which is binding on employers and employees. The employer thus has a statutory obligation (under the 'Collective Labour Agreement Act') to honour that pension promise for all employees. An employee is not free to opt out, unless the agreement permits exceptions. Industry funds are always based on collective bargaining in the branch of industry in question. Membership of an employer's pension scheme is automatic for new entrants, whether or not they receive a separate 'promise' from the employer.

If no collective labour agreement applies, the employer needs the prior consent of the works council (where one exists) to set up a pension fund. A company with 35 employees or more is obliged to set up a works council. Therefore, if the trade unions are not involved in a pension fund through an industry-wide pension fund or via the regulations in the collective labour agreement, employees have a voice in discussions on the pension scheme through their representatives on the works council.

The employer who chooses to establish a pension fund must comply with certain requirements laid down in the Pension and Savings Fund Act (*Pensioen-en-Spaarfondsenwet, PSW*). Employers must ensure that the pension rights of each employee are safeguarded, by investing funds earmarked for pensions outside the company.

This act gives the employer the following options:

- joining an existing pension fund (but where there is an industry fund with compulsory participation, the employer has of course no choice);
- setting up a company pension fund. A company pension fund may operate for one company or a number of companies which are legally or economically linked;
- entering into a pension insurance agreement with an insurance company. In this case the employer acts as the policy holder and the employee as the beneficiary;
- allowing the employee to enter into an independent pension insurance agreement with an insurance company. In this case, the employee acts as policy holder and is also the beneficiary.

Under the *PSW* act pension funds are independent legal entities separate from the sponsoring employer, holding their own assets. Pension funds generally have the legal status of a foundation, or occasionally that of a limited company or association. Insurance companies (public or mutual) are legal entities separate from the sponsoring employer.

Pension funds are managed by a board of management with equal representation of employers and employees. In industry funds the representatives of the employers' organisation must have at least as many seats on the board as representatives of the employees' organisation. In company funds the representatives of the employees must have as many seats as the employers' representatives. With company pension funds, therefore, employees may represent a majority on the board.

There is no legal provision for the participation of retired persons or of early leavers in the management of pension funds. The *PSW* does, however, prohibit the statutory exclusion of former members. A participants' council is established at the request of either an association of members (industry funds) or of at least 5% of the workforce (company funds). Former members are allowed representation in the council, whose role is to advise management on proposed amendments to the statutes, or on the rules of the fund, and on other important matters (transfers, liquidation, etc.).

In cases of disagreement the council has the power to lodge a complaint with the insurance chamber against decisions on the management of the fund.

PORTUGAL

A significant growth of voluntary supplementary pension provision has taken place since 1987 as a result of new fiscal incentives introduced by the government.

A distinction is made between closed pension funds and open pension funds. Closed pension funds are established at the initiative of an employer, of a group of employers (in the same branch of activity) or of an association of members of a given occupational group. Occasionally the employer and the trade unions come to a joint agreement concerning the establishment of supplementary provision (collective bargaining). Open pension funds are established at the initiative of authorised fund management institutions (see below), offering membership to individual persons, independently of their occupation or branch of activity.

The regulatory framework covering both types of voluntary funds is set out in:

- Decree Law No. 225/1989 and Decree Law No. 415/1991;
- the new 'Code of Mutual Associations' (*Mutualidades*) approved by Decree Law No. 72/90.

The pension plan is the contract which defines the entitlements and the obligations of the partners in the pension commitment. Since employers generally provide all the resources to cover the benefits, they have ample discretion to choose the profile of the pension plans, without a great deal of participation by employees.

Pension fund assets (closed or open) are compulsorily and formally entrusted, by contract, to a fund management institution which has legal status separate from the sponsoring enterprise or association. Such institutions are either financial companies specifically and exclusively established to manage supplementary pension funds (a minimum stock capital is required), or life insurance companies duly authorised to write business in the country.

Mutual associations (*Mutualidades*), which have a long tradition in Portugal, offer, among other activities, retirement, disability and death benefits for individual members. However, some mutual associations also manage collective pension plans and funds entrusted to them by their sponsors.

Pension legislation does not include provisions specifically dealing with the composition of, and representation in, the governing bodies of fund management institutions. A special feature is that open funds, managed by either of the institutions mentioned above, issue certificates of or shares in the fund which may be purchased by employers on behalf of their workers (as well as by individuals).

Employers who wish to establish pension commitments other than under the provisions of the 1986 legislation are free to do so by making alternative arrangements (insurance policies, book-reserves) which, however, do not attract privileged fiscal treatment.

SPAIN

The oldest institutions are mutual benefit institutions (*Mutualidades* and *Montepíos*) referred to as '*Entidades de Previsión Social*'. Traditionally, they offered pension coverage to their members on the basis of legislation dating back to 1941 and 1946. The liabilities were not systematically covered by assets; many institutions followed the pay-as-you-go approach. In 1984 a reform of these institutions imposed rules on these institutions similar to those applicable to insurance companies (i.e. compulsory funding). In 1987, following the new Pension Act, the *Entidades de Previsión Social* were encouraged to take on the legal and technical profile of the new qualified pension funds (see below) and were given until 1997 to build up full actuarial cover of their liabilities. Employers may also follow the route of a direct pension promise, supported by book reserves entered in the company's balance sheet according to prescribed accounting standards.

A new framework was established according to the provisions of the 1987 Pensions Act. All pension plans established under the 1987 Pensions Act are called qualified plans and receive favourable tax treatment. Employers or groups of individuals who do not wish to meet such requirements are entitled to sponsor and to operate unqualified plans, which are not granted tax advantages.

The regulatory framework includes:
- Law 33/1984 regulating private insurance and dealing in particular with the legal requirements applicable to the *Entidades de Previsión Social.*
- Law 8/1987 (referred to here as the Pensions Act) regulating plans and pension funds, and its subsequent enactments (regulations, orders).
- Company law (*Ley de Sociedades Anónimas*).

Voluntary provision under Law 8/1987

A qualified supplementary pension plan can be established by (i) an employer (enterprise, corporation, company); (ii) an association, a trade union or any other recognized collective body of persons; (iii) an individual, provided that the resources used to finance the plan are derived from the individual's employment income.

Legislation lays down the procedure to be followed by a plan sponsor, leaving little choice as far as the institutional framework is concerned. Two separate steps have to be taken: first, a pension plan must be established which complies with requirements laid down and which is sanctioned by the formal approval of the supervisory authority. Secondly, the pension fund must be constituted in the hands of a distinct managing institution.

The pension plan is the legal instrument which defines the rights and obligations of the partners in the pension commitment, i.e. the sponsor and the beneficiaries. The pension plan is drawn up by the sponsor with the assistance of a control committee (a minimum of five members) where plan members have a majority representation. Formal approval of the plan is granted by the supervisory authority, subject to being satisfied that the legal requirements have been met (full funding of liabilities, no discrimination, etc.). Pension plans have independent legal status.

The pension fund does not have separate legal status merely because it holds assets generated by the implementation of a pension plan. The pension fund has to be entrusted to an asset management institution (*Entidad Gestora*) which, for its authorisation has to fulfil the following requirements:

(i) it must be registered as a joint-stock company;
(ii) it must have a minimum capital;
(iii) its sole object must be the administration of a pension fund, except in the case of a life insurance company duly authorised to conduct business in Spain;
(iv) it must be subject to the authority of representatives of the plan sponsors and of the plan members. The *Entidad Gestora* shall deposit in custody its assets with an *Entidad Depositaria*, an independent custodian (i.e. a bank) also falling under the supervision of the control committee.

The control committee of the plan has the choice of the *Entidad Gestora* and may change its choice if it is not satisfied with the way in which the pension fund is managed.

The structure described has two important characteristics. One is that the nature of the benefit and contribution provisions, as well as the management of assets or its day-to-day administration, are in the hands of bodies (control committees) where the majority is held by the members of the plan (employees, beneficiaries). This feature may have discouraged certain employers from establishing a qualified plan, preferring alternative pension commitments. The second feature is that the legislation imposes on the parties concerned a fairly rigid set of procedures, controls, and requirements in all the areas of operation of qualified plans.

At 31 December 1992 the number and characteristics of voluntary qualified plans was as follows:

	Number of qualified plans	Number of members
Employment related:	442	196 294
Non-employment related:	85	26 358

Employment-related plans are found in the service sector (337), in industry (98) and in agriculture and mining (7). The non-employment-related plans are established by associations of a different nature, the majority of which cover self-employed persons (58 plans). The trade unions have established 4 plans. The above data does not include voluntary individual retirement plans, under Law No. 8/1987, purchased freely from a financial institution.

Other forms of voluntary provision

The most important alternative form of pension coverage is constituted by the *Entidades de Previsión Sociál* (mentioned earlier), reorganised as private insurance institutions in 1984. They are non-profit organisations and have the characteristic of a mutual benefit society.

Responsibility for management decisions rests with the general assembly of members upon proposals submitted by the governing body. The general assembly gathers all members of the society, or their representatives, as the case may be. The number of members of the governing body is laid down in the plan's statutes. Members are elected by secret ballot at a general assembly. Three members, other than those belonging to the governing body, are also elected to form a supervisory committee whose responsibility is to prepare an annual report on the financial situation of the pan.

To complete the picture, mention is made of the fact that employees may obtain supplementary retirement benefits directly through the employer, mainly as a result of collective agreements. Apart from promises supported by a book reserve arrangement, the employer normally takes out individual or group policies with insurance companies. An employer can also fulfil his promise in the framework of the so-called 'labour foundations', which have, however, only marginal coverage of employees.

UNITED KINGDOM

There is no specific legislative framework for occupational pension schemes in the United Kingdom. The main constraint on the form these schemes take is the need to obtain approval from the *Inland Revenue* (the taxation authority) in order to qualify for beneficial taxation treatment.

In order to qualify for tax privileges, a scheme must be established under an irrevocable trust, with the administration and financial management of the scheme in the hands of trustees (see above, under Ireland, for an explanation of trust terminology). The trust fund has to be maintained quite separately from the assets of the sponsoring employer and money can only be lawfully returned to the employer in special circumstances. This applies to schemes in both the private and public sector, apart from a few public service schemes which are established under their own legislation and do not require Inland Revenue approval (e.g. the civil service, the armed forces, teachers and health service workers).

Pension schemes are usually established by individual employers for their employees (or for certain categories of employees). A single pension scheme may be established in respect of the employees of a group of related companies. There are also a few industry-wide pension schemes established for all the employees in a particular industry. The employer must contribute to the scheme for it to be approved for tax purposes (or must contribute to another scheme of which the employee is also a member).

There are no legal requirements regarding the composition of the trustees. In practice, about 60 per cent of members of private sector schemes are in schemes administered by trustees, some at least of whom are elected or nominated as representatives of the members. The employer usually has the power to appoint the trustees.

With one exception, there are no formal requirements for consultation with members or employers. The exception is the obligation to consult relevant trade unions on the decision whether to contract out of state second-tier provision. In practice, pension scheme issues often form part of negotiations between the employer and employee associations (or trade unions) with respect to remuneration and conditions of service. Changes to pension scheme rules, including benefit improvements, are usually a matter for the employer. Trustees do not usually have the power to change the rules, but their consent is usually required before changes can be made. These provisions are set down in the trust deed, prepared by the employer's advisers, which establishes the scheme. Unless the deed contains a power of alteration, the law does not permit changes except where approved by the *Occupational Pensions Board.*

Once trustees have been appointed they are not expected to behave as representatives of any particular sectional interest. It is their responsibility to administer the trust deed in accordance with the rules of the scheme. The responsibilities of the trustees are laid down in general trust law, which is of ancient origin and does not have specific principles to deal with pension scheme issues. Trustees have a personal and fiduciary responsibility to invest the scheme monies in a prudent way, in compliance with the trust deed and rules. The trustees can delegate the tasks of administration and investment to employed staff or to external experts, but they retain ultimate responsibility for the sound management of the affairs of the pension scheme.

Trustees have the option of either managing the pension scheme as a self-administered trust fund, or to entrust the administration or the investment or both, to an insurance company. Trustees of large enterprises prefer the self-administered approach while smaller companies often have recourse to contracts with an insurance company. Unit trusts and similar investment funds are part of the institutional framework for pension provision, which is available to individuals (personal pensions) or to trust funds.

Employees cannot be forced to join a pension fund operated by their employer. Self-employed persons or employees who are not members of a pension fund can take out their own personal pension arrangement with an authorised pension provider, such as an insurance company, a building society or a bank. On reaching retirement age the proceeds of the pension investment must be used to purchase an annuity from an insurance company, although one quarter may usually be taken in lump sum form. Dependants' benefits can also be purchased. There are limits on the amount of earnings which can be invested in a personal pension, ranging from 17.1/2% of earnings at most ages to almost double that level at ages close to normal retirement.

Personal pensions can also be used as a vehicle for contracting out of the state earnings-related additional pension. These are available to members of contracted-in schemes and to employees who are not members of any pension scheme. They must be taken at retirement in the form of a pension.[12]

Schemes with fewer than 12 members may be established as an alternative to a trust on a self-administered basis under special discretionary powers available to the Inland Revenue. These schemes are technically employers' schemes, but in the vast majority of cases are set up for a small number of senior executives (or directors) of a company where these executives have a large measure of control over the scheme's investments. Substantial numbers of these schemes were set up from 1976 onwards.

Persons covered

Voluntary pension provision freely negotiated or organised by employers and employees generates a flow of funds and a consequent expectation of benefits which tends inevitably to cover and to protect the middle and higher income layers of the social and occupational structure of the population. The probability of being excluded from supplementary pensions is higher, as indicated earlier, for low paid workers, part-time workers, women, employees of small undertakings and more generally the weaker and more vulnerable sectors of the labour market (see Chapter 4).

Such a general statement needs to be qualified because some EU countries have a wider voluntary coverage than others, both as regards employees and the self-employed. On the other hand, a survey of present economic and political conditions indicates that the further extension of voluntary provision to hitherto unprotected persons who may, one day, find state social security benefits inadequate, comes up against obstacles that are not easily overcome. An alternative, as explained earlier, is to introduce compulsory second-tier state pension schemes.

Table 13: Germany: Proportion of enterprises and of employees covered by supplementary pensions, by size of enterprise in manufacturing (1990)		
Size of enterprise (number of employees)	% of enterprises covered	% of employees covered
20 to 49	44	19
50 to 199	76	44
200 to 999	89	65
1000 or more	99	90
All sizes	64	70

In 1993, voluntary coverage, whether contractual or independently sponsored by the interested parties, has reached large sections of the working population in Denmark, in Germany, in Ireland, in the Netherlands, and in the United Kingdom.

In Denmark, 247,000 persons are covered by industry-wide pension schemes established before 1989, while 610,000 persons are covered by the pension schemes which have been negotiated since 1989. Approximately 250,000 persons are covered by company schemes. There are 232,000 public officials who are entitled to a pension from the state budget. This leaves about 1.1 million persons outside collective voluntary coverage within a labour force estimated at about 2,900,000 in 1991. Among the groups excluded, about 230,000 persons have taken out a personal pension plan. The self-employed and young people are the categories most frequently found without supplementary pension coverage.

Table 14: Germany: Proportion of enterprises and of employees covered by supplementary pension schemes, by size of enterprises in trade and commerce (1990)		
Size of enterprise (number of employees)	% of enterprises covered	% of employees covered
3 to 5	24	10
6 to 9	33	13
10 to 19	38	13
20 to 49	50	15
50 to 199	66	25
200 to 499	82	35
500 or more	93	65
All sizes	31	29

In Germany, according to preliminary results of a new survey of the Federal Statistical Office, 46.7% of private sector employees were covered by supplementary pension arrangements in 1992. Coverage of full-time employees is, however, much higher (51.6%) than that of part-time employees (19.9%).

Tables 13 and 14 are taken from the results of a study by the *IFO Institut für Wirtschaftsforschung.* In trade and commerce where firms tend to be smaller than in manufacturing the situation was as shown in Table 14.

Another source indicates that, overall, the coverage of private sector employees is much higher for males (55.9%) than for females (33.1%).

In Germany, the vast majority of public sector employees belong to one of several supplementary pension schemes. Membership reached approximately

4 million persons at the end of 1990.

The situation in Ireland is well documented. In 1992, the number of employees who were members of occupational pension schemes was 438,000, rising to approximately 500,000 if account is taken of intermittent employees and those who will be joining a scheme when they have satisfied the eligibility conditions. This total would represent 53% of persons currently employed (excluding the unemployed and the self-employed).

The most recent data on membership of occupational pension schemes by employment sector was obtained in a national survey of schemes carried out in 1985 for the Department of Social Welfare. The majority of employees who are not members of occupational pension schemes fall into the following categories:

- employees in smaller and less well-established firms;
- employees in the agricultural and fishing sectors;
- part-time, temporary and contract employees;
- employees who were over the maximum entry age when a scheme was introduced (this is very much a declining group); and
- employees who opt not to join a scheme when membership is not compulsory.

Table 15:
Ireland:
Estimates of Occupational Pension Scheme Coverage by Sector, 1985

	Covered		Not Covered		Total	
Sector:	'000	%	'000	%	'000	%
Industrial and large service firms (excluding building and construction)	234.8	56.4	181.6	43.6	416.4	100.0
Small service firms and non-agricultural self-employed	0.0	0.0	213.6	100.0	213.6	100.0
Agriculture, forestry and fishing	0.0	0.0	182.0	100.0	182.0	100.0
Private sector building and construction	48.8	72.8	18.2	27.2	67.0	100.0
Non-commercial public sector	231.0	100.0	0.0	0.0	231.0	100.0
All sectors	514.6	46.4	595.4	53.6	1110.0	100.0

Source: Keogh and Whelan (1985), *National Survey of Occupational Pension Schemes*, Dublin: Economic and Social Research Institute.

The highly developed coverage of public pensions in Italy is the main reason for which second-tier arrangements are not widespread. The best estimates available indicate that in 1991 there were about 1,000 pension plans with about 1,500,000 members. The majority of plans were insured (923), covering 512,000 employees. Self-administered funds, few in numbers, had about 675,000 members. At the beginning of 1994, the situation had not significantly changed in spite of the enactment of a new legislative framework in April 1993.

Coverage of supplementary pension provision is very wide in the Netherlands. A first source of information was the 1985 study by the 'Netherlands Pensions Chambers' which covered all sectors of the economy. Out of a total of 3,629,000 employees between the ages of 25 and 65, it was found that 2,938,000 employees had some form of supplementary retirement provision. The groups excluded from coverage thus represented 17.9% of the total. The reasons for exclusion were either that the employer took no initiative to sponsor a scheme, or that part-time workers or married women were not eligible to belong to the employer sponsored scheme.

Employers who did not sponsor a scheme fell within the following categories:

- small employers with less than 10 employees aged 25 or older;
- employers with a mainly part-time staff;
- employers not belonging to an employers' association and not falling within the scope of a collective labour agreement;
- employers in the trade and business service sectors.

A more recent source gives an idea of the recent growth of membership of supplementary pension schemes in the private sector; the following figures include members of industry funds or single-employer pension funds:

Year:	Membership (Netherlands)
1985	1,949,421
1991	2,735,658

For the United Kingdom the last set of complete figures reflects the situation in 1991 (Table 16).

Table 16:
United Kingdom:
Employees in supplementary pension schemes
1953-1991 (millions)

Year	Private sector	Public sector	Total members	Total employed	Coverage (%)
1953	3.1	3.1	6.2	21.9	28
1963	7.2	3.9	11.1	22.9	48
1971	6.8	4.3	11.1	22.5	49
1975	6.0	5.4	11.4	23.1	49
1979	6.1	5.5	11.6	23.4	50
1983	5.8	5.3	11.1	21.1	52
1987	5.8	4.8	10.6	21.6	49
1991	6.5	4.2	10.7	22.5	48

Remark: Not counted are employees who have some pension rights, but who are not accruing benefits in respect of current employment.

In 1991, out of 10.7 million members, 6.8 million were males who represented 57.0% of total employed males, while 3.9 million were females representing only 37.0% of the total number of women employed. Coverage was much higher in the public sector - 4,200,000 members out of 5,800,000 employed (72.4%) - than in the private sector with 6,500,000 members out of 16,700,000 employed (38.9%).

As in other countries, the size of establishment was a very important determinant of pension coverage, as table 17 illustrates. The following remarks will help to clarify the figures in Tables 16 and 17.

As indicated, coverage is generally very high in the public sector, except among women, where lower coverage is due to the prevalence of part-time working. There are often objective administrative grounds for excluding part-timers: they are only allowed to join many public sector schemes if they work a minimum level of hours per week (usually 10 hours). Very few part-timers in the private sector are members of pension schemes (about 7 per cent). In 1987, part-timers accounted for 3.3 million employees in the private sector and 1.5 million in the public sector, of whom only 230,000 and 310,000 respectively were members of pension schemes.

Table 17:

Coverage according to size of establishment: private sector, full-time employees, United Kingdom, 1987 (thousands)

Size of establishment (number of employees)	Employees	Members	Percentage of members
1,2	390	80	21
3-24	3,590	890	25
25-99	2,990	1,270	42
100-999	3,680	1,290	62
1,000 and over	1,250	1,040	83
Total	11,900	5,570	47

In the private sector, coverage is generally very high in large companies and relatively low among small firms. These figures do not, however, include personal pensions, which can be expected to be more common among employees of small enterprises.

Of the 10.6 million members of occupational pension schemes in 1987, 9.3 million were contracted-out of the state earnings-related additional pension (*SERPS*). All of the 1.3 million members of schemes not contracted-out were in the private sector, so that 100% of public sector pension scheme members were contracted-out, as were 78% of private sector pension scheme members.

The general picture in other EU countries is generally one of limited voluntary coverage for the reasons explained above. In Belgium the estimates available indicate a figure of 650,000 employees affiliated or insured, of which 474,000 are salaried employees and 176,000 are wage-earners, that is respectively 52% and 15% of the total at work in each category. The great majority, probably 400,000 persons, were covered by group insurance contracts. These figures compare with an estimated total private sector employment of about 2,000,000. Furthermore, there is evidence that the large majority of persons covered are found in the highest income brackets.

In Spain, at 31 December 1992, only about 225,000 workers had been affiliated to collective supplementary pension plans which were qualified under the 1987 legislation. The most developed form of supplementary provision under this legislation was the individual purchase of a retirement plan from banks, which covered about 875,000 persons in 1992. Data on membership of the mutual benefit associations was not available.

In Greece and in Luxembourg only a few large industrial companies have promoted voluntary retirement benefit plans. Portugal, on the contrary, has experienced a marked development of private voluntary provision since the enactment of the 1985/86 legislation: membership rose rapidly to 185,000 in 1990 and further to 217,000 employees in 1991. These figures remain modest, however, when compared to an estimate of total employment of 4,717,500 in 1990.

Two points should be made here. The first is that, as indicated earlier, a further significant extension of voluntary second tier coverage is unlikely in the short term. Unemployment rates are high and new jobs are often created in sectors of the labour market which are less well covered by employer-sponsored plans. Early retirement, which is frequent, is not matched by a corresponding number of entrants in the labour market.

The second point is that there are objective and real obstacles to further voluntary sponsorship of supplementary pensions, even if the economic conditions were to improve. Public policy may well wish to see a further shift of responsibility for retirement from public to private arrangements, but one wonders whether the state is in a position to efficiently tackle the emerging obstacles to such a policy and whether it can increase the fiscal incentives beyond the present limits. Rather, the contrary trend on the fiscal front has been seen recently, such as in Belgium and Italy. It is worth noting, for instance, that in 1993 in Germany only 1.6% of enterprises without a supplementary pension arrangement were considering establishing one.

Design strategies for pension plans

Once the decision to establish a particular type of supplementary pension arrangement has been taken, the parties concerned, in particular employers, have considerable freedom of choice as to plan design and to the method of financing the pension commitment. Such freedom is naturally subject to the constraints laid down by the regulatory framework. It is moreover greatly influenced by the tax environment.

Some aspects of the design of a pension plan are more important than others. For example, should the sponsor promise a retirement pension related to the employee's final salary? Should any parallel future social security benefit be discounted or ignored when the promise is made? Should the employer's commitment be restricted to contributing into an employee's retirement account, leaving the latter the investment risk and the choice of converting the capital into a pension at retirement? For the worker, the fact of belonging to a defined benefit rather than a defined contribution plan makes a considerable difference as far as benefit expectations and security are concerned.

Should membership be open to all employees or restricted to some? Should benefit entitlements vest immediately or after a minimum period of membership or employment? Should the sponsor rely for plan management and asset investment on profit-making institutions or should the plan be self-administered? And, most importantly, how much are the voluntary plan sponsors ready to contribute?

Across Europe the answers given to such questions are extremely varied. In countries where voluntary pension provision is at the initiative of individual companies the variety of solutions as to plan design is particularly broad. In the present study, no attempt is made to draw up a full inventory of individual rules, practices and features of plan design across Europe. The subject is treated in voluminous reference books available to specialists.[13] The following are selected country highlights showing prevailing benefit design practice on the basis of information available at the end of 1993.

BELGIUM

Defined benefit schemes are the most common form of pension plan, representing approximately 70%-80% of Belgian plan membership. However, there is growing interest in defined contribution plans.

Multinational companies normally provide pensions based on final salary, permitting partial or full lump sum commutation. Typically, the company plan will aim to provide between 1.25%-2% of final average earnings for each year of service, minus the state pension earned during company service. Plans are integrated with the state social security system, either by a direct offset of the assumed state pension, or by defining different accrual rates for earnings below and above the state social security ceiling (on average 6.9% of gross earnings for salaried employees and 0.73% for wage earners).

Employees are usually required to make small contributions on earnings up to the state social security ceiling and to contribute in the range 1%-6% for earnings above the social security ceiling. Employers provide the bulk of the required resources.

The most common method of funding supplementary pension is by insurance contracts. Members' rights vest immediately, in both insured and non-insured plans (those organised as non-profit association, *ASBL*). Most plans are designed to cater for the needs of white-collar workers or senior executives.

DENMARK

Multi-employer plans: All these are defined contribution plans. In the schemes established before 1989 the employer contributes 8% or 10% of earnings and the employee 4% or 5% of earnings. The pension schemes established since 1989 are still being built up, and therefore contribution rates are still low. They are, however, expected to reach about 9% of earnings in the coming years. The balance of the accumulated individual contributions may be paid as from age 60 in the form of a life annuity. At age 67, a lump sum is frequently provided (2 or 2.5 times the annuity). Invalidity and survivors' benefits are included in the plan.

Single employer plans: Most of the plans are defined benefit, final salary arrangements. Membership rules are stricter, and there may be provisions laid down as to minimum age and duration of employment.

Insured plans: The design pattern is more flexible. Plans are contribution defined but give the employee a wider benefit choice at retirement than is possible under other plans. The prevailing choice is to opt for a lump sum benefit. The employee is promised a minimum annual interest yield on his accumulated contribution balance, which may be increased by the insurance company if investment experience permits.

In practice, all benefits vest immediately in all the three types of the plans described above.

FRANCE

Coverage by second-tier compulsory schemes being very comprehensive, voluntary provision is practically confined to executives and senior staff of large companies and to selected groups of public servants who have taken upon themselves the initiative of creating an appropriate provident institution.

Retirement plans in large firms: The benefit plan will typically be integrated with state social security, including within it any compulsory second-tier benefits. For instance, the plan may promise 1.8% to 2% of final salary per year of service gross of social security. An alternative is to modulate the integrated accrual rate by earnings bands. Plans which are not integrated with social security have also been offered by a few firms (*plans additifs*): they may provide 5% or 10% of final salary for a given period of service.

It follows that the large majority of plans are defined benefit plans. Interest in introducing contribution-defined plans is more recent, and is confined to insurance products (under Art. 83 of the Tax Code).

Contributions are normally paid entirely by employers. Full funding of liabilities is not common, even if the plan is insured. Most large companies pay benefits out of current income with possible balance sheet reserve cover.

Retirement plans for public servants: The *PREFON* plan is adapted to the nature of the relevant institution, which is a non-profit provident association sponsored by the trade unions of public servants, whose assets are managed by a consortium of leading insurance companies. Liabilities are fully funded because the *PREFON* plan is contribution-defined on the basis of employees' contributions only. Benefits are only in the form of supplementary pensions, using a technique similar to that of *ARRCO/AGIRC* (see Chapter 4). Survivors' benefits are included.

The second institution, *CREF*, is a mutual provident association covering selected groups of public servants. The employees are the contributors; they have a choice of contribution rates and, consequently, of pension levels. Pensions are indexed after award according to civil servant salaries. Survivors' benefits are provided. The plan is partly funded. A constraint is that the employee who wants to join *CREF* must commit himself to contributing for at least 10 years.

GERMANY

Supplementary pension plans designed for local German companies have a variety of benefit targets: many plans guarantee fixed lump sums at retirement, others (mainly in multinational or larger enterprises) are final salary arrangements. The benefit is calculated on the basis of 1% to 2% per year of service on earnings above the social security ceiling. The accrual rate below the ceiling ranges from 0.25% to 0.75%. Defined contribution plans are far less common. Survivors' benefits are generally included.

The contributors to the pension plan are as follows:

- book reserves: only the employer;
- support funds or direct insurance: mainly the employer;
- pension funds: two thirds employer, one third employee.

The total rate of contribution for comprehensive plans ranges most frequently between 5% to 7% of earnings. Less generous plans require only contribution rates of 2% to 3%. Pension plan benefits vest after the age of 35 and after 10 years' participation in the plan or, alternatively, 12 years' service with 3 years' participation in the plan. Exceptions to the vesting rules can be negotiated among different enterprises (i.e. for executives).

A special feature is the salary replacement insurance, whereby the employee is free to entrust part of his salary to the employer for the purpose of purchasing insurance on his behalf. This arrangement is additional to the ordinary pension plan and it does not carry any vesting requirements, since the funds belong to the employee.

GREECE

Strictly voluntary plans are not very developed in Greece, where supplementary pension provision is compulsory and broad-based.

Provident associations (caisses mutuelles, *etc.):* The retirement benefits administered by these private, autonomous associations are financed through members' contributions, although employers may also agree to contribute. The range of benefits and the qualifying conditions vary from one association to another. Typically, a pension is paid only after a minimum period of contribution (10 to 15 years). Pensionable age is, as a rule, higher for men than for women. The investment of assets is frequently entrusted by the association to an insurance company.

Group insurance plans: Coverage is normally extended to all full-time employees who have attained the age of 21 (or 25) and have completed one year of service. Employees generally may receive a pension at age 65 (60 for females) under the *IKA* rules. Actuarially reduced benefits are normally payable. The benefits insured may take different forms: (i) defined benefit plans designed to pay an annuity; (ii) defined benefit plans paying a lump sum; (iii) defined contribution plans to which the employer pays 3% to 5% of salary.

Most retirement plans do not have a vesting provision. The majority of plans are financed by the employer; employees' contributions are not common.

IRELAND

In 1992 the large majority of members of occupational pension schemes were covered by defined benefit plans (2,621 schemes with 385,200 employee members). Defined contribution arrangements were more numerous because they typically cover just one or several employees. In total these arrangements only cover 52,780 employees.

In the case of defined benefit schemes, the maximum limit set by the *Revenue Commissioners* (tax authorities) for schemes to be approved for the special tax treatment is two-thirds of final pensionable salary.

The most common accrual rate is 1/60th of final salary for each year of service, leading to a pension of two thirds of final pensionable salary for a member who completes 40 years of pensionable service. Schemes may offer accelerated accrual of benefits to members who enter a scheme late in their career and full tax approval is given in these cases for a maximum two-thirds pension, where there has been at least 10 years' service at normal pension age.

Members can be given the option of converting part of their pension into a lump sum at retirement, up to a maximum of 1.5 times final salary. This lump sum is fully tax free, while pensions in payment are subject to tax.

A significant number of schemes do not provide benefits up to the Revenue limits, as allowance is made for the fact that members will have an entitlement to a pension under the state social insurance scheme. The method of integration of the occupational and social insurance entitlements may involve either a straight deduction from the member's occupational pension of the amount of the social insurance pension, or an adjustment of the amount of salary for the calculation of pension entitlements.

The accrual rate for most schemes in the public sector is 1/80th of final salary for regular pension payments and 3/80ths for the lump sum for each year of service up to a maximum of 40 years' service. This means that the maximum pension payable is 50 per cent of final salary and the maximum lump sum payable at retirement is 1.5 times final salary. The target of these final salary plans normally also includes the state social insurance pension, in the case of those public sector employees who are covered for pensions under social insurance.

Provision is also usually made for pensions for surviving widows, widowers and children. The pension is normally 50% of the pension the deceased member would have received at normal pension age, but tax approval can be given for a level of pension up to two thirds of the maximum pension the deceased member would have received. Pensions are usually payable in respect of dependent children in the form of an increase of the widow or widower's pension or as a separate pension, where there is no surviving parent. A lump sum payment is normally given for death in service, calculated as a multiple of annual salary up to a maximum of 4 years' salary, the upper limit for tax approval purposes, but it is more usual to give 1.1/2 to 2 years' salary. This lump sum is payable irrespective of whether there are surviving dependants.

Many schemes make provision for retirement on grounds of ill health. The provision made can vary from receiving a pension based on accrued entitlements to date of commencement of ill health retirement, to a level of pension that would have been payable if the member had remained in employment until retirement age.

Members who leave service before retirement age (e.g. a change of job), and who have been members for at least 5 years, are entitled under the Pensions Act to have the benefit rights accrued in the period after 1 January 1991 either preserved in the scheme they are leaving or transferred to a new scheme or to a life assurance company retirement bond. The preserved benefits in a defined benefit scheme must be revalued in the period after 1 January 1996 by 4% a year, or in line with the consumer price index, if price increases are less than 4% for that year, until they become payable. Preserved benefits normally become payable at retirement age, or death if this occurs before retirement age. Early leavers who are not entitled to preserved benefits in respect of periods of pensionable service may receive a refund of their contributions paid during these periods.

Most public sector schemes are exempt from the preservation of benefit requirements under the Pensions Act, as they have arrangements for preservation which are in some respects different, but at least as favourable as those provided for under the Pensions Act.

Retirement pensions under occupational schemes are usually payable for life and are in any event guaranteed for 5 years. Accordingly, if death occurs within that time, the balance of the 5 years' guaranteed period will be paid to the surviving dependants or to the deceased member's estate.

Recent surveys have shown that a majority of funded schemes (72%) provided for increases of pensions in payment on a regular basis, which are mainly in line with or related to the consumer price index. Most public sector schemes provide for indexation of pensions in line with pay increases for the category and grade of employee to which the pensioner had belonged before retirement.

The 1985 survey of schemes carried out for the Department of Social Welfare (Keogh and Whelan, *National Survey of Occupational Pension Schemes*, Dublin: Economic and Social Research Institute, 1985) showed that a quarter of occupational pension schemes were non-contributory, that is wholly financed by the employer. The remainder (75%) were contributory, requiring a contribution from the employee that is based on a percentage of earnings in 70% of these schemes. The average weighted contribution per member was 4.43% of pensionable pay (Hughes: 1994, see note 10). To qualify for the special tax treatment afforded to occupational pension schemes, the employer must contribute at least one sixth of the total cost.

Members have the option in many schemes of making additional voluntary contributions (AVCs) to the main scheme or to a separate scheme established for this purpose, in order to secure additional benefits.

ITALY

Funds with segregated assets represent 88% of all plans surveyed in 1991. Typical contribution rates ranged from 4% to 6% of earnings depending on economic activity. Joint employer/employee contributions are most frequent in banking and industry. Out of 1,078 plans 953 were defined contributions. Options to convert the lump sum benefit into a pension are available.

LUXEMBOURG

Coverage is normally extended to employees having reached a prescribed age, often 25 years, and who were under 50 or 55 when they joined the firm. Vesting is generally allowed after five years for retirement benefits, but there is no vesting for disability and death benefits.

The typical benefit received at state pensionable age is an annuity. However, part commutation into a lump sum is allowed in many plans.

Defined benefit plans (often final salary arrangements) are integrated with the state social security system. Benefit indexation clauses are not common.

The majority of plans provide survivors' benefits. Contributions to insured plans are paid by employers and occasionally employees. Employees' contributions are not permitted if a pension promise is financed by a book reserve technique.

NETHERLANDS

The large number of retirement pension plans currently tax-approved in the Netherlands show a broad range of rules and benefit design features. The following are the main categories.

(i) Salary-related benefit schemes with two principal variants;
- final salary schemes;
- career average salary schemes.

(ii) Defined contribution schemes.

In addition there are plans which only provide payment at retirement of a fixed amount (independent of salary and sometimes also independent of length of service). The relative importance of the various types of scheme is illustrated by the figures in Table 18 relating to private sector schemes in 1987.

There is a consensus among the social partners that a good quality pension scheme should provide a pension of 70% of final salary, including state social security, after 40 years' service.

Pension plans are integrated with state social security schemes. In the past, integration with state social security took into account the different amounts payable to single persons or to couples under the state scheme *AOW*. Recently, objections have been raised against this practice, because of the concern that this may be a form of sex discrimination in occupational pension benefits. There are suggestions that the supplementary pension for equal periods of service and salary should be the same for men and women, irrespective of the different benefits from the *AOW* scheme.

As far as benefit targets are concerned, the most usual rate for a maximum period of membership is 70% of final salary (integrated with state social security). Other plans provide lower rates, such as 50% or 60% of final, or career average salary.

Table 18: Types of pension plans in the Netherlands

	% of membership		
	Men	Women	Men and women
(a) Final pay	69.8	80.6	72.1
(b) Career average	16.3	11.8	15.4
(c) Combination of (a) and (b)	5.7	3.8	5.3
(d) Defined contribution	7.5	3.1	6.6
(e) Fixed amount	0.7	0.7	0.6
All plans	100.0	100.0	100.0

The accrual rate works out at 1.75% to 2% per year of service. Retirement takes place at age 65 with very few exceptions. Entry age is frequently 25. Widows' pensions are normally included in the plan. Full vesting after one year's scheme membership is compulsory.

Early leavers are entitled to a deferred benefit proportional to the amount of pension that they would have received if they had continued participating in the scheme until retirement age. Vested rights of former plan members must be indexed if pensions in payment are increased through indexation.

Contributions may be paid by employers and employees. Employees are normally required to contribute either one half or one third of the required contributions. There also exist non-contributory plans. Another formula is to require the employee to contribute at a given rate of salary (between 3% and 12%) and to ask the employer to finance the difference.

PORTUGAL

Company plans are typically designed to provide a retirement benefit related to final salary earnings. Most plans integrate with state social security but some are targeted to provide a fixed percentage of final pay irrespective of the state benefit.

Vesting is unusual, except in defined contribution plans. The large majority of plans are financed exclusively by employers' contributions.

SPAIN

At the end of 1992, out of 527 qualified plans, 160 were defined contribution plans, 19 only were defined benefit and the balance (348 plans) were a combination of both methods.

In past years the benefit target was approximately 100% of final salary, integrating supplementary and social security pensions. Recent experience shows that plan sponsors prefer to avoid integration with the state pension. Moreover, the present economic situation induces employers to set a maximum limit on their contributions to the plan, irrespective of the benefit target. The 1987 legislation has moreover prescribed a 'cap' or a maximum amount that, every year, can be earmarked for pension fund contributions. The 'cap' was, in 1992, the lower amount of (i) 750,000 pesetas per member covered, or (ii) 15% of the net amount of payroll plus the corporate profit of the year, and 15% of net income for self-employed persons.

Vesting is immediate in qualified plans.

UNITED KINGDOM

By far the majority of members of pension schemes in the United Kingdom belong to the defined benefit type of scheme. Most of these provide benefits based on salary at or near to retirement. The most common arrangement is for pension to be a fraction of final salary, with a pension of 1/60th payable in respect of each year of service. However, other fractions are also sometimes used. Final pensionable salary is defined in the rules of the scheme and may be the earnings in the last year before retirement, or an average over several years. Where an average is used, the earlier years may be revalued to the level at retirement using an index, usually the retail price index.

In order to qualify for tax approval it is also necessary to satisfy certain maximum benefit rules. The maximum permissible pension at normal retirement age is two-thirds of final salary, subject to a limit of £75,000 a year (in 1993/94, raised to £76,800 in 1994/95) on pensionable earnings for persons who have changed jobs or entered new pension arrangements. Although this maximum would usually only be attained by those with 40 or more years of service, some schemes offer accelerated accrual of benefits for late entrants. The maximum two-thirds pension may be paid provided there has been at least 20 years' service.

Table 19: United Kingdom: Number of members of occupational schemes by pension accrual fraction (thousands)

Pension accrual fraction	Private sector	Public sector
Better than 60ths*	895	195
60ths	3,695	300
Between 60ths and 80ths	140	285
80ths	820	3,405
Less than 80ths	30	15
Total	5,580	4,200

* If service is less than 40 years (40/60ths is the maximum permitted by the Inland Revenue).

Part of the pension can be commuted (converted) into a lump sum on retirement, subject to limits laid down by the tax authorities. This lump sum is payable free of all taxes, whereas pensions are taxable as earned income.

Many public sector schemes provide a pension of 1/80th of final pensionable salary for each year of service, together with a lump sum equivalent to 3 years of pension. In the private sector there is often a different pension accrual rate, the fraction of pensionable salary per year of service which is used to calculate the retirement benefit. This is shown in Table 19, which includes both members in final salary schemes and those who are eligible for a pension and an additional lump sum.

There are also many defined contribution plans in existence for smaller enterprises. Recently, employers setting up a first plan have tended to favour defined contribution arrangements.

Personal pensions taken by contracted-out employees build up rights in proportion to the sums contributed by the individual, less the expenses and charges of the insurance providers.

Normal retirement age is defined for each scheme. Until recently it was common for schemes to follow the state pension ages, although some adopted a different approach, such as age 60 for both males and females, or age 65 for both. As a result of the judgment of the Court of Justice of the European Communities of 17 May 1990 (Barber v. GRE) most schemes have now equalized the pension age for men and women, at least for service since the date of the judgment. At the end of 1993, legislation was enacted to equalize the state pensionable age of men and women progressively at age 65.

Most defined benefit pension schemes also provide pension benefits on ill-health retirement and lump sum benefits on death in service, as well as pensions to surviving widows, widowers and children. Widows' and widowers' benefits are also usually related to final pensionable salary, defined as at the date of death of the member, or at the date of retirement if death occurred after the normal pension had begun to be paid. Widows' and widowers' pensions are usually 50%, or occasionally 2/3 of the deceased member's pension. Many schemes increase the payment to the widow or widower if there are dependent children and pay orphans' pensions if there is no surviving spouse. A lump sum benefit is also usually payable on death in service, regardless of family status and whether or not there are surviving family members. This can be up to 4 years' salary, but 2 years' salary is the most common amount.

Anyone who leaves employment (or the pension scheme) before normal retirement age, with 2 or more years' pensionable service, must be granted entitlement to the accrued benefit, although the benefit is not usually payable until retirement age (or, if before, until death). Accrued rights deferred to normal retirement age in this way are required by law to be revalued at 5% a year, or in line with the retail price index if this increases at less than 5% a year over the period of deferment.

Early leavers with less than 2 years' service can be given a simple refund of their own contributions. As an alternative to retaining accrued rights in the pension scheme which they are leaving, or taking a refund of contributions, early leavers may have the cash equivalent of their accrued rights (i.e. a transfer value) paid to another pension scheme or into a personal pension arrangement. Where a transfer value is paid to another scheme, it will usually be used to provide credited years of pensionable service to be added to the years of actual future membership in the new scheme. Sometimes, however, the transfer value is used to provide credits on a money purchase (defined contribution) basis.

The rules often provide for pension in payment to be increased by a fixed percentage each year (say 3% or 5%). The trustees however have a discretion to award additional increments as the finances of the pension fund permit, with a view to maintaining more closely the real value of the pension at the time of award. Most public sector pension schemes currently provide automatic or near-automatic indexation of pensions in line with changes in the retail price index.

Recent legislation provides that for pension rights acquired in respect of future service, pensions in payment must be increased by 5% a year or by the increase in the retail price index if this has been less. However, this provision has not yet been brought into effect.

Tax treatment

As explained earlier, governments wishing to promote a second tier of pension provision can either introduce suitable schemes on a compulsory basis or can encourage enterprises and individuals to do so through tax incentives. All EU countries have granted privileged tax treatment to private pension funds and similar forms of voluntary retirement provision; some more generously than others. If the motivation of governments is clear, the implications on their fiscal policies in this particular area raise a number of important questions.

The first question is whether savings for retirement deserve privileged tax treatment as compared with other forms of saving. The arguments in favour are that voluntary pension provision has a social value in the sense that society approves any provident behaviour which is bound to avoid hardship in old age and subsequent dependency on the state welfare and social assistance. More recently, the value of the 'social return' of private provision has been emphasised by governments facing escalating costs of public pension schemes (see Chapter 1).

The arguments against are that on grounds of equity it is not fair to grant tax privileges to a section of the working population that is bound to be the least poor, not to say the better paid. Data and information on the coverage of voluntary provision in EU countries (set out earlier in the Chapter) seem to justify such a view.

Table 20: United Kingdom: Value of tax relief granted to occupational pension schemes (£ million)		
	1986-87	1991-92
Relief for:		
Employees' contributions	1,700	2,400
Employers' contributions	3,300	3,400
Investment income of funds	3,500	5,100
Lump sum payments from unfunded schemes	250	300
Total reliefs (1)	**8,750**	**11,200**
Less tax liable on:		
Pension payments	2,500	3,400
Refunds to employers	-	161
Total tax liability (2)	**2,500**	**3,561**
Net tax relief: (1)-(2)		
Total net reliefs (rounded)	**6,300**	**7,700**
Source: table 6.9 of Inland Revenue Statistics, 1992		

On the other hand, it is sometimes argued that if middle and high income employees did not have access to a second pension through private provision, they might put pressure on the state for better public pensions, which in turn would cause greater taxation that would affect everyone. The fact that withdrawing tax incentives from private provision would involve similar or greater overall costs for the state has been emphasised in Ireland where the state pays flat-rate old age pensions without a second earnings-related tier.

A second question is whether tax relief on pension funds and similar arrangements deprives the Treasury of large sums which may be badly needed by Member States, particularly those experiencing severe budget deficits. It is very difficult to evaluate the overall financial impact of pension tax relief because there are offsetting factors and shifts over time. The general practice is to grant tax relief on contributions to voluntary pension provision but to tax the resulting benefits when they become due.

Governments are, however, aware of the possible inconsistency resulting in times of fiscal austerity from the simultaneous increase in the overall fiscal burden and the granting of tax relief for retirement schemes. Recent legislation in Italy shows the reluctance of finance ministers to provide generous incentives. Belgium has recently tightened the rules on tax advantages. In the Netherlands the issue has been raised, although no action has been taken. At the other extreme, Portugal's generous tax incentives granted since 1985/86 have generated a sudden surge in the number of private pension funds.

In countries where private provision has reached significant dimensions, estimates have been made of the consequences of providing tax incentives in this area. For the United Kingdom the relevant estimates are given in Table 20. The net value of tax reliefs in 1992-93 was estimated in the 1992 *Autumn Statement Statistical Supplement* as £8,100 million. The value of tax relief given on contributions to personal pensions (including retirement annuity considerations and free-standing additional voluntary contributions) was estimated as £1,600 million in 1992-93.

In Ireland, it has been estimated that on a standard cash-flow basis the value of the tax reliefs in 1989 ranged from IR£160 million to IR£216 million (Hughes: 1994, see note 10). In 1989, the total cost of pensions under the Social Welfare system (social insurance and social assistance) in respect of retirement, old age and survivors amounted to IR£1,022 million (excluding administration costs). The estimated value of tax reliefs on funded occupational pension schemes, therefore, ranged from 16% to 21% of that amount. In 1989, total revenue for income tax amounted to IR£2,810 million. Accordingly, the estimated value of the tax reliefs ranged from 5.7% to 7.7% of income tax.

To appreciate fully the various arguments, a budgetary appraisal should be accompanied by an assessment of the impact on individual persons. From the perspective of individual scheme members it can be argued that there is no significant net gain in real terms as they ultimately pay tax on the money set aside to finance their pensions when these pensions become payable. However, the tax concessions do favour them in two ways. Tax relief on the contributions is usually provided at higher marginal tax rates than the tax rates which will apply when the scheme members are receiving payment of their pensions in retirement, as their overall income is generally lower at that stage than when they were in employment. Most scheme members also receive lump sum benefits which are often tax free or taxed at advantageous rates.

A final important question relates to employers' behaviour. Should they spontaneously introduce pension arrangements for their staff because of the tax relief on their contributions or for other reasons? An objective answer, valid for all employers, cannot be given. As explained earlier, motivations vary and respond to a complex set of circumstances. Experience shows, however, that in designing a private pension arrangement, its sponsors are always fully aware that different options may attract more or less tax relief; consequently they inevitably tend to prefer the solution which is the most tax effective.

BELGIUM

Employers' and employees' contributions to an approved pension plans (*ASBL* or insured) are tax deductible provided that the estimated total pension (state social security plus supplementary pension) does not exceed 80% of the employee's presumed final salary at retirement. As from 1994, a restriction has been imposed to the tax treatment of employees' contributions: only a part (30-40%) is deductible, rather than 100%, and this penalizes high income earners who are subject to high marginal tax rates. In addition, an annual tax of 4.4% will become payable on both employers' and employees' contributions to supplementary pension arrangements (*ASBL* or insured).

Capital sums paid at retirement by pension funds or under insurance policies are taxed (at age 60) once for all at a rate of 10% to 16% according to whether the benefit has been financed by the employer (16%) or jointly with the employee (10%).

Supplementary pensions are taxed as normal earned income, although a flat-rate tax credit is granted. Assets and investment income are not exempt from tax. The assets of an *ASBL* are subject to an annual tax of 0.17%. Dividends of investments are subject to withholding taxes, depending on their origin. Insurance companies are not subject to the above because they are taxed on their profits.

DENMARK

Employers' and employees' contributions to a supplementary pension plan are fully tax deductible (without any ceiling on annual contributions). Capital sums paid at retirement from age 60, or at an earlier age, are subject to a flat-rate tax of 40%, while pensions are taxed as earned income every year, even if the pensioner takes up residence abroad.

The returns on pension asset investment by insurance companies or by pension funds are subject to a special flat-rate tax (called 'real interest tax') up to a maximum of 56 per cent. An elaborate formula ensures that the yield on investment which eventually will benefit future pensioners is not excessive (i.e. not more than 3.5% above price inflation).

FRANCE

Employers' pension contributions to insurance companies, pension funds, or similar provident institutions are fully deductible. Allocations to book reserves are not deductible. Employees' contributions are deductible provided that coverage is compulsory for the employee (for instance contributions to *AGIRC* and *ARRCO* or contributions to defined contribution plans), that they do not exceed 19% of eight times the social security ceiling and that the employer is also contributing for pension purposes (not for lump sums).

Voluntary defined benefit plans offered by insurance companies can offer a more favourable tax treatment of pension contributions, provided there are no vesting conditions.

Exceptionally the two supplementary schemes *PREFON* and *CREF* allow affiliated public employees an unrestricted tax deduction on contributions. Benefits, irrespective of the scheme awarding them, are taxed as earned income.

Pension institutions which are non-profit making enjoy favourable tax treatment on their current transactions, including returns from sums invested.

GERMANY

Tax treatment depends on the method of financing the pension commitment.

Book reserve plans:

- employers' allocations to reserves are fully deductible provided the liability is calculated according to approved conditions and assumptions (no employee contributions are allowed);
- benefits are taxed as earned income;
- employers' premiums paid to reinsure the liability with the compulsory insolvency insurance *PSV* are deductible.

Pensionskassen *and direct insurance:*

- employers' contributions are fully deductible but are included in the taxable income of employees;
- pensions are subject to reduced income tax rates (as are social security pensions); lump sums are tax free.

Support funds:

- employers' allocations are deductible if they do not exceed prescribed limits;
- benefits are taxed as earned income.

The yields of investments made by *Pensionskassen* and support funds are not taxed provided that the corresponding assets have been accumulated in compliance with the rules prescribed.

GREECE

Full tax deductibility is granted in respect of employers' and employees' contributions to compulsory supplementary pension funds (*IKA/TEAM*, auxiliary funds, etc.) while their benefits are taxed as earned income.

Any insurance premiums paid by an employer to cover a pension contract for his employees are deductible from corporate tax on profits. Premia paid by employees are deductible only up to a prescribed ceiling. Benefits are taxed as earned income.

Investment returns are not taxed if they accrue to compulsory pension funds. Insurance companies fall under the fiscal framework applied to public companies which includes taxes on net, not allocated, profits.

IRELAND

The tax treatment of occupational pension schemes is governed by the 1972 Finance Act. To qualify for the tax reliefs available, schemes must obtain approval from the *Retirement Benefits District* of the *Revenue Commissioners*, which is the regulatory authority for tax approval purposes. One of the main conditions for revenue approval in the case of pre-funded schemes is that the fund must be set up as an irrevocable trust.

All schemes must also comply with certain maximum benefit requirements. These include a maximum pension on retirement of two-thirds final pay (after 10 years or more service), with an option of commuting part of the pension into a lump sum which cannot exceed 1.1/2 years' salary after 20 years of service. Similar constraints apply in the case of pensions for retirement on grounds of ill health and for survivors' benefits.

The employee's contribution is tax deductible up to a limit of 15% of pensionable pay in the year in which contribution is paid, i.e. tax and social insurance contributions are assessed only on the net income after deduction of the pension scheme contributions.

The employer's contributions to the pension scheme are tax deductible as a business expense in computing the employer's profits for tax purposes and, in addition, are not taxed as employee's pay. An employer is required to finance at least one sixth of the cost of the benefits to which each employee is entitled at normal retirement age, if the scheme is to qualify for full approval for tax purposes. To prevent pension funds being used as a method of tax avoidance, approval can also be withdrawn by the Revenue Commissioners if a large surplus is built up. Revenue approval can be maintained in these circumstances if proposals are submitted for reducing the surplus by either providing for improved benefits up to the benefit limits permitted, or reducing contributions, or a combination of both.

The income from investment of the scheme's assets and capital gains are exempt from tax. Tax paid on company dividends can be re-claimed, and dealings in government securities are exempt from stamp duty. Pension funds are also exempt from *Deposit Interest Retention Tax* with effect from 1 January 1993.

Lump sums payable on retirement up to 1.1/2 years' salary are fully exempt from income tax. In the case of death in service, lump sums up to 4 years' salary payable to surviving dependants are tax exempt. These exemptions apply to lump sums paid under both funded and unfunded schemes.

Refunds of personal contributions to members who do not have an entitlement to a preserved benefit are exempt from the standard rate (27%) and higher rate (48%) of tax: a special rate of 25% is payable by them. This rate had been set at 10% until 1992.

Income tax is payable in the normal way on regular pension payments. State social insurance pensions and any other income the pensioner may have are included in assessing tax liability.

ITALY

A new fiscal framework for supplementary pensions was established by the legislation adopted in April 1993, which was subsequently amended by Decree Law 585 of 30.12.1993. Employers' and employees' contributions to a pension fund are deductible from corporate or personal income tax, subject to the following:

- aggregate employer/employee contributions are deductible up to a ceiling of 10% of remuneration on which the annual levies for the compulsory termination indemnity (*TFR*) are assessed;
- employers' contributions are deductible up to a ceiling equal to 50% of the annual amount paid into the *TFR* scheme;
- employees' contributions are deductible up to a ceiling equal to 3 million Lira per year;
- the share of the annual *TFR* levy transferred to a pension fund is totally deductible;
- benefits are taxed as earned income;
- a special levy equal to 15% of aggregate employer/employee contributions is due to the Treasury by pension funds as from July 1994. This levy shall be reimbursable to fund members at the time of benefit payment, in the form of a tax abatement on the amount of tax due on benefits;
- transfer values are not subject to tax;
- taxes are levied on the investment yield of the assets of a pension fund at a rate of 0.125%.

The tax treatment of premiums paid to purchase an annuity with a lump sum benefit at retirement has been made more favourable by Decree Law No.585.

LUXEMBOURG

Contributions paid by an employer into an employee benefit plan are tax-deductible. These contributions are, however, treated as a benefit-in-kind and are added to the employee's taxable income if the plan is funded through a direct group insurance contract or through a self-administered pension fund set up as a separate legal entity. They are not taxed as a benefit-in-kind to the employee when the plan is financed through allocations to internal pension reserves, with or without re-insurance.

An employer who wishes to assume the employee's tax liability for the employer contributions to an employee benefit plan, can pay a flat-rate tax of 6.31%, subject to certain conditions stipulated by the tax authority. The tax treatment of employee contributions to an employee benefit plan depends on the funding method of the plan.

Employees' contributions to group insurance contracts and to private pension funds are treated as ordinary life assurance premiums and are tax-deductible up to LFR 6,000 per annum, provided these contributions are paid to pension funds established in Luxembourg or to group insurance contracts under-written with an insurance company established in Luxembourg.

Pension benefits payable from both the social security system and a supplementary company plan, irrespective of the funding method, are taxed as earned income. Lump sum benefits payable from an occupational pension plan on retirement, are not subject to tax if they are paid from a directly insured plan or from a separate pension fund. Lump sum benefits payable on retirement from a book reserve arrangement with re-insurance are taxable at a separate rate of 34 per cent.

NETHERLANDS

Employers' and employees' contributions to approved pension plans (self-administered or insured) are fully tax deductible. A plan is not approved if the level of promised benefits is considered excessive according to prevailing social standards. Pension benefits are taxed as social security pensions, that is more favourably than normal earned income. Pension fund assets and the yield from their investment are not taxed.

PORTUGAL

Employers' contributions to supplementary pension plans are deductible up to the equivalent of 15% of payroll, or up to 25% if the covered workers are not insured under the state social security system. Employees' contributions are treated, for tax purposes, as education expenses or insurance premiums. The taxable income can accordingly be reduced by a maximum amount of ESC 180,000 (single persons) or ESC 360,000 (married persons). Yield from pension plan investments is tax free.

SPAIN

Qualified plans:

Employees' contributions to supplementary pension plans are fully tax-deductible. They are individually allocated to members' accounts and they are added to the employee's taxable income (as if it was additional salary). However, employees are simultaneously allowed to deduct the imputed employers' contributions plus their own (if any) up to the lowest of the two following amounts:

- 15% of gross remuneration from work (as an employee or as a self-employed person); or:
- PTA 750,000 per annum, per member.

Benefits are taxed as earned income. If they are lump sums, a notional redistribution over the number of years of membership is effected for tax purposes.

The institutions established to manage the assets (*Entidades Gestoras*) are exempt from VAT and from withholding or similar taxes on investment yield.

UNITED KINGDOM

There are four main taxation consequences of being a tax approved occupational pension scheme:

- employers' contributions are an allowable expense against profits;
- employees' contributions are tax deductible, i.e. tax is assessed only on the net income after deduction of pension scheme contributions;
- employers' contributions to the scheme are not treated as taxable remuneration in the hands of the employee, and
- no tax is payable on investment income or capital gains within the pension fund (although the recovery by the pension fund of tax paid by companies in which shares are held, in respect of their dividends, is less than 100%).

In order to qualify for tax approval, the scheme must be established under an irrevocable trust and the employer must contribute to the scheme. Employee contributions must be limited to a maximum of 15% of earnings and the scheme must comply with certain maximum benefit requirements. These include a maximum pension (after 20 or more years' service) of 2/3 final remuneration (defined in one of several approved ways) and a variety of constraints on other benefits, including invalidity pensions, survivors' pensions and lump sums.

A lump sum of up to 4 years' salary may be paid on death in service. This is tax free provided it does not pass automatically to the member's estate. A lump sum of up to 1.1/2 years' salary may be paid to the member on retirement, subject to 20 or more years' service and a corresponding reduction in the member's pension benefit. This is also completely tax free. All other benefits are taxable as earned income in the hands of the recipient.

The tax privileges of belonging to a tax-approved occupational pension scheme are not available in respect of earnings in excess of £76,800 a year (about 4.5 times national average earnings), except for those individuals who remain in the pension scheme of which they were a member prior to 1 June 1989. However, earnings up to £76,800 a year can qualify for benefits under a tax approved scheme, even for new members.

Pension funds which are approved must show that the level of funding (i.e. the size of assets matching the liabilities) is within the actuarial limits set by supervisory authorities. Approved funds are exempt from tax on investment income and on capital gains tax on disposal of assets (non-approved pension arrangements are subject to basic rate income tax).

Protection of members' rights

Much interest has been generated in Europe in recent years around the question of whether the legitimate rights of members of voluntary and private pension arrangements are sufficiently protected. Protection is needed at several levels. First, protection is needed against unjustified discrimination (for instance on grounds of sex, age, employment status, etc.). A second aspect is protection against mismanagement of resources and assets, depriving present or potential beneficiaries of their benefit rights. The third is protection in case of unforeseen events which may negatively affect individual rights, such as bankruptcy, insolvency or liquidation of the sponsoring enterprise, mergers and acquisition of companies, and similar situations. The final aspect is protection against practices which diminish the members' expectations to a fair and just benefit, including protection against the risk of inflation.

Safeguards and guarantees are built into all the national regulatory frameworks as well as in the specific rules that plan sponsors draft when establishing a pension fund. In certain countries ordinary legislation (civil or commercial law) contains provisions enabling beneficiaries of pension arrangements to claim their rights in cases, for instance, of misconduct or violation of specific obligations by those responsible for managing the pension assets.

In the following sections, national details are provided only in respect of four countries: Germany, Ireland, the Netherlands and the United Kingdom. These countries represent different typical patterns of protection of members' rights. A full 12 country survey would have required a separate study. Before examining the country information, it will be recalled that there is no legal substitute for honesty, integrity and goodwill. Fraud cannot be prevented with absolute certainty, but legal safeguards and enforcement of appropriate sanctions can reduce their number and alleviate their damaging consequences.

GERMANY

The legal framework for protection of pension rights is essentially found in labour legislation. Safeguards have also been put in place by specific supervisory bodies. Labour court jurisprudence is equally important; its main principles have been consolidated in the act on the improvement of occupational pensions *(Gesetz zur Verbesserung der betrieblichen Altersversorgung, BetrAVG)*.

Duties and responsibilities of management bodies:

Employers are mainly responsible for guaranteeing that pension promises are kept. There are no special duties or responsibilities imposed on them, other than to respect the financial safeguards described below and to consult with trade unions and work councils as necessary (see earlier in this chapter). Authorisation of insurance carriers may be refused if managers are not reliable.

Financial safeguards:

Financial safeguards against insolvency depend on the type of arrangement that the employer has made to finance the pension promise. Legal insolvency coverage applies to any kind of pension promise with a direct or indirect liability on the sponsoring company. Under book-reserving and support funds, therefore, protection for employees is secured using compulsory insolvency insurance provided by a single carrier, the *PSV (Pensions-Sicherungs-Verein)*. Any assets held by employers in respect of these kind of pension promises are not subject to any kind of supervision from the authorities. The existence of insolvency insurance means that members' pension rights can be secured whilst allowing full self-investment of the money set aside to meet these pension promises.

In contrast, the assets built up in *Pensionskassen* and under direct insurance represent the security against employer insolvency and are therefore subject to the stringent supervising requirements of the insurance supervisor in Berlin (the *Bundesaufsichtsamt für das Versicherungswesen - BAV*). Accordingly, *Pensionskassen* and direct insurance contracts do not fall under the coverage of compulsory insolvency insurance. Direct insurance contracts are, however, affected under very special circumstances: where rights are non-irrevocable rights and where the employer has borrowed on the policy or the policy has been surrendered to a third party. These are in fact very rare cases.

Table 21:
Germany: Compulsory insolvency insurance

Number of *PSV* members (employers)	37,758
Contribution rate, proportionate to the total volume of benefits insured	0.08%
Number of pensioners drawing *PSV* benefits	2,939,182
Number of employees with vested rights insured with *PSV*	4,259,508
Number of insolvency claims in 1992	185
Cost of 1992 claims	DM 140 mio.
Total *PSV* expenditure	DM 525 mio.

The statutory carrier of insolvency coverage is the *Pensions-Sicherungs-Verein (PSV)* ('pension guarantee association'), having the legal form of a mutual insurance association *(Versi-*

cherungsverein auf Gegenseitigkeit, VVaG). The *PSV* was founded by associations of employers, of industries and of life insurance companies. The *PSV*'s constitution very much reflects its origins and the threats to the book-reserving system which prompted its creation.[14]

The act on the improvement of occupational pensions explicitly defines the circumstances under which the *PSV* has to assume a liability. The main circumstances are as follows. In the event of an employer going into receivership or becoming bankrupt, the *PSV* takes the place of all the beneficiaries in petitioning the administrators/courts as a creditor of the company. Another important situation is the reduction or termination of benefits due to the poor financial condition of the employer company, provided this has been approved by a decision of a court of law. In the case where the *PSV* deems the reduction or termination of benefits permissible, no court decision is required.

The *PSV* takes out annuity contracts with a consortium of insurers in order to 'buy-out' the benefits of the former employees of the company in question. The *PSV* charges a levy to all employers who use a book-reserve or support fund financing method so as to meet the annual shortfall between income obtained from bankruptcy proceeds and the cost of purchasing the relevant annuity contracts. This levy (or 'insolvency insurance premium') is expressed as a percentage of the liabilities of each employer when these liabilities are calculated on a standard, specified actuarial basis. In case of book-reserving, the premium basis is the total book-reserve allowed for tax purposes in respect (only) of already vested benefits and pensions in payment.

Insolvency coverage is compulsory for every company and any kind of benefit concerned. This has been considered of particular importance to avoid negative selection, thus to allow its carrier to operate satisfactorily.

As previously pointed out, legal insolvency insurance is intended to cover pensions in payment and preserved future benefit entitlements (i.e. the legal vesting terms must be fulfilled). Thus insolvency insurance only covers the minimum, non-escalating leaving service benefit that must be provided according to German law. Insolvency coverage does not only apply to old age and post retirement benefits but also to pre-retirement benefits such as disability, early retirement, death in service, lump sum payments and certain kinds of prescribed salary related benefits. Benefits which are regarded as salary-in-kind are not covered, e.g. so-called *'Vorruhestandsleistungen'*.

The upper limit of benefits covered amounts to three times the social security contribution ceiling (1993 = DM 259,200). This limit is rarely attained. The carrier of legal insolvency coverage has to make pension increases in line with inflation only if explicitly promised by the plan. The basic data about insolvency insurance in 1992 are shown in Table 21.

Another aspect of the protection of members' rights relates to the rules applied in the event of company mergers and acquisitions. These rules are:

- that the liability arising from book-reserves is transferred to the new company owner (both the plan and the liabilities);
- pension funds are not automatically transferable to the new company owner. Funds may continue to operate if the responsible parties so decide;
- insurance contracts can be continued by the new owner or transferred to another insurance carrier;
- support funds are not transferable by law to the new owner, but may be transferred on a contractual basis.

In connection with plan termination the prevailing rules are that:

- an employer may at any time decide to close the plan to new entrants;
- acquired rights (including accrued rights in respect of past service) must be guaranteed, while prospective accruals can be altered if sound reasons can be put forward;
- vested rights of current pensioners and of deferred pensioners must be guaranteed;
- pension funds and support funds remain in existence, if necessary, to guarantee the payment of benefits;
- insurance contracts generate a direct relationship between the insurance carrier and the employee, who holds the right to the benefits stipulated by the policy.

Indexation:

Benefits in course of payment must be adjusted for inflation at the discretion of the employer, at least every three years, provided the financial situation of the enterprise is sound. Partial inflation proofing is acceptable if resources are insufficient. Retrospective adjustments are to be made as soon as the financial situation improves.

Disclosure of information:

Works councils with co-determination rights have access to full information about the nature and status of the pension arrangement with which they are involved. As far as members' information is concerned the legal requirement is that the employee must have the right to see the pension plan document outlining the benefits, and that vested terminated employees have the right to be informed about their vested retirement benefits. Information is usually provided to members by handing out the pension rules, an explanatory booklet or the insurance contract. Members of pension funds and support funds are normally given information concerning the financial status of the fund. It is not normal practice to provide information to members concerning the level of any book-reserves.

Supervision:

Book-reserve arrangements and support funds are supervised by the Ministry of Finance, which can remove tax advantages if fiscal legislation is infringed. Pension funds and insurance contracts are supervised by the insurance supervision authority *(BAV)*. Authorisation can be withdrawn where there is a violation of the rules.

IRELAND

To qualify for tax approval and come within the scope of the Pensions Act, funded schemes must be set up as irrevocable trusts. The nature of trusts and their administration in Ireland has already been described in an earlier section of this chapter (*Establishment procedures and institutions involved*). There are three essential features of trusts that are of particular importance in relation to protection of pension rights.

- the trust fund must be separate from the employer's business and its assets may not be made available to the employer's creditors;
- a trust deed and rules, with which trustees must comply, sets down how the scheme is to be administered and members' entitlements awarded;
- trustees do not have any right to benefit from the fund but have a duty to act in the best interests of the main beneficiaries - the active members (current employees), the deferred members (early leavers), current pensioners and those categories of dependants for whom provision is made under the trust deed and rules.

Pension scheme trustees are subject to legal obligations set down in trust law and associated case-law, and may be sued under civil law for fraud or other breaches of trust. However, this legal framework on its own does not provide adequate protection of pension rights. There are no specific requirements to provide comprehensive and clear information to members as to how their scheme is being administered, its financial viability and on their own personal entitlements. There would normally be substantial costs and delays involved in suing trustees for a breach of trust. In addition, even where such legal action succeeds, trustees may not have sufficient assets against which a decree for damages could be executed.

Because of the deficiencies in the legal framework for the protection of pension rights under trust law, the Pensions Act was introduced in 1990 to complement the provisions of trust law and remedy its shortcomings. This Act provides that trustees have the main responsibility for administering schemes and complying with the Act's other requirements, and in this way is designed to achieve a proper balance between ensuring that pension rights are adequately safeguarded and avoiding over-regulation.

Duties and responsibilities of trustees:

The specific duties and responsibilities of the trustees of occupational pension schemes are laid down in section 59 of the Pensions Act, and these are:

- to ensure, insofar as is reasonable, that contributions payable by the employer and members of the scheme, where appropriate, are received;
- to provide for the proper investment of the resources of the scheme in accordance with the rules of the scheme;
- where appropriate, to make arrangements for the payment of the benefits as provided for under the rules of the scheme as they become due;
- to ensure that proper membership and financial records are kept;
- to arrange for members' rights to be secured if a decision is taken to wind up a scheme, and to ensure that the wind up is completed without undue delay; and
- to comply with the other provisions of the Pensions Act.

This has the effect of providing that trustees are now accountable for carrying out these duties not just to members under trust law, but also to the Pensions Board under the Act (see below).

The Pensions Act also requires trustees to be specifically accountable to members by:

- giving members the right to participate in the selection of a proportion of the trustees (described in the previous section on *Establishment procedures and institutions involved*); and
- requiring trustees to disclose specific information to members on the scheme, its ongoing administration and financial viability and on members' personal entitlements.

Disclosure of information:

Trustees are required to disclose to the members a comprehensive range of information about the scheme. Basic information about the scheme must be made available covering such matters as eligibility, conditions of membership, calculation of contributions, type and level of benefits and conditions for entitlement, and the addresses for enquiries about the scheme. This information is normally made available in a scheme booklet and spouses of members and employees who will become eligible to join the scheme are also entitled to receive the information.

Members are entitled to receive full information on their own personal entitlements on request at least once every 12 months. They are also automatically entitled to receive such information on leaving the employment, on retirement, on the death of a member or a beneficiary and in the eventuality of the scheme being wound up.

Trustees are required to account for the administration of the scheme by making a wide range of documents available, including the trust deed and rules and an annual report.

The annual report must be made available not later than 9 months after the end of the scheme year. In the report, trustees must account for such matters as the collection of the contributions due, the investment of the scheme's resources, payment of benefits and, if it is a defined benefit scheme, the actuarial valuation of the scheme's assets and liabilities. They must also disclose whether more than 5% of the scheme's assets are invested in the employer's business or in any one shareholding or property.

These requirements not alone enable members and their trade unions to monitor how their scheme is being administered, but the requirements to disclose can also deter trustees from taking actions that might place members' pension rights in jeopardy.

Financial safeguards:

The other major protection provided for in the Pensions Act involves a requirement for defined benefit schemes to comply with a funding standard. The aim of this is to ensure that the scheme has sufficient assets to meet accrued liabilities, as set down in the Act, should the scheme have to be wound up. The future pensions of those already receiving pensions must be fully secured straightaway, as well as the preserved rights in respect of service from 1 January 1991 of those yet to retire. Other pre-1991 rights must be 100% funded by 1 January 2001.

To comply with the standard, trustees must arrange to have an actuarial valuation of the scheme's assets and liabilities carried out and an actuarial funding certificate prepared by a qualified actuary and submitted to the Pensions Board at least every three and a half years.

Where the certificate specifies that the scheme does not satisfy the funding standard, a funding proposal must be prepared in consultation with the employer and the actuary, which is designed to ensure that the scheme will satisfy the standard by the time the next certificate is due. This proposal must be submitted to the Pensions Board.

If it is not possible to make a funding proposal, the trustees may have to arrange to reduce the benefits due to members currently in employment to which the scheme applies (active members) and notify these members of the position. If trustees fail to take this action the Pensions Board may intervene and direct them to do so.

Any self-investment or concentration of investment in excess of a prescribed percentage of the resources of the scheme cannot be taken into account for the purposes of complying with the funding standard.

The measures described are designed to ensure that schemes are administered in such a way that there are sufficient assets in the scheme at all times to meet accrued liabilities. If there is a shortfall as a result of, for instance, poor investment performance or a failure to pay the full contributions due, then it either must be made up by increased contributions from the employer and, if appropriate, active members, or the pension entitlements of active members may have to be reduced.

As there is in general no legal requirement on employers to establish and continue with occupational pension schemes, it is open to employers at any stage to reduce the level of pension entitlements promised in respect of future service or to discontinue the scheme. The same applies in the case of schemes where the company sponsoring the scheme is merged with or is taken over by another company. The fact that the trust fund must be separate from the employer's business and that defined benefit schemes must comply with a funding standard should normally ensure that accrued entitlements are protected. However, it is a matter for the merged company or the new company in a takeover situation whether to continue with the scheme in its existing form or make different pension provision or no pension provision in respect of future service.

The provision made for the protection of accrued entitlements in the event of a scheme winding up is also designed to deal with situations where the employer becomes insolvent. In these situations the scheme invariably has to be wound up. In defined contribution schemes, the contributions are allocated to specific members and, if the scheme is being wound up, the member's entitlement is directly linked to the value of the contributions linked to him or her.

Contributions are normally not allocated among individual members in defined benefit schemes. The member's entitlement is determined instead by the scheme rules, and the scheme's assets are allocated on a global basis to provide for entitlements as laid down in the scheme rules. The Pensions Act provides that, notwithstanding the scheme rules, the priorities on winding up of a defined benefit scheme should be pensions currently in payment, preserved benefits in respect of service after 1 January 1991 and additional voluntary contributions after the expenses associated with the winding up of the scheme are met. Current employees, therefore, have the lowest level of protection in the event of a scheme winding up with insufficient assets to meet accrued entitlements.

The Protection of Employees (Employers' Insolvency) Act of 1984 provides for the payment to the pension scheme from the Redundancy and Insolvency Fund of unremitted employee contributions up to a maximum of employee contributions due in the preceding twelve months and any unpaid employer contributions due in respect of the preceding twelve months.

Indexation:

There is no legal requirement to provide for the increase of pensions after award to maintain the purchasing power of pensioners. However, recent surveys show that indexation of pensions in payment is now becoming a feature of a majority of schemes (more information was given in the earlier section on *Design Strategies for Pension Plans*).

Other protections provided for:

The Pensions Act also provides for the preservation of benefits of early leavers, e.g. those changing jobs, which accrue in respect of service after 1 January 1991 (see also the section on *Design strategies for pension plans*) and for the application of the principle of equal treatment for men and women.

Public sector unfunded schemes:

Public sector schemes which are unfunded are established under legislation enacted by Parliament, with the detailed rules set down in statutory regulations. They are administered by the relevant state authorities under the general supervision of the Department of Finance. Accordingly, legal protection afforded to members' pension rights is similar to that afforded to entitlements under state social security schemes. Most members of these schemes are in fact exempt from full social insurance cover on the grounds that they are members of state backed occupational pension schemes.

Provision is made for increases in pensions in line with increases in the pay of current employees. Benefits are fully preserved in the case of early leavers who have been members of the scheme for at least 5 years. Given the level of statutory protection of members' pension rights under these schemes, the Pensions Act only applies to such schemes in relation to the disclosure of information and equal treatment requirements.

Supervision:

The Pensions Board was established under the terms of the Act to monitor and supervise its implementation and pension matters generally. Pension schemes must register with the Board within 12 months of being established, and most schemes are required to pay annual fees to the Board which finance its administrative expenses. The Board's main functions are:

- to issue guidelines to trustees on their duties and responsibilities, and codes of practice on specific aspects of their responsibilities;
- to encourage the provision of appropriate training for the trustees of schemes and to advise the Minister for Social Welfare on standards for trustees;
- to provide guidance for scheme administrators on compliance with the requirements of the Act in relation to disclosure of information, preservation of benefits, the funding standard and equal treatment;
- to ensure that scheme members are fully informed of their rights under the Act and, in particular, their rights to information on how their scheme is being administered and on their own individual entitlements;
- to investigate complaints concerning possible non-compliance with the provisions of the Act and, if necessary, to take legal proceedings for breaches of the Act.

Persons convicted of an offence under the Pensions Act are subject to heavy fines and/or two years imprisonment. The Board also has the power to request courts to order the removal of trustees, if it is considered that such action is necessary in the interests of members of schemes, and, in certain circumstances, to appoint new trustees.

NETHERLANDS

The legal framework for protection of pension rights is found in (i) the Pension and Savings Fund Act *(PSW)*, (ii) legislation which has empowered the state to make compulsory an industry-wide fund based on collective agreements, (iii) collective agreements and individual fund rules and (iv) the powers entrusted to the supervisory bodies, such as the insurance chamber.

Duties and responsibilities of management bodies

There are no special duties or responsibilities imposed on the managers of pension arrangements, appointed or elected according to the procedures described earlier, other than in respect of the financial safeguards and the disclosure practices described below.

Financial safeguards

The Pension and Savings Fund Act (*PSW*) requires that funds intended for pensions are separated from the company by being paid into a pension fund or an insurance company and cannot be claimed by that company or its creditors. It also requires that at all times assets (including insurance arrangements) together with future contributions can be expected to be sufficient to meet all liabilities. Within this general requirement, there is scope for flexibility in designing the funding plan to be followed to meet the overall long-term objective. Pension funds must be subject to actuarial control and an actuarial valuation must be made at least every five years and submitted to the insurance chamber. Where the arrangement is with an insurance company, contributions are paid at the rates agreed between the arrangement sponsor and the insurance company; the insurance company's business as a whole being subject to supervision by the insurance chamber.

If assets are not sufficient to cover past-service rights, the Dutch courts have decided that non-payment of contributions is a property debt and that in the event of the bankruptcy of the employer, these contributions must be paid prior to paying the claims of preferential and ordinary creditors. With regard to future service accruals, the 'Unemployment Act' requires that the relevant trade associations will take over the insolvent employer's liability for pension contributions for a maximum period of one year.

If there is a company takeover by means of a transfer of assets, the acquiring employer is not bound to continue to honour the pension promises made by the first employer. Generally the employee will terminate participation in the pension scheme of the transferring employer and the minimum entitlement will be to the benefits that would have been available had the employee left service. Whether there will be a pension provision for the employee with the new employer depends on whether that employer makes a pension promise, or falls within the scope of compulsory participation in an industry-wide pension fund. If the new employer operates a pension arrangement, transfer of pension rights from the previous arrangement is possible if the pension funds or insurance companies concerned are prepared to cooperate. If the employee has already been a member of a compulsory industry-wide pension fund with the transferring employer, this membership will generally continue after the transfer of the company.

In the event of the transfer of shares, an employee's participation in a pension scheme is unaffected as a transfer of shares changes nothing in the contract of employment. However, this may not always be the case. For example, in the case of a company being detached from a larger industrial corporation, its employees may no longer be able to participate in the corporation's pension scheme. As is the case where there is a transfer of assets, their minimum entitlement will be to the benefits that would have been available had they left service in normal circumstances.

Indexation

There is no requirement that pensions must be increased once in payment. However, it is common practice for increases to be made to take account of increases in the cost of living. In this case, the same level of increases must be applied to the benefits of those who have left service but where the pension has not yet come into payment.

Information and disclosure

Under the present rules either the industry-wide pension fund, or a company fund, must ensure that employees can have access to the statutes and pension regulations. At the beginning of May 1993, a bill was presented to Parliament aimed at giving all those in active employment an annual summary and balance of accrued pension rights.

Supervision

The supervision of pension funds and insurance companies in the Netherlands is the responsibility of the insurance chamber *(Verzekeringskamer)*.

Pension funds must register with the insurance chamber within three months of their establishment. Amendments to statutes and pension regulations must also be communicated to the insurance chamber. In addition, pension funds must submit annual reports, inspected by a chartered accountant, to the chamber, detailing the financial state of the fund.

The insurance chamber has the following powers with regard to pension funds:

(a) to request and obtain information, summon witnesses and experts, consult records;

(b) to make observations, request changes and bring such matters to public awareness;

(c) the insurance chamber can submit a request through the Amsterdam court of appeal that an administrator be appointed to a pension fund if:
- there is evidence of mismanagement of the funds;
- the board of the fund fails to provide information;
- the management of the fund is found wanting.

The supervision of insurance companies in the Netherlands is laid down in the 'Insurance Industry Supervision Act', which has been adjusted in line with the life and non-life directives of the Council of the EU.

UNITED KINGDOM

The main protection for pension scheme members is provided by the trust fund and the role of the trustees. The trust fund has to be maintained separately from the assets of the sponsoring employer and money can only be lawfully returned to the employer in special circumstances. This applies to schemes in both the private and public sectors, apart from a few public service schemes which are established under their own regulations and do not require Inland Revenue approval (e.g. the civil service, the armed forces, teachers and health service workers).

Duties and responsibilities of trustees

Once trustees have been appointed they are not expected to behave as representatives of any particular sectional interest. It is their responsibility to administer the trust deed in accordance with the rules of the scheme. The responsibility of trustees is laid down in general trust law, which is of ancient origin and does not provide specific principles relating to pension scheme issues. The trustees have a personal and fiduciary responsibility to invest the scheme monies in a prudent way, in compliance with the trust deed and rules. The trustees can delegate the tasks of administration and investment to employed staff or to external experts, but they retain ultimate responsibility for the sound management of the affairs of the pension scheme.

Financial safeguards

In principle, the assets of the trust fund should be maintained at a level that is at least sufficient to ensure that accrued liabilities can be met should the arrangement be discontinued. If the assets should at any time be shown by an actuarial valuation to be insufficient to meet the accrued liabilities, it is the responsibility of the trustees to seek to rectify the situation, usually by means of additional contributions from the employer over a future period. Employee contributions may also be increased in some cases. If the employer is unable or unwilling to increase contributions, it may be necessary for the trustees to wind up the scheme (or apply to the Court for directions) and secure benefits for past service. The law then requires the employer to meet any deficit.

A full actuarial valuation must be carried out at least every 3.1/2 years. The actuary must comment on the funding position in relation to accrued rights had the scheme been wound up on the valuation date, and must also advise on the contributions necessary in the future to support the benefits. A surplus can only be removed from a continuing scheme with the approval of the Inland Revenue and, in the case of some contracted-out schemes, the Occupational Pensions Board.

In the event of the insolvency of the employer, or a decision by the employer to cease contributing to the scheme, it is the responsibility of the trustees to ensure that the assets of the trust fund are applied to meet the accrued liabilities, insofar as is possible, in accordance with the rules of the scheme. The assets of the scheme cannot be called upon by the liquidator of the employer's business.

If there is a deficiency in the assets of the scheme when they are applied to meet the discontinuance liabilities, the balance is treated as a debt on the employer. In the case of insolvency of the employer, this debt will rank with other creditors in the liquidation. If the debt is not paid, the trustees must reduce the benefits payable. This will be done in accordance with the priorities laid down in the trust deed and rules.

There are no specific provisions in the law to safeguard the interests of scheme members in the case of mergers or acquisitions of companies sponsoring pension schemes. However, the trustees of the scheme or schemes involved must comply with the provisions of the relevant trust deeds and rules, which, under Inland Revenue requirements, must provide for this situation. The provisions depend on the terms required by the employer when establishing the scheme (subject to any subsequent alteration agreed with the trustees). Members will by law receive at least benefits appropriate to leaving service. Invariably there will be a power (but not an obligation) to transfer assets to a purchaser's scheme or in some other way to provide continuity of pensionable service. The extent of any unfunded liability, or any surplus, in the pension scheme(s) will often be (or should be) a major consideration in negotiating the terms of any merger or acquisition. An unfunded liability is a debt on the employer, and on any successor employer.

Indexation

The rules often provide for pensions in payment to be increased by a fixed percentage each year (say 3% or 5%). Trustees have a discretion to award additional increments as the finances of the pension fund permit, with a view to maintaining more closely the real value of the pension at the time of award. Most public sector pension schemes currently provide automatic or near-automatic indexation of pensions in line with movements in the retail price index. (See also the section on *Design strategies for pension plans*, above.)

Disclosure to scheme members

Trustees are required to make regular disclosure of certain prescribed documented information to scheme members. It is considered sufficient for some details to be available on request, for example the trust deed and rules, but members must receive a written notification that the annual report and accounts (which include an actuarial certificate) are available. A large volume of basic information about the scheme must actually be supplied to members. This obligation can be met by issuing a scheme booklet, together with an update in the annual report. The information includes:

- tax approval and contracted-out status;
- eligibility and conditions for membership;
- how contributions are calculated;
- whether contributions have been paid in accordance with the rules and the recommendations of the actuary;
- benefit information;
- rights of early leavers;
- names of trustees;
- investment policy;
- extent of any employer-related investments;
- review of financial development of the scheme.

A statement by the actuary must be included in the annual report, referring to the latest valuation and the recommended rates of contribution. A full copy of the actuary's valuation report is available to a member on request.

Supervision

There is no general system of supervision of pension schemes in the United Kingdom, although, as mentioned above, certain requirements are laid down regarding authorised investment managers, actuarial valuations and the disclosure of information to members. There are numerous statutory provisions for the protection of members but their enforcement relies upon the integrity of trustees and the legal rights of members in the Courts (or before the

Pensions Ombudsman). In view of the fiscal advantages for an approved pension fund, the Inland Revenue exercises strict control on the compliance by pension funds with approved fiscal and financial requirements.

Schemes which are contracted-out of the state earnings-related additional pension are monitored by the Occupational Pensions Board, an independent statutory body, to ensure that they have, and are likely to continue to have, adequate resources to meet accrued liabilities in respect of guaranteed minimum pensions. The actuary has to provide a regular certificate to this effect and the supervision relies heavily on this certification process. However, no specific funding standards are laid down.

The 1993 report of the Pension Law Review Committee (the 'Goode Committee'*)*

On 30 September 1993 the Report of the Pension Law Review Committee was presented to the Secretary of State for Social Security. The report contained 218 recommendations, covering a broad range of issues in occupational pension provision in the United Kingdom, having particular regard to the importance of strengthening the security of the rights of members of pension schemes. The report recommends the creation of a post of 'Pensions Regulator' with adequate staffing to supervise the operation of occupational pension funds and with powers to intervene in their affairs in order to safeguard the interests of members.

It is recommended that the trustees of each scheme should appoint an 'appointed scheme actuary' with responsibility for monitoring the financial affairs of the scheme, for reporting annually on the solvency status of the scheme, and for advising the trustees on the level of funding necessary to ensure a satisfactory continuing financial condition.

Pension schemes would be required to meet a minimum solvency requirement based on 100% of the cash equivalents in respect of active members and former members with preserved benefits, together with 100% of the cost of purchasing annuities to buy out the liabilities in respect of pensions in payment and contingent pensions payable to the dependants of such pensioners. Cash equivalents are already used in the context of transfers between pension schemes, and represent the present value of the preserved pension and other benefits to which an early leaver would be entitled.

Pension schemes falling below the minimum solvency standard of 100% of cash equivalents would be required to present a plan to demonstrate how the solvency position was to be restored. Should solvency fall below a 'base level' of 90% of cash equivalents, the Pensions Regulator would require an immediate injection of cash into the scheme or, failing that, consider whether to wind up the scheme and invoke the 'debt on the employer provisions' of the UK pensions legislation.

It is recommended that a compensation scheme should be established to handle the problem of shortfalls in pension scheme assets, restricted however to shortfalls arising from fraud, theft and other misappropriation. The compensation scheme would be funded by means of a post-event levy on all occupational pension schemes which might be covered by the compensation arrangements.

The Committee argues that the scheme auditor and actuary and (ideally) the administrator should not be trustees and that, in schemes with more than fifty active members and pensioners, active members should be entitled to appoint a proportion of the trustees. In money purchase schemes, where the employer's liability is limited, this proportion should be two-thirds, while in other schemes it should be one-third, with a minimum of two trustees in each case. The provision of information for scheme members should be improved, both in content and in clarity and presentation.

No fundamental change is proposed in the basic legal structure of UK pension funds, relying as it does on the ancient precepts of trust law. However, there should be a consolidated Pensions Act, and the Pensions Regulator would be responsible for administering it.

Following receipt of the report of the Pension Law Review Committee, the Government has consulted on the shape of future pensions legislation and is expected to publish a White Paper in June 1994.

CHAPTER 6
PENSION FUNDS, SAVINGS AND INVESTMENT

A growing concern

The technique of funding supplementary pension liabilities is used to varying degrees in all the countries of the EU, with the result that the size of funds available for investment varies greatly from one country to another. Setting aside capital to cover future commitments is a mandatory requirement for pension insurance policies written by life insurance companies. It is also prudent practice for self-administered pension funds relying on sources which may not flow indefinitely, such as firms which, after having undertaken long-term pension commitments may cease to exist because of liquidation, merger, or cessation of activity. Moreover, the security of members' rights, present and future, is enhanced by the existence of matching assets.

It is therefore understandable that governments often only afford a full range of tax relief to occupational pension schemes subject to the condition that the relevant liabilities are adequately funded (Italy, Ireland, Portugal, Spain, the Netherlands, the United Kingdom and others). Funding (or the equivalent term often used: 'pre-funding') is also frequently considered as an important alternative to the pay-as-you-go system in coping with the effects of an ageing population on the financing of old-age pensions. The aim of this alternative is to reduce the burden on future generations of the contributions or taxes needed for financing pensions.

The economic and financial implications of funded supplementary pension arrangements have attracted increasing attention in Member States and from the European Commission for a number of reasons. First, the large accumulation of assets for pension purposes can have an effect on savings patterns. Secondly, because the investment of these assets has an impact on the volume and behaviour of capital markets. Third, because the yield of pension fund investments regulates both the long-term level of the pension contributions required and the amount of retirement income that fund members receive. Finally, some Member States have highly developed financial markets, attracting capital from abroad, while others do not, and the latter hope to increase their domestic market by developing funded second-tier schemes.

The theoretical treatment of the relationship between pension funds, savings and investment can be found in specialized economic literature and studies. However, views expressed by economists often diverge, and a distinction needs to be made between theory and contemporary practice. The present chapter focuses on observed national policies and the practical results achieved. Hereafter, the term 'pension fund' is used, in short, to refer generally to all forms of voluntary or compulsory supplementary pension arrangements (second tier) which fund all or part of their liabilities.

The size of pension funds

The financial importance of pension funds can be measured by the volume of its flows (receipts, expenditure), or by the stock of assets held at any given time. This second measure is more revealing since it provides an indication of the size of resources held to match future liabilities and of the investment potential in the hands of pension fund managers. Available aggregate country data on assets held is not always comparable because of the difficulty of separating supplementary pension portfolios within the balance sheet of life insurance companies. Criteria for valuing the portfolio may also vary from country to country. The following information is the last reported by individual Member States.

BELGIUM

Table 22:
BELGIUM
Value of assets held to cover supplementary pension liabilities (million Belgian francs, 1986-1991)

Categories:	1986	1988	1990	1991
Group insurance	308,378	396,804	467,557	503,442
Pension Funds	160,000	180,000	192,000	206,000
Total	468,378	576,804	659,557	709,442

Source: Neyt (1993), *Les trois piliers des pensions*, Document de travail pour la Table Ronde 'Pensions'.

DENMARK

Table 23:
DENMARK
Value of assets held to cover supplementary pension liabilities, 1982-1991 (million Kroner)

Year	Industry-wide funds	Company funds	Insurance companies
1982	25,800	13,400	74,400
1983	37,800	13,400	85,600
1984	45,700	16,300	105,800
1985	53,500	18,700	125,200
1986	61,700	19,500	142,800
1987	68,400	21,100	156,800
1988	77,400	22,000	174,200
1989	86,900	22,500	184,600
1990	95,400	23,600	201,100
1991	104,400	24,800	222,000

Source: *Finanstilsynet*
The above figures do not include personal pension plans purchased by individuals from banks. However, the figures for insurance companies also include pension plans taken out by individuals.

FRANCE

Répartition schemes, such as *AGIRC* and *ARRCO*, hold assets only as contingency reserves since they do not fund their liabilities. As their coverage is vast, however, their contingency reserves represent substantial asset holdings: 140 billion French francs in 1991. The handicraft pension fund *CANCAVA* showed assets worth 16.8 billion francs to cover compulsory supplementary pension liabilities. Reserves have also been accumulated by funded pension schemes of large industrial companies (about FF 15 billion), those of the banking and agricultural service sector (about FF 26 billion), the public sector schemes *PREFON* and *CREF* (about FF 21 billion); the pharmacists' fund and other minor funded schemes account for an estimated asset volume of 75 billion francs.

Company savings plans (*PEE*) had an aggregate asset value of 90 billion French francs at the end of 1992. A few tens of billion French francs were in company frozen benefit accounts, although not necessarily matching retirement benefits.

GERMANY

Only very broad estimates of the amount of funded pension liabilities are available for 1992. A survey carried out in 1991 of the 40 largest *Pensionskassen*, covering 2,335,000 employees, showed that the total volume of assets invested amounted to DM 75.8 billion. The amount of book reserves has been growing at a fast pace: in 1986 these had been estimated by the *Bundesbank* at DM 168.4 billion.

GREECE

Reliable data is available for assets held by the compulsory supplementary pension funds. However, it is not possible to identify the amount of reserves held by insurance companies in respect of group (or personal) insurance contracts. The overall amount of assets of the compulsory funds was Drs 398,100 million in 1989.

IRELAND

The figures in Table 24 show that the volume of assets grew at an annual compound rate of nearly 30 per cent in the 14 year period under review. According to surveys carried out by the Irish Association of Pension Funds[15], the growth of the value of assets continued after 1989, rising to IR£ 9,300 million at the end of 1991 and to IR£ 9,700 million at the end of 1992.

Table 24:
IRELAND: Value of assets held to cover supplementary pension liabilities, 1975 - 1989
(IR£ million, end of year)

Year:	Value of assets:
1975	210
1980	882
1983	2,249
1984	2,513
1986	4,000
1987	5,527
1988	6,690
1989	7,940

Source: *Private Pensions in OECD Countries - Ireland* (Hughes: 1994, see note 10)

ITALY

The most recent available figures from the databank of the *Centro Europa Ricerche (CER)* show a total value of assets, held by 1078 pension funds, amounting to 11,250 billion lire in 1991.

NETHERLANDS

Table 25: NETHERLANDS: Value of assets held to cover supplementary pension liabilities in the private sector, 1989-1992 (million Guilders)			
Year:	Single employer funds	Industry-wide funds	Total
1989	102,256	98,057	200,313
1990	104,209	103,421	207,630
1991	111,407	111,496	222,903
1992	119,917	120,568	240,485*

Source: *Social-economische maandstatistiek (CBS)* 93/4
* An amount of 736 million should be deducted from this figure to obtain the amount of assets net of non-pension financial liabilities.

The most recent (1992) estimates of the assets held by the pension funds in the public sector were:

Fund:	Amount of assets:
Civil Service (*ABP*)	Dfl 177,044 million
Railways	Dfl 10,031 million

PORTUGAL

Table 26: PORTUGAL: Value of assets held to cover supplementary pension liabilities, 1990-92 (million Escudos)			
Year:	Closed Funds	Open Funds	Total
1990	167,556	3,176	170,732
1991	282,866	7,757	290,623
1992	436,730	15,873	452,603

Table 27:
SPAIN:
Value of assets held to cover supplementary pension liabilities of qualified plans under the 1987 Pensions Law*
(million Pesetas)

Year:	Employment related plans **	Plans for members of associations	Total
1990	348,839	15,898	364,737
1991	503,332	22,804	526,136
1992	628,402	29,950	658,352

Source: INVERCO

* Excluding individual plans which had accumulated by the end of 1992 assets valued at 424,619 million Pesetas.

** The amount of assets shown does not reflect the full volume of liabilities, since employers have until 1999 to transfer gradually to the pension fund - from the company balance sheet - the assets backing past service liabilities recognised, but unfunded, when the 1987 Law came into effect.

Table 28:
SPAIN:
Value of assets held to cover supplementary pension liabilities of Mutual Benefit Societies 1987-1992 (million Pesetas)

Year:	Value of assets:
1987	225,437
1988	270,052
1989	344,877
1990	580,955
1991	674,695
1992	850,000

UNITED KINGDOM

Information is available about pension fund assets, while data for pension contracts handled directly by insurance companies is not readily identifiable.

Table 29: UNITED KINGDOM: Market value of assets held to cover supplementary pension liabilities of pension funds in the public and private sector 1984-1991 (£ million, end of the year)

Year:	Net asset value:
1984	139,290
1985	168,059
1986	211,220
1987	227,551
1988*	267,446
1989*	338,950
1990*	302,714
1991*	343,667

* Figures from 1988 are subject to revision

Table 30:
Summary of recent estimates of the value of assets held to cover supplementary pension liabilities in the EU (national currency and ECU equivalent)

Country:	Type of institution holding assets:	Year:	Estimates of assets held (million): nat. currency:	ECU:
BELGIUM	- group insurance	1991	BF 503,442	11,923
	- pension funds	1991	BF 206,000	4,879
DENMARK	- life insurance	1991	Dkr 222,000	28,071
	- personal plans in banks	1991	Dkr 76,400	9,660
	- pension funds	1991	Dkr 129,200	16,337
FRANCE	- *AGIRC/ARRCO*	1991	Fr 140,000	20,077
	- other funds	1992	Fr 168,800	24,648
GERMANY	- book-reserves	1992	DM 250,000	123,743
	- *Pensionskassen*	1992	DM 95,000	47,022
	- other	1992	DM 88,000	43,557
GREECE	- pension funds	1989	Drs 398,100	2,226
IRELAND	- pension funds	1992	Ir£ 9,700	12,751
ITALY	- pension funds	1991	Lit 11,250,000	7,337
NETHERLANDS	- private sector funds	1992	Dfl 240,485	105,716
	- public sector	1992	Dfl 187,075	82,237
PORTUGAL	- pension funds	1992	Esc 452,000	2,587
		VI/1993	Esc 556,400	3,185
SPAIN	- pension funds	1992	Pst 658,352	4,968
	- individual plans	1992	Pst 424,619	3,204
	- Mutual Associations	1992	Pst 850,000	6,414
UNITED KINGDOM		1991	£ 344,000	490,719

Notes:

Germany:	'Other' assets include those of support funds and direct insurance.
Greece:	Compulsory auxiliary funds only.
Luxembourg:	Pension assets do not represent a significant volume.
United Kingdom:	Total net assets of all UK insurance companies were £277,000 million in 1990; this figure includes life insurance, general insurance and pension business.

The available data shown above provides a basis for making a broad comparison of the value of assets held to cover supplementary pension liabilities in Member States. The comparisons should be interpreted with care, taking into account the reservation made earlier as to the quality and comprehensiveness of the data. The purpose of the comparison is to demonstrate that there are wide differences in Europe as to the financial dimension acquired to date by supplementary pension funds.

UNITED KINGDOM, 1991 (million ECU)	
(a) Assets	490,719
(b) GDP	816,535
(c) Stock Market capitalisation	2,725,700
% (a)/(b)	60.1
% (b)/(c)	18.0

NETHERLANDS, 1992 (million ECU)	
(a) Assets	187,953
(b) GDP	247,589
(c) Stock market capitalisation	169,900
% (a)/(b)	75.9
% (b)/(c)	110.6

GERMANY, 1992 (million ECU)	
(a) Assets, incl. book-reserves	214,322
(b) Assets, excl. book-reserves	90,579
(c) GDP	1,383,050
% (a)/(b), incl. book-reserves	15.5
% (b)/(c), excl. book-reserves	6.6

For the countries with the largest accumulation of assets (or reserves), a comparison has been made with relevant macro-economic aggregates. The aggregate (c) in the table for the United Kingdom excludes a small volume of non-UK securities (Irish, etc.). It should be borne in mind that if account could be taken of the volume of assets matching insurance pension business (groups contracts, personal pensions) the ratios above would be significantly increased.[16]

As far as Germany is concerned, comparisons can be made including book-reserves (i.e. the earmarked pension assets remaining in the employer's balance-sheet, that is the self-financing assets) or excluding them.

Comparable figures about stock market capitalization are not available for Germany as a whole. As a matter of broad reference, however, it can be recalled that in 1988 the total market capitalization of domestic shares in Frankfurt was ECU 215,290 million. The data for Denmark and Ireland is equally interesting. In Ireland, pension fund assets represent 25% of national savings.

IRELAND, 1992 (million ECU)	
(a) Assets	12,751
(b) GDP	33,039
% (a)/(b)	38.6

DENMARK, 1991 (million ECU)	
(a) Assets	54,068
(b) GDP	105,370
(c) Stock market capitalisation	40,120
% (a)/(b)	51.3
% (b)/(c)	134.8

As mentioned above, the empirical evidence of the net effect on national savings of funded supplementary pensions is scarce. However, the fact remains that personal net savings of households in life insurance companies and pension funds may represent a very significant proportion of net national savings. In 1991 the proportion was 56 per cent of national savings in the Netherlands and 30 per cent of national savings in the United Kingdom.

The total amount of assets held by pension funds normally covers two types of liabilities: the present value of pension rights already acquired by existing pensioners and the present value of pension rights in course of acquisition by employees who will retire in future years.

If separate figures could be obtained for the two groups of liabilities, and of the corresponding number of pensioners and of prospective beneficiaries, it might be possible to calculate other indicators such as (i) the average asset holdings per active fund member and (ii) the average asset holdings per pensioner. Such indicators would throw light on the magnitude of pension provision actually available at any given time for specific groups of individuals through supplementary arrangements. The macro-economic indicators discussed above reflect, on the contrary, the relevance of such arrangements for the economy and for the financial market rather than for individuals.

The behaviour of pension funds in financial markets

Accumulating capital against future pension liabilities is prudent and reasonable behaviour but - it has often been said - it is not beneficial *per se* to the national economy. What ultimately is of importance to the economy is the use made of the capital, that is its investment in specific real assets.

The behaviour of fund managers as institutional investors is conditioned by several factors: those which determine the supply of financial and non-financial assets, those which may restrict their demand, and finally the structure and cost of financial services available on the market.

Without entering into detail, it will be recalled that the supply of capital depends mainly on: (i) macro-economic factors, such as the level of public debt, aggregate domestic savings, or the rate of industrial investment; (ii) inflation trends, interest rate trends and the profitability of companies which seek finance on the market, and (iii) the institutional, legal and regulatory context having a bearing on investments. All these elements are highly country-specific.

As far as demand is concerned, pension fund managers may be in a privileged position compared to other institutional investors. Pension rights accrue over a long period and forecasts can easily be made for the time when pension payments fall due. Accordingly, pension fund managers can develop long-term investment strategies within which the traditional considerations as to asset risk, yield and liquidity can be accommodated. Naturally, if the regulatory context provides for mandatory investment requirements (limits, etc.) pension fund investment managers are less free to direct as they may wish the demand for assets.

The structure and the cost of the financial services available to pension fund managers is also bound to have an influence on their choices, in particular because insurance companies, banks and investment companies compete for customers. The pattern of performance of the providers of financial services and the fees they charge may change in the future with increased competition and the gradual integration and liberalisation of the European financial markets.

The distribution of the portfolio of assets held by pension funds at any time reflects the interaction of all the factors described above. The pattern of such portfolios in today's Europe varies from country to country for historical and behavioural reasons which may also be the reflection of investment rules and regulations issued, in the public interest, by supervisory authorities. The brief country review which follows highlights the differences observed. Luxembourg has been omitted because of the small volume of assets involved.

BELGIUM

Pension fund investment is regulated by the supervisory authority. Both pension fund and insurance carriers have to invest no less than 15% of their assets in Belgian government securities. Maximum permissible holding of other assets is prescribed:

Investment restrictions	Pension Funds	Insurance companies
	(Maximum permitted as a % of total investment)	
Belgian bonds	85	50
International bonds	85	10
Investment funds	85	5

In 1991, Belgian bonds represented on average 45% of all invested assets by the institutions concerned.

Table 31:
BELGIUM:
Asset Volume by Class
(million Belgian francs)

Type of investment:	Life insurance	Pension funds	Retirement savings*	Total
Fixed yield	732.2	119.8	44.8	896.8
Variable yield	205.8	75.1	38.1	319.0
Other	26.4	10.7	2.3	39.4
Total	964.4	205.6	85.2	1,255.2

Source: *OCA* (Insurance Supervisory Body)
* Retirement savings are plans subscribed by individuals, (normally considered as 'third tier' provision).

DENMARK

The Act on Insurance Business (applicable to industry-wide pension funds and to life assurance companies) and the Act on the Supervision of Pension Funds (applicable to company pension funds) stipulate that at least 60 per cent of the assets which cover pension liabilities shall be invested in:

(a) securities issued by the Danish Government or guaranteed by it;

(b) securities issued by Danish mortgage banks, by the Danish Finance Institute for Municipalities or other Danish financial institutions placed under public supervision;
(c) deposits in banks;
(d) loans (backed by fixed property) not exceeding two thirds of the estimated value of the property at the last fiscal assessment;
(e) assets which must be considered to have the same security as the assets mentioned under (a)-(d) above (this rule is used for foreign assets).

(Rules in the Act on Insurance Business governing the investments are to be modified to comply with the EC Third Life Assurance Directive.)

Similar provisions are found in *ATP* legislation, with the exception that at least 75 per cent of the assets must be placed in assets mentioned under (a)-(e) above. In addition, under the *ATP* scheme an employer has the possibility to borrow an amount not exceeding 50 per cent of his contribution to the *ATP* at current bank loan rates. The results of such policies are shown in the following table.

Table 32:
DENMARK:
***ATP* Asset Volume by Class**
(million Kroner, end of year)

Year	Bonds	Equities	Loans	Property	Other
1983	25,500	2,600	100	100	2,400
1984	29,900	3,200	100	200	2,900
1985	35,200	4,000	100	600	3,100
1986	41,500	5,000	200	1,500	2,500
1987	46,100	6,200	200	1,700	2,500
1988	51,900	7,400	200	2,200	2,700
1989	57,600	8,400	200	2,200	2,800
1990	64,100	10,100	700	2,200	3,300
1991	71,100	11,900	600	2,500	3,200
1992	77,400	13,500	700	2,700	3,500

At least 80 per cent of assets (life assurance companies and industry-wide funds) have to be held in the same currency as the liability. In the case of an EU currency, up to 50 per cent of the liabilities can be covered by assets denominated in ECU. These rules correspond to those of the EU Second Life Directive. Company funds are still obliged to cover 100 per cent of their pension liabilities by assets denominated in the same currency. However, the supervisory authorities have shown considerable flexibility in the application of this rule.

Table 33: DENMARK: Asset Volume by Class (%) Private Pension Funds and Insurance Companies					
	Percentage of total invested in:				
Year:	Bonds	Equities	Property	Associated companies	Loans
1982	73.3	2.9	2.3	-	8.2
1983	73.0	4.4	2.2	-	7.5
1984	74.8	4.5	2.7	-	6.5
1985	74.1	5.7	3.4	-	5.7
1986	75.6	5.8	4.0	-	5.5
1987	75.5	6.3	4.1	-	5.0
1988	74.1	8.9	4.1	-	4.4
1989	72.6	10.4	4.3	2.3	4.9
1990	70.6	10.5	4.2	4.7	4.4
1991	66.8	12.0	4.1	7.2	3.8

A noticeable trend is the recent increase in equity investments to the detriment of bonds. Two main themes are dealt with in relation to pension fund and life assurance investments in Denmark. First, it has widely been regarded as an advantage, also by the authorities, that institutional investors place a larger proportion of their assets in shares. This has meant that during the 1980s ceilings in pension funds and on life assurance companies concerning the investment in 'safe assets' have been lowered, making more room for investment in shares. Furthermore, changing governments have, on various occasions, prompted pension funds to take an active part in venture capital finance.

Secondly, fund managers tend to take a growing interest in the management of industrial companies, criticizing the Danish system of differential voting rights for shares, which makes it difficult for managers to exercise influence over them.

FRANCE

The Social Security Code contains general guidance for pension institutions as regards the investment of their reserves. One half of assets must be represented by securities issued or guaranteed by the state. *AGIRC* and *ARRCO* have developed their own rules within the overall guidance and have adopted investment policies which suit their financial organisations. Since their liabilities are not funded, the contingency reserves held are mainly invested on a short-term basis to ensure the necessary liquidity.

ARRCO's prudent management practice requires that assets earmarked for investment are invested in bonds (not less than 68% of the total), in loans (not more than 12%) and in equities or real estate (not more than 20%).

AGIRC's rules require that loans should not have more than 10 years' maturity and that specific investments do not exceed a given percentage of the total (real estate: 25%; personal loans: 25%; securities of a single enterprise: 30%). Not more than 10% of the total should be invested in any one security.

The above rules apply only to assets invested in the medium and long-term. As of November 1991 the asset distribution concerning short-term as well as medium and long-term investments was as follows:

ARRCO: 54% of assets are liquid
45% of assets are invested medium or long-term

AGIRC: 44% of assets are liquid
56% of assets are invested medium or long-term

In general, bonds represent the largest holding. In the federations, *AGIRC* and *ARRCO*, as well as in their member funds, in-house asset management is most common but there are exceptions. Data on average yield is scant. It is believed that the rates of return in recent years were close to 9% or 10% per year.

Insurance companies obey the overall investment guidelines set for the whole industry by the supervisory authority. Bonds are well represented in their portfolios.

GERMANY

The Insurance Control Act *(VAG)* regulates the investment of life insurance companies and of *Pensionskassen*. Section 54 of *VAG* sets out the types of investment authorized, together with limitations on their proportion within the total volume of assets held. The main constraints are as follows. Certain types of investments are authorized without specific limit, except that any one investment cannot represent more than 50% of the total held: mortgages, debt, loans on insurance policies, bearer bonds, term and fixed deposits or savings, unit-linked policies.

The following investments are subject to prescribed limits:

Property	5% (freehold) residential 10% non-residential
Debentures, bonds, loans	5% outside Germany
Ordinary shares (including investment trusts)	20% for 'tied' reserves 25% in 'non-tied' reserves ,and 5% in any one German company

A general constraint applicable to all investments is that not more than 2% of the total can be placed in any one bank. Currency matching requirements are also set out in the *VAG*. 'Tied' reserves have to observe full currency matching, subject to one-half being in ECU denominated assets. For premium reserves, 5% of non-matching reserves are allowed while for other liabilities the allowance is up to 20%.

Portfolio distribution information is available only as regards the investments of a sample of 147 large *Pensionskassen*.

Table 34: GERMANY: Asset volume by class *Pensionskassen*, end of 1992 (million Marks)		
Class of assets:	DM million	%
Equities	1,676	2.1
Real property	5,626	7.0
Notes receivable and loans	8,356	10.4
Registered bonds	17,953	22.3
Fixed-interest securities	20,290	25.2
Mortgages	8,759	10.9
Shares in investment trusts	15,499	19.3
Other	2,210	2.7
Total	80,369	100.0

GREECE

The legal framework concerning the investment of the capital accumulated by the compulsory auxiliary funds has been simplified and made more flexible since the entry into force of Law 2042 in 1992. Previously, pension funds were obliged to deposit all their surplus with the Bank of Greece, or alternatively an appointed Bank which normally invested in state securities and, to a lesser extent, in shares and real estate.

Since 1992 pension funds can withhold every year up to 20 per cent of the accumulated capital from the amounts deposited with the Bank of Greece (or its appointed substitute) and can invest directly. Restrictions still exist because direct investment must respect prescribed maximum limits: not more than 40% in real estate and the rest in bonds or shares of quoted enterprises. Separate legislation from 1990 has opened the door to the establishment of mutual funds to be managed by specialised investment companies. The latest development (Law 2076/1992) consists of enabling a pension fund to establish, independently or jointly with another fund, an investment management company (*A.E.D.A.K.*).

The trend towards greater flexibility in pension fund investment has, however, been accompanied by the imposition of strict procedures for obtaining the relevant authorisations from the competent government departments, a situation which may be justified by the fact that the pension funds concerned are compulsory and government regulated.

At the end of 1989, the breakdown of the assets held by compulsory auxiliary funds under the supervision of the Ministry of Health and Social Security was as follows:

Bank deposits	103.1 billion Drs
Equities and bonds	110.9 billion Drs
Real estate	184.1 billion Drs

As far as voluntary supplementary provision is concerned, investment management is entirely in the hands of insurance companies which have to comply with the rules on prudent management laid down in EU insurance directives.

ITALY

A recent estimate (1991) of the composition of the portfolio of Italian pension funds gave the following breakdown.

Treasury stock	61.0
Bonds	10.5
Property	10.0
Investment trusts	10.0
Shares	3.5
Others	5.0

The strong preference for Treasury stock (highly remunerative) is also typical of investments made by life insurance companies handling group pension insurance.

IRELAND

The trustees of pension funds have the primary responsibility for the proper investment of the scheme's resources under Trust Law and the Pensions Act. This involves pursuing a prudent investment policy and, in particular, ensuring that there is a diversification of investments. They are required to inform members in the trustees' annual report if more than 5% of the scheme's assets are invested in the employing company or in any one shareholding or property. There are also limits on the extent to which these investments can be taken into account in meeting the funding standard which applies to defined benefit schemes.

Table 35:
IRELAND:
Asset Volume by Class (%), end of year

Class of asset	1980	1988	1991
Domestic Equities	16.0	23.3	24.2
Domestic Bonds	30.0	44.8	31.5
Property	19.0	4.4	7.0
International assets	23.0	21.0	32.0
Other	12.0	6.5	5.3
Total	100.0	100.0	100.0

Sources: Heffernan: 1991 and IAPF: 1992 and 1993, see notes 15 and 17.

One of the main influences in Ireland on the investment of pension scheme assets in recent decades was the imposition of exchange controls in 1979 and their subsequent removal in 1988. Ireland was part of the Sterling area up to 1979 when Ireland joined the European Monetary System and the link with Sterling was broken.

Exchange control regulations were introduced at that time to protect the currency and remained in force until 1988. These regulations did not require repatriation of assets already held abroad. Instead they laid down that no more than 10% of cash flow (contribution plus investment income less all outgoings) could be converted into foreign currency to purchase non Irish punt denominated assets.

The average distribution of assets in Irish pension funds shortly after the exchange controls were introduced (1980), at the time of their removal (1988) and in 1991 is shown in Table 35. The small size of the equity market in Ireland meant that investments in bonds were at an artificially high level by 1988, because of the operation of the exchange controls. Accordingly, when these controls were removed Irish pension funds reduced their exposure to bonds and switched a significant proportion of fund assets into foreign equities. The fact that this was mainly a change to investment into foreign equities can be illustrated by the fact that in 1988, 9.2% of assets were invested in European (other than Irish) equities and this increased to 14.8% in 1991, and in 1988, 8.2% of assets were invested in non-European equities and this increased to 13.1 in 1991.

Table 36: Ireland: Pension fund investment returns	
3 Year Periods	Real investment returns (%)
1971/74	-14
1975/77	20
1978/80	0
1981/83	4
1984/86	12
1987/89	15
1990/92	-2
Source: Investment Returns in the 1990s (Faherty: 1993, see note 17)	

In Ireland, the liabilities of pension schemes are mainly salary linked and the net return required on investment of scheme assets has to be in excess of salary inflation. It is estimated by actuaries that salary inflation in the longer term equals price inflation plus 2% and, therefore, the return required to meet pension scheme liabilities should average price inflation plus 4% over the life cycle of a scheme (Faherty: 1993).[17]

Table 36 shows in 3-yearly cycles the volatility in the investment returns for pension funds in Ireland in the period 1971 to 1992. The relatively high return on investments during the 1980s had to compensate for the low and negative return during periods in the 1970s and in the period since 1990. For instance, in 1992, investments in Irish equities and Irish property gave a negative rate of return while European and North American equity investments were profitable.

NETHERLANDS

The supervisory body (*PSW*) does not lay down rigid investment requirements. It confines itself mainly to recommending prudence and to suggesting the diversification of assets. The Insurance Chamber monitors actual investment practice.

In practice, investment by company pension funds in shares of the sponsoring employer and in loans to that employer is permitted only up to a maximum of 5% of the assets of the pension fund or, including the free reserve, 10%. The recent portfolio distribution of both industry-wide funds *(BPF)* and company pension funds *(OPF)* is summarized in Table 37. Investment in equities has significantly increased to the detriment of loans.

Table 37: NETHERLANDS: Volume by Class, 1990-1991 (In million HFL and %)						
Investment:	*BPF*		*OPF*		Total	
	1991	1990	1991	1990	1991	1990
Real estate	17,048	14,739	8,666	7,376	25,714	22,115
Mortgages	5,283	5,141	2,822	2,021	8,105	7,162
Equities	19,649	14,746	23,980	19,531	43,629	34,277
Bonds	17,379	13,954	36,280	31,899	53,659	45,853
Loans	44,189	45,647	27,340	27,963	71,529	73,610
Other investments	13,457	12,971	4,774	5,264	18,231	18,235
Deposits	3,917	3,732	3,773	3,817	7,690	7,549
Total	120,922	110,930	107,635	97,871	228,557	208,801
Per cent of total volume						
Real estate	14.1	13.1	8.1	7.5	11.2	10.6
Mortgages	4.4	4.6	2.6	2.1	3.5	3.4
Equities	16.3	13.3	22.3	19.9	19.1	16.4
Bonds	14.4	12.6	33.7	32.6	23.5	22.0
Loans	36.5	41.1	25.4	28.6	31.3	35.3
Other investments	11.1	11.7	4.4	5.4	8.0	8.7
Deposits	3.2	3.4	3.5	3.9	3.4	3.6
Total	100	100	100	100	100	100
Source:	Insurance Chamber *(Financiele gegevens pensioenfondsen 1991, Verzekeringskamer)*					

SPAIN

Pension fund legislation contains flexible rules regarding the choice of investments by qualified pension funds. Permissible investments include: securities, bank deposits (not more than 15% of the total), mortgages, real estate. All these may absorb 90% of investments, with the remaining 10% being freely used.

Limits are set as to the amount invested in securities issued by any one enterprise (not more than 5% of the total), excluding securities issued by public bodies, both domestic and foreign. As a rule loans to fund members are not permitted. Exceptions are strictly limited.

As mentioned earlier, in the years immediately following the 1987 legislation, plan sponsors were allowed a 10 year period of grace to bring the reserves up to fully funded standards. The actual available assets have so far been invested as shown in Table 38.

Table 38: SPAIN: Asset Volume by Class (%), 1992		
Class:	Qualified funds	Mutual benefit societies
Real estate	3.4	16.4
Fixed-income securities	86.9	58.5
Variable income securities	2.0	8.8
Bank deposits	7.1	1.1
Mortgages	0.6	0.8
Other	-	14.7
Total	100.0	100.0

PORTUGAL

Decree-Law No.415/91 of 25 October 1991 lays down in Articles 27 and 28 the principal rules concerning the investment of pension funds. These provisions set out authorized, as well as forbidden, investments. Investment is authorized in:

(a) Treasury bonds;
(b) Bonds, participation securities or other negotiable bonds, including cash bonds;
(c) Equities;
(d) Investment in risk capital funds;
(e) Participation units in mutual funds;
(f) Mortgage loans, excepting those for industrial estate;
(g) Loans made to fund participants;
(h) Cash, bank and monetary market deposits;
(i) Real estate mentioned in the land registry as part of the fund, other than industrial estate;
(j) EU Member States: equities and bonds quoted on the stock exchange of Portugal.

Investment is not authorized in:

(a) Securities issued or held by pension fund managing institutions;
(b) Securities issued or held by members of the managing or supervising bodies of the managing institutions or of those holding more than 10 per cent of their capital stock;
(c) Securities issued or held by enterprises if more than 10 per cent of their capital stock is held by one or more directors of the managing institution in their own name or on behalf of another person, their spouses and relatives or their relatives by marriage of the first degree;
(d) Securities issued or held by enterprises having in their respective managing or supervising bodies one or more directors of the managing institution in their own name or on behalf of another person, their spouses and relatives or their relatives by marriage of the first degree;
(e) Securities issued or held by the fund associates or by societies under their control, unless the latter issue or hold stock exchange securities or national debt bonds.
(f) Real estate used by fund associates or by societies under their control.

Purchase and sale financial operations of stock exchange movable assets must always be carried out by these institutions. The *Instituto de Seguros de Portugal* supervises the adequacy of the fund assets with regard to their respective liabilities. Table 39 shows the volume and allocation of pension funds investments.

The data shows a representative sample which covers only the allocation of 88.0% of the total volume of invested assets (i.e. Esc.334 billion out of a total of Esc.380 billion in 1992).

Table 39:
PORTUGAL:
Asset Volume by Class (%), end of 1992

Treasury bonds (minimum 15%)	42.1
Bonds, equities, participation securities quoted on the stock exchange	26.4
Bonds, equities, participation securities (non-quoted, maximum 15%)	5.0
Risk capital fund securities (maximum 15%)	0.4
Bonds, EU stock exchange foreign equities and participation in mutual funds (maximum 40%)	0.8
Real estate, mortgage loans* (maximum 50%)	5.9
Cash, deposits and treasury bills (minimum 2%)	19.4
Total	100.0

* Including loans to fund members, representing 0.01 of the total.

UNITED KINGDOM

Since the majority of pension fund liabilities depends on future earnings inflation during the period up to retirement and on future price inflation for pensions in payment, fixed interest assets such as bonds and mortgages are not in general thought to be suitable investments. In recent years emphasis has been on investment in real assets, such as equities, property and index-linked government securities.

Pension fund trustees are required under trust law to invest fund assets in the best interests of the members. This is usually regarded as precluding investment in the employing company, or in related organisations, unless the terms are fully competitive with those available in the market. Any significant equity investment in the employing company is regarded as unsound, since it reduces the security of members' pension rights. Insolvency of the employer would affect not only their jobs but also the value of their accrued pension rights. Regulations have been introduced to restrict self-investment of this type, generally to a maximum of 5% of total assets. Contracted-out defined contribution schemes are required to invest in certain prescribed assets (including insurance policies), some within certain limits, but these requirements are not unduly restrictive and are mainly for the purpose of ensuring appropriateness of investment and adequate diversification. Apart from this there are no regulations or laws which place restrictions on the investment policy of pension funds.

Some pension funds are managed on a fully discretionary basis. In other cases, trustees establish a benchmark distribution, for example 60% United Kingdom equities, 20% overseas equities, and 20% index-linked government securities. The investment manager is then monitored against the performance of such a portfolio. They can deviate from the benchmark to achieve improved returns, but will need to be able to justify to the trustees the more 'risky' profile adopted.

Over the 10 years from 1982 to 1991, the median return of all pension funds participating in a major performance measurement service was just over 16% a year. This may be compared with average price increases of 5.6% a year over the same period and earnings increases of 8.2% a year.

Table 40: UNITED KINGDOM: Asset Volume by Class (end of 1990) £ million

UNITED KINGDOM INVESTMENTS	
Cash, deposits and other short-term assets (net of short-term liabilities and borrowing)	20,307
Government fixed interest securities	18,160
Local authority fixed interest securities	32
Company fixed interest securities (including convertibles)	6,213
Loans and mortgages	227
All fixed interest	44,939
Government index-linked securities	9,780
Ordinary shares	142,147
Unit trust units	4,139
All equity shares	146,286
Land, property and ground rents	26,363
Property unit trust units	1,656
All property	28,019
Other investments	18,552
TOTAL UNITED KINGDOM INVESTMENTS	247,576
INVESTMENTS OUTSIDE THE UNITED KINGDOM	
Cash, deposits and other short-term assets	620
Government securities	5,442
Ordinary shares	47,460
Other	1,566
TOTAL OVERSEAS INVESTMENTS	55,088
TOTAL INVESTMENTS	302,664
Source: Financial Statistics (HMSO)	

CHAPTER 7
A LEGISLATIVE FRAMEWORK FOR SUPPLEMENTARY PENSIONS AT EU LEVEL?

While there is no comprehensive legal framework for supplementary (occupational) pensions to be found in Community law, there are nonetheless numerous rules in the Treaty itself or in secondary legislation which have a direct impact on occupational pension schemes.

Such rules exist already in the areas of equal treatment of men and women, and with respect to the protection of workers in the event of insolvency of their employer and of transfer of ownership of the business they work in. Furthermore, accounting standards laid down in Community directives[18] require occupational pension liabilities to be clearly shown in financial statements. In addition to this existing legislation, the Commission has proposed directives on the freedom to invest and to manage assets of private institutions for retirement provision and on the protection of so-called atypical workers, i.e. mainly part-time and temporary workers. The Commission has also started to look at obstacles to the mobility of labour which result from an insufficient protection of occupational pension rights of mobile workers.

In this chapter, a brief overview on existing and proposed EU legislation concerning pensions will be given. The issue of labour mobility which has not yet given rise to specific legislative proposals at Community level will be discussed separately in Chapter 8.

Equal treatment of men and women

The Commission and the Council first addressed the question of equality of treatment in social security legislation with the *Council Directive of 19 December 1978 on the progressive implementation of the principle of equal treatment for men and women in matters of social security (79/7/EEC).* This directive allows Member States to make a number of derogations to the principle of equal treatment. These derogations are set out in Article 7(1), and cover the determination of pensionable age, certain provisions concerning family supplements and certain qualifying conditions concerning invalidity and old-age benefits of wives of insured persons.

In 1986, a parallel instrument was adopted to deal specifically with second-tier social security schemes, namely the *Council Directive of 24 July 1986 on the implementation of the principle of equality of treatment for men and women in occupational social security schemes (86/378/EEC).*

A major development came several years later when the European Court of Justice (ECJ) delivered its judgment in Case C-282/88 (Barber V GRE) against the following jurisprudential background. Article 119 of the Treaty lays down the obligation for Member States to ensure that men and women receive equal pay for equal work. 'Pay' is defined in the second paragraph of Article 119 as *"the ordinary basic or minimum wage or salary and any other consideration, whether in cash or in kind, which the worker receives, directly or indirectly, in respect of his employment from his employer".* Since its judgment in the first Defrenne case, the Court has developed a broad interpretation of the concept of 'pay'. In this case the Court held that pay includes: *"...any other consideration, whether in cash or in kind, whether immediate or future, provided that the worker receives it, albeit indirectly, in respect of his employment from his employer".*

In the second Defrenne case (C-43/75, judgment of 8 April 1976), the Court went on to hold that Article 119 *"applies directly, and without the need for more detailed implementing measures on the part of the Community or the Member States, to all forms of direct and overt discrimination which may be identified solely with the aid of the criteria of equal work and equal pay referred to by the Article in question".*

As far as the interpretation of 'consideration' in Article 119 is concerned, the Court stated in its first Defrenne judgment (case C-80/70, judgment of 25 May 1971) that social security schemes and benefits, in particular old age pensions, although in principle not entirely separate from the concept of pay, did not fall under the concept of 'consideration'. The Court came to this decision on the basis of the following characteristics of social security systems: (i) they are directly governed by legislation without any element of agreement within the undertaking or trade concerned and are obligatorily applicable to general categories of workers; and (ii) they provide workers with the benefit of a statutory scheme to which workers, employers and in some cases the public authorities contribute financially in a measure determined less by the employment relationship between the employer and the worker than by considerations of social policy, so that the employer's contribution cannot be regarded as a direct or indirect payment to the worker for the purposes of Article 119.

In its judgment of 13 May 1986 in the Bilka-Kaufhaus case (C-170/84), the Court, applying those criteria, came to the view that benefits paid under an occupational pension scheme originating in an agreement between the employer and the staff committee and forming an integral part of the contract of employment are to be classified as 'consideration' within the meaning of Article 119.

In the Barber case (C-262/88), the Court had to consider whether a 'contracted-out' pension scheme approved under United Kingdom legislation fell within the scope of Article 119. The particular scheme at issue was a type of occupational pension scheme established in consultation between the social partners or by unilateral decision of the employer, financed by the employer alone or by employer and employees combined, and which employees may join in partial substitution for their statutory pension. From the principles set out above the Court deduced that *"a pension paid under a contracted-out scheme constitutes consideration paid by the employer to the worker in respect of his employment and consequently falls within the scope of Article 119 of the Treaty"*.

The above ruling left unanswered a number of technical questions (see below) but, on the whole, it left no doubt that, in principle, supplementary pension provision would have to ensure equality of treatment for men and women in the following main areas: (i) eligibility conditions when joining a scheme, (ii) pensionable age and (iii) survivors' benefits. It was also understood that the ECJ was aiming at enforcing a broad principle of equality in contributions and benefits, although the Court's ruling of 1990 did not provide sufficient guidance as to how such a principle could, in practice, be implemented in certain concrete cases.

Fear that such legal provisions would have undesirable financial consequences for pension funds in a number of countries and concern about the lack of clarity of the ECJ ruling had three immediate consequences. One consequence was that Member States intervened to avoid full retrospection in the interpretation of the Barber ruling by adopting a special protocol annexed to the Maastricht Treaty. This protocol provided that benefits under occupational pension schemes shall not be considered as remuneration (pay) according to the meaning of Art.119 if and insofar as they are attributable to periods of employment prior to 17 May 1990 (the date of the ruling in Barber).

Furthermore, Member States (with the exception of the United Kingdom) amended Article 119 of the Treaty, by adding to the original text a third paragraph, which says:

> *"This Article shall not prevent any Member State from maintaining or adopting measures providing for specific advantages in order to make it easier for women to pursue a vocational activity or to prevent or compensate for disadvantages in their professional careers."*

The third reaction to the Barber ruling was that several cases (i.e. Coloroll, Moroni, Ten Oever, Neath) were brought to the ECJ with the specific object of obliging the Court to be more specific on matters of retrospection, on the freedom of pension fund actuaries to use sex-related actuarial factors and on the treatment of survivors' benefit entitlements. At the end of 1993 the ECJ had not yet issued full clarification on all issues under review but their views began to emerge.

In its judgement of 6 October 1993 in case C-109/91 (Ten-Oever), the Court confirmed that the direct effect of Article 119 of the Treaty may not be relied upon in order to claim entitlement to an occupational benefit which was acquired in connection with periods of employment served prior to the date of the Barber judgment of 17 May 1990, except in respect of persons who have before that date initiated legal proceedings or raised an equivalent claim under the applicable national law. The Court also confirmed that a widower's pension of the kind in question at issue in case C-109/91 (an occupational scheme) is to be regarded as 'pay' within the meaning of the second paragraph of Article 119 of the Treaty.

On the actuarial question, the Court ruled ('Neath', case C-152/91, judgment of 22 December 1993) that the use of actuarial factors differing according to the sex of the insured person or beneficiary does not contravene the principle of equality of treatment provided they apply in defined benefit occupational pension schemes. Further clarification is still awaited in the Coloroll case (C-200/91), at present pending before the ECJ.

Returning to the initiatives of Member States (see above), it should be pointed out that the coexistence of two different versions of Article 119 raises difficult legal questions which may yet have to be resolved by the ECJ or by the Community legislator.

Before ending our discussion on equality of treatment it is worth taking a brief look at the situation actually prevailing in Member States at the end of 1993. As far as social security is concerned, most Member States either already have equal pension ages or have taken decisions to achieve this on a gradual basis, with the exception of Italy. Most have, or are planning to, implement a minimum pension age of 65. The nature of implementation varies: Portugal will equalize pension ages at 65 over a three year period beginning in 1994; the United Kingdom has recently stated that the state pension age will be raised to 65, but that equalization will be phased in between 2010 and 2020; Greece has equalized state pension age at 65, but only for all new members to the national insurance scheme. In France, a full pension is due from age 60 to men and women. In Belgium the flexible pension is due between age 60 and 65 to both sexes, but further change will be required to comply with a ruling of the ECJ which held in 1993 that the pension formula did, in practice, cause men (financial) disadvantage.

In relation to other provisions (i.e. the treatment of survivors) national legislation is broadly in conformity with Community requirements, at least with regard to the avoidance of direct discrimination between men and women. The general picture is that the process of adjusting rules and practices to the European requirement of equality of treatment for men and women in supplementary pensions has definitely started, although it is far from being completed.

Much time may elapse before the goal is fully achieved, and there are a number of reasons for this. Sponsors of voluntary pension arrangements are generally slower to comply with 'European requirements' than civil servants responsible for state controlled and managed schemes. Secondly, the ECJ does not have the legal competence to prescribe the remedy or the solution which employers (or even the state) must adopt to comply with its rulings. The ECJ can only stipulate that the remedial measures taken be non-discriminatory.

On the other hand, signals from the Court are not always clear or exhaustive and leave open the possibility of further challenge and further interpretation. It is equally important to realise that the definition of a right (to equal treatment) has immediate cost and implementation implications. The prompt reaction of governments in order to pre-empt a costly interpretation of the notion of retroactivity in the Barber ruling (see above) is clear proof that cost considerations are important. The rights to benefit in the area of social security, and in that of pensions in particular, are a body of economic and social rights, which gain substance through transfers of financial resources and are not mere reflections of legal enactments.

In the process of aligning pension fund rules and regulations to EU requirements some Member States are, in specific areas, more advanced than others. Pension funds in Ireland and in the United Kingdom have made good progress both in the area of eligibility rules and in the alignment of retirement age conditions for men and women. In the Netherlands and in Germany the relevant questions and the possibility of enforcing changes are currently being discussed. In France the main issue seems to be the difference between widows and widowers in survivors' benefit entitlements (supplementary schemes). Sometimes, as in Greece and to some extent in Ireland, full equality is only introduced for new entrants or for newly established schemes.

Doubts concerning the final ECJ position on the use of sex-related actuarial factors was only resolved at the end of 1993, and the decision has raised important unanswered questions in countries like Denmark where defined contribution benefits are widespread.

A final problem in this particular area is that even if direct sex discrimination can be easily identified, the concept of indirect sex discrimination is much more elusive. Existing EU legislation bravely attempts to address this issue as well.[19]

The protection of supplementary pension rights under European labour law

The European Union has never left any doubt about the fact that the process of European economic integration should lead to a general improvement of living and working conditions. However, the process of integration often requires adjustments in individual countries, regions or industries which may have painful effects in individual companies. The process of economic integration will only be acceptable if there are adequate safeguards for workers against the negative effects of economic restructuring which it causes.

Such safeguards are required by a series of labour law Directives which the Council adopted following the Commission's first social action programme of 1974. The Directives concern the protection of workers' rights in the event of transfers of undertakings[20] and in the event of insolvency of their employer[21]. Both Directives refer to occupational (supplementary) pension schemes and require Member States to take the necessary measures to protect the interests of past and present employees regarding their pension rights.

According to Article 3, paragraph 3, of the directive on the transfer of undertakings, *"Member States shall adopt the measures necessary to protect the interests of employees and of persons no longer employed in the transferor's business at the time of the transfer ... in respect of rights conferring on them immediate or prospective entitlement to old-age benefits, including survivors' benefits, under supplementary schemes ..."* The term 'supplementary schemes' refers to company or inter-company pension schemes outside the statutory social security schemes in the Member States.

Article 8 of the Insolvency Directive reads as follows: *"Member States shall ensure that the necessary measures are taken to protect the interests of employees and of persons having already left the employer's undertaking or business at the date of the onset of the employer's insolvency in respect of rights conferring on them immediate or prospective entitlement to old-age benefits, including survivors' benefits, under supplementary company or inter-company pension schemes outside the national statutory social security schemes."*

It should, however, be pointed out that there is no Community definition of supplementary pension rights which could be used in conjunction with Article 8. On the contrary, according to its Article 2, the Insolvency Directive, *"... is without prejudice to national law as regards the definition of the terms ... 'right conferring immediate entitlement' and 'right conferring prospective entitlement'."*

The effectiveness of the protection given by the Insolvency Directive therefore depends on the recognition of expected occupational pensions as a legal entitlement within the legal framework of Member States. As a result of national legislation and jurisprudence, occupational pension benefits are becoming more clearly defined in legal terms, and it can thus be expected that better protection can also be achieved against the consequences of insolvency.

In the future, the issue of non-standard labour relations will have to be addressed at Community level. The Commission has proposed legislation which would, in particular, require Member States to guarantee an equivalent social protection, including in occupational schemes, between non-standard employees and persons in full-time employment of indefinite duration.

Finally, it is worth mentioning here that the ECJ has been asked to express an opinion on whether or not the provision of pensions by an appropriate institution is an 'economic activity' to which EU's requirements and rules on competition should apply. The answer has been negative so far as regards a public social security institution providing pensions on the grounds of its reliance on the principle of social solidarity. A further ruling has recently been requested in respect of Dutch industry-wide funds established as a result of collective agreements (cases

C-430/93 and C-431/93, J. van Schijndel and J.N.C. van Veen vs. *Stichting Pensioenfonds voor Fysiotherapeuten*). A decision was still awaited at the end of 1993.

Pension funds and financial freedoms in the European Union

Another aspect of the possible impact of EU provisions and/or goals on national institutions responsible for managing supplementary pension provision needs to be addressed, namely the implications for pension funds of the freedom of establishment (Art.52-58 of the Treaty), the freedom to provide services (Art.59-66 of the Treaty) and the freedom of movement of capital (Art.66-73 of the Treaty).

It may be recalled that this issue was raised by the Commission in debates on financial services for the following reasons. Having advanced and found broad agreement in the proposed liberalization of life insurance (First and Second Life Assurance Directives), as well as in the proposed harmonization of investment guidelines applicable to insurance and banking, the Commission recognized that it had actually entered the supplementary pension field.

In fact, by virtue of the Second Life Assurance Directive (1990), group insurance contracts taken out by employers and/or trustees to cover retirement benefits for their employees could eventually be bought and sold freely throughout the Community. Free competition meant that pension plan sponsors would seek the best or the cheapest insurance arrangements available in Europe or will even establish a captive insurance company in any one Member State to handle their pension plans. The Life Assurance Directives also set in motion a process of harmonization of rules concerning the investment of the reserves held by the insurance companies, including those arising from group pension insurance policies.

Having gone thus far, the Commission took the view (in 1990) that it was necessary to create, by means of a new, separate directive, a 'level playing field' between insured and non-insured supplementary pension plans, in particular as regards investment choices and investment management. A draft directive was circulated and consultations began in 1990 with Member States. It was argued that the proposal would create no new freedoms and would confine itself to clarifying the types of restrictions on full freedom of movement of capital that were already applicable under Community law.

The proposed directive was meant to cover financial institutions falling within the definition of 'pension funds'. As far as possible, these have been defined - not without difficulty, given Community-wide differences - so as to exclude social security institutions and to include all institutions and funds established to provide supplementary (second-tier) pensions and which accumulate segregated reserves (assets) capable of being invested. It was made clear that institutions financed on a pay-as-you-go basis would be covered only insofar as they have balancing reserves which are invested. Book reserve schemes would be outside the proposed directive since there are no identifiable assets.

In relation to the freedom of investment, the proposal laid down a number of general investment principles, referring to criteria by which assets should be funded, the issue of diversification and the principle that investments should be restricted to prudent levels. The proposal specified the types of restrictions which cannot be maintained in view of capital movements freedom. First, there may be no privileged access for governments (such as requirements on pension funds to invest up to a given percentage in particular categories of assets). Secondly, there may be no requirements to localize assets in a particular Member State. Thirdly, there may be no currency matching requirements which cannot be justified on prudential grounds.

Notwithstanding numerous subsequent amendments and changes of emphasis, no agreement had yet been reached by the end of 1993. There are two important issues of contention which remain to be resolved. The first concerns the extent to which supervisory authorities should be able to intervene with the providers of investment management or (custodian) services. The proposed directive would allow Member States to require that the contract between the pension fund and the service provider contains clauses to allow Member States to have direct access to information held by a service provider, either through him or through the pension fund itself. In the exceptional case that a service provider would refuse to meet its contractual obligations, supervisory authorities in one Member State would be able to directly request the intervention of the supervisory authorities (of the service provider) in another Member State.

The second issue relates to rules for currency matching. The draft directive originally introduced two ceilings: where liabilities are fixed in monetary terms (such as life assurance), Member States may require pension funds to hold a maximum of 80% of their assets in the same currency as the one in which the liabilities are expressed. Where liabilities are not fixed in monetary terms, but determined for instance by final salary, this maximum is lowered to 60%. In the Council, a majority of Member States opted for a single 80% ceiling, but the Commission is of the opinion that a single limit is not justified on prudential grounds and could be harmful to the interests of members and beneficiaries of pension funds, especially in relatively small capital markets.

A general observation can be made concerning the proposals under review. Community action towards harmonization of rules, practices or behaviour has, in general, a chance of success when, in the relevant field, Member States present a fairly homogeneous situation from the start or when they can easily accept change in a particular area of policy. The insurance market, life or non-life, operates in a technical, economic and commercial environment which is fairly homogeneous across the EU.

Admittedly, some countries have larger or stronger insurance companies and the range of products offered to consumers is not identical. But there is a basic similarity in the business, in the style of domestic supervisory frameworks and in the outcome of the provision of insurance services. On the contrary, supplementary pensions provision outside the insurance vehicle is not at all homogeneous between Member States. Methods of financing, the size of assets held, the legal and institutional profile, and even the measure of legal compulsion applied, present wide differences. Country specificity is moreover rooted in solid traditions which are jealously preserved and defended.

The Commission's intention of creating a 'level playing field' between the insurance and the pensions industry has proved to be somewhat unrealistic, and may explain the current deadlock on the draft pension directive. Some analysts go as far as to argue that the proposed directive was probably unnecessary in view of the fact that pension fund assets are already covered by the Freedom of Capital Movement Directive agreed in 1988. To this objection the Commission has replied that the 1988 Directive did not go far enough, insofar as it would not prevent Member States from applying certain restrictions to the investment of pension fund assets, some of which may well be considered either unreasonable or contrary to the wider interests of the Community. The draft directive - it was argued by the Commission - was intended to give much clearer guidance (in fact an obligation) as to what restrictions could be justified on prudential grounds, and more importantly, what could not be justified. Unfortunately, not all Member States share the views of the Commission. It remains to be demonstrated that the interests of fund members will be better served by a policy of total liberalization and deregulation in this area.

Be that as it may, the draft directive has probably helped to reveal and to fuel a latent conflict of interest between EU Member States. In recent years, an active promotion of supplementary pension funds has been made by those governments (Italy, Spain and Portugal among others) who believe that such a development would be beneficial to the national economy. They believe that an increase in savings and investment in the domestic economy should contribute to growth, employment creation, the transfer of public assets to private enterprise and the broadening of the domestic stock market. Such goals would be to some extent defeated if directives were to facilitate the expatriation of domestic pension savings for the benefit of financially 'stronger' markets. Such fears have grown since the 1992-93 crisis of the European Monetary System (EMS) and the currency devaluations which followed.

An example of the present mood can be found in Ireland. Much emphasis has been placed in recent years by government on the need for pension funds to invest in Ireland to create jobs, particularly since the removal of exchange controls resulted in a significant increase in the proportion of assets invested abroad. The Minister for Finance in his 1993 budget speech stated that, *"[t]he Government considers that Irish pension funds have a national responsibility to take the needs of the Irish economy, particularly the need for more jobs, into account when making their investment decisions ... These funds should invest as much of their assets as possible in Ireland ..."*

Against the official view, experts have pointed out that the main difficulty posed for pension funds investing in Ireland is the relatively small size of the Irish equity market. Accordingly, it is argued that to obtain a more balanced portfolio, pension funds may have to invest abroad. However, the issue is a complex one and the government's attitude cannot be readily dismissed. First, experience shows that investing in Irish quoted companies does not necessarily mean fully investing in the Irish economy. Secondly, foreign institutions are also major investors in Ireland. The general consensus in the country appears to be that what is lacking is not funds for investment, but opportunities to make worthwhile investments apart from equities, which obviously do not provide the full answer to the government's concern. [22]

In conclusion, it is beyond doubt that the Treaty's guarantee of freedom in the provision of financial services and in the movement of capital should also apply to institutional investors whose assets belong to supplementary pension funds. However, questions which may well deserve further discussion in this area are the following:

- which specific 'financial' guidelines are strictly needed for pension funds, independent of the existing Community regulations applicable to the insurance market;
- which of the above guidelines deserve to be binding and which may be issued by the Commission as recommendations only.

A general remark of relevance is that, with few exceptions, institutions for retirement provision are essentially non-profit bodies, while banks and insurance companies charge for their financial services. In fact, the latter *provide* financial services, while pension funds *buy* financial services, a difference that is important to keep in mind.

Article 58 of the Treaty of Rome makes it clear that non-profit institutions are in principle excluded from making use of the directly applicable provisions of Article 52, under which Member States must eventually guarantee freedom of investment and freedom of services. The Treaty's authors must have realized that free competition has little meaning among institutions who do not actually compete for customers and who do not charge commercial fees for their services.

CHAPTER 8
FREEDOM OF MOVEMENT, LABOUR MOBILITY AND PENSION RIGHTS: PRESENT SITUATION AND PROPOSED STRATEGIES

The background to the Commission's initiatives

The European Commission paid early attention to the practical implications for social security schemes of the right to free movement of workers and citizens between Member States.[23] Shortly after the entry into force of the Treaty of Rome, Member States began to develop a system of multi-lateral coordination of social security legislation which culminated in regulations 1408/71 and 574/72. The coordination achieved has proved successful in establishing equality of treatment between nationals and non-nationals in social security and in individuals taking up residence or employment in any country of the Community without having to fear undue loss of their social security rights, that is without being at significant disadvantage compared to persons who remained in their own country throughout their life.

As far as pensions are concerned, the system of multilateral coordination has been applied only to the first tier of pension provision, i.e. mandatory social security. When the above-mentioned regulations were developed it was believed that, at a later stage, a parallel multilateral system of coordination could eventually be put in place in respect of supplementary pension schemes, in particular occupational pensions, whether based on legislation or on contractual and/or private arrangements.

However, a closer scrutiny of the legal, institutional and fiscal environment typical of supplementary pensions in Europe showed that the technique of multilateral coordination used in regulations 1408/71 and 574/72 was not suitable for overcoming the potential obstacles to freedom of movement of persons within the Community posed by the pattern, both complex and diversified, of existing supplementary pension provision in Europe. Yet the possible negative impact of supplementary pension provision on the free movement of workers remained a major concern of the Commission, and the search for solutions continued.

The next step, taken in 1991, was to issue a Communication (originating in DG V, 'Employment, Industrial Relations and Social Affairs') from the Commission to the Council.[24] The document set out the Commission's views and concerns, particularly on those aspects of supplementary pension provisions which had implications for cross-border labour mobility within Member States. It was recognized in this Communication that supplementary pensions are an important element of social protection and that public policy in this area had taken different paths according to national traditions and preferences.

The document recognized that supplementary pension provision had not been subject to specific regulations at Community level, except for the question of equality of treatment between men and women and the possible impact of various directives regulating the life insurance business. However, the Commission's view was that further initiatives should be encouraged because it should be possible to agree on a number of practical and/or legal arrangements to enable workers moving from one country of the EU to another to avoid losing supplementary pension rights or being frustrated in their pension expectations.

On balance, the Communication has made a useful contribution towards initiating a discussion on this subject at European level, and raising awareness that solutions do exist, even if they are not easy to find. Confirmation of the difficulties in making progress came under the United Kingdom presidency of the Council during the second half of 1992.

The Presidency presented a draft Council resolution on the implications, for workers who move from one Member State to another, of the nature and diversity of supplementary retirement provision. The draft resolution requested: *"that measures be implemented by Member States, or by management and labour where they already have a role under national legislation or* *practice, which recognize the principle that each worker should be able to move from one Member State to another without having to fear undue loss of rights to future occupational retirement pension benefits, when such benefits play an important role in overall retirement income."*

The draft resolution subsequently pointed to the type of measures deemed to be most desirable to achieve the stated objective. It encouraged Member States to explore in greater depth how the obstacles to labour mobility attributable to supplementary pension provision could be removed. The draft resolution failed to secure unanimity at the Council.

A more recent initiative (originating in DG XV, 'Internal Market and Financial Services') having a bearing on the issues described, was taken at the end of 1992. It was suggested that, to facilitate labour mobility within the Single Market, it would be desirable to avoid the many legal and practical problems which may result from a change of membership in occupational pension arrangements, caused by moving abroad to work.

Since it was not seen as very realistic, at that stage, to attempt a general application of the principle of freedom of cross-border membership to all categories of employees and to all types of pension arrangements, the proposal - set out in an initial working paper[25] - dealt exclusively with transfers abroad of employees remaining with the same employer. Within this limited context, the proposal was to consider the feasibility of taking appropriate steps at EU level in order to guarantee to the employees concerned the right to continued membership in the supplementary pension scheme or arrangement to which the employees belonged before moving abroad.

The working paper pointed out that in some countries the right to continued membership is legally denied, or cannot be effectively exercised in specific situations. Legal obstacles did not appear to be unsurmountable, but it was likely that legal barriers would be raised for fiscal reasons. In other words, tax-driven obstacles to continued membership were described as complex and central to the issue.

The paper also recognized that for employees going abroad while remaining with the same employer, the possibility of continued membership in the social security pension system of the 'home country' was already contemplated, for a limited period, by regulation 1408/71. Clearly any new parallel rule on continued membership in supplementary pension provision would have to be consistent with this earlier regulation, for the obvious reason that the interface between first and second tier of pension protection was specific to each country.

The process of consultation about the proposal was initiated in 1993. It is likely to continue in 1994 (and possibly beyond) because the fiscal and technical questions involved are complex and require further study.

Some national reactions and realities

Before returning to the global issues described above and exploring which avenues could be opened for making further progress at European level towards the removal of what is perceived as an undesirable obstacle to the freedom of movement of individuals within the Union, it is important to review the position of different Member States and to become acquainted with some of their realities.

Occasionally, reference will also be made to the results of a comparative survey of cross-border and national obstacles to mobility in Europe, carried out by outside consultants commissioned by DG V. This source of information, additional to that provided by members of the Observatory Network, will hereafter be called 'the Survey'.

BELGIUM

In Belgium an employee who leaves a supplementary pension arrangement before retirement (or death or disability) has a right to a refund of her/his own contributions, while those paid on her/his behalf by the employer are not taken into consideration unless the employee has had a minimum of five years' membership or service with the employer.

Upon a change of employment an employee who was covered by a group insurance policy has a choice. He can continue voluntarily to pay all the insurance premiums required by the group policy, or collect the policy's surrender value, or leave any past acquired rights with the insurance company until retirement.

Employee members of a pension fund (i.e. an *ASBL*) withdrawing prematurely are entitled to a preserved deferred annuity based on their past service. As an alternative, they can obtain a cash payment to be transferred to another pension fund. As a rule, preserved rights are not revalued or adjusted after withdrawal from membership.

Employees who transfer abroad are subject to the above conditions but suffer specific disadvantages in case of a payment of a 'transfer value' from a domestic to a foreign pension plan. According to the Survey, the discrimination was recently formally enshrined by Articles 93 and 94 of the Law of 28 December 1992 introducing Articles 364bis and 364ter in the Income Tax Code. The joint effect of these two new articles is that the payment of a transfer value to a foreign pension plan must be considered as if it had been paid directly to the employee concerned; moreover, if the employee is a foreign tax resident at the time of payment of the transfer value, tax is assessed on the transfer value as if it had been paid the day before the employee changed his tax status. In Belgium transfer values were formerly the preferred solution for employees moving permanently abroad.

DENMARK

Supplementary pensions in Denmark are, as a rule, contribution-defined and accordingly pre-funded. In addition, Danish pensions rest on the 'equivalence principle', implying that on average the value of benefits accruing to a single wage earner corresponds to his/her contributions.

A Danish wage earner (or a foreign wage earner who has worked in Denmark) who takes on a job in another EU country has four options as regards his/her old pension scheme:

- the employee may retain the accrued pension rights in the old pension scheme and become a member of a new pension scheme in another EU country. At the time of retirement, the wage earner will receive benefits from both schemes. If the person returns to a job in Denmark, he/she can resume contributions to a Danish scheme;
- the employee may transfer the accrued capital value of her/his contributions to a new pension scheme, buying pension rights in the foreign scheme;
- the employee may remain as an active member in the Danish scheme and continue to pay contributions, thus earning full pension rights in Denmark;
- the employee may have the accrued capital value of past contributions and investment returns paid out in cash to him in Denmark.

Seen from the perspective of job mobility, none of the four alternatives mentioned above give rise to serious difficulties, as in one way or another the employee will receive the full accrued pension rights when she/he moves to a foreign country. However, some obstacles to labour mobility may arise when an employee moves to a foreign job. As regards the first option, it may be seen as a disadvantage by the employee that past contributions are administered by a Danish pension scheme which is highly likely to place them in assets denominated in Danish Kroner in compliance with the relevant investment restrictions. The second option would be impossible where there is no pre-funded pension scheme in the host EU country.

The second and the last options pre-suppose that the employee withdraws the funds from the Danish scheme. In this case, according to Danish tax rules, a substantial amount of tax will have to be paid on the funds withdrawn. Funds transferred abroad are taxed due to the tax-deductibility of contributions.

Cross-border migration in Denmark is limited. In 1987 the number of Danish migrants to another EU country was 2,351, while 1,331 Danish persons returned home. The figures for non-Danish migration are equally small.

FRANCE

The broad-based occupational pension schemes federated under *AGIRC* and *ARRCO* in some cases allow members taking up employment abroad to continue to contribute for pension purposes to a French fund affiliated to these federations. Employees who do not continue membership preserve their accrued rights in France (accrued pension points), and are entitled to a revalued benefit at retirement according to the evolution of the value of a pension point. For temporary expatriation, membership in the French supplementary fund is maintained while the employee remains subject to French social security.

Apart from the above, *AGIRC* and *ARRCO* apply the 'principle of territoriality', meaning that the place of employment (as opposed to nationality) determines eligibility to participate in a federated supplementary scheme. Thus, a foreign worker coming to work in France is eligible for coverage as a national.

Different rules apply to the less widespread arrangements such as defined benefit retirement plans in large firms under Art. 39 of the *Code Général des Impôts* and defined contribution plans qualified under Art.83 of the *Code*. Transfers abroad imply termination of membership in France (unless the transfer is made within the same company). Transfer capital values are not available for rights acquired under Art. 39 defined benefit plans, while the opposite is true for the contribution-defined Art. 83 plans.

GERMANY

An employee moving abroad to work (with the same employer or otherwise) has several options. It is legally possible to remain in the German company book-reserve plan, but it is highly unusual. The accrued pension rights of employees covered in Germany by pension funds or support funds are fully preserved if they are vested. It is, however, difficult to transform such acquired rights into a cash transfer value for buying past service pension rights in a fund abroad. Employees moving abroad but remaining in company service enjoy preferential treatment.

Restrictions on cross-border labour mobility also arise from fiscal legislation. In cases of pension coverage by way of direct insurance or by pension funds, contributions and/or premiums are deductible only if the relevant insurer is established in Germany.

Another possible restriction would be that insolvency insurance (*PSV*) only covers pension rights of employees working in Germany. More generally, Germany follows a taxation pattern that is different from that of other countries: yield from the investment of insurance and pension reserves is taxed while the benefit paid out is not.

GREECE

Preservation and aggregation of pension rights within Greece is guaranteed to employee members of compulsory supplementary pension schemes, that is the large majority of second tier pension arrangements. The technique of totalizing membership or insurance periods during an employee's career is used instead of calculating and paying a 'transfer value' to an employee who moves to a different fund.

Difficulties may arise if the job change implies taking up an activity (such as self-employment) which is not covered by a compulsory second-tier arrangement. In this case, the employee would be entitled to a refund of contributions, or to voluntary continuation of membership.

Cross-border transfers within the EU are, in principle, only treated as described above if the employee remains with the same employer. In practice, however, many supplementary schemes tend to impose limits on continued membership (limited to a fixed period, or to special circumstances).

In the case of other cross-border transfers within the EU, supplementary pension rights are only protected to the extent that accrued rights in Greece are preserved and deferred. Tax advantages for contributions paid to a supplementary scheme only apply to transactions and employment within Greece. A future revision of existing rules and practices, with a view to removing obstacles to cross-border transferability of pension rights, would be desirable.

Non-compulsory second-tier schemes do not afford employees sufficient guarantees with regard to either preservation, or aggregation, or indeed transferability of accrued second-tier benefit rights.

IRELAND

The Pensions Act (Part III) requires occupational pension schemes to provide for the preservation of pension rights in respect of post-1991 service. The following are the main elements of these preservation requirements.

- Employees who leave a scheme after 1 January 1993 with at least 5 years' scheme membership are entitled to a preserved benefit.
- The amount to be preserved will relate to the benefit rules of the scheme and will represent rights accrued (or contributions paid under a defined contribution scheme) after 1 January 1991; under a defined benefit scheme it is assumed that the rights accrue uniformly over total scheme membership.
- If the employee dies after leaving, but before pension age, a death benefit must be paid equal to the actuarial value of the preserved benefit or, alternatively, a pro-rata survivor's pension, if that is provided for under the scheme rules.
- The preserved benefit under a defined benefit scheme must be revalued each year by the lesser of 4% or the increase in the Consumer Price Index, from 1 January 1996, or the date of leaving, if later.
- Employees may, as an alternative, opt for a transfer payment to the scheme of their new employer or to a Life Assurance Company retirement bond, subject to certain conditions (see below).
- Employees leaving, who are entitled to a preserved benefit, cannot obtain a refund of their contributions paid since 1 January 1991. Contributions (including AVCs) paid prior to that date may be refunded.
- A scheme may provide higher benefits to employees leaving.

Employees may opt for a transfer payment within two years of leaving the scheme, but thereafter this option is subject to the agreement of the trustees. Trustees may also make transfer payments to Life Assurance Company Retirement Bonds without the employee's consent at the end of the two year period after leaving, provided the transfer payment is less than a prescribed amount (currently IR£3,000). In the case of defined benefit schemes, a transfer payment must be the equivalent of the actuarial value (as defined in the Pensions Act) of the preserved benefit on the date on which the member applies for the transfer.

Transfer payments can only be made to the scheme of a new employer or a Life Assurance Company retirement bond. The schemes must come within the scope of the Pensions Act, and the Life Assurance Company must be established within Ireland. This normally precludes transfer payments being made to schemes or Life Assurance Companies in other States. The trustees of the receiving scheme are required to accept transfer payments and to provide benefits of an actuarial value that is equivalent to the amount of the transfer payment.

As explained above, the Pensions Act only requires schemes to provide for preservation in respect of post-1991 pension rights. Many schemes, however, provide for the preservation of pre-1991 pension rights and the Pensions Board is urging all schemes to make similar provision for current members on a voluntary basis.

Most public sector schemes are exempt from the preservation of benefit requirements under the Pensions Act, as they have arrangements for preservation which are in some respects different, but at least as favourable as those provided for under the Act. There is a public sector transfer system in place whereby employees who change jobs while remaining employed within the public sector are automatically credited in the new scheme with the period of service in the previous employment. Where employees leave the public sector, they qualify for a preserved pension and lump sum, provided they have completed at least 5 years' pensionable service.

These preserved benefits are revalued in line with the salary of persons holding the position of the leaver and are normally payable from age 60.

There is a relatively high level of emigration from Ireland. It has been estimated that the number of employees with occupational pension rights who have emigrated from Ireland to other EU countries could be about 77,000. It is also estimated that up to 93% of emigrants from Ireland go to the United Kingdom and that 97% of immigrants from other EU countries to Ireland are from the United Kingdom. This latter group represents 19% of the total number of United Kingdom emigrants to other EU countries.

Consideration has been given by the Pensions Board to the provision that should be made for the protection of the pension rights under occupational schemes of the following categories of employees:

(i) posted workers, i.e. employees who are posted by their employer to work for a specified period in another state, while still remaining with the same employer or group of employers and who intend to return to work in the 'home country' with the same employer, after the period of posting;
(ii) employees who move to different employments in another state;
(iii) scheme members who have entitlements to preserved benefits and/or are in receipt of a pension under a scheme, the main administration of which is established in a state other than the state where they reside and/or are employed;
(iv) persons who are employed in and subject to the social security legislation of one state and in respect of whom it would not be economical to establish a separate scheme in the country of employment and who, as a consequence, are permitted to be members of an occupational pension scheme, the main administration of which is based in another state.

The Board would envisage such provision being made by means of an EU directive or regulation or by reciprocal agreements concluded on a bilateral basis with other EU Member States. The Board outlined its views on these matters in a note for the information of the UK Pension Law Review Committee (the 'Goode Committee'). This committee in their report published on 30 September 1993 recommended *'that the approach suggested by the Irish Pensions Board for progress through bilateral agreements for occupational pension rights should be explored in discussions between the UK and Irish Governments'.*

LUXEMBOURG

Supplementary pension provision is not common and lacks a specific legal framework. Under these circumstances, the question of benefit preservation and, possibly, transferability within the country is a matter left to the discretion of plan sponsors. Cross-border transfers are not, in this respect, approached in a different way.

NETHERLANDS

Preservation of accrued rights is guaranteed by legislation (*PSW*). This provides that an 'early leaver' is entitled to a benefit amount proportional to the length of membership and that this amount is preserved until normal retirement age. The indexation of the preserved amount becomes compulsory only to the extent that pensions in course of payment by the relevant fund are also indexed.

In addition, regulations permit the transfer of accrued pension rights ('transfer values'). When an employee changes jobs, a pension fund or insurance company is empowered to transfer the value of the accrued pension rights to the body administering the new employer's pension fund. At present, the employee alone cannot effect the transfer. However, a bill was recently submitted to Parliament which aims to give employees a statutory right to obtain a transfer value. The measure is due to come into force on 1 May 1994.

The position regarding employees involved in cross-border transfers is the following. Dutch legislation applies only to employment in the country. Accordingly, in the case of workers going to work abroad, participation in the domestic pension scheme is terminated and the early leaver will obtain a preserved benefit as explained earlier. In this respect it makes no difference whether the employee works with the same employer abroad or with a different employer.

The transfer of pension rights is only permitted to a pension fund or insurance company under the supervision of the Netherlands Insurance Chamber, which means that foreign pension funds and insurance companies are not eligible to receive transfer values. However, the *PSW* does allow the possibility of definitively surrendering pensions and pension rights in the case of emigration or intended emigration. This option makes transferring pension rights abroad possible in practical terms, since with the surrender value the employee can buy into a pension fund abroad according to the rules applying in that country.

A bill was recently put before Parliament aimed at amending the *PSW*, making it possible to transfer pension rights to a foreign-based pension fund or insurance company. The tax implications will have to be worked out because normally transfer values would be subject to tax in the host country.

Employees who move jobs from abroad to the Netherlands will come under the scope of the *PSW*. If they work in a branch of industry where compulsory participation in an industry-wide pension fund applies, they will also be obliged to participate in that fund. In the case of temporary secondment in the Netherlands, however, the Minister of Social Affairs and Employment can grant an exemption both from the *PSW* and from the obligation to participate in an industry-wide pension fund.

Though the acceptance of transfer values from abroad is permitted on the basis of Dutch legislation, tax rules form an obstacle. There are no special fiscal regulations applying to this kind of transfer payment. This means that the general rule applies, which is that in order to qualify for tax concessions a pension scheme must be related to one's period of service in the country. However, if on the basis of a transfer payment pension rights are also granted for service abroad, the requirements for eligibility for tax facilities are no longer met.

PORTUGAL

Supplementary pension arrangements (pension funds, book reserves) have developed so far without paying attention to the problems of preservation or transferability which affect mobile employees. In the future, however, the situation is likely to change. In Portugal the competent circles believe that EU intervention in this area would be necessary to remove possible obstacles to cross-border labour mobility. One suggestion is to make an individual employee more involved and self-reliant in handling the transfer of his accrued rights on an individual basis.

SPAIN

Preservation and transferability of accrued supplementary pension rights (both within the country and cross-border) are severely restricted under current regulations. Employees leaving a company's pension plan have the option of retaining their entitlement to their accrued rights (preservation with deferred rights). A transfer of the entitlement to another plan is only allowed within Spain, and provided that the receiving plan is a 'qualified' arrangement under the 1987 legislation.

With respect to cross-border job changes, continued participation in the home country plan is not allowed. Payment of transfer values to the host country plan is not permitted either.

UNITED KINGDOM

As indicated earlier, occupational pension benefits must vest after 2 years' pensionable service. Early leavers with vested benefits may normally choose between preserving their accrued benefit in the scheme which they are leaving, or taking a transfer value to a new occupational pension scheme, to a personal pension, or to purchase an annuity.

Preserved benefits must by law be revalued at 5% a year, or the rate of increase of the retail price index if less, over the period to retirement age, when the pension (and any lump sum) becomes payable.

A transfer value taken as an alternative to a preserved pension is assessed on the advice of the scheme actuary so as to be the cash equivalent of the preserved benefit, i.e. the present value at the date of payment of the transfer value of the benefits which would otherwise have been payable. The actuary is expected to take into account the market value of the underlying assets and he or she may have regard to the funding level of the scheme.

A transfer value from a contracted-out occupational pension scheme can only be paid to another contracted-out scheme, as it will include an amount in respect of the accrued guaranteed minimum pension (GMP). However, this GMP element can be repurchased from the state scheme and a transfer value paid to any other scheme in respect of the balance of the accrued liability, or used to purchase an annuity.

Where an individual is contracted-out of the state additional pension (SERPS) by means of an appropriate personal pension or a contracted-out money purchase scheme, benefits accruing in respect of the minimum contribution (equivalent to the contracted-out rebate) are referred to as protected rights. Although such rights can be transferred from scheme to scheme, they must retain their protected rights status and be used to purchase benefits in approved form. Protected rights can be bought back into the state scheme, with a corresponding reduction in the notional guaranteed minimum pension offset.

In order to satisfy the requirements of the Inland Revenue for tax exempt approved status, transfer values may only be paid to an overseas scheme (occupational pension scheme or personal pension) if the country of residence of the scheme, the employer and the individual coincide, and if the transferee has left the UK on a permanent basis with no intention of returning either to work or to retire. Reference to the Inland Revenue Pension Schemes Office (PSO) is usually required, except for small amounts and for transfers to countries or schemes with which there is a reciprocal agreement. Benefits may always be preserved in the scheme which the employee is leaving, providing the accrued rights have vested.

However, there are other conditions which restrict payment of transfer values abroad: transfers cannot be made to pay-as-you-go social security systems such as the French *régimes complémentaires* or to internal book-reserve schemes such as are common in Germany, Luxembourg, Spain, Portugal and Italy. Subject to certain conditions imposed by the Inland Revenue, transfers may be made to independent funds (including insured schemes) in EU Member States.

The relevant conditions are:

- the move to the other country must be permanent;
- the member must have requested the transfer or given written consent;
- the receiving scheme must be a tax approved bona fide arrangement;
- guaranteed minimum pension (GMP) benefits are not usually transferable.

Notwithstanding the possibility of making transfers as above, the relevant receiving fund in another Member State may not be willing to accept a transfer of funds with immediate vesting of accrued rights.

A transfer value may only be accepted from a scheme outside the UK with the specific authority of the PSO. It will normally be necessary for the transferring member to have been employed for at least 2 years in the overseas employment to which the transfer benefits relate. The resulting benefit rights to the member would, however, be subject to the overall limit on benefits applicable to UK schemes.

Benefits accrued in an occupational pension scheme in another Member State are usually ignored in relation to benefit entitlement in the UK. An expatriate worker coming to the UK may have the choice of:

- remaining covered by a home country pension arrangement;
- joining a UK scheme;
- participating in an off-shore arrangement.

Benefits from an exempt approved scheme may be paid to a pensioner or a beneficiary resident in another Member State (or in any other country).

There are no specific legislative requirements, other than conditions for obtaining exempt approved status, which limit cross-border movement of scheme members. Individuals may, under certain conditions, remain members of an approved scheme in the UK whilst working in another country. The conditions cover secondments for periods of less than 3 years, work overseas where the earnings are still chargeable, at least in part, to UK tax, and service with a subsidiary of the UK employer (or within the same group) which is expected to last no more than 10 years.

Alternative strategies for the future

It is reasonable to assume that the European Commission will continue to consider in future that the principle of freedom of movement of workers and, more generally, persons within the Union is a paramount goal. Current legal, fiscal and 'technical' arrangements for supplementary pensions in a number of countries do not facilitate, and often clearly inhibit, the free cross-border movement of persons with supplementary pension rights.

Two questions deserve consideration in this context:

- is further intervention of the Commission in this area desirable and
- if so, what strategies are likely to lead the Commission to achieve tangible results?

Let us recall first that not every party concerned is, in principle, in favour of further Community involvement in regulating or coordinating the area of supplementary pension provision. Dissenting views are a minority and are voiced only in few circles. But it would be imprudent to dismiss them entirely: the rejection of the 1992 draft Council resolution submitted on this subject by the UK Presidency of the Council has shown how fragile the prospect is of reaching unanimity in this area. The point is that supplementary pension provision is largely based on voluntary initiatives and on freely negotiated contractual arrangements. It is often argued that a European regulatory framework could - if it was too rigid - discourage rather than encourage supplementary pension provision.

It has also been pointed out that the number of cross-border movements involving loss of supplementary pension rights is, on the whole, modest. Moreover, multinational companies find ways and means to compensate their senior expatriates for any pension disadvantage suffered in moving abroad.

It is nevertheless suggested that, as a matter of principle, the Commission should continue to explore how to improve the present position. Two strategies may be at hand. The first would be to limit any new initiative to stating broad principles and requesting Member States to comply with them either voluntarily or with a minimum of compulsion. The second would go further than formulating goals, and would attempt to give specific guidance on how to achieve goals in specific technical areas, using binding legislation if necessary.

(a) The strategy confined to matters of principle

This approach could take as a point of departure the principle which was first put forward in the Communication of 1991, and then embodied again in the unsuccessful UK draft Council resolution of 1992. The principle is that each worker should be able to move to a job (or to a place of retirement) in another Member State without having to fear any undue loss of rights to benefits (whether acquired or in course of acquisition) from supplementary pension arrangements.

However, the meaning and implications of the above principle would have to be spelled out in future proposals. For instance, Member States could be invited to ensure that plan rules (or their equivalent) of supplementary pensions should, in all cases, guarantee the option, for the employee ceasing membership, of obtaining either the preservation of his past service rights or a corresponding transfer value based on his full vested rights. Independent of the financial vehicle adopted to implement the plan, preservation and transfer values should be available on request in all cases.

Going further, Member States could be invited to accept the principle that a transfer abroad should not be treated less favourably in scheme rules than a transfer within the country, leaving each Member State to make its own comparison and to take the necessary measures.

A weakness of such an approach is that the possible loss of tax advantages by employers, employees or pension funds consequent on cross-border transfers are not a matter dealt with in the scheme rules but in fiscal or pension legislation. It does not seem very realistic to expect that Member States will give up their traditional fiscal stance in this area in order to solve the problems of a minority of employers and employees. The ECJ ruling in Bachmann (1992) in fact strengthened the position of domestic tax authorities.

A possible solution to such an apparently intractable problem would be to suggest, in any new proposal, that, in exchange for full tax deductibility in the host country for any pension contributions sent abroad, the mobile employee would undertake to pay tax at a favourable (not just symbolic) rate on any transfer value taken out of the country when changing jobs. The suggestion is that all countries would apply the same, moderate, preferential tax rate on transfer values and similar entitlements, even if such exit tax is not required for transfers within the domestic scene.

At first sight this could seem a very bold proposal and one that is not entirely favourable to a mobile employee. This being the case, it is also abundantly clear that in the short term at least national tax authorities will effectively oppose any further attempt by the Commission to reduce their prerogatives in the area of pension transferability unless some compensation is offered to them. It could be further argued that if the employee should return, retire and pay income tax (including on his pension), the tax authorities of the country concerned should refund to the former employee the 'exit tax' that he may have paid on leaving his home country.

Another principle which could be embodied in a new Commission proposal is the guarantee of continued membership in a pension arrangement for employees temporarily seconded or transferred abroad and remaining with the same employer. The application of such a principle would have limited effect because of the necessary alignment of the duration of the continued membership in a supplementary scheme to the duration stipulated for social security coverage in Regulation 1408/71/EEC. Having stated this principle, the Commission could leave to Member States the responsibility of finding suitable 'technical solutions' by means of bilateral agreements, to be monitored by the EU. Alternatively, some possible types of solution (i.e. mutual recognition) could be mentioned in an EU instrument as examples to stimulate bilateral agreements.

The above approach may have more chances of success than the approach now pursued by DG XV (see above); it is only an illustration of how a strategy confined to principles may be given substance. More preparatory work would be required. In any event, it would be up to the Commission to decide whether to propose a binding instrument (directive) or a recommendation.

To the extent that supplementary pensions are sponsored voluntarily by employers and employees, it might be expedient for the Commission to raise initially the above questions within the framework of the 'social dialogue'. Ultimately, even if a proposed European instrument was not binding, a strong and clear EU statement of principles and objectives in this area may nevertheless have an impact on the practice in the Member States. In many Member States supplementary pension provision is closely linked to collective bargaining where EU guidelines and recommendations may already have some weight. The same could be said more generally of the likely attitude of national supervisory authorities.

(b) A strategy which attempts a technical coordination of schemes

While the strategy described in (a) above might lead to results which are similar to those pursued by the Community Charter of Fundamental Social Rights for Workers and the Council Recommendation on Convergence of Social Protection Objectives and Policies of 27 July 1992 (92/442/EEC), an alternative strategy, briefly outlined below, may be to coordinate supplementary pension provision at European level.

In addition to asking Member States to observe and to apply a number of fundamental principles, proposals could in theory be developed which would include promoting common rules or reciprocity on various aspects of supplementary pensions. These aspects could relate for instance, to (i) sponsoring and establishing pension plans and the degree of representation of employers and plan members; (ii) vesting and waiting periods; (iii) the separation of assets of plan sponsors from those of the pension institution (pension fund, etc.) or equivalent arrangements for securing payment of accrued rights in the event of the insolvency of the plan sponsor; (iv) preservation of rights and fair transfer values; (v) taxation issues and (vi) the protection of members' rights (including information and disclosure).

Even if such coordination, expressly excluding any attempt at harmonization, was only expressed through minimal rules and requirements and was limited to the specific goal of enhancing labour mobility, both within a country and across borders, it is doubtful whether the exercise would be worthwhile given the present state of affairs.

The relevant political considerations are unequivocally stated in the Council Recommendation of 27 July 1992 on Convergence of Social Protection Objectives and Policies: *"because of the diversity of the schemes and their roots in national culture, it is for Member States to determine how their social protection schemes should be framed and the arrangements for financing and organizing them".*

This principle which is valid for social protection as a whole is, *a fortiori*, relevant for one of its components, namely supplementary pension provision, whether compulsory or voluntary. The above suggests, in conclusion, that it would be preferable for the Commission to explore the acceptability of the first alternative strategy outlined above, namely that the Commission should develop a few guiding principles capable of receiving broad acceptance and strictly aimed at the improvement of the supplementary pension situation of workers who move to a job in another Member State (or who retire abroad). This approach could, moreover, focus both DG V and DG XV on a common proposal, enhancing the effectiveness of any further EU initiative.

CHAPTER 9
AN AGENDA FOR THE FUTURE

The overview of supplementary pension provision in the countries of the European Union leads naturally to a number of general conclusions about the present situation, while also inevitably raising questions about the future direction of policy in this area.

It is beyond question that the second tier of pension provision, whether voluntary or compulsory, public or private, contractual or freely sponsored, has a solid foundation in all the countries of the EU. Its importance, in terms of the number of persons protected and of the volume of assets held by funded schemes, varies greatly from one country to another due to its relationship with first tier social protection.

National specificity goes beyond coverage or financial strength. It reveals itself in the options chosen and the techniques used to achieve the otherwise common objective of enabling an increasing number of employees and self-employed persons to have access to a 'second pension'. A distinct 'pensions culture' seems to have developed around the national pattern of supplementary pension provision, a culture that breeds self-confidence in the soundness of one's own solution and a rejection of foreign models and patterns, even those which have proved successful elsewhere.

For example, believers in pension trusts, in segregated assets invested heavily in equities, and more generally, in fully funding future pension liabilities, along the lines of the Anglo-Saxon experience, remain sceptical about the choices of French or German employers and policy makers, who have secured substantial supplementary pensions for large sections of the labour force without funding future liabilities and/or segregating the funds and/or investing heavily in equities.

Believers in the free and voluntary approach to sponsoring supplementary pensions remain unconvinced that the right answer is compulsory provision as in Greece, Denmark, France or the Netherlands where compulsory provision was used to achieve broader coverage.

However, if one takes the view that the best system is one which effectively improves social protection at retirement for as many citizens as possible, then the lack of similarity between national approaches or techniques used at second tier level should not matter much. It is the result that counts. The problem, though, is that not all countries have achieved optimum results in terms of coverage or effectiveness of the second tier and that, at the same time, reliance on the second pension is increasing because of growing doubts as to the capacity of the first tier to sustain its traditional role into the next century.

Another concern is that cross-border diversity is perceived, sometimes vaguely, as an obstacle or as a nuisance along the path towards constructing and consolidating the European Union. The concern has a legitimate foundation but the effects of this diversity can be exaggerated unless clearly understood and approached from a realistic viewpoint.

In the area of supplementary pensions, free cross-border labour mobility - which is a goal of the Union - only compounds the difficulties which may exist and, in fact, often do exist, in securing smooth and fair portability of accrued pension rights in respect of persons moving within the domestic borders.

It would be too easy to argue that "charity begins at home" or, in other words, that Member States should give priority to order and fairness in the area of preservation and portability of accrued pension rights within their own country first, before arguing for the adoption of European rules designed to remove obstacles to cross-border labour mobility. On the other hand, the argument that European legislation on such cross-border issues should come first because it would trigger parallel improvements in the provision for domestic transfers of pension rights is not entirely convincing. This is for several reasons to do with the evident rigidity of different supplementary pension structures observed from country to country, the different degrees of involvement of traditional insurance contracts, and the voluntary nature of various pension arrangements. Naturally, much would depend on the kind of European directives which

Member States agree to. Past experience dictates prudence in formulating expectations about obtaining European consensus in such matters.

It is important to realise that Member States have no specific incentive and, in fact, no compelling reasons for spontaneously modifying their approach to legislating, financing and supervising the various forms of supplementary pension provision which have emerged in the past or which have been shaped by their policy choices.

Hence, one might realistically conclude that, under these circumstances, the pursuit of the European Union's goals will gain more from a policy of building bridges between different systems and situations, whenever this is feasible (which is not always the case), rather than imposing exacting rules on employers and employees, or on the authorities whose duty it is broadly to safeguard the public interest as well as that of consumers.

The agenda for the future includes European issues, such as those sketched above, but is wider than this. The future of supplementary pension provision is likely to prove extremely challenging. The issues to be tackled will not be the same in each Member State, as the following examples may help to demonstrate.

Occupational pensions are part of social protection: the concern with equity, with the desire to avoid 'two-speed' societies, cannot forever be confined within the boundaries of the welfare debate about the first tier. It has been shown that equity was part of the rationale on which some Member States relied in the past when they opted for a compulsory second tier or, at least, when they deliberately encouraged the extension of coverage through voluntary initiatives. Member States which followed another path, either deliberately, or because of different political priorities, may have to come to grips in future years with the question of explaining to the public the virtues and shortcomings of leaving employers and individuals entirely free to decide whether it is worthwhile to save for retirement within an appropriate pension framework.

The above challenge is particularly relevant for countries such as Belgium, Italy, Luxembourg, Portugal and Spain where social security pensions are still aiming at fairly high replacement rates and where the 'second pension market' has not yet reached the position which it may do in future years.

Countries where private pension funds have developed a key position as leading institutional investors on domestic, and occasionally international, financial markets, may have to face other challenges in future years. Here the cultural element which seems to have remained in the background is predominantly a social one. The fact is that not all parties perceive occupational pensions as a concession of paternalistic employers, as a simple device to gain a tax advantage, or as a convenient support for financial markets. The majority's concern is with the standard of living of the ever growing number of pensioners in Europe and this depends directly on the level of their basic and supplementary retirement income.

Pensioners are increasingly being identified as a category which has an important electoral influence. Their interests as a group as well as that of the active membership of pension funds is primarily the expression of a social concern with security in old age, rather than with the performance of financial markets. Their representatives are bound to become more vocal, to claim more information and control, basing their claims on the argument that company pensions are deferred wages and that in a way the assets accumulated in pension funds belong to them.

No matter which view is taken about the legitimacy of such arguments, one question for the future is the extent to which the vast pools of pension fund resources - in some countries their magnitude approaches the amount of the annual Gross National Product - can remain insulated from the mainstream national debate on jobs, public finance or defining the public interest. Another question to be answered is whether pension assets will actually be directed towards expanding the long-term investments badly needed for economic growth as, in theory, they are better placed to do.

The seemingly never-ending debate about the respective role of public and private pension provision, also includes challenges for supplementary pension policies in future years. It has been shown that in the recent political debate about social security, private retirement provision seems to have become desirable mainly as a remedy for the difficulties encountered by the state in sustaining the growing cost of mandatory benefits. The danger is that, unless circumstances are favourable and incentives are generous, the remedy may not provide the cure expected, particularly in societies which still firmly believe in the virtues of social solidarity.

In a similar context, the future relationship between supplementary pensions and the labour market acquires new relevance. One reason is that changes in work patterns are likely to take place, together with increased flexibility, a trend which could have a further impact on the accrual of supplementary pension rights and on the pattern of retirement, and hence on the respective roles of the various forms of retirement income. The definite and irreversible trend towards a higher pensionable age which is now observed in mandatory social security schemes is a related factor which will gradually affect individuals in the years to come, and will raise the question of whether or not the second tier of retirement benefits should be tied to the mandatory pensionable age.

Before concluding, two other thoughts come to mind. The first is that inflation, now apparently under control, could return, along with economic growth, as a major challenge for privately provided retirement benefits. Compulsory indexation techniques are ill-adapted to the voluntary environment in which many forms of pension provision operate in Member States.

The second is that, looking further ahead, one should also anticipate the possible consequences on the debate concerning supplementary pensions of an increased membership of the European family. The arrival of countries which have already decided to join the EU, and of other possible entrants, will bring yet more diversity onto the European pensions scene.

NOTES

1. From a general point of view, compulsion may be either legal, by way of mandatory legislation or contractual by agreement between the social partners. If it is contractual, it arises as a rule from membership of an employers' or workers' organisation. Compulsion may apply to the employer, to the employee, or both.

2. The Beveridge Plan published in the United Kingdom during the Second World War gave both the signal and the significance to the modern doctrine of social security. At international level the essential landmarks were the Recommendations No.68 (Income Maintenance) and No.69 (Medical Care) adopted by the International Labour Organisation (ILO) in 1948.

3. Commission of the European Communities. Draft Proposal for a Council Directive on the Coordination of Laws, regulations and administrative provisions relating to institutions for retirement provision. Doc. XV/198/91-EN, Brussels, July 1991 (and subsequent revisions).

4. See for instance: Organisation for Economic Coordination and Development, OECD. *Private Pensions and Public Policy*, Paris, 1992 (ISBN 92-84-13790-4).

5. Many publications provide an insight into the historical factors having influenced pension policy. Among the numerous studies covering an international scene the following deserve mention:
   - *The evolution of social insurance*, 1881-1981 edited by P.A. Köhler and H.F. Zacher in collaboration with Martin Partington published for the Max Planck Institut für ausländisches und internationales Sozialrecht (Munich, 1982) by Frances Pinter, 5 Dryden Street, London (ISBN 0 86187 242 8).
   - Lucien Féraud: *Complementary Pensions, a Comparative Analysis*. International Social Security Association, Studies and Research, No.7, Geneva, 1975.
   - Lucy apRoberts, Emmanuel Reynaud: *Les systèmes de retraite à l'étranger, Etats Unis, Allemagne, Royaume-Uni*. IRES, 1 rue de la Faisanderie, 75116 Paris (ISBN 2-9506473-0-8).
   - International Social Security Association. *Conjugating public and private: the case of pensions*. Studies and Research No.24, Geneva, 1987 (ISBN 92-843-1025-3).

6. A survey, the results of which were published in 1993 by the Department of Social Security in the United Kingdom, set out to find out why employers had made voluntary pension provision for their employees. Respondents identified three main motives: (i) paternalism (people are not naturally good at making provision for their own future and the employer felt obliged to help); (ii) to attract and retain high quality staff, especially white collar workers and (iii) as a reward for loyalty and for long service. See DSS Research Report No.17, *Employer choice of pension schemes*. HMSO Publication Center, London SW8-5DT.

8. Ruellan, Rolande: Retraites: l'impossible reforme est-elle achevée? in: *Droit Social*, no.12, décembre 1993, Paris.

9. In 1993 EUROSTAT launched a second study on replacement rates in order to refine the methodology and, in particular, to respond to such observations as those made in Chapter 2 of the present report.

10. Hughes (1985): *Payroll Tax Incidence; The Direct Tax Burden and the Rate of Return on State Pension Contributions in Ireland*, Dublin: Economic and Social Research Institute, General Research Series Paper No. 120.
Hughes (1994): *Private Pensions in OECD Countries: Ireland*, Paris: OECD, Social Policy Studies No. 13.

11. *EC Citizens and Social Protection. Main results from a Eurobarometer Survey.* Bruxelles, November 1993 (available through Division V/E/2 of the European Commission).

12. At the end of 1993, the press reported allegations that many people had been wrongly advised to transfer their pension rights from a company scheme into a personal pension plan. This mis-selling of personal pensions in the UK, recently uncovered, has attracted the attention of the Securities and Investment Board (SIB), a regulatory body, and caused claims for redress or compensation.

13. Detailed and updated information is found, for instance, in:
- *International Benefits Information Service (IBIS)*, published monthly by Charles D. Spencer Associates Inc., 250 S. Wacker Drive, Chicago IL 60606, United States of America. IBIS also publishes selected country profiles.
- The Wyatt Company. *Benefits Report, Europe, U.S.A.* Published every year. Avenue Herman-Debroux 52, Box 3. 1160 Brussels, Belgium.
- European Actuarial Consultancy Services (EURACS). *EURACS Pension Summaries.* Published every year. Watson House, London Road, Reigate, Surrey RH2 9PQ, United Kingdom.

The three following recent publications contain useful information and analysis on detailed aspects of supplementary pensions in European countries:
- Winfried Schmähl (editor). *The future of basic and supplementary pension schemes in the European Community - 1992 and beyond.* Nomos Verlagsgesellschaft, Baden-Baden 1991. ISBN 3-7890-2491-0.
- *Il risparmio previdenziale e i fondi pensione. A cura di Daniele Pace,* introduzione di Luigi Spaventa. Centro Europa Ricerche/Associazione per lo sviluppo degli studi assicurativi. Editore Franco Angeli, Milano 1993. ISBN 88-204-7774-2.
- European Financial Management and Marketing Association (EFMA). *Pensions at stake, who will make a bid?* Papers of a Conference held in Brussels in June 1993. Distributed by EFMA, 16 rue d'Agnessau, 75008 Paris.

14. Brigitte Hiegemann. *The German Company Pension Insolvency System.* Büro Dr. Heubeck, 53 Lindenallee, 5000 Köln 51, Germany.

15. Irish Association of Pension Funds (1992 and 1993), *IAPF Investment Surveys 1991 and 1992.*

14. Brigitte Hiegemann. *The German Company Pension Insolvency System.* Büro Dr. Heubeck, 53 Lindenallee, 5000 Köln 51, Germany.

15. Irish Association of Pension Funds (1992 and 1993), *IAPF Investment Surveys 1991 and 1992.*

16. In the United Kingdom it is estimated that pension funds own about one-third of all the quoted shares of British industry.

17. Faherty, P. (1993) *Investment Returns in the 1990s.* Paper presented to the Irish Association of Pension Funds seminar.
Heffernan, E. (1991) *Investment of Pension Assets.* Paper presented to the International Benefits Information Service (IBIS) conference, The Hague, May 1991.

18. See in particular: Fourth Council Directive 78/660/EEC of 25 July 1978 based on Article 54(3)(g) of the Treaty on the annual accounts of certain types of companies.

19. For a full analysis of the ECJ's decisions see: *Equality of Treatment between Women and Men in Social Security.* A European conference at Lincoln College, University of Oxford: 4-6 January 1994. Documentation available through Lincoln College.

20. Council Directive 77/187/EEC of 14 February 1977 on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of businesses (OJ no. L 61 of 5.3.77).

21. Council Directive 80/987/EEC of 20 October 1980 on the approximation of the laws of the Member States relating to the protection of employees in the event of insolvency of their employer (OJ no.283 of 28.10.80).

22. A study entitled *'Pension Fund Investment'* by Michael Walsh and John Murray has recently been published in Ireland, which deals with the potential role of pension funds in providing venture and development capital. The report was funded by the Irish Association of Pension Funds, the Irish Association of Investment Managers, the Irish Insurance Federation and the Department of Finance.

23. Commission of the European Communities, DG V: *Social Europe*, 3/92, 'Social Security for Persons Moving within the Community'.

24. Communication from the Commission to the Council: *Supplementary Social Security Schemes: The Role of Occupational Pension Schemes in the Social Protection of Workers and their Implications for Freedom of Movement.* SEC(91)1332 Final.

25. European Commission, Directorate-General XV. Working Paper: *Cross-border membership of occupational pension schemes for migrant workers.* Doc.XV/2040/92/EN, Brussels, 16.9.1992.