

Towards adequate, sustainable and safe European pension systems

Green paper

Social Europe



European Commission

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Directorate-General for Employment, Social Affairs and Equal Opportunities
Unit E.4

Directorate-General for the Internal Market and Services
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1. Introduction

An adequate and sustainable retirement income for EU citizens now and in the future is a priority for the European Union. Achieving these objectives in an ageing Europe is a major challenge. Most Member States have sought to prepare for this through pension reforms.

The recent financial and economic crisis has aggravated and amplified the impact of the severe trend in demographic ageing. Setbacks in economic growth, public budgets, financial stability and employment have made it more urgent to adjust retirement practices and the way people build up entitlements to pensions. The crisis has revealed that more must be done to improve the efficiency and safety of pension schemes⁽¹⁾ which not only provide a means for a decent life in old age but also represent the reward for a lifetime of work.

In his political guidelines for this Commission, President José Manuel Barroso highlighted the importance of adequate and sustainable pensions for strengthening social cohesion:

“Millions of Europeans are wholly dependent on pensions. The crisis has shown the importance of the European approach to pension systems. It has demonstrated the interdependence of the various pension pillars within each Member State and the importance of common EU approaches on solvency and social adequacy. It has also underlined that pension funds are an important part of the financial system. We need to ensure that pensions do the job intended of providing the maximum support to current and future pensioners, including for vulnerable groups.”

Member States are responsible for pension provision: this Green Paper does *not* question Member States' prerogatives in pensions or the role of social partners and it does *not* suggest that there is one 'ideal' one-size-fits-all pension system design. The principles of solidarity between generations and national solidarity are key in this regard. At EU level, national retirement systems are underpinned by a framework of activities spanning from policy coordination to regulation. Some common themes need to be addressed in a coordinated way such as the functioning of the internal market, the requirements of the Stability and Growth Pact, or ensuring that pension reforms

are consistent with the Europe 2020 strategy. Sound and adequate pension systems, enabling individuals to maintain, to a reasonable degree, their living standard after retirement, are crucial for citizens and for social cohesion. The impact of public pension expenditure on public finances in one Member State may have serious repercussions in others. EU policy coordination on pensions has proven useful and necessary to make progress at Member State level. Pension funds are an integral part of financial markets and their design can promote or inhibit the free movement of labour or capital.

Following a decade of reforms that have altered pension systems in most Member States, there is now a need to thoroughly review the EU framework. Demographic ageing has been faster than previously expected and the recent financial and economic crisis had a dramatic impact on budgets, capital markets and companies. There have also been deep structural changes such as new intergenerational balances, shifts from Pay-As-You-Go (PAYG) to funded pensions and the shift of more risks to individuals. This Green Paper launches a European debate through extensive and early consultation on the key challenges facing pension systems and how the EU can support Member State efforts to deliver adequate and sustainable pensions.

This Green Paper takes an integrated approach across economic, social and financial market policies and recognises the links and synergies between pensions and the overall Europe 2020 strategy for smart, sustainable and inclusive growth. It takes into account work by the Economic Policy Committee and the Social Protection Committee on pensions. The Interim Joint Report was noted by the 7-8 June 2010 Council (ECOFIN and EPSCO)⁽²⁾. The goal of generating adequate and sustainable retirement incomes through pension reforms and the goals of Europe 2020 are mutually reinforcing. Europe 2020 emphasises higher and better quality employment and positive transitions: both are decisive for workers (women and men) to accrue pension rights. Its 75% employment target requires employment rates significantly higher than the present levels in the age group 55 to 65. Addressing gaps in pension adequacy, which can be a significant cause of poverty among the elderly, can also contribute to achieving the Europe 2020 poverty reduction target.

(1) The European Parliament is also engaging in a policy discussion on the lessons learnt from the crisis under the auspices of the Special Committee on the Financial, Economic and Social Crisis.

(2) Report available at http://europa.eu/epc/publications/index_en.htm, see Council Conclusions http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/114988.pdf

Policies in many areas can help to reduce poverty in older ages and this will in turn contribute to enhancing adequacy, thus complementing pension reforms. Other goals include tackling bottlenecks in the completion of the single market, for example making the internal market in financial products safer and more integrated and facilitating the mobility of all workers⁽³⁾ and

citizens across the EU⁽⁴⁾. In turn, pension reforms will contribute towards reaching the Europe 2020 goals for employment and long-term sustainability of public finances. Moreover, completing the internal market for pension products has a direct impact on the EU's growth potential and therefore directly contributes towards meeting the Europe 2020 objectives.

⁽³⁾ Including highly mobile workers such as researchers, see Council Conclusions 2 March 2010: http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/intm/113121.pdf

⁽⁴⁾ The Commission will issue a Report on Citizenship in 2010 on the entire life cycle of EU citizens, covering i) obstacles in the effective exercise of citizens' rights, including free movement rights, and ii) the solutions envisaged to remove these obstacles, along with a Roadmap for their adoption.

2. Key challenges

2.1. Demographic ageing

Whilst it is well known that Europe is facing a major demographic challenge⁽⁵⁾, we are reaching a critical stage as the first cohorts of baby boomers are now approaching retirement and Europe's working-age population is set to start shrinking from 2012 onwards.

Living longer than ever before is of course an enormous achievement: over the last 50 years, life expectancy has risen by about five years in the EU. The latest demographic projections⁽⁶⁾ reveal that a further rise of about seven years could materialise by 2060. Combined with low fertility rates this will lead to a dramatic change in the age composition of the population (see figure 1). As a result, the old-age dependency ratio will double: where at present there are four people of working age for every person over 65, by 2060 there will be just two people of working-age for every person over 65 (see figure 2).

There are also other longstanding trends in labour markets: starting full-time working lives later because of the increased need for education and retiring earlier due to labour market age management and prevailing policies. Although the trend of early retirement has started to reverse, most people, and women in particular, still leave the labour market significantly before the typical pensionable age of 65 (see figure 6 and 7), highlighting the gender aspect.

On present trends the situation is untenable. Unless people, as they live longer, also stay longer in employment, either pension adequacy is likely to suffer or an unsustainable rise in pension expenditure may occur. The impact of the demographic challenge as aggravated by the crisis will tend to reduce economic growth and put pressure on public finances. The 2009 Ageing Report⁽⁷⁾ showed that, on account of the shrinking labour force, the only source of growth by 2020 will be labour productivity.

While reforms have already significantly reduced the impact of ageing on future pension costs, age-related public expenditure is still set to increase overall by almost 5 percentage points of GDP by 2060, half of which is due to spending on pensions (see figure 3 for public pension expenditure projections for Member States).

Another longstanding trend is societal change – such as single households, couples without children and different generations of a family living far apart from each other – which is fuelling more formal provision of care services otherwise provided within the family. This poses further challenges to the financing of the cost of health care and long-term care.

Funded pensions could also be affected by demographic ageing. Ageing societies would reduce the potential growth rate of the economy, implying lower real rates of return and this could also affect financial asset prices. Such potentially lower returns on pension fund investments may lead to higher contributions, lower retirement benefits, increased capital outflows to emerging markets or greater risk taking.

Against the background of demographic ageing, the 2001 Stockholm European Council agreed a three-pronged strategy for dealing with the impact on public budgets consisting of:

- * reducing debt rapidly;
- * raising employment rates and productivity; and
- * reforming pension, health care and long-term care systems.

Moreover, the 2001 Laeken European Council agreed a set of common objectives for pensions emphasising the need to make them adequate, sustainable and adaptable⁽⁸⁾.

⁽⁵⁾ Commission communication on Ageing of 29th April 2009 "Dealing with the impact of an ageing population in the EU (2009 Ageing Report)" and Commission staff working document *Demography Report 2008 – Meeting social needs in an ageing society* (SEC (2008) 2911).

⁽⁶⁾ European Commission and Economic Policy Committee (2009) "2009 Ageing Report: Economic and budgetary projections for the EU-27 Member States (2008-2060)", *European Economy*, No 2.

⁽⁷⁾ *Ibid.*

⁽⁸⁾ "Quality and viability of pensions – Joint report on objectives and working methods in the area of pensions" [10672/01 ECOFIN 198 SOC 272].

2.2. Changes in pension systems

While Member State systems differ markedly, a majority have been adapted so as to put them on a more sustainable footing over the past decades. At the same time, Member States have attempted to protect adequacy and to respond better to changes in labour markets and gender roles. Key trends have been ⁽⁹⁾:

1. Encouraging more people to work more and longer so as to obtain similar entitlements as before: increases in pensionable ages; rewarding later and penalising earlier retirement (see figure 8); moves from benefits based on earnings in best years towards entitlement based on working career average earnings; closing or restricting early exit pathways; labour market measures to encourage and enable older workers to stay in the labour market and encouraging greater gender equality in the labour market.
2. The move from largely single to multi-tiered systems. This is a result of the trend in most, but not all, Member States to lower the share of public PAYG pensions in total provision while giving an enhanced role to supplementary, prefunded private schemes, which are often of a Defined Contribution (DC) nature (see figure 10).
3. Measures to address adequacy gaps, e.g. through efforts to broaden coverage, support building up rights, ease access to pensions for vulnerable groups and increase in financial support for poorer pensioners.
4. Gender dimension: women tend to predominate among those with atypical contracts, they tend to earn less than men and tend to take career breaks for caring responsibilities more often than men. As a consequence, their pensions tend to be lower and the risk of poverty tends to be higher among older women, also because they live longer. While periods of care are recognised in some PAYG systems, this is less straightforward in funded pension schemes, with the question of how to finance such solidarity.

Reforms have underpinned recent increases in effective retirement ages and opened new avenues to delivering adequate pensions in a sustainable manner. At the same time, reforms have given and will continue to give rise to greater individual responsibility for outcomes. While people have more choice, they are also exposed to more risk. For reforms to be successful, all pension schemes must deliver their part and risks must be well understood and managed. Future pension adequacy will rest on a combination of returns in financial markets and labour markets delivering opportunities for longer and less broken contributory careers. To strengthen social cohesion, a number of Member States may want to address outstanding issues such as minimum pensions, coverage of atypical workers and crediting of some involuntary employment breaks, for example when caring for frail dependents.

The reformed pension systems increase adequacy risks for a considerable number of workers. Net replacement rates will decline in many Member States, though the starting position and the degree of reduction vary significantly, and some countries, especially those with very low initial levels, have increased them (see figure 5). Delaying labour market exit can reduce the decline.

In many Member States additional reforms may be needed given the scale of demographic changes ahead and to ensure the lasting success of implemented reforms. For Member States where the reform process is not sufficiently advanced, there is an urgent need to review the pension promise in view of what the rest of the economy – and public budgets – can be expected to provide.

2.3. Impact of the financial and economic crisis

The financial and economic crisis has seriously aggravated the underlying ageing challenge. By demonstrating the interdependence of the various schemes and revealing weaknesses in some scheme designs it has acted as a wake-up call for all pensions, whether PAYG or funded: higher unemployment, lower growth, higher national debt levels and financial market volatility have made it harder for all systems to deliver on pension promises. Private schemes can relieve some of the pressure on public pension provision. However, increasing reliance on private schemes has fiscal

⁽⁹⁾ The Interim Joint Report on pensions of the Economic Policy Committee and the Social Protection Committee contains a more detailed assessment, see footnote 2.

costs, given the widespread practice of providing tax incentives during the accumulation phase. The costs of tax relief can be considerable and its effectiveness and redistributive impacts questionable⁽¹⁰⁾. With public budgets under heavy pressure, some Member States are now reconsidering the efficiency of this spending. Better sharing of information on its costs and effectiveness may help policy makers across the EU⁽¹¹⁾. Furthermore, if private schemes cannot deliver their promises, there will inevitably be pressures on the public purse to pick up part of the tab.

With secure incomes from public pensions, which generally have been allowed to perform their role as automatic stabilisers, current pensioners have so far been among those least affected by the crisis. Exceptions apart, benefits from funded schemes still play a marginal role and just a few Member States with very acute public budget problems or well-anchored automatic adjustment mechanisms were compelled to reduce public pensions in payment. But the crisis and lower growth prospects will affect all types of pension schemes.

The scale of fiscal deterioration following the crisis is equivalent to offsetting 20 years of fiscal consolidation, implying that fiscal constraints will be very strong in the next decade. Estimates suggest that the crisis will put further pressure on public pension spending over the long-term because economic growth is set to be considerably lower and there is great uncertainty as to the timing of the full recovery⁽¹²⁾. In a number of Member States some social security contributions were diverted to newly established mandatory funded pensions. The crisis has underscored this double payment problem and has caused a few governments to halt or lower contributions to private pensions to improve public pension finances.

In the short term, the return rates and solvency of funded schemes have been affected through falls in interest rates and asset values: private pension funds lost over 20% of their value during 2008⁽¹³⁾. Moreover several sponsors of occupational pension funds were hindered in their ability to honour their obligations. However, as few schemes had to lock in losses to meet

their current liabilities, supervisors were able to ease valuation and solvency regulations to allow time for markets to recover. Pension funds were able to recoup some of their losses in 2009⁽¹⁴⁾ but many still remain far off the required solvency levels.

Variations in the ability of funded schemes to weather the crisis have demonstrated that differences in design, regulation and investment strategy clearly matter. Losses vary with investment practices and the ability to absorb the shock depends also on how well the burden is shared among providers, contributors and recipients. Unfortunately, schemes in countries where solvency requirements were lower and asset value losses particularly large also tend to have poorer protection of accrued entitlements and the least flexible mechanisms for burden sharing. As a result, entitlements can be lost and providers inclined to discontinue schemes, since they cannot afford to bring schemes back to solvency.

The crisis will also have a serious impact on future pensions as many workers will have lost their jobs and have been unemployed for a certain period and others might have had to accept lower earnings or shorter working hours⁽¹⁵⁾. One of the challenges will be to ensure that adequate levels of pensions can be maintained also in these situations (see figure 9).

The crisis has, therefore, added the following dimensions to the pre-existing reform agenda:

- * a more pressing need to address adequacy gaps;
- * a more pressing need for reforms that improve the sustainability of public finances;
- * an increased emphasis on raising effective retirement ages;
- * a need to revisit the regulation of funded pension schemes to ensure that they are efficient and remain safe in the wake of major financial crises whilst ensuring regulation is proportionate and does not push employers into insolvency or into abandoning pension schemes;
- * a need to ensure that financial market regulation is effective and intelligent given the growing role of pension funds. The G20 Pittsburgh and Toronto summits emphasised that all financial institutions should be regulated and that there is a greater need for common rules.

⁽¹⁰⁾ Section 4.2 p. 26 of SPC Report "Privately managed funded pension provision and their contribution to adequate and sustainable pensions" (2008) <http://ec.europa.eu/social/main.jsp?catId=752&langId=en>

⁽¹¹⁾ This could include sharing experience on approaches such as 'communicating vessels' whereby the amount of tax relief available for voluntary individual savings is inversely related to the amount of statutory and occupational pensions an individual already has. See the "Proposal for a pension model with a compensating layer" by G.J.B. Dietvorst, EC Tax Review 2007 nr.3 p.142-145.

⁽¹²⁾ See footnote 6.

⁽¹³⁾ OECD, "Pensions and the crisis – How should retirement income systems respond to financial and economic pressures" 2009.

⁽¹⁴⁾ OECD "Pension Markets in Focus", October 2009, Issue 6.

⁽¹⁵⁾ Chapters 3.3 – 3.5 of the Interim Joint Report on pensions, see footnote 2.

3. Priorities for modernising pension policy in the EU

The overarching objectives of pension reforms are to ensure that pension systems are adequate and sustainable. There has been a tendency to treat the three-pronged Stockholm strategy as a list from which to pick and choose. But if pension systems are to deliver and if the Europe 2020 strategy is to succeed, it will now be necessary to address all three issues in a coordinated way.

3.1. Overarching objectives: adequacy and sustainability

Adequacy and sustainability are two sides of the same coin. If pensions are at risk of being inadequate, there may be pressure for *ad hoc* increases in pensions or higher demand for other benefits, jeopardising sustainability. Equally if a pension system is unsustainable it will prove to be inadequate in the long run when sudden corrections are needed. The issues of pension adequacy and sustainability need to be considered jointly.

Addressing pension adequacy

Ensuring adequate retirement income is the purpose of pension systems and is a matter of fundamental inter- and intra-generational solidarity. Most reforms of pension systems so far have been aimed at improving sustainability. Further modernisation of pension systems will be needed to address adequacy gaps. As public pension replacement rates in most cases will decline (see figure 4), it is important to provide sufficient opportunities for complementary entitlements: e.g. enabling longer working lives and increasing access to supplementary pension schemes. The lack of compensatory crediting for periods of unemployment, sickness or caring duties can also lead to gaps, as can lack of coverage of vulnerable groups, such as short-term contract and atypical workers, or insufficient minimum pension guarantees or income provision for older people, but these raise questions about financing. In funded schemes, reducing investment risk, notably close to and in the pay-out phase, and improving risk sharing between pension savers and pension providers, building on the advantages of collective insurance, can boost the adequacy of retirement income. Broadening the sources of retirement income beyond pensions may also need to be considered.

Securing sustainability

Many pension reforms have contributed to limiting the increase in future public pension spending, but additional steps are urgently needed to put systems on a more sustainable footing, thereby contributing to the long term sustainability of public finances, notably in countries where future public pension spending is projected to be high. Failing to take resolute policy action to enhance sustainability will push the burden of adjustment forward either to future workers or to future pensioners who might not have prepared for lower than expected pensions, as underlined by the European Council⁽¹⁶⁾. Given the dire state of public finances and the projected unsustainable increase in public debt levels with unchanged policies, fiscal consolidation will be a binding constraint on all policies, including pensions. The Stability and Growth Pact (SGP) provides the framework for monitoring the sustainability of public finances, including pension systems⁽¹⁷⁾. Moreover, there could be further pressure for spending on care for the elderly should formal care increasingly replace informal care in the future. Reforms that enhance the EU's economic growth potential, e.g. by stimulating labour supply, are therefore particularly important. Higher labour productivity growth benefits all citizens, as it enables higher living standards. As regards fiscal sustainability, achieving higher employment rates in particular for older workers is even more important.

- 1. How can the EU support Member States' efforts to strengthen the adequacy of pension systems? Should the EU seek to define better what an adequate retirement income might entail?**
- 2. Is the existing pension framework at the EU level sufficient to ensure sustainable public finances?**

⁽¹⁶⁾ Presidency conclusions of the 23 March 2005 COUNCIL OF THE EUROPEAN UNION 7619/1/05, REV 1, stressed the need "to safeguard the sustainability of public finances in the long run, to promote growth, and to avoid imposing excessive burdens on future generations."

⁽¹⁷⁾ In relation to the SGP the Commission has proposed to also take account of implicit liabilities, notably related to ageing, amongst other factors to reflect future risks (COM(2010) 367/2).

3.2. Achieving a sustainable balance between time spent in work and in retirement

Time spent in retirement has increased considerably over the past century and there are large variations between Member States. Currently, typically about one third of adult life is spent in retirement and this share will increase substantially with future gains in life expectancy⁽¹⁸⁾ unless the length of working life increases and people retire later. Less than 50% of people are still in employment by the age of 60. This goes against Member State commitments at the Barcelona European Council to postpone the age at which people stop working by five years⁽¹⁹⁾. It is also inconsistent with the objective of reaching the Europe 2020 75% employment rate target and impacts negatively on growth potential. The steep rise in old-age dependency ratios could be largely avoided if people would work longer (see figure 2). Without this a painful combination of lower benefits and higher contributions would be inevitable.

Ensuring that the time spent in retirement does not continue to increase compared to time spent working would support adequacy and sustainability. This means increasing the age at which one stops working and draws a pension. Many Member States have already decided to raise the eligibility age for a full pension in their public pension schemes (see figure 6). There is a growing awareness that this represents an important signal to workers and employers, which motivates them to aim for higher effective retirement ages. A number of Member States have demonstrated that a promising policy option for strengthening the sustainability of pension systems is an automatic adjustment that increases the pensionable age in line with future gains in life expectancy. While this approach of contingent adjustments could be contemplated for other risks as well, committing to periodic reviews of the adequacy and sustainability of pensions could be an alternative or complementary way to facilitate a timely and smooth response to changing conditions many of which are hard to predict.

The feasibility of universal pensionable ages has always been debated due to occupational differences in labour market entry ages and the health status of workers in different occupations. Most Member States address this challenge through resolute policies to improve health and safety at work while providing access to pathways for those in real need before the pensionable

age. National efforts are underpinned by the European Health and Safety Strategy. A few Member States have acknowledged differences in entry ages by combining measures to increase pensionable ages with those increasing the number of contributory years required for a full pension. Furthermore, whilst taking measures to extend working lives, it will also be important to address issues such as gender gaps in both pay and the labour market.

As labour market exit ages are still low, the question is whether common EU principles and pathways to adequate and sustainable pensions, applied in a differentiated manner, to cater for differences in pension systems, would be helpful? Such pathways would aim to enable people to build adequate entitlements whilst also making EU economies more sustainable. This requires pension system reforms to be supplemented with substantial efforts to allow workers to maintain their employability throughout their working lives, offering appropriate retraining opportunities. New technologies and services to provide flexible work arrangements through telework and upgrading of skills can help to accommodate older workers in the workplace for longer.

Key measures enabling older workers, both women and men, to remain longer in the labour market would include access for all, irrespective of age, gender and ethnicity, to labour markets, to training and disability adjustments⁽²⁰⁾. The European Social Fund supports measures to improve the employability and raise the employment rates of women and men of all working ages. The Commission is preparing a European Year on Active Ageing 2012 which should encourage Member States, social partners and other stakeholders to create better opportunities and working conditions for the participation of older workers in the labour market.

This could involve adapting social and financial incentives to work, including Member States examining the role of their tax rules. Other measures could include adjusting age management, working arrangements and attitudes in labour markets and work-places, and considering conditions for older self-employed workers. Prolonging working lives to reflect continuous gains in life expectancy over time would bring a double dividend: higher living standards and more sustainable pensions. In order to achieve more sustainable and adequate pensions, it is important that workers, and very often younger ones, spend more time in jobs with wages and working hours entitling them to future pension rights.

⁽¹⁸⁾ Chapter 3.2.1 of the Interim Joint Report on pensions, see footnote 2.

⁽¹⁹⁾ Presidency conclusions of the 15-16 March 2002 EUROPEAN COUNCIL SN 100/1/02 REV 1.

⁽²⁰⁾ A better transposition and application of the Employment Equality Directive (2000/78/EC) and the realisation of the added value of older staff is needed. Age is the most common perceived disadvantage when seeking a job, see http://ec.europa.eu/public_opinion/archives/ebs/ebs_317_en.pdf

Member States are already taking measures to support longer working lives⁽²¹⁾. Health policies aimed at helping citizens age in better health can contribute to extending working lives, reduce pressure on pension systems and can improve sustainability⁽²²⁾. Poor health is one of the drivers of early retirement.

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

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

3.3. Removing obstacles to mobility in the EU

Policies and regulation need to facilitate the free movement of production factors, notably labour and capital, so as to use resources efficiently and create favourable conditions to maximise incomes. Greater flexibility in job mobility supports the adjustment capacity of the economy and strengthens the European social model. Unleashing the full potential of the single market could bring significant benefits for all citizens⁽²³⁾.

3.3.1. Strengthening the internal market for pensions

The adoption of the Directive on Institutions for Occupational Retirement Provision (IORP) in 2003 was a major achievement. But this Directive only covers those funded pensions that are occupational in nature and not even all occupational schemes fall under its scope (e.g. book reserve schemes are excluded). It is not a framework directive, which makes it difficult to adapt regulation to market changes. First experience has shown that there are still considerable barriers to cross-border activity. They prevent the full realisation of efficiency gains arising from scale economies and competition, thereby raising the cost of pensions and restricting consumer choice. Barriers are in many cases the result

of regulatory differences and legal uncertainties, such as an unclear definition of cross-border activity, a lack of harmonisation of prudential regulation and complex interaction between EU regulation and national law. Removing these obstacles may require a review of the IORP Directive, further supervisory convergence and more transparency about national differences. Moreover, aspects concerning custodianship⁽²⁴⁾ and pension fund governance need to be addressed, including an adequate understanding and supervision of investment decisions, remuneration, incentive structures for service providers and socially responsible investment (SRI).

Appropriate and comparable accounting standards are important to enhancing transparency about pension liabilities. The International Accounting Standards Board (IASB) has undertaken a project to review its pension accounting standard IAS 19⁽²⁵⁾. The European Commission jointly with its technical advisor, the European Financial Reporting Advisory Group (EFRAG), closely monitors the IASB project to improve pension accounting, possibly also for pension funds themselves, in accordance with the endorsement process established under the IAS Regulation⁽²⁶⁾.

The free movement of capital is facilitated by Member States giving the same tax treatment to dividends and interest received by IORPs investing in their territory but established elsewhere in the European Economic Area (EEA). Following the Commission's decision to launch infringement action against several Member States because of discriminatory features of their tax rules in this area, some Member States have already aligned their pension's tax legislation with the requirements of EU law.

Although the Internal Market for insurance products has been in place for a longer time, cross-border activity for life assurance products has also remained limited, representing well below 10% of total life assurance premiums written in most Member States. The Internal Market could also be helpful in extending access to additional sources of retirement income beyond pensions, such as reverse mortgages. There have also been calls to create a regulatory framework for an EU-wide private pension regime alongside the existing pension regimes in Europe⁽²⁷⁾.

⁽²⁴⁾ See Commission report on some key aspects concerning Directive 2003/41/EC on the activities and supervision of institutions for occupational retirement provision (IORP Directive) of 30.4.2009, COM(2009) 203, available at http://ec.europa.eu/internal_market/pensions/docs/legislation/iorp_report_en.pdf

⁽²⁵⁾ IAS 19 Employee Benefits applies to the sponsoring undertakings.

⁽²⁶⁾ IAS Regulation 1606/2002.

⁽²⁷⁾ The Monti Report also suggests an option to explore the 28th regime for supplementary pension rights, see A NEW STRATEGY FOR THE SINGLE MARKET AT THE SERVICE OF EUROPE'S ECONOMY AND SOCIETY, Report to the President of the European Commission José Manuel Barroso by Mario Monti, 9 May 2010, p.58.

⁽²¹⁾ Chapter 2.1 of the Interim Joint Report on pensions, see footnote 2.

⁽²²⁾ See Commission Staff Working Document SEC(2010)830.

⁽²³⁾ See footnote 22 for more information on the current EU framework on pensions.

5. In which way should the IORP Directive be amended to improve the conditions for cross-border activity?

3.3.2. Mobility of pensions

EU Regulations on the coordination of social security systems have been protecting pension rights of mobile EU citizens and their family members for the past five decades. The new Regulations 883/2004 and 987/2009 expand this protection and ensure that for the accrual of pension rights, insurance periods acquired in another Member State will be taken into account. These Regulations are limited to statutory and occupational pension schemes where rights are based on legislation: recent national reforms as outlined above may thus require an extension of the coordination regulations and minimum standards to improve mobile workers' access to supplementary pension rights within and between Member States.

The Commission proposed a Directive in 2005 to set minimum standards for the acquisition, preservation and transferability of supplementary pension rights. Internal mobility was included because a separation of internal and external mobility was impractical.

The proposal was revised by the Commission in 2007 to drop the transferability element which had been opposed by some as technically difficult and potentially burdensome or open to abuse. This left the emphasis on the timely acquisition of pension rights and their subsequent preservation. However, it has still not been possible to achieve the unanimity needed in the Council to pass the Directive.

Fresh impetus is needed to reach a solution for all mobile workers⁽²⁸⁾. In today's labour market, with the added challenges from the financial and economic crisis, people need to be able to change jobs easily throughout their working life and employers should be able to recruit the right person with the right skills. Further need for action comes from the rise in the importance of funded pensions in diverse forms. This raises the issue of scope: e.g. should statutory mandatory funded schemes be included in EU measures?

Some Member States operate pension tracing services which help people keep track of their pension rights from different sources within that Member State. Given the growing degree of labour mobility and reliance on a broader set of public and private sources of retirement

income, an EU level tracking system could help mobile individuals keep track of their pension rights.

Discriminatory tax rules can be an obstacle to the mobility of pensions. The Court of Justice has ruled that it is contrary to EU law to tax transfers of pension capital from domestic pension funds to funds established elsewhere in the EEA if transfers of pension capital between domestic pension funds are tax free⁽²⁹⁾. The Commission intends to examine whether there are any other Member States with similar rules.

6. What should be the scope of schemes covered by EU level action on removing obstacles for mobility?

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

3.4. Safer, more transparent pensions with better awareness and information

Safety in pensions is important to support adequacy. Moreover, the macroeconomic benefits can be felt quickly as pensioners are a growing source of stable and regular consumption. The disparate developments in Member States' pension systems and the trend towards DC schemes, however, raise new policy questions.

3.4.1. Closing gaps in EU regulation

As pension provision moves from single to multi-tiered systems and from simple to complex pension packages, the fragmented and incomplete character of the present European framework may no longer be sufficient.

1. Reforms have led to some funded pension schemes, both public and private, being covered by EU regulation in some Member States but not in others. This is not consistent with the relevant G20 Pittsburgh declaration ("13. [...] All firms whose failure could pose a risk to financial stability must be subject to consistent, consolidated supervision and regulation with high standards. [...]"), as reinforced at the G20 Toronto summit, nor

⁽²⁸⁾ For example, setting up a cross-border EU pension fund for highly mobile workers (e.g. researchers) could be an option. See "Feasibility Study of a Pan-European pension fund for EU researchers", Hewitt Associates on behalf of the European Commission (DG RTD), May 2010.

⁽²⁹⁾ *Commission vs. Belgium*, Case C-522/04.

does it reflect the fact that pension funds have become major players in financial markets.

2. Similar pension schemes are covered by different EU rules thus raising issues of consistency.
3. There are unclear boundaries between: social security schemes and private schemes; occupational and individual schemes; and voluntary and mandatory schemes.
4. It is not always clear what differentiates general saving from pensions. This raises the question whether the label 'pension' should not be restricted to a product that has certain features such as security and rules restricting access including a payout design which incorporates a regular stream of payments in retirement.

Moreover, the trend towards DC schemes, away from defined benefit (DB) schemes, is continuing. The aim of tying employees to the company through occupational pension promises is losing ground: employers are less reliant on firm-specific skills due to technological advances and employees are increasingly preferring flexibility and mobility. Furthermore, while occupational DB schemes provide greater certainty about future retirement income and reduce costs because of their size and risk sharing, they can be an untenable burden on employers.

Today, nearly 60 million Europeans are enrolled in DC schemes⁽³⁰⁾. Such schemes are much more prevalent today than they were a decade ago and will continue to grow in importance. The sponsor does not bear the financial risk and DC schemes are more likely to promote longer working lives. But a key implication is that they shift the investment, inflation and longevity risks to scheme members, who are less well placed to bear these risks individually. There are, however, ways to reduce these risks. Minimum return guarantees and life-styling portfolio compositions come at a cost but good practice across Member States has shown that they can reduce short-term volatility. Market performance can be enhanced by good economic and public finance policies and better regulation. Better investment practice and scheme design can substantially mitigate risk and increase capacity for shock absorption thus achieving a better balance between risks, security and affordability for both savers and providers.

Collective risk sharing through hybrid schemes, such as a DC scheme with a minimum return guarantee

or a part-DB and part-DC scheme, could change the current trend to individualised DC schemes. Moreover, high quality schemes are being promoted by industry initiatives. Some occupational DB schemes have also adapted to demographic and structural changes by increasing risk sharing between sponsors, workers and pensioners. Existing collective governance structures in DB schemes facilitate this. Examples include moving from final salary to career average schemes, establishing cash balance schemes, allowing for longevity adjustments, changing accrual rates, adjusting the normal pension age, and applying conditional indexation.

International policy discussions raise the question whether current EU regulation is able to cope with the shift towards DC schemes⁽³¹⁾. A reassessment of the IORP Directive may be required in areas such as governance, risk management, safekeeping of assets, investment rules and disclosure. In addition, the current EU framework does not address the accumulation phase. This includes (i) plan design to mitigate short-term volatility in returns and (ii) investment choice and default investment options. Moreover, given that the size of the pension in DC schemes can depend on the year in which the pensioner retires, market regulation needs to address the payout phase such as rules on purchasing an annuity (e.g. whether it is mandatory or voluntary, and the timing).

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

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

3.4.2. Improving the solvency regime for pension funds

The IORP Directive's minimum prudential requirements include solvency rules for DB schemes. These solvency rules are currently the same as those that apply to life assurance undertakings. With the entry into force of the Solvency II Directive in 2012, insurance undertakings will be able to benefit from a three-pillar, risk-based solvency regime and the question is

⁽³⁰⁾ EFRP survey on DC pensions 2010.

⁽³¹⁾ OECD Pension Market in Focus Oct. 2009.

whether this new regime should also apply to IORPs. There is little agreement among stakeholders, partly reflecting the difference in the ways occupational pensions are delivered: book reserve, pension fund or insurance contract.

As regards pension funds, Member States have also taken different approaches to protecting acquired pension rights⁽³²⁾. The Commission conducted a consultation on this subject in 2008 and organised a public hearing in May 2009. During this process, stakeholders signalled that there needs to be a *sui generis* solvency regime for pension funds and that it is important to avoid pro-cyclical solvency rules. The Solvency II approach could be a good starting point, subject to adjustments to take account of the nature and duration of the pension promise, where appropriate. The suitability of Solvency II for pension funds needs to be considered in a rigorous impact assessment, examining notably the influence on price and availability of pension products.

A related question is whether, reflecting developments in banking, insurance and investment, there is a need for promoting pension benefit guarantee systems in the Member States, possibly coordinated or facilitated at EU level. Such systems can not only address failures in sponsor-backed DB schemes or book reserve schemes, but could also compensate for excessive losses in DC schemes. There are, however, important aspects to address such as moral hazard and potential implicit public support in very turbulent times.

10. What should an equivalent solvency regime for pension funds look like?

3.4.3. Addressing the risk of employer insolvency

Given the important role of sponsoring undertakings in the provision of benefits and the funding of IORPs, their insolvency presents a particular risk. The Insolvency Directive⁽³³⁾ provides for the protection of employees' rights to supplementary occupational pensions in the event of the insolvency of their employer. However, there is no obligation on the Member State to fund the rights nor do full guarantees need to be provided, thus leaving considerable latitude on the level and modalities of protection. Moreover, the IORP Directive does not apply to companies using book reserve

schemes for the payment of retirement benefits to their employees. The need to ensure the protection of supplementary occupational pensions in those instances becomes more acute in the present situation, since the financial and economic crisis will increase the number of company insolvencies.

The Commission presented a Staff Working Document⁽³⁴⁾ on the implementation of the provision concerning supplementary occupational pensions contained in the Insolvency Directive. As a follow-up to this document, the Commission has launched a study in 2009⁽³⁵⁾ covering DB and book reserve schemes and is currently gathering information on the protection of unpaid contributions to DC schemes in case of employer insolvency.

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

3.4.4. Facilitating informed decisions

The trend towards DC schemes underlines the need for transparent and clear communication. The IORP and the Life Directives contain information disclosure requirements. But these provisions are based on minimum harmonisation and national approaches differ markedly. Moreover they were designed for DB schemes and may therefore need to be adjusted. In going forward, it would seem important to review the key information specifically for pension schemes and products (e.g. risk, nature of promise, cost/fees, payout method, etc.). This should take into account what is being developed for other financial products, seeking to ensure comparable information. Consumer testing combined with economic research could be used to improve the quality of information in terms of clarity and comparability.

Shifting choice and responsibility to the individual requires that people understand the information in order to make informed choices, especially as pensions have become more complex. Financial education can help as demonstrated by the work of the OECD and the EU already works with Member States on this. Financial education complements regulation of the industry, both prudential (e.g. the IORP Directive) and market conduct rules, and product disclosure rules. It is important that individuals are properly equipped with economic literacy and planning skills to adequately assess their need for financial and

⁽³²⁾ Security mechanisms used today rely on a realistic valuation of technical provisions, own funds, sponsor covenants, pension protection funds or a combination of those elements (CEIOPS SSC report).

⁽³³⁾ 2008/94/EC.

⁽³⁴⁾ SEC(2008) 475, 11.4.2008.

⁽³⁵⁾ OJ 2009/ S 230-329482.

social protection and to avoid behavioural biases. For example, with the growing importance of DC schemes people need to make informed decisions about investments. It is also important that people have a competent body to turn to that can answer their questions relating to pensions, especially in a cross-border mobility context.

At the same time, national experiences suggest that the engagement rate that can be obtained through disclosure and financial education has an upper limit. It is therefore important to envisage an in-depth examination of the merits of auto-enrolment with opt-out clauses.

Informed decisions go hand in hand with adequate pension provision. When making saving decisions it is important that individuals be offered appropriate options. There could therefore be a case for defining what exactly the desirable features of pensions are:

if they lack certain key characteristics, not only could this lead to confusion, but it could also lead to under provision in retirement, for example if early withdrawals lead to a depletion of savings or if no steady income is generated from the accumulated assets. Member States may consider putting in place a reliable pensions advice service to facilitate consumer choices.

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

13. Should the EU develop a common approach for default options about participation and investment choice?

4. Improving EU statistics on pensions

Data about pension systems available from the different national and EU-level sources could be streamlined to increase their comparability and make substantial cost savings. Building on existing international work (e.g. the OECD) and various EU initiatives, the development of an EU methodology for pension statistics could facilitate the assessment of the common policy and regulatory challenges. Pension funds are important institutional investors and their investment behaviour can affect financial stability. Citizens would benefit from the

collection of accurate statistics about their retirement income from the different sources. Pensioners are set to grow as a group of consumers and firms would benefit from reliable and timely information about total disposable income.

Furthermore, the monitoring of implicit liabilities could be strengthened to allow for a better assessment of the impact on the sustainability of public finances of pension schemes run by both public and private entities.

5. Enhancing governance of pension policy at EU level

Europe must help address citizens' concerns about future pensions and revisit how a strategy can be defined to deliver adequate, sustainable and safe pensions, including through better use of EU instruments.

Whilst Member States generally are responsible for the design and organisation of their pension systems, some specific areas relating to pensions fall directly within the EU's competencies. Member States have also recognised that acting together can be more effective and efficient and that the EU level can add value, not least since the challenges are similar across the EU and reform policies need to be consistent with existing frameworks such as the Stability and Growth Pact and Europe 2020.

As part of this strategy, the EU contributes with measures such as surveillance, coordination and mutual learning. Examples include best practice sharing, peer reviews, agreeing objectives and indicators, and gathering comparable statistics. EU regulation covers social security coordination of public pensions, rules for occupational pension funds, portability and the protection of supplementary pension rights in the event of the insolvency of the employer, as well as rules for life assurance undertakings.

If the EU is to offer appropriate support to national reform efforts, the framework of policy coordination

must take an integrated approach to reflect the increasing complexity of pension systems. Moreover, given increasing economic and financial integration, the EU-level regulatory framework, as well as good coordination across the EU level policies and Member States' policies, is becoming ever more important.

Pension policy is a common concern for public authorities, social partners, industry and civil society at national and at EU level. A common platform for monitoring all aspects of pension policy and regulation in an integrated manner and bringing together all stakeholders could contribute to achieving and maintaining adequate, sustainable and safe pensions. The Commission is therefore keen to explore how this can best be achieved in support of the EU's wider economic and social objectives.

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

6. How to respond to the consultation

The Commission invites all interested parties to respond to the questions set out in this Green Paper, together with any additional comments, **by 15 November 2010** by means of the online questionnaire available at:

<http://ec.europa.eu/yourvoice/ipm/forms/dispatch?form=pensions>

Alternatively, for those without web access, responses can be sent by post to:

European Commission
Directorate-General for Employment, Social Affairs & Equal Opportunities
Green Paper on Pensions consultation
Unit E4
rue Joseph II
Office J-27 1/216
B - 1040 Brussels

Please note, received contributions, together with the identity of the contributor, will be published on the Internet, unless the contributor objects to publication of the personal data on the grounds that such publication would harm his or her legitimate interests. In this case the contribution may be published in anonymous form. Otherwise the contribution will not be published nor will, in principle, its content be taken into account.

7. Glossary

Accumulation phase – Period during which contributions are made and invested in a defined contribution scheme. (See also: Defined contribution (DC) schemes).

Accrual rate – Rate at which future pension benefits are built up. It is used in defined benefit schemes and based on the formula linked to the scheme. For example, a pension accrual rate could be 1.5% of final pensionable salary for each year of pensionable service (See also: Defined benefit (DB) schemes).

Annuity – A financial contract, sold by a life insurance company for example, that guarantees a fixed or variable payment of income benefit (monthly, quarterly, half-yearly, or yearly) for the life of a person(s) (the annuitant) or for a specified period of time. It differs from a life insurance contract which provides an income to the beneficiary after the death of the insured. An annuity may be bought on instalments or by paying a single lump sum. Benefits may start immediately or at a pre-defined time in the future or at a specific age. An annuity is one way of securing a regular retirement income for individuals who have saved in a defined contribution scheme. (See also: Defined contribution (DC) schemes).

Automatic (or auto-) enrolment – Generally refers to employees being members of their employer's pension scheme as a default choice, with the possibility of opting out on request.

Automatic adjustment mechanisms – Generally refers means of adjusting benefits, rights and/or contribution levels to changing circumstances, e.g. economic conditions, financial market returns or longevity assumptions.

Book reserve pension scheme – A method of accounting used by some sponsoring employers to finance pension promises. Sums are entered in the balance sheet of the scheme sponsor as reserves or provisions for scheme benefits. Some assets may be held in separate accounts for the purpose of financing benefits, but they are not legally or contractually pension plan assets. (See also: Defined benefit (DB) schemes).

Career average scheme – A defined benefit scheme where the future pension benefit earned for a specific year depends on the level of the member's earnings for the given year. (See also: Defined benefit (DB) schemes).

Cash balance schemes – A scheme where the employer guarantees a pension pot to scheme members, payable at the normal pension age, with which they can purchase an annuity. (See also: Normal pension age; Annuity).

Conditional indexation – Refers to defined benefit schemes where the provision of indexed benefits (generally revalued to inflation or wages) is conditional on the financial performance of the scheme's investments. (See also: Defined benefit (DB) schemes).

Defined benefit (DB) schemes – Pension schemes where the benefits accrued are linked to earnings and the employment career (the future pension benefit is pre-defined and promised to the member). It is normally the scheme sponsor who bears the investment risk and often also the longevity risk: if assumptions about rates of return or life expectancy are not met, the sponsor must increase its contributions to pay the promised pension. These tend to be occupational schemes. (See also: Defined contribution (DC) schemes).

Defined contribution (DC) schemes – Pension schemes where the level of contributions, and not the final benefit, is pre-defined: no final pension promise is made. DC schemes can be public, occupational or personal: contributions can be made by the individual, the employer and/or the state, depending on scheme rules. The pension level will depend on the performance of the chosen investment strategy and the level of contributions. The individual member therefore bears the investment risk and often makes decisions about how to mitigate this risk. (See also: Defined benefit (DB) schemes).

Effective retirement age – Age at which an individual actually retires. Not necessarily the same as the labour market exit age or normal retirement age. (See also: Labour market exit age, and Normal pension age).

Equity Release Scheme – Term used to describe both the process and the products that allow homeowners to secure substantial lump sums or regular income payments by realising part of the value of their homes, while being able to continue to live in it.

Final salary scheme – A defined benefit scheme where the pension benefit is typically based on the last or the last few years' of earnings before retirement. (See also: Defined benefit (DB) schemes).

Funded scheme – A pension scheme whose benefit promises are backed by a fund of assets set aside and invested for the purpose of meeting the scheme's liability for benefit payments as they arise. Funded schemes can be either collective or individual. (See also: Pay-As-You-Go schemes).

Governance (of pension funds) – The operation and oversight of a pension fund. The governing body is responsible for administration, but may employ other specialists, such as actuaries, custodians, consultants, asset managers and advisers to carry out specific operational tasks or to advise the scheme administration or governing body.

Hybrid pension scheme – In a hybrid scheme, elements of both defined contribution and defined benefits are present or, more generally, the risk is shared by the scheme's operator and beneficiaries.

Individual pension scheme – Access to these schemes does not depend on an employment relationship. The schemes are set up and administered directly by a pension fund or a financial institution acting as pension provider without the involvement of employers. Individuals independently purchase and select material aspects of the arrangements. The employer may nonetheless make contributions to individual pension schemes. Some schemes may have restricted membership.

Information disclosure regulations – The rules prescribing the periodicity, procedure, type and extent of information to be provided to members of pension plans and/or the supervisory authority.

Institutional investor – Generally refers to a group of investors such as pension funds, insurance companies, investment funds and, in some cases, banks.

Labour market exit age – Age at which an individual actually leaves the labour market. For data availability reasons labour market exit age is often used as a proxy for the effective retirement age. Differences between the two may exist, as some people leave the labour market before they actually retire while others continue working after retirement. (See also: Effective retirement age).

Lifestyling or life-cycling strategies – Investment strategies used in defined contribution pension schemes to reduce investment risk and volatility by gradually and automatically reducing the investment risk taken by the scheme member as they approach retirement. (See also: Defined contribution (DC) schemes).

Minimum return guarantees – Minimum level of pension benefit paid out regardless of investment performance in a defined contribution scheme.

Normal pension age – Age at which a member of the pension scheme is eligible to receive full pension benefits.

Occupational schemes – A pension plan where access is linked to an employment or professional relationship between the plan member and the entity that sets up the plan (the plan sponsor). Occupational pension schemes may be established by employers or groups of employers (e.g. industry associations) or labour or professional associations, jointly or separately, or by self-employed persons. The scheme may be administered directly by the sponsor or by an independent entity (a pension fund or a financial institution acting as pension provider). In the latter case, the sponsor may still have responsibility for overseeing the operation of the scheme.

Old-age dependency ratio – Population aged over 65 as a percentage of the working age population (usually defined as persons aged between 15 and 64).

Operational risk – The risk of loss arising from inadequate or failed internal processes, personnel or systems, or from external events.

Own funds (regulatory) – Refers to the additional assets of a pension funds above its technical provisions serving as a buffer. Regulation usually requires that these assets are free of all foreseeable liabilities and serve as a safety capital to absorb discrepancies between anticipated and actual expenditure and profits. Also referred to as regulatory capital. (See also: Technical provisions).

Pay-As-You-Go (PAYG) schemes – Pension schemes where current contributions finance current pension expenditure (See also: funded schemes).

Payout phase or decumulation phase – Period during which assets accrued in the accumulation phase are paid out to the pension scheme member in a funded scheme. An example of a payout phase is a period in which regular retirement income is received through the purchase of an annuity. (See also: Annuity).

Pension benefit guarantee system – An arrangement to pay compensation to members or beneficiaries of pension schemes in the event of insolvency of the pension fund and/or sponsoring employer. Examples of a pension benefit guarantee systems include the Pensions-Sicherungs-Verein Versicherungsverein auf Gegenseitigkeit (PSVaG) in Germany and the Pension Protection Fund in the UK.

Pension pillar – Different types of pension schemes are usually grouped into two, three, four or more pillars of the pension system. There is however no universally agreed classification. Many pension systems distinguish

between statutory, occupational and individual pension schemes, or between mandatory and voluntary pension schemes. Participation in occupational and individual pension schemes, usually private pension arrangements, can be mandatory or voluntary.

Replacement rate – Generally refers to an indicator showing the level of pension income after retirement as a percentage of individual earnings at the moment of take-up of pensions or of average earnings. Replacement rates measure the extent to which pension systems enable typical workers to preserve their previous living standard when moving from employment to retirement.

Solvency – The ability of a pension scheme's assets to meet the scheme's liabilities. The scheme's liabilities cover all future pension payments and must therefore be discounted well into the future, thus making substantial assumptions about longevity. The value of a scheme's assets is dependent on the type of accounting standard used. If a scheme is not deemed to have a sufficiently high solvency level, it needs to consider whether to increase contribution levels or reduce entitlements, where scheme rules permit.

Sponsor covenant – Refers to a sponsoring employer's ability to support pension fund volatility by providing additional funding if required. The 'covenant' in this

context is a very similar concept to 'creditworthiness' for borrowers. At a simple level, if a pension fund has a deficit then it is in many respects similar to a bond holder in financial market terms. It depends on the ability of the company to pay additional contributions in the future if investment returns are not sufficient to make up the shortfall.

Statutory pension scheme – Social security and similar statutory programmes administered by the general government (that is central, state, and local governments, plus other public sector bodies such as social security institutions). Public pension plans have traditionally been of the PAYG type.

Supplementary pension schemes – Mandatory or voluntary pension schemes which generally provide additional retirement income to the statutory pension scheme.

Technical provisions – The amount of liabilities corresponding to the financial commitments of a pension fund which arise out of its portfolio of existing pension contracts. See also Article 15 of Directive 2003/41/EC.

Transferability – The right to transfer accrued benefits or accumulated capital from one pension scheme to another, for example to the pension scheme of the new employer.

8. Statistical annex

Figure 1: Demographic structure of the population in 2008 and 2060

Figure 2: Old-age dependency ratios under different average exit age scenarios

Figure 3: Change in public pension expenditure as a share of GDP over 2007-60 (in percentage points)

Figure 4: Benefit ratios in EU Member States in 2007 and 2060

Figure 5: Change in theoretical replacement rates for an average wage earner retiring at 65 after 40 years career between 2006 and 2046 in percentage points

Figure 6: Standard pension eligibility age and average labour market exit age in EU-27

Figure 7: Overall, female and older workers employment rates in EU-27, 2000-2008, in percent

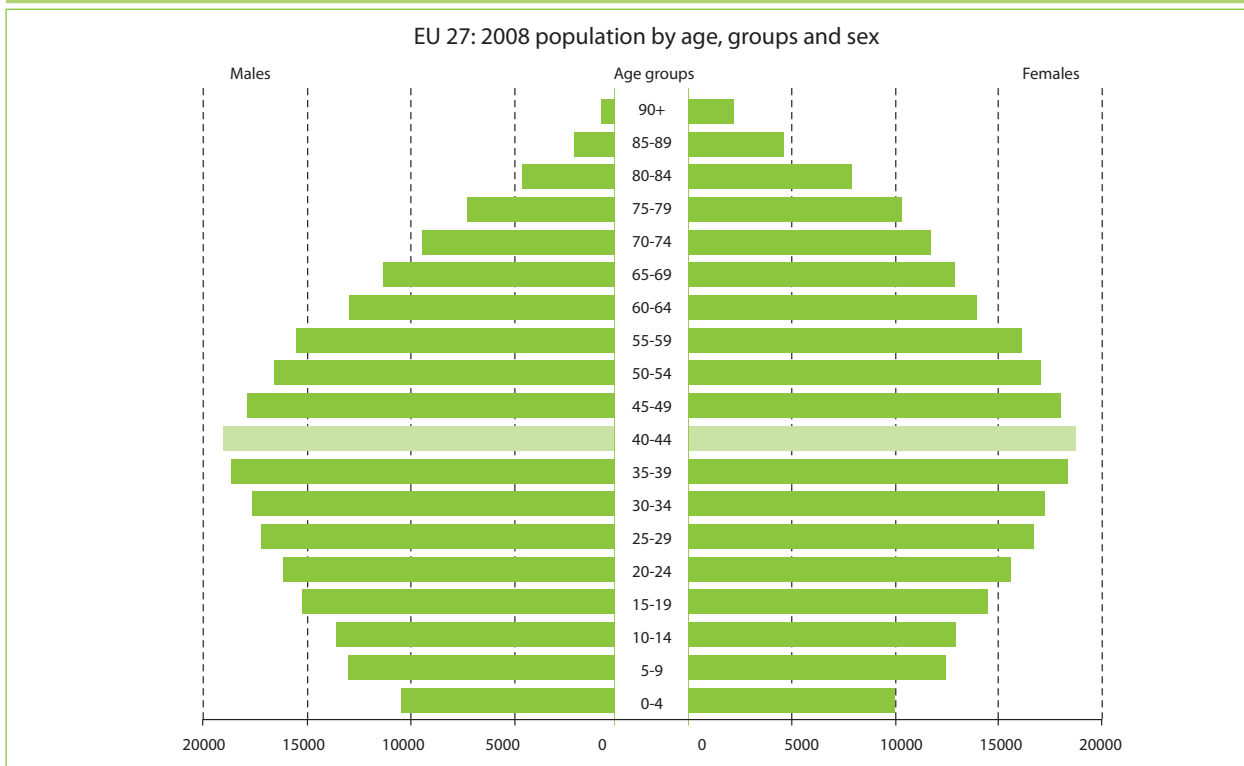
Figure 8: Pension benefit impact of shorter and longer working lives

Figure 9: Pension benefit impact of career breaks due to unemployment

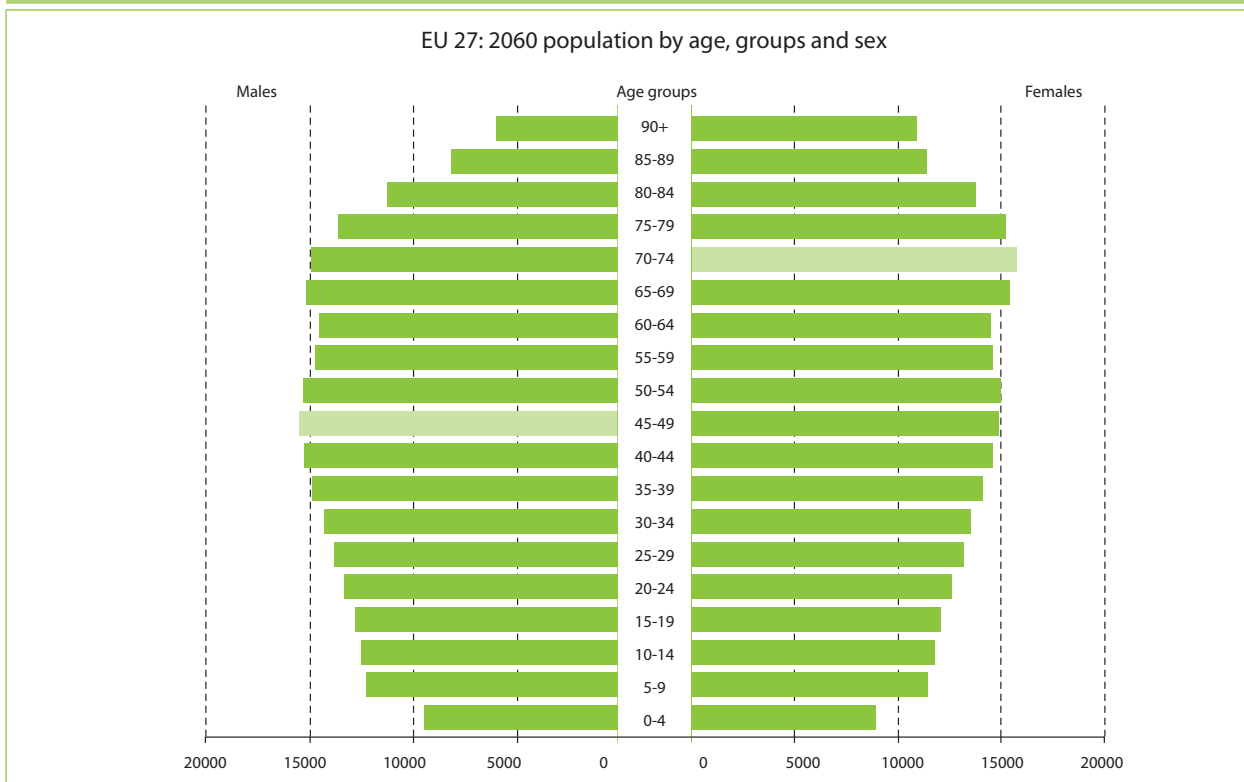
Figure 10: Increasing significance of funded pensions

Figure 1: Demographic structure of the population in 2008 and 2060

2008



2060

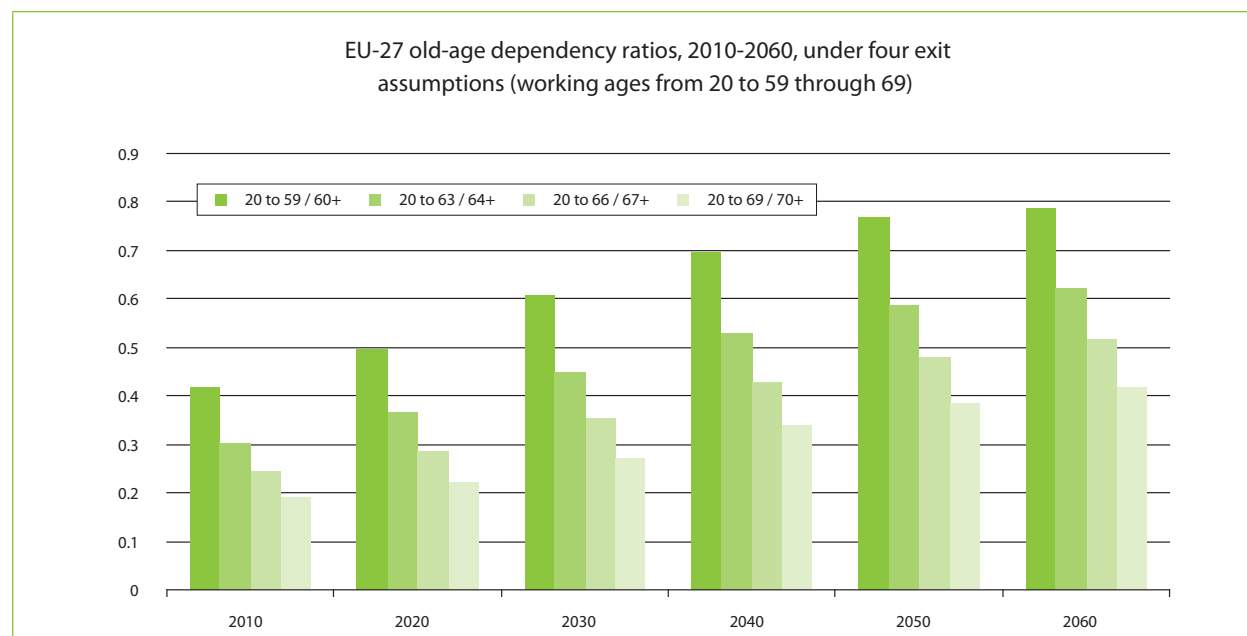


Source: Commission services, graph published in the 2010 Interim Joint Report on pensions of the Economic Policy Committee and Social Protection Committee, noted by the 7-8 June 2010 EPSCO and ECOFIN Councils, p. 9, available at: http://europa.eu/epc/publications/index_en.htm

Note: the light green bar indicates the most numerous cohort.

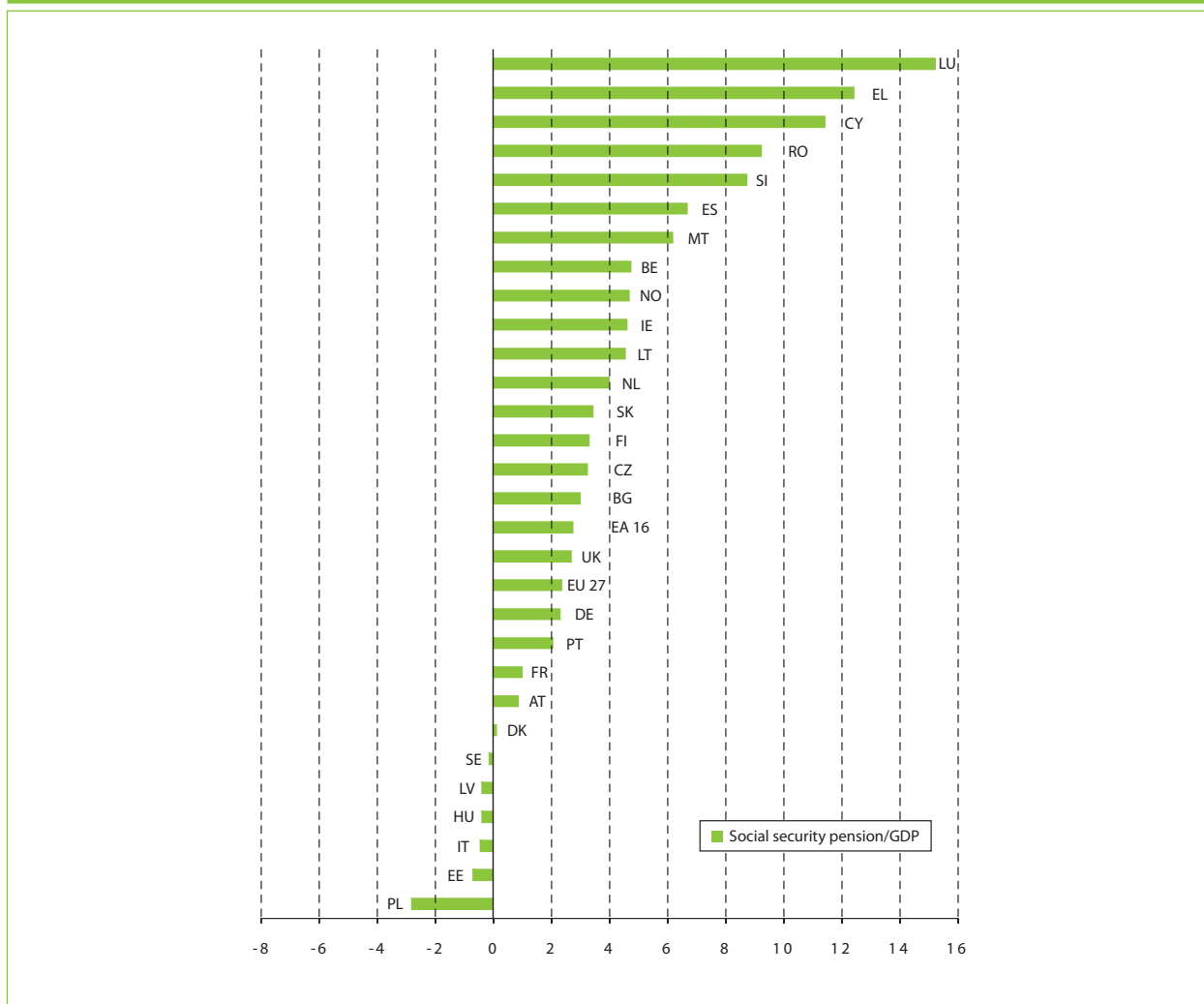
Figure 2: Old-age dependency ratios under different average exit age scenarios

In 2010, when it is assumed that people leave the labour market on average at age 60, the dependency ratio, i.e. the number of people of working age relative to the number of people above age 60, amounts to 5 to 2. If by 2040 people were to remain until 67 the corresponding ratio would stay constant and the increase by 2060 would far less dramatic than at lower exit ages. There would be no increase if the exit age would increase another 3 years between 2040 and 2060.



Source: Eurostat, Population Projections, 2008 data.

Figure 3: Change in public pension expenditure as a share of GDP
over 2007-60 (in percentage points)



Source: Ageing report 2009, available at:

http://ec.europa.eu/economy_finance/publications/publication13782_en.pdf, data as updated at the Ageing Working Group in 2010.

Note: Hungary reformed its pension system in 2009. Following the reform, its impact was assessed through a peer review by the AWG, and endorsed by the EPC at their 22 February 2010 meeting. According to the revised pension projections, public pension expenditure is projected to decrease from 10.9% of GDP in 2007 to 10.5% of GDP in 2060, i.e. by 0.4 p.p. of GDP, compared with the projection in the 2009 Ageing Report, where an increase of 3 p.p. of GDP between 2007 and 2060 was projected.

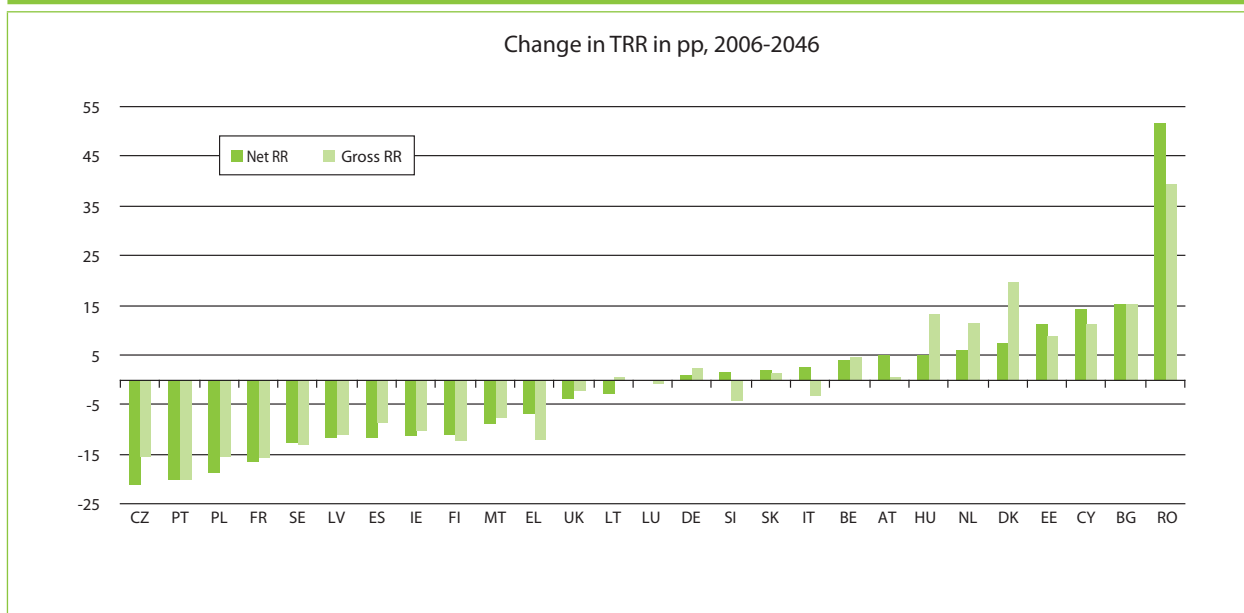
Figure 4: Benefit ratios in EU Member States in 2007 and 2060

	Benefit ratio (%)					
	Public pensions			Public and private pensions		
	2007	2060	% change	2007	2060	% change
BE	45	43	-4			
BG	44	36	-20	44	41	-8
CZ	45	38	-17			
DK	39	38	-4	64	75	17
DE	51	42	-17			
EE	26	16	-40	26	22	-18
IE	27	32	16			
EL	73	80	10			
ES	58	52	-10	62	57	-8
FR	63	48	-25			
IT	68	47	-31			
CY	54	57	5			
LV	24	13	-47	24	25	4
LT	33	28	-16	33	32	-2
LU	46	44	-4	46	44	-4
HU	39	36	-8	39	38	-3
MT	42	40	-6			
NL	44	41	-7	74	81	10
AT	55	39	-30			
PL	56	26	-54	56	31	-44
PT	46	33	-29	47	33	-31
RO	29	37	26	29	41	41
SI	41	39	-6	41	40	-2
SK	45	33	-27	45	40	-11
FI	49	47	-5			
SE	49	30	-39	64	46	-27
UK	35	37	7			
NO	51	47	-8			

Source: Ageing report 2009, available at: http://ec.europa.eu/economy_finance/publications/publication13782_en.pdf

Note: The 'Benefit ratio' is the average benefit of public pension and public and private pensions, respectively, as a share of the economy-wide average wage (gross wages and salaries in relation to employees), as calculated by the Commission. Public pensions used to calculate the Benefit Ratio includes old-age and early pensions and other pensions. Private pensions are not included for all Member States. Hence, the comparability of the figures is limited. The value of indicators might change as some Member States consider reforms of their pension systems (e.g. Ireland).

Figure 5: Change in theoretical replacement rates for an average wage earner retiring at 65 after 40 years career between 2006 and 2046 in percentage points



Source: Indicators' Subgroup of the Social Protection Committee (ISG) 2009 report on Theoretical Replacement Rates, "Updates of current and prospective theoretical pension replacement rates 2006-2046", p.17, available at: <http://ec.europa.eu/social/main.jsp?catId=752&langId=en&moreDocuments=yes>

Note: Replacement rates are defined as the level of pension income during the first year of retirement as a percentage of individual earnings immediately before retirement. For countries with a projected drop in replacement rates it should be noted that the decrease can usually be counterbalanced by working longer.

It should be noted that EE, like other countries with a more positive evolutions in replacement rates (RO, BG and CY), start off from rather low initial levels of the rates.

Figure 6: Standard pension eligibility age and average labour market exit age in EU-27

There has been a more or less pronounced increase in the average exit age from the labour force of nearly all Member States between 2001 and 2008, with an EU27 average exit age of 61.4 years in 2008. For those countries with increasing pensionable ages until 2020 and beyond, the average exit age is expected to continue to increase. It appears that most countries are gradually moving to a universal pensionable age of at least 65, but countries such as DK, DE and UK have already legislated further increases in order to respond to continued advances in longevity.

Member State	Average exit age from the labour force in 2001	Average exit age from the labour force in 2008	Statutory retirement age for M/W in 2009	Statutory retirement age for M/W in 2020	Further increases in the statutory retirement age for M/W after 2020
Belgium	56.8	61.6*	65/65	65/65	
Bulgaria	58.4	61.5	63/60	63/60	
Czech Republic	58.9	60.6	62/60y8m	63y8m/63y4m	65/65
Denmark	61.6	61.3	65/65	65/65	67+/67+***
Germany	60.6	61.7	65/65	65y9m/65y9m	67/67
Estonia	61.1	62.1	63/61	63/63	
Ireland	63.2	64.1**	65/65	65/65 (66/66)	(68/68)
Greece	61.3°	61.4	65/60	65/60	65/65
Spain	60.3	62.6	65/65	65/65	
France	58.1	59.3	60-65	60/60	
Italy	59.8	60.8	65/60	65/60****	***
Cyprus	62.3	63.5*	65/65	65/65	
Latvia	62.4	62.7	62/62	62/62	
Lithuania	58.9	59.9**	62y6m/60	64/63	65/65
Luxembourg	56.8	:	65/65	65/65	
Hungary	57.6	:	62/62	64/64	65/65
Malta	57.6	59.8	61/60	63/63	65/65
Netherlands	60.9	63.2	65/65	65/65 (66/66)	(67/67)
Austria	59.2	60.9*	65/60	65/60	65/65
Poland	56.6	59.3*	65/60	65/60	
Portugal	61.9	62.6*	65/65	65/65	
Romania	59.8	55.5	63y8m/58y8m	65/60 (65/61y11m)	(65/65)
Slovenia	56.6°	59.8**	63/61	63/61 (65/65)	
Slovakia	57.5	58.7*	62/59	62/62	
Finland	61.4	61.6*	65/65, 63-68	65/65, 63-68	
Sweden	62.1	63.8	61-67	61-67	
United Kingdom	62.0	63.1	65/60	65/65	68/68
EU 27 average	59.9	61.4			

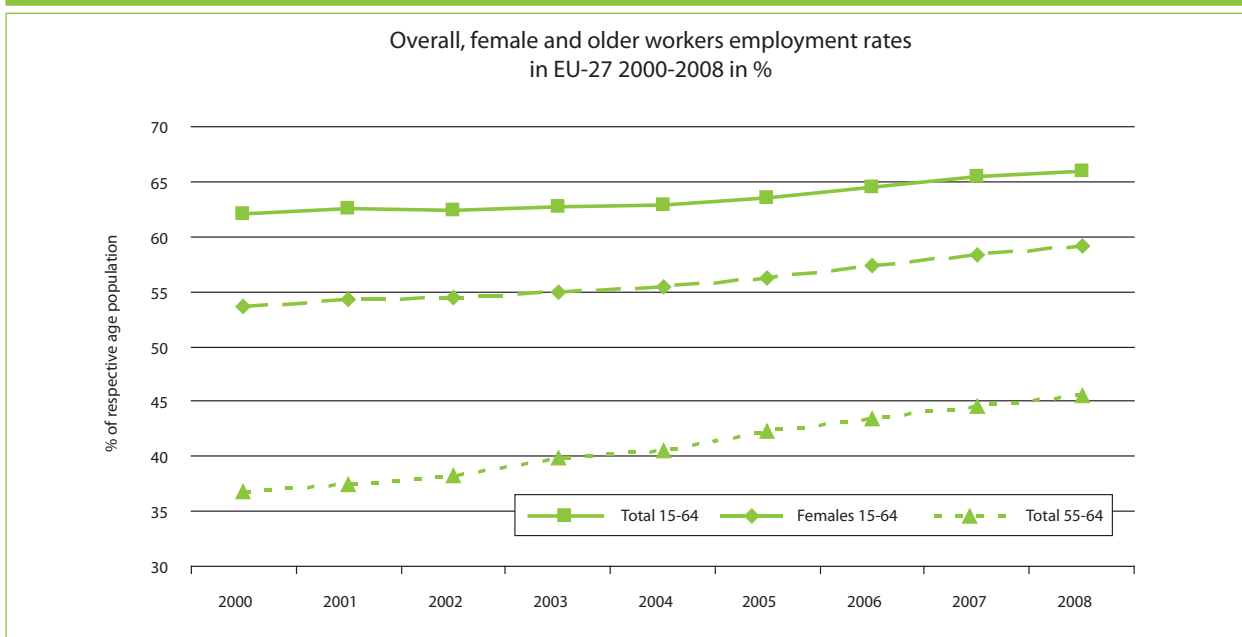
Source: Eurostat, MISSOC, Ageing Report, 2010 Interim Joint Report on pensions of the Economic Policy Committee and Social Protection Committee, noted by the 7-8 June 2010 EPSCO and ECOFIN Councils, available at: http://europa.eu/epc/publications/index_en.htm

Note: ° - 2002, * - 2007, ** - 2006, in brackets – proposed, not yet legislated, *** retirement age evolves in line with life expectancy gains over time, introducing flexibility in the retirement provision. **** For Italy 65/65 for civil servants, starting from 2018.

Sweden: guarantee pension is available from the age of 65.

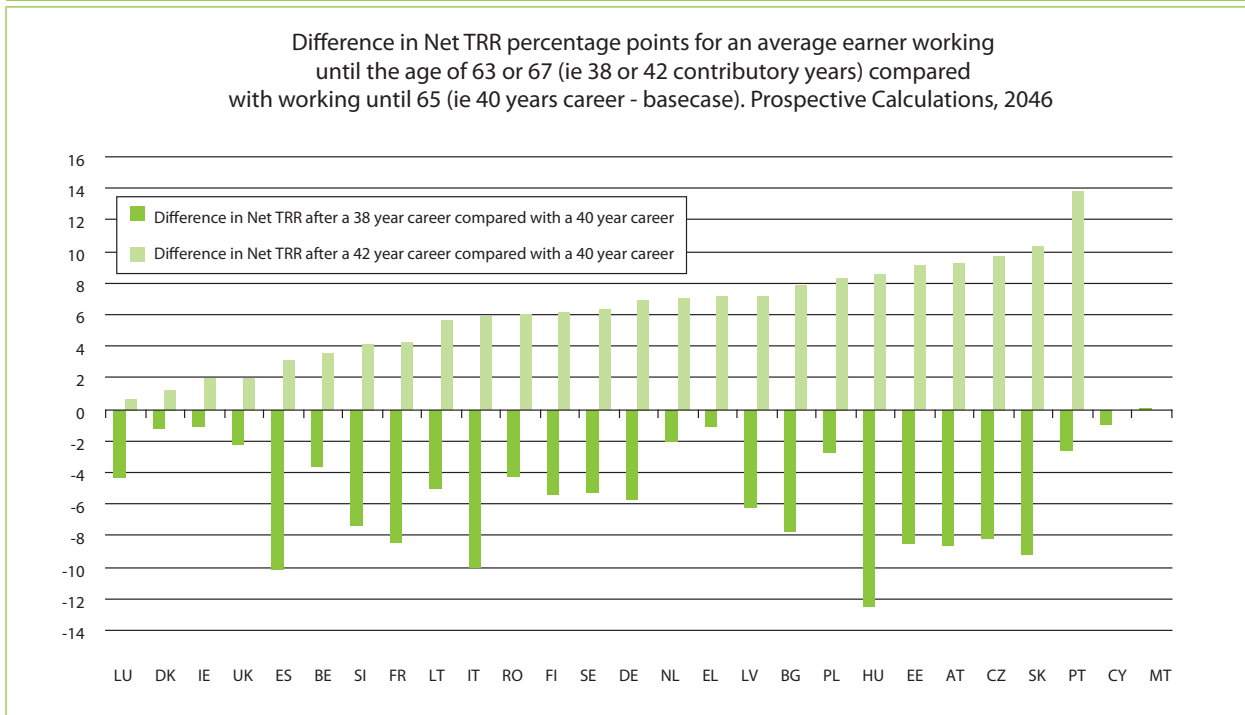
Romania: the National House of Pensions and other Social Insurance Rights.

Figure 7: Overall, female and older workers employment rates in EU-27, 2000-2008, in percent



Source: Eurostat, LFS annual data, graph published in the 2010 Interim Joint Report on pensions of the Economic Policy Committee and Social Protection Committee, noted by the 7-8 June 2010 EPSCO and ECOFIN Councils, p.10, available at: http://europa.eu/epc/publications/index_en.htm

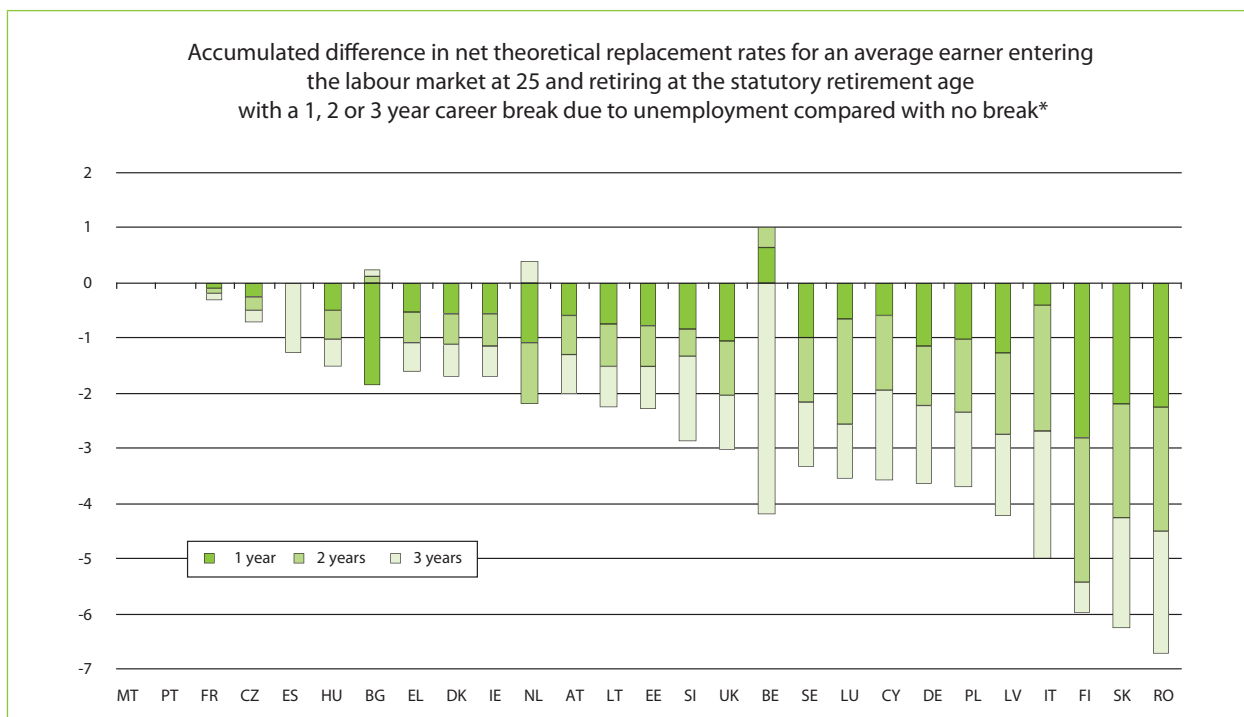
Figure 8: Pension benefit impact of shorter and longer working lives



Source: Indicators' Subgroup of the Social Protection Committee (ISG) 2009 report on Theoretical Replacement Rates (TRR), "Updates of current and prospective theoretical pension replacement rates 2006-2046", p.22, available at: <http://ec.europa.eu/social/main.jsp?catId=752&langId=en&moreDocuments=yes>

Figure 9: Pension benefit impact of career breaks due to unemployment

Accumulated difference in net theoretical replacement rates for an average earner entering the labour market at 25 and retiring at the statutory retirement age with a 1, 2 or 3 year career break due to unemployment compared with no break*



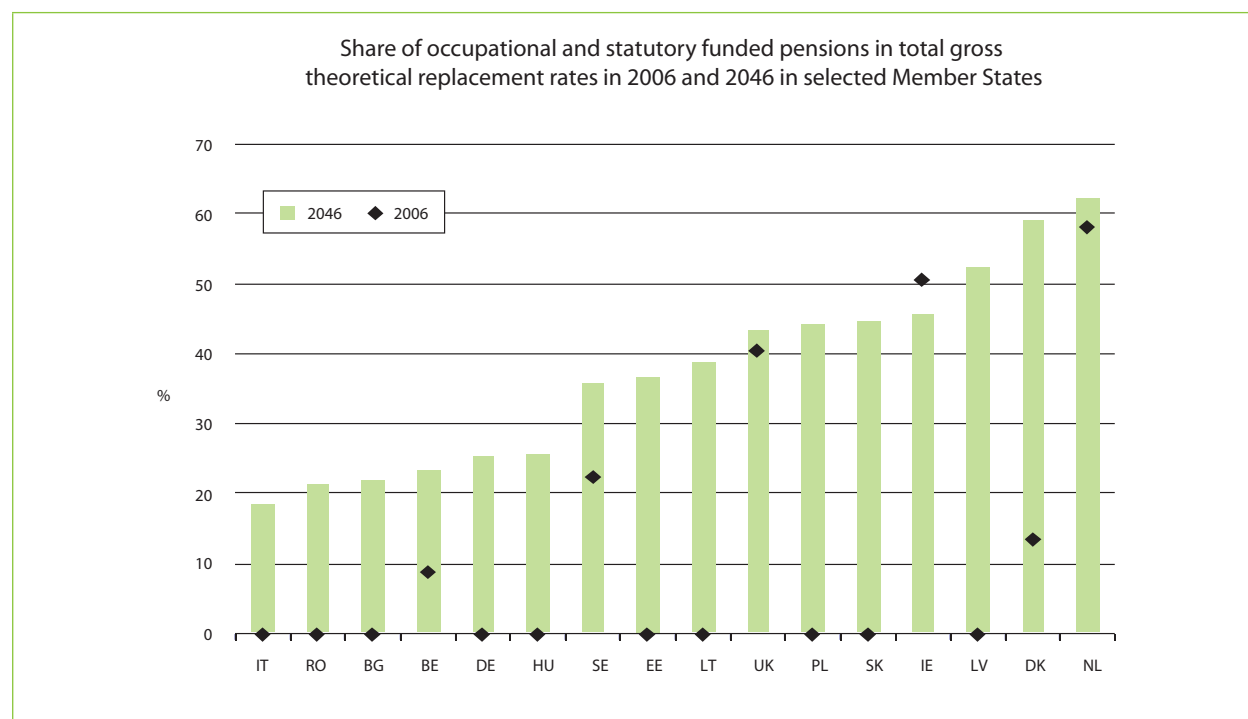
Source: Social Protection Committee/Indicators' Subgroup of the Social Protection Committee (ISG). Graph published in the 2010 Interim Joint Report on pensions of the Economic Policy Committee and Social Protection Committee, noted by the 7-8 June 2010 EPSCO and ECOFIN Councils, p.50, available at: http://europa.eu/epc/publications/index_en.htm

*The unemployment break is assumed to take place in the years just prior to old age retirement which is assumed here to be the statutory retirement age for men

Note: the values for MT and PT are equal to 0 and should not be interpreted as missing. The values are validated by Member States. Conditions of crediting unemployment breaks might have a positive impact on the replacement rate of a hypothetical worker in the base-case scenario, for whom values in the Figure are provided.

Figure 10: Increasing significance of funded pensions

This figure shows that for most of those countries represented, funded pensions will provide for a larger share of retirement income in 2046 than in 2006 as a result of pension reforms (measured by gross theoretical replacement rates).



Source: Indicators' Subgroup of the Social Protection Committee (ISG) 2009 report on Theoretical Replacement Rates, "Updates of current and prospective theoretical pension replacement rates 2006-2046", Annex – country fiches, available at: <http://ec.europa.eu/social/main.jsp?catId=752&langId=en&moreDocuments=yes>

Note: Data available only for a number of Member States

European Commission

Towards adequate, sustainable and safe European pension systems — Green paper

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The European Commission's Green Paper "Towards adequate, sustainable and safe European pension systems" invites interested parties to submit their views on future pension provision and how the EU can best support national-level efforts. The Paper reviews the current EU pensions framework and goes on to set out the main challenges to providing adequate, sustainable and safe pensions and the priorities for modernising pension policy in the EU. It also looks at the need to improve both pension data collection and EU-level governance of pension policy. Finally, the Paper provides information on how to contribute to the consultation, as well as a glossary of terms and detailed statistical annex.

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