UNICE
Union of Industrial and Employers' Confederations of Europe
Union des Confédérations de l'Industrie et des Employeurs d'Europe

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Commission Green Paper on Supplementary Pensions in the Single Market

UNICE Comments

I. General comments

UNICE welcomes publication of the Commission's "Green Paper on Supplementary Pensions in the Single Market". The issue of adequate retirement provision is of fundamental importance to all EU member states. Driven by demographic pressures, liberalisation and the trend towards contractual savings, it is likely that the part of supplementary (funded) pension schemes in total retirement provision will grow considerably in the near future. Given the increasing importance of supplementary pension schemes, UNICE considers it entirely appropriate that the Green Paper should open the debate on measures aimed at improving the internal market in capital.

As a preliminary comment, UNICE would like to point out that not all the information contained in the Green Paper is entirely accurate. Some of UNICE's member federations have noted that the statistics relating to their country are partly incorrect or that special systems – such as the Danish contribution system or the German book reserve system, for example – have not been well understood. UNICE also considers it a regrettable omission that figures from the three new member countries (Sweden, Finland and Austria) have not been taken into consideration.

In addition, UNICE notes that there are other types of pension scheme than those mentioned and discussed in the Green Paper. Their existence and function should be acknowledged in any further debate on this theme, which should also describe the impact of other forms of supplementary pension scheme on the capital market and national economies. Pension funds are only one form of supplementary pension scheme and, in this context, UNICE considers that the Green Paper places insufficient emphasis on the fact that supplementary pensions are an integral part of labour-market factors.

UNICE highly values the present diversity in pension schemes in the member states and would oppose any form of supranational regulation if it were to prejudice this diversity. However, UNICE would encourage the Commission to focus on bringing investment rules into line with the Treaty freedoms, avoiding double taxation (harmonisation of tax laws), and improving the transferability of vested pension rights.

The Green Paper identifies issues of concern in four areas: restrictions on investments and their impact on EU capital markets, application of appropriate prudential rules, facilitating the free movement of workers and the issue of taxation of supplementary pensions. UNICE comments below on the Green Paper's conclusions in these four areas.

II. RETIREMENT PROVISION AND EU CAPITAL MARKETS

At the present time, EU pension fund assets represent only 20% of EU GDP, whereas in the US the figure is 60% and in Japan 45%. UNICE agrees with the analysis in the Green Paper that, as the share of supplementary pension schemes in the total retirement provision within the EU is likely to grow, the total volume of European pension fund assets could rise considerably in the near future.

UNICE believes that the current changes in employment relationships in national labour markets – leading to an increased number of workers alternating between employed work and free-lance/self-employed/part-time work – call for adequate transparency not only in the statutory state pension system, but also in the pillars 2 and 3 of supplementary pension schemes.

Mainly due to legal restrictions, pension fund managers in some member states have until recently been unable or reluctant to invest in risk-bearing assets such as equity. However, a bias towards domestic, fixed-income assets does not necessarily produce the best rates of return. UNICE fully agrees with the argument put forward in the Green Paper that, because their liabilities are long-term, pension funds can afford to take advantage of the generally higher returns offered by equities held in the long-term. If these funds could improve their rate of return, even slightly, by holding a wider spread of assets, this could make a significant difference over an individual's working lifetime, and could ease funding pressures and improve pension incomes.

UNICE believes that modern risk management techniques allow pension fund managers to spread risks while investing in assets (such as equity) which individually present greater volatility but potentially higher rates of return. Therefore, UNICE is of the opinion that restrictions on asset allocation by pension funds should not go further than is required under the ‘principle of prudence’ and on the understanding that the necessary control is exercised by the competent supervisory authorities.

Prudential management of pension fund investment schemes supports international efforts to raise fresh risk capital for industrial investment. Secondly, it leads to an increased number of indirect private shareholders which – in a second step – might also in many cases lead to a higher number of direct private shareholders. Thirdly, it could encourage a more sophisticated and more positive attitude towards business within the population (employees and pensioners). Fourthly, it could also stimulate the industrial bond market.

In order to absorb future increases in pension fund and life insurance investments, the efficient functioning of an EU capital market needs to be guaranteed. If member states' capital markets are kept separate, they will be less liquid and less able to take up these funds successfully. Although it is true that the Investment Services Directive has already removed some of the barriers to the efficient

functioning of an EU-wide capital market, various obstacles such as transaction costs, differences in taxation and asset allocation requirements still exist.

UNICE is of the opinion that, while its effects should not be overestimated, the introduction of EMU has the potential of providing strong impetus for the removal of more barriers to cross-border pension investment.

III. THE APPLICATION OF APPROPRIATE PRUDENTIAL RULES

On the different questions in Chapter III of the Green Paper, UNICE has the following comments.

A. Role of supervision of pension and life insurance funds and fund managers

UNICE accepts that, with regard to investments, both occupational pension schemes and the insurance industry should be regulated by regimes that provide employers, employees and pensioners with an assurance that their interests will be protected and their rights secured. UNICE is of the opinion that the authorisation requirements and minimum prudential rules mentioned in the Green Paper provide an appropriate basis for regulation.

B. The effect of excessive rules on pillar 2 pension fund investments

The Commission has expressed concern that, in some member states, arbitrary quantitative investment restrictions prevent risk diversification and the use of best practice fund management techniques. UNICE agrees with this view and supports the replacement of these restrictions by the prudential management of pension schemes. This should produce a better return on pension fund investments. However, the concept of ‘prudential management’ might be defined differently in the various legal systems of member states. On this point the Commission's approach requires further clarification.

C. Rules on pillar 3 life assurance investments

UNICE is committed to the principle of free flow of capital / investment and it therefore believes that national quantitative limits imposed on life insurance funds should be adapted to EMU-market conditions. EU currency matching rules are no longer required.

D. Should there be similar EU rules for pillar 2 and 3 schemes ?

While UNICE can accept that the rules for assessing the technical liabilities of occupational pension funds (present value of commitments) should be similar whatever financing vehicle is chosen, it cannot accept the notion that solvency margins identical to those applied in the insurance sector should be imposed on the whole of the second pillar beyond external risk coverage with a third party.[1]

E. Fund managers

UNICE very much favours freedom of financial management. Fund managers – or rather *asset* managers, as UNICE prefers to refer to them – should be able to provide their services freely

[1] Conseil National du Patronat Français (CNPF) and Federation of Greek Industries (FGI) believe that similar rules should apply.

throughout the EU and compete for pension fund management. Differences in fiscal regimes, which constitute considerable impediments in this regard, should be dealt with.

F. *The way forward*

Regarding the question of how to carry out the changes envisaged in the Green Paper, three possibilities are presented, all of which contain positive elements. Firstly, introduction of the Euro, which UNICE welcomes, could free up investment to some extent. However, to rely exclusively on introduction of the Euro seems inadequate.

Secondly, UNICE endorses application of the current Treaty freedoms. But, for reasons outlined in the Green Paper – slowness, legal uncertainty and disparate interpretations − this option might result in a lengthy and inflexible process.

UNICE strongly believes that, keeping in mind the principle of subsidiarity, the Commission should seek to secure agreement on a short directive setting out basic principles rather than try to cover too much ground in a lengthy and detailed instrument.

IV. SAFEGUARDING SUPPLEMENTARY PENSION RIGHTS OF WORKERS MAKING USE OF THEIR RIGHT TO FREE MOVEMENT

UNICE considers it highly important to eliminate existing obstacles to the mobility of labour within the Community. UNICE therefore can support a proposal for a Community directive on safeguarding the supplementary pension rights of workers making use of their right to free movement. However, as stated in its position paper on “The Commission consultation document on safeguarding supplementary pension rights of workers making use of their right to free movement” dated 8 July 1997, such a directive should respect the following three principles:

- Workers moving from one member state to another should not be treated differently, worse or better, that workers moving within one member state. It is essential that the wording used to express this principal does not imply any obligation extending rights beyond those already acquired by the person moving to another member state in order to work for a new employer and that he/she would have remained entitled to had he/she moved to another employer within the country of origin.

- Cross-border payments of pensions due under supplementary schemes in other member states should be facilitated.

- Workers temporarily seconded by their employer to another member state should be allowed to remain affiliated to the supplementary scheme in their home country. It is essential that the envisaged directive does not imply any requirements for employers or emplyees to contribute to a scheme in the host state in addition to contribution in the country of origin. In any case, maintenance of membership of the scheme in the country of origin should be an option and not an obligation.

The development of supplementary pension schemes should be encouraged as part of the necessary reforms to make social protection systems more “employment-friendly”. In this context, the other problems raised in the Green Paper – burdensome qualifying conditions for acquiring pension rights, difficulties with transferability of vested pension rights, tax difficulties and problems in changing schemes if the employee is not on temporary secondment – should be taken into account.

However, UNICE points out that supplementary pension systems have developed in a way which corresponds to the specific circumstances of each country and in particular in the light of the characteristics of statutory social security systems.

UNICE does not believe that it will be possible to find a harmonised European solution to these problems. It therefore considers that the Commission should encourage member states to remove obstacles to the development of supplementary pensions as part of the necessary reform of national social protection systems but should not seek to impose a unique solution across the EU.

UNICE rejects the formation of a 'Community Pension Forum', as suggested in the Green Paper, to discuss these matters. Such a platform would provide no added value to co-operation between existing institutions, while in contrast it carries a serious risk of becoming an institutionalised agency reducing the need to listen to the different stakeholders in this area. In addition, it would be very difficult for such a platform to represent all interested parties.

V. THE IMPORTANCE OF TAXATION FOR SUPPLEMENTARY PENSIONS

Differences in national taxation regimes for supplementary pensions form one of the biggest obstacles to completion of the Single Market in this area. Perhaps the only similarity between these systems is that all member states in one way or another encourage private pension schemes by way of tax relief. However, as a result of differences in the level of deductibility and other conditions, tax discrimination (double taxation) can occur which hampers the free movement of workers.

Bearing in mind subsidiarity and fiscal sovereignty of member states, UNICE is of the opinion that these obstacles could best be dealt with on a bilateral or multilateral basis. The Commission could act as a facilitator to develop consensus for the most suitable tax system governing these agreements. A possible alternative solution could be to agree on a Convention on these matters, to which member states could sign up if they wished.

That the 'Exempt, Exempt, Taxed' (EET) system is today the most widely used and UNICE believes it to be the most suitable basis for consensus between the member states. The EET system provides for:

- Exemption from tax on contributions by both employee and employer to approved funds or schemes.
- Exemption from income and capital gains tax on the investments made by these funds or schemes.
- Taxation of the benefits as income when payment is made.

The overall effect of the EET system is the deferral of taxation to the moment the pension becomes payable and thus avoidance of double taxation, without the need to harmonise the level of taxation on benefits.

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