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European
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EUROPEAN COMMISSION GREEN PAPER CONFRONTING DEMOGRAPHIC CHANGE

EFRP RESPONSE -

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INTRODUCTORY REMARKS

EFRP welcomes the Commission's Green Paper on Demographic Change and its objective to generate a wide ranging consultation on the impact of ageing in our society.

Although we realise that the mere topic of pensions policy (including social security and private pensions) is quite complex, we wonder why the impact of ageing on this policy area is not touched upon. Some of the aspects (see sections 3.3. and 3.4.) are considered without any reference to **income policies for the elderly**. Incomes which are for the largest part of the population primarily drawn from pensions – both statutory and private.

This consultation, in our view, could have provided an opportunity to consult on a **multi-pillar pension system**. The 1st, 2nd and 3rd pillar pension approach is in place in almost every Member State but in a great variety of forms. The "safe and adequate" pensions objective (Objective 17) of the integrated guidelines for growth and jobs (2005 – 2008) could have been included to the same extent as other Lisbon strategy objectives such as the 'active ageing' (sections 3.1., 3.2.).

Demographic change is putting the financing method (Pay-as-you-go -PAYG) of public pension systems (= 1st pillar basic) under pressure. In most Member States pension reform includes the establishment or strengthening of funded private pension provision (including both 2nd and 3rd pillar). **There is abundant economic evidence that private pensions will have to take up to avert old age poverty,**

We attach as **Annex 1** a broad brush model for a multi-pillar pension system that could be promoted at EU level to streamline retirement income policies. It seems recommendable to EFRP that the Commission were to consider a multi-pillar pension

provision model that could fit in the existing multi-pillar pension systems of a large majority of Member States.

EFRP has found that some Member States seem to move to a two-pillar system: a **two-tier¹ first pillar** (statutory and basic pension) and a **private pension pillar**. This model merges the 2nd pillar (occupational pension, voluntary or not) with the 3rd pillar (individual and voluntary pension). Our federation is wondering whether this development is appropriate.

GREEN PAPER QUESTIONNAIRE

1. INTRODUCTION

Q1. Do you take the view that the discussion of demographic trends and managing their impact should take place at European level?

Q2. If so, what should be the objectives, and which policy areas are concerned?

Q1

It is important for public opinion to realise that an ageing society will imply policy change, including social protection. Therefore, it is more than necessary that the debate on demographic trends and especially the managing of their impact takes place at EU level provided the right questions are put. As stated in our introductory notes, we think the omission of any reference to retirement income is a missed opportunity to put the issue on the table.

Q2

EFRP strongly supports the European Commission initiative to debate and to study in depth the consequences of demographic change at European level.

- According to EFRP following policy areas are affected although this does not mean we think they all deserve action steered from the EU level. As stated in the Green Paper "many of the issues associated come within the exclusive competence of the Member States or their regional authorities or social partners." It is paramount if measures are deemed necessary and appropriate – after an in-

¹ A certain percentage of the statutory social security contribution is allocated to an individual account of a privately managed pension vehicle.

depth impact assessment – those measures be **in line with the subsidiarity principle**

Taking this in consideration European level action could focus on **information exchange, profiling “best practice”** and even **promoting a politically agreed model for old age income policy**. For this exercise the Lisbon Strategy along with the OMC seems instrumental. The use of existing Community processes and methods should be maximised. Recommendations can also be a valuable measure to generate reform at national level.

The **objective** should be to **adapt the social protection to the ageing society** while taking into consideration **economic sustainability, societal coherence, growth and competitiveness**. This includes – almost as a pre-requisite – the optimal functioning of **pan-European financial markets**². The **promotion of increased reliance on private pension systems** also fits into this objective.

Policies that are most directly affected by ageing include:

1. HEALTH POLICIES
2. SICKNESS AND INVALIDITY POLICY
3. LONG TERM CARE POLICY
4. INCREASED FLEXIBILITY IN LABOUR MARKET POLICIES, including reconciliation between family and professional occupation, flexible retirement formulas (i.a. combined retirement and part-time work, flexible retirement age with raising the average effective retirement age in most Member States, combat ageism, young work force integration, occupational training and re-training, flexible entry and exit of labour market).
5. EMPLOYMENT POLICY
To safeguard the financial sustainability of the public pension systems, Europe needs to have higher activity rates. The European Commission action to promote flexible labour markets and to increase the participation rates, especially for women, young and older people should be continued and strengthened.
6. PENSIONS POLICY – statutory, occupational and individual pensions
See attached Annex 2

² EFRP Response – EU Commission: Green Paper on Financial Services Policy (2005-2010)

7. EDUCATION (including life long learning possibilities outside occupational area, education that prepare young generations for the labour market)

We fully agree with the importance of life-long learning programmes to avoid early exit of the labour market. Employees need to stay a long enough in the labour market to obtain, upon retirement, adequate pension benefits.

8. FAMILY POLICY (families as micro-employeurs of domestic services, including house hold work, child caring, elderly assistance and caring, as users of proximity services, family allowances design, etc.)

9. FINANCIAL MARKETS³

In pension systems - partly - based on asset accumulation (= capitalisation) **financial stability** matched to **optimal functioning** of financial markets are paramount to ensure adequate income during retirement. Such capitalisation systems require consistently higher than inflation investment returns to generate a sufficient income stream while providing investment capital for today's business needs.

Especially in defined contribution (DC) pension systems the return of the pension savings is critical since the income stream upon retirement will depend on the aggregate capital amount saved during active career⁴.

10. IMMIGRATION

11. HOUSING PROGRAMMES

Personal income tax and pay roll tax are often used as a steering mechanism for policies as stated under 4-5-6-7-8.

It should be understood that this list – probably incomplete – is only intended to illustrate the range of policy areas that call for reform/change due to the ageing of our society. There is no intention whatsoever to suggest EU level legislative action in

³ There are different opinions in the literature of the consequences of ageing on asset prices and financial markets - See: EFRP response – EU Commission Green Paper on Financial Services Policy (2005-2010).

Following the predictions of the **life-cycle theory**, changes in the age structure of the population will affect total savings in the economy and thus asset prices. A few critical questions with regard to the outcome of the life-cycle theory can be formulated:

- People do not run down their assets as fast as the life-cycle theory suggests. (People do not know when they will die; people want to leave something for their children)
- The knowledge that the baby-boomers are near retirement implies that today's market prices should already be taking account of future demographic developments.

⁴ It should be noted though that the interest rate for conversion of capital into annuity is equally critical at the moment of retirement. The risk for adverse selection in the annuity market may increase the price of an annuity and consequently reduce the income of the pensioner.

each of them. **EU level action should seek to inspire reform**, if possible, streamlined according to a model with a number of variety options.

2. Challenges of European Demography

2.1 THE CHALLENGES OF A LOW BIRTH RATE

Q1. How can a better work/life balance help to tackle the problems associated with demographic ageing?

Q2. How best to ensure an adequate income for both parents on parental leave?

Q3 : Should the award of certain benefits or advantages (leave, etc.) be linked to an equal distribution of tasks between the sexes ? How best to ensure an adequate income for both parents on parental leave?

Q4. How can the availability of childcare structures (crèches, nursery schools, etc.) and elderly care structures be improved by the public and private sectors?

Q5. Can a reduced rate of VAT contribute to the development of care services?

Q6. How can parents, in particular young parents, be encouraged to enter the labour market, have the career that they want and the number of children they want?

Generally speaking, **family friendly labour markets** are of utmost importance if young couples are to be given optimal opportunities to have the children they want.

Q1: Good work/family balance is an overall objective for labour markets which should not only keep elderly in active career but also allow men and women to tailor their working career to their family needs.

Q2: Balanced distribution of household and family tasks between men and women can be encouraged by promoting image building campaigns illustrating the "right" role model.

Q3: Speaking about pension systems, attention is required to ensure that **effective equal pay is realised**. As long as female employees earn less – on average – than male employees in similar or comparable jobs, the family will always be tempted to sacrifice the lowest income and keep the highest income intact. It does not make

sense trying to off set the gender pay gap by specific benefits in the leave arrangements; it needs to be addressed by itself not by its consequences. Having in mind reform of pension systems, the issue arises whether maternity leave and/or parental leave periods should be factored into the supplementary pension benefits. Individual DC occupational pensions do not necessary guarantee coverage during such leaves. Collectively organised occupational pensions seem to be better equipped to provide this kind of cover. Third pillar pensions are not affected by this issue since they are purely personal/individual and voluntary arrangements.

Q4: Families should be considered as micro-employeurs for catering in child care, elderly care and household jobs in general. This can be promoted by making the hiring of this kind of personnel as easy as possible though not exclusively through structures – be them public or private. Structures are very much needed but equally care delivered by the self-employed should be encouraged. Especially the demand for elderly care will become exponential with insufficient investment capacity to provide help and care through, by and in structures only. “Proximity jobs” are proponent for low qualified people to enter and stay on the labour market.

Q5: Rather than reduced VAT we forecast that deductibility of salaries or other costs for children and elderly for personal income tax purpose, will contribute to the development of care services. In those countries with pay roll tax for financing social security, it seems sensible to eliminate this pay roll tax in order to make that labour affordable for families and take the financing of that type of “family care jobs” on to the general government budget.

Q6: See Q1 and Q4.

2.2 THE POSSIBLE CONTRIBUTION OF IMMIGRATION

3.1 BETTER INTEGRATION OF YOUNG PEOPLE

Q4. What forms of solidarity can be fostered between young people and elderly people?

Q4: This question is not introduced or further explained in the full text of the Communication. Nevertheless, EFRP wishes to put forward a couple of ideas.

- Younger generations are only prepared to join the public (= statutory 1st pillar) pension system if the system guarantees them upon retirement the same benefits as current pensioners receive today. It is therefore critical **to keep up the statutory systems and reform them to the demographic change**, building in inter-generational fairness. This may imply decrease of statutory benefits also for generations that are close to retirement. **Public debt reduction** is part of this policy since it will make future budgets more robust when the impact of demographic change will be most severe and decrease interest rates (the latter effect has already been evidenced).

- As to occupational pensions (2nd pillar), the idea **to shorten vesting and acquisition periods** is to be pursued. This is important since
 - o long coverage periods to an occupational pension plan maximises the potential of saving
 - o integration of younger cohorts in collective capitalisation pension systems is beneficial for all fund Members. These systems have **built-in solidarity within and between generations** provided the fund will be continuing its activities in the long term. The same goes for public systems.In pure defined benefit (DB) systems, the solidarity aspects could be illustrated as follows:
 - There is no link between the risk and age profile of the individual and his/her contribution.
 - The participation of young people allows to opt for a more equity oriented investment strategy and thus to gain higher investment returns which allows either higher pensions or lower contributions, or the two combined.
 - The risk of old-age poverty is severely reduced if pensioners obtain interesting annuity conditions. An optimal mix between young and elder members allows the pension fund to manage longevity risk and to offer a life time income stream that is not available on the market.

3.2 A GLOBAL APPROACH TO THE WORKING LIFE CYCLE

Q2. [...] How can we enable older people to work more?

Q2: We think the question should be: "How can we enable older people to work longer?" Older people should not work more than younger people but should retire at the legal retirement age rather than stop working in their fifties.

The strategy to lengthen the active career is a critical line of action to avert ageing. This is agreed EU policy since ever the Lisbon strategy has been adopted by the European Council.

Increasing the **effective retirement age** is **the most powerful parametric measure** to make pension systems financially sustainable. It therefore deserves more focus in EU policy recommendations for an ageing society.

This objective can be pursued by:

- **lifelong learning possibilities** – both work place promoted/sponsored or in the general education system. This is essential to ensure the adaptability of the workforce to changes in the labour market
- ensuring that **social benefits and tax system** do not contain any incentives that induce older workers to retire earlier than set by the legal retirement age
- combating **ageism** in society as a whole and in the work place in particular

3.3 A NEW PLACE FOR ELDERLY PEOPLE

Q1. Should there be a statutory retirement age, or should flexible, gradual retirement be permitted?

Q2. How can elderly people participate in economic and social life, for example, through a combination of wages and pensions, new forms of employment (part-time, temporary) or other forms of financial incentive?

Q.3. How can activities employing elderly people in the voluntary sector and the social economy be developed?

Q4. What should be the response to pensioners mobility between Member States, in particular with regard to social protection and healthcare?

Q5. How should we be investing in health promotion and prevention so that the people of Europe continue to benefit from longer healthy life expectancy?

Q1: EFRP thinks that there can be a statutory retirement age according to national practices. However, it is strongly recommended to promote equally **flexible and gradual retirement**. EU level action should focus on measures aiming at **increasing the effective retirement age** including measures promoting part-time retirement with unlimited income from part-time work.

Q4: There still are barriers to the free movement of persons and capital as occupational pensions are concerned. In this respect, pensioners are hindered by:

- **lack of integrated pan-European pension vehicles** that would be able to provide one single occupational pension for the whole career. This problem is not only an internal market problem but equally originates from national work place pension systems that do not allow for transfers of accrued pension entitlements.

This remark is also valid for statutory (1st pillar) pensions.

- **taxation** is also a barrier for mobility when it comes to occupational and personal pension systems.

The Commission has already displayed action in this field and EFRP strongly recommends continuing the work to dismantle tax barriers to occupational pension provision. For pensioners the transfer of pension capital is of particular relevance as well as the taxation of the retirement income when paid across borders.

Q5: In a first approach, we are inclined to state that the current trend in society is a strong support for launching or promoting any “health promotion and prevention” policy: “it is in the air”. However, there may be a need for information that has a stronger scientific base than is often the case.

3.4 SOLIDARITY WITH THE VERY ELDERLY

Q1. In particular, should a distinction be drawn between retirement pensions and dependency allowances?

Q5. What can be done to reduce inequality between men and women when they reach retirement age?

Q1: The consumption pattern of very old people differs significantly from elder people that are more or less self-sufficient. The very old people prefer access to appropriate care services instead of cash money. The dependency allowance is certainly an interesting idea since it reflects the objective need for more assistance, hence more service, hence more money. Providing a specific allowance implies the policy choice to provide for low cost services to the elderly. This can be provided at home by local care networks, self-employed carers or even specialised interim agencies. Access to good quality care institutions (intra mural care) will also become a highly demanded service for the very dependant people where home assistance becomes insufficient.

In respect of occupational and personal pensions the European Commission could research the feasibility of innovative pension solutions which offer pensioners access to old-age care services upon a certain age or an increase in their annuities as from a certain age.

Q5: We repeat (re 2.1. Q3) that addressing the gender pay gap is the number one priority. Reducing that will automatically reduce the gender pensions gap, in both statutory and work place pensions.

EFRP believes that **occupational pension provision by itself is gender neutral** provided the career pattern is not gender biased. Collective capitalisation systems are properly equipped to solidarise the life expectancy difference between men and women.

The conversion of pension capital into an annuity on the private insurance markets is under increased legal attention since the adoption of Dir. 2004/113/EC⁵.

4. CONCLUSION

Q1. Should the European Union be promoting exchanges and regular analysis of demographic change and its impact on societies and all policies concerned?

Q3. How could European coordination of employment and social protection policies better take on board demographic change?

Q1: It seems obvious that the EU would promote exchanges and regular analysis of demographic change and its impact on society and all policies concerned. Account should be taken and in due extend to the economics – both macro and micro level - of the picture.

Therefore it occurs to EFRP that the European Commission should

- analyse the impact of ageing on the budget of the Member States, including their regional and local authorities
- model the national pension systems into different multi-pillar⁶ types, including statutory, work place and personal pensions

⁵ On equal treatment between men and women in the access to and the supply of goods and services

⁶ The aim of a well structured pension pillar model is to provide the pensioner an adequate and well diversified income upon retirement. The key idea of this pension model is to find a balance between the collective and the individual interests. Since the State pension (first pillar) does not allow pensioners to maintain life standard upon retirement, private pension provision is generally accepted as a solution to fill this gap. Occupational pension provision, known as second pillar, is linked to employment or self-employment. The main idea of occupational pension provision is to organise collectively an additional income for the employees of the company or industry branch. Third pillar

- promote the acceptance of a multi-pillar model that can inspire pension reform in a large majority of Member States (see our Annex 1)
- promote financial education programmes to help citizens make the right pension choices throughout their life time
- raise awareness of young people in particular on the importance to save for retirement and start as early as possible

Attached:

Annex 1 – EU 25 pension pillar terminology

Annex 2 – Impact of ageing on retirement income policies

Annex 3 – About the EFRP

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pension provision is based on an individual approach and offers the possibility to top up first and second pillar arrangements with a long term pension savings plan.