Towards adequate, sustainable and safe European pension systems

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PURPOSE: to open a debate on whether and how the EU level pensions framework should be developed to best support Member States in their difficult task of ensuring they provide their citizens with adequate, sustainable and safe pensions – both now and in the future (Green Paper).

BACKGROUND: 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.

Reforms have underpinned recent increases in effective retirement ages and opened new avenues to delivering adequate pensions in a sustainable manner.

Over the last 50 years, life expectancy has risen by about five years in the EU. The latest demographic projections 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. 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**.

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.

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.

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.

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**.

CONTENT: this Green Paper seeks the views of all stakeholders in the EU on whether, and how, the EU level pension framework should be adjusted to best support Member States in ensuring they achieve their agreed goal of adequate and sustainable pensions for EU citizens. It 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.

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.

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. It does however lay down a number of p**riorities to modernise pension policy in the EU:**

(1) Overarching objectives: adequacy and sustainability of pension systems: 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. 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.

The Green Paper asks how the EU can support Member States' efforts to strengthen the adequacy of pension systems. Should it seek to define better what an adequate retirement income might entail. It also asks if the existing pension framework at the EU level sufficient to ensure sustainable public finances.

(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. 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. 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. 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.

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. 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.

The Green Paper asks the question 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? Lastly, 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) Removing obstacles to mobility in the EU: greater flexibility in job mobility supports the adjustment capacity of the economy and strengthens the European social model.

With a view to **strengthening the internal market for pensions**, it may be necessary to review the IORP Directive, further supervisory convergence and more transparency about national differences. Moreover, aspects concerning custodianship 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.

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.

Lastly, the question is asked whether the EU should 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.

(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 defined contribution schemes, however, raise new policy questions on the following issues:

- reviewing current EU legislation to ensure a consistent regulation and supervision of funded (i.e. backed by a fund of assets) pension schemes and products (would 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?);
- improving the solvency regime for pension funds;
- addressing the risk of employer insolvency
- facilitating informed decisions by modernising the current minimum information disclosure requirements for pension products (e.g. in terms of comparability, standardisation and clarity).

Enhancing governance: the Green Paper stresses that 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.

The consultation period will run for four months (ending 15 November 2010) during which anyone with an interest in the subject can submit their views.