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Update on…

The impact of the financial crisis on retirement pensions

In December 2008, the Social Protection Committee sent a questionnaire to the Member States, seeking their views regarding the impact of the financial crisis on social protection systems, especially retirement pensions.

Social protection, as the Member States and the European Commission are aware, provides an effective cushion. They still regard the deep effects on the economy as a threat.

The Social Protection Committee emphasizes that States with pay-as-you-go pension schemes foresee no crisis, or even pension reductions, unless the crisis has enduring effects on the economy.

As for states with fully funded pension schemes, the OECD has measured the effects of the crisis where pension funds are most prevalent (the United States, Canada, Australia, Japan, the United Kingdom, Ireland, and the Netherlands, where managed assets represent more than 50% of the GDP). It has also considered Central European countries (Hungary, Poland, the Baltic states) whose chief source of retirement financing is defined contribution plans. In conclusion, OECD pension fund assets, which had nearly doubled from 2001 to 2008, have dropped nearly 20%, from $30 trillion to $25 trillion, thanks to the financial crisis *(see box on page 3)*. The OECD nevertheless wants to discourage measures like those taken by Argentina, which has "renationalized" its scheme.

In matters of insurance, the European Commission does not consider Wall Street's string of failures as substantially altering the negotiations underway in Brussels on the European insurance sector's future. For the EC, European insurers are in a different situation from that of their American counterparts.

The Commission attributes the failure of certain American insurers to their investment strategy, which resembles that of banks and is not very common in Europe.

A group of high-level experts presided over by Jacques de Larosière will nevertheless make recommendations to shore up and coordinate European oversight of all financial sectors (securities, banking, and insurance).

CEIOPS (the Committee of European Insurance and Occupational Pensions Supervisors) seeks to restore confidence through comprehensive, transparent financial information, in harmony with the practices of American banks. To this end, it is joining with the Committee of European Securities Regulators (CESR) and the Committee of European Banking Supervisors (CEBS) to urge emergency adoption of the directive on IAS 39 and IFRS 7 *(See p 2)*.

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[1] CEIOPS, or CECAPP, founded in 2003 and combining all of the sector's Member State supervisory authorities.

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SOLVENCY II

The Council of the European Union revises its proposal for a directive

On December 2, 2008, the Economic and Financial Affairs Council, which comprises the finance ministers of the 27 Member States, reached a compromise on the Solvency II Directive to revise prudential rules for insurance companies (by 2012). *(See Bref n°1/2008).*

The chief point of contention, especially for large international insurers, was the oversight of insurance groups with subsidiaries in different EU countries. The agreement abandons the original idea of "group support" — i.e., the supremacy of the supervisor in the country where an insurer's headquarters is located in determining solvency ratios for the whole group.

The new agreement would substitute a college of supervisors made up of national authorities in each country where the group is present. Proposed by the French presidency, the agreement garnered support from countries that lack international insurers (notably in Central Europe).

Critics include representatives of Northern European countries as well as the CEA (Comité Européen des Assurances), the main insurance lobby, which backed "group support" as a key element of Solvency II during the fourth CEIOPS (Committee of European Insurance and Occupational Pensions Supervisors) conference in Frankfurt on November 19, 2008.

Debate at the first reading in Parliament will likely delay the directive's application until 2013.

Pension funds and Solvency II

According to pension fund representatives, the Solvency II scheme for insurers is inappropriate for institutions for occupational retirement provision, as defined in directive 2003/41/EC. However, the standardization of solvency rules could be limited to institutions with cross-border operations (as defined in article 17 of directive 2003/41/EC).

In its response to a European Commission questionnaire, the European Association of Paritarian Institutions (AEIP) strongly recommended the term "*règles de provisionnement technique*" (rules for technical provisions), as it would avoid any confusion with solvency rules. These are already referred to by the Commission, and their short-term approach bears no relation to the workings of collective schemes. The European Federation for Retirement Provision (EFRP) believes that now is not the time to revise directive 2003/41/EC on occupational pensions. The directive, it argues, was implemented in Member States as recently as June 2007 and lists only 70 cross-border pension funds.

Both organizations favor first establishing a map, covering the 27 Member States, of existing institutions for occupational retirement provision.

☞ *AEIP Position, December 4, 2008*
www.aeip.net
☞ *EFRP Reply, November 28, 2008*
www.efrp.eu

ACCOUNTING STANDARDS

The Commission changes accounting standards

"*Considering the context of the current financial turmoil and the fact that certain financial instruments are no longer traded or related markets have become inactive or distressed, there is a need to give immediate effect to the amendments allowing for reclassification of certain financial instruments and the Regulation consequently should enter into force as a matter of urgency.*"

This preamble to the directive adopted by the European Commission on October 15, 2008, sums up the swift action called for by the Ecofin Council on October 7, 2008. The Council sought to grant EU companies the same ability as their American counterparts to reclassify assets, from the third quarter on, and not keep track of fluctuations on financial statements.

Changes in IAS 39 pave the way for companies adhering to international financial reporting standards (IFRS) to reclassify their assets, as American GAAP accounting standards already allow. Changes to IFRS 7, meanwhile, institute supplementary guarantees for reclassified assets to ensure total transparency for the end users of financial statements.

A regulation unanimously adopted by the Member States on November 3, 2008, consolidates all IFRS in force in the European Union.

As of 2005, Regulation (EC) 1606/2002 has required all listed companies issuing consolidated financial statements in the EU to prepare them in accordance with the standards of the International Accounting Standards Board (IASB).

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OECD: The state of pension funds in certain European countries

The crisis will directly affect those members of defined contribution schemes (which are particularly common in the United Kingdom and the countries of Central Europe) who decide to retire right now, but it will also affect retired members of defined benefit schemes, for which indexing conditions might be relaxed.

The United Kingdom: Defined benefit funds show a deficit of €218 billion, despite a surplus of more than €12 billion a year ago. Half of those funds, involving nearly 8,000 companies, plan to shut down, and large companies have already stopped making contributions, as current legislation permits.

Ireland: Pension funds — mostly defined benefit schemes — are under-capitalized, thanks to a 34% drop in the value of assets, and plan to revise their commitments. The National Pensions Reserve Fund has been called in to recapitalize the country's financial institutions.

The Netherlands: Defined benefit pension funds can no longer meet the required 105% minimum for coverage commitments. Measures to raise the retirement age from 65 to 67 are being debated.

Finland: With a drop of 15% in assets held to back pension commitments, Finnish pension funds are already planning to raise contributions for the next five years.

Sweden: The *Premie pension* (part of the basic Swedish fully funded scheme) has been directly affected by a 36% plunge in financial returns. Sweden plans to limit the resulting service cuts through taxes.

Latvia, Lithuania, Estonia: Having chosen basic schemes in the form of defined contribution plans, these countries have been forced to lower retirement benefits (by 10% in Estonia).

PRIVATE PENSION SCHEMES

The European Commission heads up an "Open Method of Coordination"

According to Vladimir Spidla, EU commissioner for social affairs, "privately funded schemes clearly have a major role to play in helping provide retirement incomes for the future. But we need to ensure better access for all."

The report published by the European Commission on October 20, 2008, emphasizes a tendency in the Member States to expand the role of privately funded pension schemes and lend greater importance to analyzing the effects on future pensions, especially for the people most at risk (women, the young, those with poor qualifications or low incomes). Among the priorities are:

- The need for better financial education
- The effects of career interruptions on pension levels
- Rules limiting access to retirement savings accounts, so that pension levels remain adequate throughout a person's retirement
- The appropriateness of administrative fees in privately funded pension schemes (an annual contribution of 1% over 40 years would amount to 18% of total contributions at retirement)

Kinds of privately funded pension schemes in the EU

The report finds a great variety of coverage by type of privately funded pension scheme (compulsory, occupational, and voluntary).

Compulsory schemes

Coverage by compulsory schemes varies from 25% of the population in Italy to 100% in Sweden, with normal levels of 50% to 70%. Coverage should approach 100% as the schemes develop.

Occupational schemes

As for occupational schemes, Denmark, the Netherlands, and Sweden post coverage of 75% or more, and rates in several other Member States (Belgium, Germany, Ireland, Cyprus, and the United Kingdom) vary from 40% to 75%. But in most Member States (Italy, Austria, France, Spain, Finland, Luxembourg, Portugal, and Poland), coverage is less than 20%.

Voluntary schemes

Voluntary schemes generally account for limited coverage but have a good showing in certain Member States (with 45% in the Czech Republic and lower percentages in Germany, the United Kingdom, and Ireland).

☞ *"Privately managed pension provision and its contribution to adequate and sustainable pensions"*
http://ec.europa.eu/employment_social/spsi/adequacy_sustainability_fr.htm

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TEMPORARY WORK

Adoption of the directive on temporary work

On October 21, 2008, the European Parliament definitively adopted the proposal for a directive on temporary agency work to guarantee equal treatment.

Parliament approved the Council's common position, which retained the vast majority of the amendments adopted on first reading. Among them were guarantees of equal treatment for all employees within a company in terms of "basic working and employment conditions," including pay. The principle of equal treatment applies from the very first day of employment. Exceptions must be stated in an agreement at the national level between the social partners.

Also preserved in the common position were amendments on access to jobs, public facilities, and professional training, as well as the representation of temporary workers.

In exchange, prohibitions and restrictions on hiring temp workers (e.g., in the French civil service) will be subject to periodic review and may now be justified only on the grounds of public interest. Examples include the protection of temporary workers, health and safety requirements in the workplace, and ensuring the proper functioning of the job market.

The directive comes seven years after the social partners' admission of failure, in March 2001, in negotiations started in June 2000.
http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2008:327:0009:0014:FR:PDF

POSTING AND PROVISIONS OF SERVICES

A committee of experts convened

A committee of experts on the posting of workers was convened on December 19, 2008, to examine, among other things, the practical aspects of applying European law – in this case, Directive 96/71/EC of December 16, 1996, on the posting of workers in the framework of the provision of services and related case law. *(See Bref 1/2007).*

A Commission recommendation on April 3, 2008, urged Member States to take measures to correct problems of application, execution, and control. Particular measures included more efficient information exchange, better access to information, and an exchange of best practices between national administrations.

SOCIAL SECURITY COORDINATION

Implementation of new EC Regulation 883/2004

In December 2008, the Council adopted common positions on the two draft implementing regulations for EC Regulation 883/2004, which will replace Regulation 1408/71 on the coordination of social security systems.

Both texts have been submitted to the European Parliament. Implementation of the new regulation, initiated in 1999 and adopted in April 2004, requires that both pass unanimously. *(See Bref n°1/2006).*

The regulation will establish concrete implementing arrangements for the new rules, especially those aiming to accelerate procedures. Proposed methods include uniform processing times and, for social security institutions, a paperless system for the exchange of information and standardized messages.

The regulation would also strengthen procedures for mutual assistance between institutions in matters of social security debt recovery, so as to increase efficiency and prevent fraud.

The "Pensions" chapter takes into account the specificities of schemes that do not consider periods of insurance, like point system schemes (AGIRC and ARRCO), as well as new fully funded basic schemes.

The applicable regulations are complex, and so is their coordination. In fostering trust between social security institutions and the people for whom they provide coverage, it is essential to keep both the institutions and individuals informed of new regulations.

HEALTHCARE

Proposal for a directive on cross-border medical treatment

Adopted in July 2008, the proposal for a directive to make it easier for European patients to exercise their freedom of movement in seeking healthcare will be reviewed in Parliament in the first quarter of 2009.

The proposal, along with a memorandum on improving cooperation on such matters between Member States, aims to transpose the well-established case law of the Court of Justice as of 1998, according to which the treaty confers on patients the right to seek treatment in other Member States and to be reimbursed in their own Member State for costs incurred.

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The directive on services in the internal market, or Bolkenstein directive, created a stir when the Commission presented it in early 2004. A notable point of contention was its provisions for applying the principles of free movement to health services. The European Parliament and Council rejected that line of action, so the Commission developed an initiative concerning healthcare services specifically and exclusively.

Based on article 95 of the treaty on the workings of the internal market, this proposal for a directive aims in practice to permit EU citizens to exercise their right to treatment abroad while guaranteeing the general objectives of accessibility, quality, and financial viability required by the healthcare systems.

The proposal spells out reimbursement policies for treatment costs incurred in other Member States, as well as obligations to provide patients with clear information for their healthcare decisions. It also describes guarantees for the quality and safety of treatment, provisions for treatment continuity as patients pass from one healthcare provider or organization to another, and appropriate procedures for patients to file complaints and seek indemnities for any kind of malpractice.

Two parallel mechanisms to cover the cost of cross-border healthcare

The existing regulatory framework for the coordination of social security schemes (regulation EEC 1408/71) will remain in place, as will the European health insurance card.

Patients wishing to receive planned medical treatment abroad will continue to be covered within the regulatory framework, subject to authorization from the fund to which they belong. The fund guarantees the right to seek treatment abroad to patients who cannot receive adequate treatment within an acceptable timeframe in their Member State of origin. All additional costs resulting from the treatment are covered by social security.

The new directive on cross-border medical treatment sets up a complementary mechanism, based on principles of free movement, in compliance with the decisions of the Court of Justice. Patients may travel to another Member State for the medical treatment that they would have received in their own Member State, and be reimbursed up to the amount that they would have received had they been treated in their country of origin. But they must themselves assume any financial risk involving additional costs.

http://ec.europa.eu/health/ph_overview/co_operation/healthcare/cross-border_healthcare_en.htm

AGING

Eurostat demographic roundup

The population of the EU-27 should exceed 495 million in 2008 and 521 million in 2035, then gradually diminish and stabilize at around 506 million in 2060.

Annual births should decrease between 2008 and 2060. At the same time, annual deaths should continue to increase. From 2015 on, total deaths should exceed total births, ending natural demographic growth. Starting on that date, a positive migratory balance should be the sole factor driving demographic growth. However, from 2035 on, positive migratory flows should no longer compensate for the natural negative change in population. The population should therefore begin to decrease.

The proportion of people aged 65 or more in the overall population should increase by 17% to 30%, from 84.6 million in 2008 to 151.5 million in 2060.

Additionally, the number of people aged 80 or more should almost triple, from 21.8 million in 2008 to 61.4 million in 2060. The dependency rate among the young in the EU-27 should be up moderately in 2060, to 25%, while the rate among the elderly should be up significantly, from the current 25% to 53% in 2060.

In the EU-27 in 2008, there are four people of working age (15-64) for every person aged 65 or more. In 2060, the ratio should be two to one.

http://epp.eurostat.ec.europa.eu/cache/ITY_OFFPUB/KS-SF-08-072/EN/KS-SF-08-072-EN.PDF

Social exclusion among elderly made subject of comparative study

One of the chief purposes of pension systems is to counteract social exclusion. The new report of the European Network of Economic Policy Research Institutes (ENEPRI) focuses on the social exclusion of people over 55 in European Union Member States.

The definition of social exclusion takes into account the situation of individuals in four dimensions. Two dimensions – material deprivation and social rights – are structural. The other two – social participation and normative

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integration – are tied to the social environment and to sub-cultural factors.

The methodology used to measure social exclusion was designed and tested for the Netherlands and then extended to the EU Member States.

The results suggest that social exclusion among the elderly is minimal in the Nordic countries and the Netherlands. It is slightly higher in Continental Europe and the Anglo-Saxon countries. It tends to be higher still in Mediterranean countries. The new Member States, particularly the Baltic countries and Poland, have the highest social exclusion scores.

As for access to social rights – particularly adequate housing and access to healthcare – in almost all Mediterranean and Central European countries, the elderly are more affected by social exclusion than are other age groups. In the Nordic countries, Germany, and the United Kingdom, the reverse occurs: access to social rights expands with age. In all countries, health problems significantly increase the risk of exclusion. Social security and retirement schemes, through their effects on income inequalities, have an indirect effect on changes in social exclusion.

http://shop.ceps.be/downfree.php?item_id=1700

NETHERLANDS

Encouraging employment among older workers

The Dutch government has rejected the proposal of the Bakker Commission, which was appointed by the coalition government in 2007 and submitted its report in June 2008. The proposal called for a gradual increase of the retirement age from 65 to 67 over the years 2016 to 2040. Minister of Social Affairs Piet Hein Donner has declared that the government's policy is, in fact, to avoid such an increase in the legal retirement age and instead focus on keeping workers on the job market up to the age of 65.

As of this year, companies that have employees aged 65 to 67 and hire older workers will receive cuts in payroll taxes. People over 62 who remain employed will benefit from reduced income taxes.

The government is also planning to raise basic pension benefits for workers who put off their retirement.

Currently, 51% of the Dutch population aged 55 to 64 is employed, compared with 38% in 2000. The Netherlands is close to full employment, with the lowest unemployment rate in Europe: 2.8% in 2008. Workforce shortages are beginning to have an effect.

EURO

Slovakia adopts the euro

On January 1, 2009, the euro became the official currency of Slovakia. After a 16-day transition period, during which the national currency circulated with the euro, the Slovakian koruna vanished forever.

The date marks the tenth anniversary of the euro's launch in 11 countries, though these kept their own coins and banknotes in circulation until the beginning of 2002.

Greece adopted the single currency in 2001, with Slovenia following in 2007, then Malta and Cyprus in 2008. The entry of these countries into the euro zone required several years of economic and fiscal reform.

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