COMMUNICATION FROM THE COMMISSION

Second stage consultation of social partners on measures to improve the portability of occupational pension rights

1. INTRODUCTION

On 12 June 2002, the Commission launched the first stage consultation of the social partners on the portability of supplementary pension rights, i.e. on the possibility of acquiring and keeping pension entitlements in the event of professional mobility (by preserving them in the previous employer's scheme or transferring them to a new scheme). The term "supplementary pensions" was used in this framework to broadly refer to second pillar "occupational pensions", which are characterised by their link to employment. Third pillar individual pension plans (that can be taken out by any individual without regard to an employment relationship), as well as pension schemes covered by Regulation 1408/71/EEC, were excluded from the scope of the initiative.

In accordance with Article 138(2) of the EC Treaty, the social partners were asked to give their opinion on the need and possible direction of a Community action on the portability of occupational pension rights. In particular, the Commission consulted them on the usefulness of a Community action in this field, the form such action should take (collective agreement, directive, recommendation, code of practice, etc.), what the main features of such a measure might be, whether action in the form of collective agreements at cross-sectoral and/or sectoral level should be considered and the possible material scope of the measure envisaged (type of pension schemes to be covered).

Having examined the reactions of the social partners and considering that action to improve the portability of occupational pensions is advisable, the Commission has decided to launch the second stage consultation of the European social partners, on the possible content of Community action to improve the portability of occupational pension rights, pursuant to Article 138(3) of the EC Treaty.

2. BACKGROUND

The mechanisms of co-ordination provided for by Community legislation to remove obstacles to the mobility of workers in the field of statutory pensions (Regulations 1408/71/EEC[1] and 574/72/EEC[2]) do not apply to non-statutory occupational pension schemes. As long ago as 1991, the Commission had acknowledged the implications of the absence of equivalent mechanisms regarding occupational pensions for labour

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1 Regulation (EEC) 1408/71 of 14.06.1971 on the application of social security schemes to employed persons, to self-employed persons and to members of their families moving within the Community, OJ L 149, 05.07.1971, last codified by Council Regulation (EC) 118/97, OJ L 28, 30.01.1997.

2 Regulation (EEC) 574/72 of 21 March 1972, fixing the procedure for implementing Regulation (EEC) No 1408/71 on the application of social security schemes to employed persons and their families moving within the Community, OJ L 074, 27.03.1972.

mobility[3]. In 1992, the Council invited the Member States to promote changes to the conditions governing the acquisition of supplementary pensions, with a view to eliminating obstacles to the mobility of employed workers[4]. Following the difficulties encountered by a first Commission proposal for a directive in 1995[5], the issue was referred back to the High Level Panel on Free Movement of Persons chaired by Mrs Simone Veil. A consultation of all the interested parties was simultaneously launched with a Green Paper in 1997[6]. As a result of this debate, Directive 98/49/EC[7] was adopted, with the aim of safeguarding the supplementary pension rights of employed and self-employed persons moving within the Community. This Directive guarantees the right to equal treatment between those who change jobs within a country and those who move across borders and ensures that posted workers can continue to make contributions to the pension scheme in the Member State of origin. However it fails to address the obstacles to mobility linked to the conditions for the acquisition of rights, their preservation or their transferability.

In its Communication of 1999 "Towards a single market for supplementary pensions"[8], the Commission took stock of the results of the consultation of 1997, and addressed in a comprehensive way all the obstacles linked to the establishment of an internal market for supplementary pensions. Moreover, it suggested "to open a debate at European level with the social partners, in order to examine how this obstacle to the free movement of persons can be overcome".

As a result of the debate launched in 1997 a consultative committee - the Pensions Forum – was established and started to work in 2000[9], gathering representatives of all interested parties (governments, social partners, pension funds and their beneficiaries) to assist the Commission in tackling the obstacles to labour mobility in the area of supplementary pensions. The work undertaken by the Pensions Forum has provided substantial technical input to the present consultation document.

The issue of portability of occupational pension rights was taken up again by the Social Policy Agenda 2000-2005[10] which included the promotion of mobility as one of the key actions targeted at realising Europe's full employment potential and reaffirmed the intention of the Commission to propose concrete solutions to the problems encountered by workers exercising their right to free movement in the field of supplementary pensions.

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3 Communication from the Commission to the Council of 22 July 1991 on "Supplementary social security schemes: the role of occupational pension schemes in the social protection of workers and their implications for freedom of movement" (SEC (91) 1332 final).

4 Council Recommendation 92/442/EEC of 27 July 1992 on the convergence of social protection objectives and policies (OJ L 245 of 26 August 1992).

5 COM(95) 334.

6 "Supplementary Pensions in the Single Market - A Green Paper (COM(97) 283 final).

7 Directive 98/49/EC, on safeguarding the supplementary pension rights of employed and self-employed persons moving within the Community, OJ L 209 of 25 July 1998.

8 Commission Communication of 11 May 1999 "Towards a Single Market for Supplementary Pensions – Results of the consultation on the Green Paper on supplementary pensions in the single market" (COM(99) 134 final).

9 The Pensions Forum first met in February 2000 and was officially established by Commission's Decision C(2001) 1775 of 9 July 2001, on the setting-up of a Committee in the area of supplementary pensions.

10 Communication from the Commission to the Council, the European Parliament, the Economic and Social Committee and the Committee of the Regions of 26 June 2000 (COM (2000) 379 final).

An Action Plan for Skills and Mobility was therefore adopted by the Commission in February 2002[11]. The Action Plan stressed that "progress should be made in the portability of the supplementary pension rights of migrant workers" and invited the social partners, the Member States and the European institutions to "intensify efforts to ensure that portability is improved" (action 14).

Finally, Member States agreed at the European Council of Laeken in December 2001 and in the framework of the open method of co-ordination in the field of pensions, on the need to ensure that labour market mobility and non-standard employment forms do not penalise people's pension entitlements[12].

It is in this context, that in June 2002 the Commission decided to launch the first stage consultation of the European social partners on the portability of occupational pension rights.

The provision of an occupational pension is part of the remuneration package agreed between the employer and the employee through collective or individual bargaining. While this takes place within a regulatory framework established by the national legislator, the main responsibility lies with the two sides of industry. The Commission therefore expects the social partners to take an active role in addressing the issue of portability of occupational pension rights.

3. THE POSITION OF THE COMMISSION

Analysis of current situation

The work of the Pensions Forum and recent surveys conducted by the actuarial profession and independent experts[13] have confirmed that the insufficient portability of occupational pensions can create important obstacles to workers' mobility, and therefore to the free movement of persons in the European Union. While it is impossible to obtain empirical evidence of the impact of limited portability on the mobility of workers, action to enhance the occupational pension rights of job changers is fully justified on the grounds of fairness and non-discrimination.

Any change from one occupational pension scheme to another is likely to cause reduced pension rights at the end of career. National mobility, just like cross-border mobility, is affected by the lack of portability. Cross-border mobility can pose

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11 Commission Communication of 8 February 2002 (COM(2002) 72).

12 Common objective 9, contained in the Joint Report of the Social Protection Committee and the Economic Policy Committee on objectives and working methods in the area of pensions, as endorsed by the European Council of Laeken and available at: www.europa.eu.int/comm/employment_social/soc-prot/pensions/index_en.htm.

13 See in particular: "Actuarial standards for transfers between pension schemes in the countries of the EU and other European countries. A survey by the Groupe Consultatif", Groupe Consultatif Actuariel Européen (GCAE), June 2001; "Actuarial Methods and Assumptions used in the Valuation of Retirement Benefits in the EU and other European countries", GCAE, December 2001; "La transférabilité des droits à pension complémentaire dans l'Union européenne", Vincenzo Andrietti, in *Révue internationale de sécurité sociale*, vol. 54, 1/2001 and, of the same author, "Employer Provided Pensions Portability in OECD Countries: Country Specific Politics and the Labour Market Effects", OECD, Private Pensions Unit, May 2001. See also: "The evolution of supplementary protection in the pension sector and the free circulation of individuals within the single market", Giovanni Tamburi, in L. Paganello, *Social protection and single European market*, 1997.

aggravated problems, notably when it requires a change to a different scheme where a national job change would have been possible while remaining in the same scheme (e.g. in case of a job change within a sector or profession covered by a sector-wide scheme, or in case of a move between different subsidiaries of the same company or group of companies with a single pension scheme) and insofar as cross-border transfers may be impossible or more complicated to achieve. The recent adoption of the directive on institutions for occupational retirement provision[14] will make it easier for companies to set up pan-European pension funds which may facilitate cross-border mobility within groups of companies covered by such a fund.

If a worker leaves a pension scheme in order to work for a new employer, a guaranteed entitlement to a pension only exists if the worker has fulfilled certain conditions (e.g. minimum age for scheme membership, waiting periods before becoming a scheme member and minimum periods of scheme membership, or vesting periods, required for acquiring a right to a pension). Moreover, even if a worker acquires the right to a pension, this right may remain frozen in nominal terms until retirement or not fully index-linked, or that the transfer of pension entitlements is simply not allowed by national legislation. Specific conditions, related to the transfer itself or to the receiving scheme, can also limit the transferability of a worker's pension capital. Finally, the methods for calculating transfer values may lead to reduced pension benefits[16].

The conditions defining the rights of early leavers are usually fixed by the occupational pension schemes themselves, in the framework of national legislation, collective agreements or common practice, and can very much vary according to the characteristics of the schemes. The specific impact of these conditions in terms of pension portability can therefore differ to a large extent.

Defined-benefit (DB) vs. defined-contribution (DC) schemes[15]

In DB schemes, members are promised a certain level of pension benefits which is typically linked to the member's earnings and length of employment. Financial and longevity risks are primarily borne by the retirement institution or the plan sponsor.

In DC schemes, benefits to members are based on the amount contributed to the pension scheme by the employer and the member plus the investment return earned on the accumulated contributions, net of taxes and administration charges. If the retirement benefit is paid out as a regular pension income (annuity), its amount will also depend on interest (annuity) rates used for the conversion of the accumulated capital into an annuity. Thus financial and longevity risks are primarily borne by members.

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14 Directive of the European Parliament and of the Council on the activities and supervision of institutions for occupational retirement provision, 2003/41/EC of 3 June 2003.

15 In practice, the distinction between DB and DC schemes based on who bears the investment and longevity risk can be somewhat artificial. In DB schemes, members can share risks for instance if the indexation of pension benefits can be reduced or suspended. In schemes where the level of contributions is fixed, employers or the scheme can guarantee a level of return.

16 For some limited information on transferability options in the EU Member States and some other European countries see: Groupe Consultatif Actuariel Européen: *Actuarial Standards for Transfers between Pension Schemes in the Countries of the EC and other European Countries*, June 2001 (available on the web site of the GCAE: http://www.gcactuaries.org). The Commission will further investigate, in cooperation with the Pension Forum, what regulatory barriers to cross-border transferability exist and, where appropriate, consider action to remove such barriers.

The distinction between defined-benefit and defined-contribution schemes plays a major role in this context. The conditions for the acquisition and transferability of occupational pension rights are in fact typically stricter for defined-benefit plans. In this case, employee's future benefits are defined in advance and determined by a specific formula linking benefit accrual to employee earnings, length of service or both.[17] The employer or the pension scheme bears the risk of guaranteeing the payment of the pension promise.

In the case of defined-contributions plans the employer and/or the employee contribute to an account established for each participating employee. Contributions are defined either in absolute terms or as a proportion of earnings. Each scheme member has an individual account with an amount that can be easily preserved or transferred to another scheme of the same type. The resulting pension annuity reflects total contributions, investment returns as well as administration charges and annuity rates at the moment of converting the accumulated capital into an annuity[18]. Problems of portability usually do not arise in defined-contribution schemes. However, in this case beneficiaries have to bear the full investment and longevity risks and thus face far greater uncertainty about their future pension income.

Recent developments in Member States

The Joint Report by the Commission and the Council, adopted in March 2003 in the framework of the open method of co-ordination in the field of pensions[19], shows that in many Member States workers who change jobs tend to end their careers with reduced occupational pension rights compared to workers who remain with the same employer, and that atypical workers continue to be less well covered by occupational pension schemes.

It also results from the information provided in the national strategy reports presented by the Member States in September 2002[20], that reforms already adopted or envisaged in response to the common challenge of an ageing population tend to foresee a greater role for supplementary pension provision, thus adding to the importance of improving the portability of occupational pension rights so as to improve the social protection of mobile workers and their families. Public policy tends to compensate for the decreasing ability of statutory pension schemes to preserve the living standards achieved before retirement by promoting supplementary pensions which therefore become an increasingly important element of social protection. Member States may make occupational pension scheme membership

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[17] In the case of defined-benefit schemes, the level of benefits may be notably defined in fixed monetary terms, perhaps dependant upon the number of years of service that the employee has achieved (flat benefit arrangements) or, more frequently, in terms of the salary of the employee in combination with the number of years of service. In this case, the definition may be based upon the salary or earnings immediately (or over a specific period) prior to the commencement of benefit payments (final salary arrangements) or upon the salary throughout service (career average arrangements).

[18] It should be noted, however, that many occupational schemes pay out retirement benefits in the form of a lump sum which does not have to be converted in an annuity.

[19] Joint Report by the Commission and the Council on adequate and sustainable pensions, as endorsed by the Council on 6 March (Employment, Social Policy, Health and Consumer Affairs) and on 7 March 2003 (Economic and Financial Affairs) as a contribution to the European Council on 20-21 March 2003, pages 8-9, Council Ref. 6527/2/03/REV 2.

[20] The 15 national strategy reports, as well as the Joint Report by the Commission and the Council on adequate and sustainable pensions, are available at: www.europa.eu.int/comm/employment_social/soc-prot/pensions/index_en.htm.

mandatory, create favourable conditions for collective bargaining, oblige employers to provide private pensions or offer fiscal incentives and grants to encourage voluntary private provision. In the context of increasingly important second pillars, the portability of occupational pensions becomes a more pressing policy issue.

All Member States where second pillar pension provision is well developed seek to ensure, by legislation or through agreements between the social partners, that obstacles to mobility are minimised.

In countries where supplementary pension funds are not very common, the issue of portability has been less adequately addressed, but it is perceived as a means to increase their attractiveness. Therefore, in such countries measures to improve the portability of occupational pensions are recognised as a necessary corollary of reforms that seek to promote second-pillar pension provision.

Need for EU action

The implementation of the fundamental principle of free movement of workers, enshrined in the EC Treaty, involves guaranteeing the portability of pension rights, either statutory or supplementary, within the European Union.

However, while co-ordination of social security pension schemes allows migrant workers to fully preserve their accrued statutory pension rights, measures to improve the portability of occupational pensions are still in their early stages.

It is widely recognised that the specific legal and technical approach adopted to ensure the free movement of persons with regard to first-pillar pension provision would not be appropriate for most second pillar pension schemes. The difficulty principally lies in the fact that the system of aggregation and apportionment of contribution or other relevant periods and of pension entitlements adopted by Regulation 1408/71/EEC works well when applied to statutory pension schemes. By contrast, the multiplicity and diversity of occupational pension schemes as well as their often voluntary nature make it difficult to apply similar rules.

Other EU initiatives have been recently undertaken to promote the integration of the EU market for occupational pension provision. The recently adopted directive on institutions for occupational retirement provision (IORP)[21] is aimed at guaranteeing the free provision of occupational pension services across Europe, as well as the free movement of capitals in this sector. Once implemented, the common prudential framework and the mechanisms for co-operation and notification established by the Directive will allow for the mutual recognition of pension funds and will therefore greatly widen the scope for cross-border management of occupational pension schemes and cross-border membership. It will therefore allow pan-European groups of companies to set up pan-European pension funds, which may facilitate labour mobility within that group.

[21] See footnote 14

On the other hand, with the Communication of 19 April 2001 on the elimination of tax obstacles to cross-border provision of occupational pensions[22], the Commission decided to ask Member States to eliminate all national tax rules that, by discriminating against occupational pension institutions established in other EU countries, infringe the Treaty provisions on the free movement of workers and capital, as well as the freedom to provide services in the field of occupational pensions. This concerns both the cross-border payment of contributions to pension schemes (necessary for cross-border membership) and cross-border transfers of accumulated pension rights. The Commission is presently examining the relevant national rules and taking the necessary steps to ensure their compliance with the Treaty. Eight infringement cases against different Member States have already been opened[23].

With these two initiatives under way, the Commission believes that the lack of measures to ensure the portability of occupational pension rights, and the ensuing obstacles to the free movement of persons, represent a major gap in the realisation of the Internal Market in the field of occupational pensions, at a time when increasing mobility and more flexible labour markets require that pension systems be adapted so as to facilitate rather than inhibit job mobility, and when occupational pension schemes are called to play an increasingly significant role in social protection systems. The present consultation document, while acknowledging the importance of taxation as an obstacle to cross-border portability, focuses on those portability issues that can be addressed by the Social Partners.

4. THE RESPONSE OF THE SOCIAL PARTNERS TO THE FIRST STAGE CONSULTATION

The social partners responded to the first stage consultation with a broad recognition of the need for action at European level to improve the portability of occupational pensions.

Their views differed, however, on the instruments needed to address the issue and ranged from proposing non-binding exchanges of information to requesting the adoption of a Community legal instrument. Some organisations invoked the possibility of engaging in negotiations on a framework agreement at European level.

A number of employers' organisations (UNICE[24], UEAPME[25], HOTREC[26]) considered that a Community initiative on the portability of supplementary pension rights should limit itself to cross-border transfers; they opposed the introduction of EU legislation on the conditions of acquisition, preservation and transferability of occupational pension rights, insofar as this would go beyond cross-border issues and thus interfere with the organisation of supplementary pension arrangements at national level. In their view, a single solution at EU level could discourage

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22 Communication from the Commission to the Council, the European Parliament and the Economic and Social Committee of 19 April 2001 "The elimination of tax obstacles to the cross-border provision of occupational pensions" (COM (2001) 214).

23 See press release IP/03/179 of 5 February 2003 and IP/03/965 of 9 July 2003 on http://europa.eu.int/rapid/start/cgi/guesten.ksh. The countries concerned are Denmark, Belgium, Spain, France, Ireland, Italy, Portugal and the UK.

24 Union of Industrial and Employers' Confederations of Europe.

25 European Association of Craft and Small and Medium-sized Enterprises.

26 European Association of Hotels, Restaurants & Cafés in Europe.

employers from offering a supplementary pension scheme to their employees. The EU should therefore foster the portability of pensions by organising exchanges of experiences and information-sharing on the solutions found in the various European countries.

Other employers' organisations (FBE[27], CEA[28], FIEC[29]) supported the setting up of a common European framework to ensure the protection of occupational pension rights in case of labour mobility, but demanded that flexible instruments, such as recommendations, guidelines or codes of best practice, be adopted, so as to respect the large diversity of supplementary pension schemes in the Union.

UEAPME recommended a detailed study to be conducted, so as to put more information at the disposal of the social partners and the Member States before deciding upon the best possible course of action. It suggested that problems of mobility within a Member State be addressed within the open method of co-ordination in the field of pensions.

The European Centre of Enterprises with Public Participation and of Enterprises of General Economic Interest (CEEP) supported EU action on the portability of supplementary pensions and suggested that the social partners take the lead, in the framework of the European social dialogue. Moreover, it considered that certain aspects of transferability could be resolved through a directive.

All the employees' organisations (ETUC[30], CEC[31], EUROCADRES[32]) clearly expressed themselves in favour of a European regulatory framework. In their opinion, the best form of action would be a Community directive, setting common principles to ensure the portability of occupational pension rights within the Union. Being aware of the difficulties linked to the question of vesting periods, ETUC suggested that negotiations could be engaged on this issue with a view to reaching a framework agreement setting broad principles at European level. EUROCADRES suggested that a directive should intervene only if the European social partners fail to engage in negotiations on a framework agreement on pension portability.

As regards the substantive issues raised in response to the Commission's first stage consultation, all the respondents recognised that unnecessarily long waiting and vesting periods or excessively high minimum ages obstruct the development of occupational pension schemes and labour mobility, and therefore have to be reconsidered. They also agreed that reductions in vesting periods should be phased in gradually, so as to limit the additional costs associated with their reduction for the employers. The social partners equally agreed that acquired occupational pension rights should be adequately preserved and that the transferability of pension entitlements should be facilitated. On the last point in particular, UNICE and UEAPME took the view that the calculation of transfer values should not be left to the discretion or interpretation of the actuary and supported the definition, insofar as possible, of some basic common actuarial principles at European level. All the

27 Fédération Bancaire de l'Union européenne.
28 Comité Européen des Assurances.
29 European Construction Industry Federation.
30 European Trade Union Confederation.
31 Confédération Européenne des Cadres.
32 Council of European Professional and Managerial Staff.

organisations also wanted to stress that improved information, transparency and simplification are needed to ensure an effective portability of occupational pension rights.

Regarding the choice between collective bargaining at cross-sectoral or sectoral level, the large majority of the social partners favoured a cross-sectoral approach to the question, while leaving open the door for sector-based agreements in those professions and sectors that are the most concerned by geographical mobility.

Finally, most organisations demanded that Community action focus on schemes financed jointly by the employer and the employees, without distinction between pension entitlements based on individual contracts and those based on collective agreements, thus leaving out of the scope of the envisaged measures all voluntary occupational pension schemes solely financed by the employer. UEAPME proposed that transnational measures apply to compulsory pension schemes.

5. SCOPE OF THE ENVISAGED COMMUNITY ACTION

Occupational pension schemes to be covered

Occupational pension arrangements (also called second pillar pensions) exist in many different forms in both the public and private sector. They are characterised by their link to employment, can be set up on a voluntary or mandatory basis and may operate at the level of individual companies, sectors or professions. The accrual of occupational pension rights may be laid down in individual employment contracts or collective agreements, or be conceived as a discretionary employment benefit offered by the employer.

Third pillar individual pensions without any link to the employment status are excluded from the scope of this initiative. The same applies to first pillar schemes already covered by Regulation 1408/71/EEC. Conversely, any specific first pillar pension schemes which are not covered by Regulation 1408/71/EEC could come within the scope of this initiative.

The scope of the proposed initiative will necessarily differ from that of the Directive on IORP[33], insofar as it addresses occupational pension arrangements from the point of view of beneficiaries and not of pension institutions as financial services providers. Whilst the IORP Directive aims at regulating the provision of supplementary pensions within the Union as a condition for an effective implementation of the principle of freedom to provide services, the present initiative aims at ensuring the free movement of persons.

The Commission is aware of the fact that changes to the rules governing the portability of pensions in the Union will affect various occupational pension schemes differently. Measures aimed at improving the portability of pension rights tend to impose additional constraints on pension schemes that may discourage some employers from offering occupational pension coverage to their employees. It may therefore be necessary to provide for a certain degree of flexibility in the portability requirements. While it would be desirable to remove obstacles to mobility in all

[33] See footnote 14.

supplementary pension schemes, the social partners may want to focus on certain types of pension schemes. Certain schemes may have been established unilaterally by the employer mainly to reward staff loyalty , whereas others represent an essential complement to the first-pillar pension scheme, in which case a lack of portability would leave the more mobile workers without adequate social protection.

The social partners could also seek to improve cross-border portability for members of pension schemes that are set up at the level of a sector or a profession. These are among the most important pension schemes, both in terms of numbers of members and in terms of their contribution to social protection and they tend to be jointly managed by the social partners. The wide coverage of such schemes already greatly facilitates mobility at the national level to the extent that a significant proportion of job moves take place within a given sector or profession covered by such schemes. However, as soon as mobility within such a sector or profession takes place across borders, members are confronted with new obstacles to portability.

Required level of action

The work of the Pensions Forum and the surveys conducted by the GCAE show that many of the obstacles identified affect both workers changing jobs within a country and workers moving from one Member State to another. If the Commission proposed measures that only apply to migrant workers, these would, as a result, be likely to enjoy a better protection of their occupational pension rights than workers changing jobs within the same country.

The Commission believes that an action aimed at removing obstacles to pension portability should not be limited to cross-border mobility, but should cover both workers moving within a country and those moving across borders.

6. POSSIBLE CONTENT OF MEASURES TO IMPROVE THE PORTABILITY OF OCCUPATIONAL PENSIONS

The Commission would favour the definition of a general framework setting the minimum requirements needed to ensure an improved portability of occupational pension rights within the European Union. Such minimum requirements, to be implemented gradually, should facilitate the acquisition of occupational pension rights, guarantee an adequate protection of dormant rights of early leavers, facilitate the transfer of acquired pension rights and ensure appropriate information of scheme members in the event of professional mobility.

Acquisition of occupational pension rights

The acquisition of occupational pension rights is subject to certain qualifying conditions which may include waiting periods (period of employment before admission to membership of a pension arrangement), vesting periods (minimum scheme membership periods in order to acquire a vested pension entitlement) and minimum or maximum age conditions, needed either for entry into an occupational pension plan or in order to achieve vesting of benefits. The length of vesting periods can vary between nil and vesting at retirement (or death/invalidity for survivors and invalidity benefits).

Workers leaving the plan before having met the qualifying conditions will not acquire any pension rights in respect of this employment period[34]. In this case, mobility can result in greatly reduced occupational pension rights compared to workers who remain during their entire career within the same pension scheme.

The Commission considers that it is important to ensure that the conditions for the acquisition of occupational pension rights (waiting and vesting periods, age requirements) do not act as a deterrent to labour mobility in the European Union.

Achieving the afore-mentioned goal would imply that pension rights become vested after the shortest possible employment period. Waiting and vesting periods could therefore be reduced to a minimum and age conditions could be eliminated. A maximum combined length of waiting and vesting periods could be set at European level. The report by a working group of the Pensions Forum suggested that vesting should occur no later than one year after starting employment[36].

The Commission is aware of the fact that employers are likely to be concerned with the cost implications of a sudden shortening of waiting and vesting periods and that this could discourage them from providing supplementary pensions to their employees. It could therefore be envisaged to reduce such periods gradually over a transitional period which could, for instance, correspond to the current length of the vesting periods themselves (e.g. 4 years for a reduction from 5 to 1 years). Any rise in the total amount of vested pension rights would therefore be gradual and spread over a reasonable lapse of time. A distinction could be made

Impact of certain acquisition rules on pension rights[35]

We assume that all employers offer a pension worth 1% of final earnings for each year of employment. The employee earns €10000 per year during a career starting at 25 and ending at 65 (40 years). There is no inflation.

Employee A remains with the same employer during the entire career: the pension will amount to €4000 per year.

A mobile career can result in significantly lower pension entitlement.

Suppose employee B works between 25 and 28 in a scheme where pension rights only vest at 30; for the next 7 years, B works for another employer with a scheme with a 10-year vesting period. At 36 years of age B still has not earned any pension rights. The third job, held between 37 and 49 (13 years) gives rise to pension rights for 11 years because of a waiting period of 2 years before being admitted into the pension scheme. A fourth job held between 50 and 55 gives rise to no pension entitlement because the employee has to be in the company at the moment of retirement in order to obtain a pension. The last job, between 56 and 65, is covered by a scheme with a waiting period of one year.

The resulting pension at the end of employee B's career would amount to only €1900 per year.

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34 However, they would usually be entitled to a refund of their own contributions.

35 Please note that the examples proposed in this and the following boxes are purely hypothetical and extremely simplistic. They are not intended to reflect the actual situation which is characterised by a high level of complexity and diversity of occupational pension arrangements. The purpose of this calculation is only to demonstrate how acquisition rules can reduce pension rights after a particularly mobile career..

36 Views on what could be achieved in terms of reducing vesting and waiting periods differ within the Pensions Forum.

between employer and employee contributions, with the latter being fully protected and statutorily refundable before the acquisition of a vested pension right.

Finally, as explained above, the social partners could consider agreeing on particularly short waiting and vesting periods for schemes covering a sector or a profession and which facilitate already mobility at the national level. Alternatively, the recognition of employment periods in the same sector or profession in another Member State could be considered.

Preservation of acquired pension rights

Vested rights accrued by early leavers can be either maintained in the scheme of origin until retirement or transferred into another pension scheme. In the first case, the accrued rights must be preserved within the scheme of origin. Such preservation may be limited to a nominal value. This implies that the real value of preserved pension entitlements would fall as a result of inflation. Moreover, pay rises are not reflected in pension entitlements. Frequent job changers who leave their entitlements in different pension schemes will therefore receive reduced occupational pensions at the end of their careers compared to people who remain within the same pension scheme.

Indexation mechanisms for preserved rights exist in a number of countries. The UK requires that "dormant" rights are up-rated in line with inflation up to a maximum of 5% per annum. In Ireland, vested benefits preserved under defined-benefit plans must be revalued by up to 4% or the annual rate of increase of the consumer price index.

However, the GCAE survey conducted in June 2001[37] shows that only about one third of the 21 countries[38] surveyed have a statutory requirement to increase part or all of the deferred benefits broadly in line with price inflation, and that in the remaining countries this may be done on a discretionary basis, but in practice in almost half of the countries increases are not granted. Similarly, post-retirement indexation of deferred benefits is guaranteed by law only in the Netherlands and in the United

Impact of preservation rules on pension rights

The same schemes as for the previous example are assumed. Employee C worked for 20 years for one employer and for another 20 years for another. Inflation is at 2% per annum during the entire period. Real wages are constant and their nominal amounts are €10000 at the beginning and €22522 at the end of the career.

Employee A (entire career with the same employer) will receive a pension of €9009 per annum (40% of final earnings).

Employee C will receive a €3031 from the first employer and €4505 from the second employer. The total pension amounts to €7536 per annum (33% of final earnings). The higher the inflation rate, the greater the mobility loss due to insufficient preservation.

The mobility loss will be amplified by the fact that individual earnings tend to rise faster than prices or even aggregate earnings.

The losses of pension rights due to acquisition, preservation and transfer rules are cumulative.

37 See footnote 16.

38 Austria, Belgium, Cyprus, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Latvia, Luxembourg, Netherlands, Norway, Portugal, Slovenia, Spain, Sweden, Switzerland, UK.

Kingdom. In the Netherlands, indexation of deferred annuities is required whenever the scheme provides indexation for normal retirement pensions in payment[39].

The Commission considers that serious consideration should be given to the preservation of dormant rights, so that they are not frozen in nominal terms.

The Commission is, however, aware of the significant costs of such indexation requirements. One option could be to introduce limited inflation adjustment, as it is currently the case in Ireland and in the United-Kingdom[40]. Other options could also be considered such as requiring that dormant rights be adjusted at the same rate as pensions in payment (i.e. if inflation indexation is applied to pensions in payment, it would also have to be applied to dormant rights) or that dormant rights be linked to the performance of the fund[41].

Transferability of acquired pension rights

Transferability refers to the possibility of transferring a capital value representing the acquired pension entitlements from one pension scheme to another. The survey realised by the GCAE in June 2001[42] found that a legal right to a transfer existed in 13 of the 21 surveyed countries. In five other countries transfer payments were a common practice, but on a discretionary basis; finally, in three countries the transfer of pension rights was not possible at all. Cross-border transfers to a pension scheme in another European country were possible in only eleven countries, in some cases subject to the approval of the regulator or tax authority. In certain countries, the tax charge could be so high that it prevented, in practice, any cross-border transfer.

Is it better to transfer one's pension rights?

Transferring one's pension rights has the advantage of administrative simplicity, both for the mobile employee and for employers: there is no need to manage a large number of small entitlements. However, the employee will normally not be better off than by leaving the acquired rights in the previous scheme: the transfer amount is at best the actuarial equivalent of the pension promise acquired by the employee. Thus the absence of an inflation guarantee will be reflected in a significantly smaller capital than in the case where the preserved pension entitlement is index-linked to prices or even earnings (see previous box for an illustration of the effect of inflation proofing).

The Commission considers that it would be desirable to ensure that the largest possible number of job changers have the possibility to choose between preserving their acquired pension rights in the scheme of origin and transferring the corresponding capital value to another pension scheme, including in another Member State.

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39 Source: "Employer Provided Pension Portability in OECD Countries. Country Specific Policies and Their Labor Market Effects", Vincenzo Andrietti, OECD Private Pension Unit, May 2001.

40 However, in practice, individual earnings tend to rise faster than inflation. A worker with an uninterrupted career with the same employer will accrue pension rights in line with rising earnings, whereas the early leaver will not get an earnings adjustment on pension rights preserved in the previous pension scheme. This will result in a lower total pension for mobile workers unless they can achieve significantly higher pay levels from subsequent employers or better occupational pension coverage.

41 In the case of defined-contribution schemes it would be important to ensure that the accumulated rights of early leavers grow at the same rate as those of active scheme members.

42 See footnote 16.

However, it would be legitimate to require that the capital to be transferred is used for pension purposes only and handed over to an institution that can guarantee the safe management of the pension rights. These could be institutions approved according to the requirements set in the IORP Directive, life insurance companies or institutions covered by Regulation 1408/71/EEC if they are authorised to accept additional voluntary contributions.

> ***The importance of actuarial assumptions in transfer calculations***
>
> *Two types of assumptions are particularly important: life expectancy (mortality tables) and technical rates of interest (needed to convert a capital into an income stream).*
>
> *Suppose that employee C has earned a pension entitlement of €1000 per year from age 65 with an employer that C has left at the age of 45. At an interest rate of 2% the transfer amount would have to be nearly €9000 for a life expectancy of 15 years and around €11000 for a life expectancy of 20 years.*
>
> *At an interest rate of 6% the transfer amount would have to be as low as €3000 for a life expectancy of 15 years and around €3600 for a life expectancy of 20 years.*
>
> *If the first employer's scheme uses a high (optimistic) interest rate assumption and the second employer's scheme a prudent one the transfer amount may only be sufficient to buy a much reduced number of years of service in the new scheme. The final pension will correspond to a shortened career.*

The GCAE survey of June 2001 also raised the problem of differing methods and assumptions used to calculate transfer payments from one Member States to another. As mentioned above, transfers between defined-contribution schemes (where the transfer value can be simply the market value of the assets held on behalf of an individual scheme member) do not pose any major problems, the only obstacle being the administrative costs linked to the transfer and taxation. Transfers between defined-benefit schemes may, by contrast, entail serious pension losses due to different actuarial methods and assumptions used by the pension institutions involved in a transfer. In the case of defined-benefit plans, the transfer value is the actuarial value of the liabilities linked to the pension promise and the assumptions used may fall within the discretion of the actuary.

> ***Tax issues***
>
> *Most Member States allow pension scheme contributions to be deducted from taxable earnings and levy income tax on pension benefits instead (deferred taxation). Tax payers gain to the extent that their marginal tax rate is higher during their working lives than after retirement. By denying the deductibility of contributions to a pension scheme in another Member State, cross-border membership is made unattractive. Moreover, there is a risk of double taxation if the country of residence after retirement taxes all pension income regardless of whether contributions were paid from taxed income or not.*
>
> *A similar issue arises in relation to transfers: The national tax authorities may reclaim the income tax that was not paid on pension scheme contributions. This could easily represent one third of the transfer amount and thus constitute a major hindrance to transfers. If a transfer is only authorised into another retirement scheme (as opposed to other forms of savings), the eventual pension benefit may still be subject to income tax.*

While an agreement on common actuarial assumptions applicable across the EU (notably the technical interest rate and the mortality tables used for calculating

transfer values[43]) seems unlikely, it might be helpful to apply the same actuarial assumptions for scheme leavers and new entrants both at the level of an individual scheme and between two schemes involved in a particular transfer.

The Commission considers that it would be desirable to ensure that job changers enjoy fair actuarial conditions when they opt for a transfer of their accrued pension rights.

Cross-border membership

The IORP Directive, which establishes the right for pension institutions to manage pension schemes on a cross-border basis, the action engaged by the Commission to address discriminatory tax treatment against cross-border provision of occupational pensions and the provisions of Directive 98/49/EC on cross-border membership of posted workers will all enhance the possibilities for migrant workers to remain in the same pension scheme while moving to a job in another Member State.

The Commission considers that the impact of these measures should be evaluated before proposing any further steps in the area of cross-border membership.

Information requirements

Article 7 of Directive 98/49/EC requires that information provided to scheme members when moving to another Member State should at least correspond to information given to scheme members in respect of whom contributions cease to be made, but who remain within the same Member State.

Nonetheless, the Directive does not contain any provision on the effective level of information provided to scheme members who leave a pension scheme. The only provisions in this respect are contained in Article 11 of the IORP Directive which provides for detailed and substantive information of scheme members and beneficiaries on the target level of benefits, on the actual financing of accrued pension entitlements and on the level of benefits in case of termination of employment. In particular, the directive provides that pension scheme members will receive every year particulars on the current level of financing of their accrued individual entitlements. Moreover, each member can receive, on request, information on the arrangements relating to the transfer of pension rights to another pension fund in the event of termination of the employment relationship. Such rights should also be guaranteed to members of occupational pension institutions that are not covered by the IORP directive.

The Commission considers it necessary to ensure that scheme members are made fully aware of their rights, notably in case of job mobility.

Action should therefore be taken to guarantee sufficient information for all pension scheme members in particular those of institutions that are not covered by the IORP

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[43] In case of defined-benefit plans, the projected flow of pension benefit payments must be discounted using a specified rate of interest to determine their present value. The higher the interest rate, the lower is the amount of contributions (or capital) needed to meet the pension promise and hence the amount available for a transfer. A differential between the interest rate applied by two institutions in the event of a transfer (higher in the scheme of origin and lower in the receiving scheme) may imply reduced pension entitlements for the employee concerned by the transfer.

directive on the rights they have acquired, on the options available to them in the event of a job change or career interruption and on the costs associated with these options.

7. QUESTIONS TO THE SOCIAL PARTNERS

In the light of the above and taking into account the provisions of Article 137(1) of the EC Treaty[44], according to which the Community shall support and complement the activities of Member States in the area of social security and social protection of workers, the Commission considers that there is scope for legislative action fixing minimum requirements to improve the portability of occupational pension rights within the European Union. However, the Commission believes that the most appropriate instrument would be a collective agreement at European level.

Given the very nature of occupational pension schemes, which are often based on the autonomous initiative of the social partners at branch or company level or at the initiative of the employer, the Commission is convinced that the European social partners are in a position to make a major contribution to the solution of problems linked to the portability of occupational pensions in the European Union.

In particular, considering that ETUC, UNICE and CEEP, in the Preamble of the framework agreement on fixed-term work[45], have already recognised that "innovations in occupational social protection systems are necessary in order to adapt them to current conditions, and in particular to provide for the transferability of rights", the Commission strongly hopes that, on the basis of the principles contained in this document, the social partners will make use of the possibilities provided for in Article 139 of the EC Treaty, in view of a European framework agreement.

The Commission invites the social partners:

(1) To present an opinion or, where appropriate, a recommendation on the possible content and scope of the envisaged initiative, aimed at improving the portability of occupational pension rights within the Union, in accordance to Article 138(3) of the EC Treaty;

(2) To inform it, where appropriate, of their resolve to undertake the negotiation procedure on the issues set out in the present document, pursuant to Article 138(4) and Article 139 of the EC Treaty, and, if so, whether they wish to adopt a global approach or concentrate on certain aspects of portability and what scope they would envisage for the negotiation process (type of pension funds to be covered).

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44 As modified by the Nice Treaty.

45 Implemented by Council Directive 1999/70/EC of 28 June 1999, concerning the framework agreement on fixed-term work concluded by ETUC, UNICE and CEEP (OJ L 175 of 10 July 1999, p.43).