



aba comment
on the
Study on the performance and adequacy of pension decumulation practices
in four EU countries

20 March 2017

The **aba - Arbeitsgemeinschaft für betriebliche Altersversorgung e.V.** - is the German association representing all matters concerning occupational pensions in the private and public sector. The aba has 1,100 members including corporate sponsors of pension schemes, IORPs, actuaries and consulting firms, employer associations and unions, as well as insurance companies, banks and investment managers. According to our statutes, our mission is to represent existing schemes as well as to expand coverage of occupational pensions independent of vehicle. We are a member of PensionsEurope, where we are active both on the board and in a variety of working groups.

The study (commissioned by the European Commission and carried out by Ernst and Young), a summary and a position paper by the Financial Services User Group¹ can be downloaded [here](#).

Main points

- **Objective of the study:** The aim of the study is to analyse the pension decumulation practices in four EU countries (UK, Netherlands, Germany and Poland) with a focus on consumer choice and the adequacy of the options chosen. However, we do not think that the study actually achieves this objective: For Germany it mostly covers Riester, Rürup and pension insurance contracts and is overall relatively superficial.
- **Scope of the study:** While the title and other aspects of the study suggest that occupational pensions are included, for Germany this is not the case, and it is not explicitly explained why they were left out. In addition, with the UK decision to leave the EU, the focus on the UK system seems questionable.
- **Quality of the study:** We find that the study falls short of quality in several areas manifesting itself as a lack of references to legal or official sources; it contains misrepresentations of the German pension system and in some areas lack clarity.
- **Lump sum payments and pensions:** From a social policy perspective certain restrictions and/or incentives to steer individuals in their decision making in the decumulation process away from lump sum payments are sensible. On this background we are surprised by the positive stance the study takes towards lump sum payments and by the lack of an overview table detailing the provisions different countries have in place.
- **Conclusions:** We would like to caution the European Commission to use the positive description of lump sum payments for the design of a potential future PEPP, because this would not be desirable from a social policy perspective. As the part on Germany is misleading and lacks quality, it should not be used as a basis for any policy-making. If it is not already the case, the European Commission should in the future contractually require international consultancies to make use of their national experts in different jurisdictions.

If you have any questions, please do not hesitate to contact:

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¹ The members appointed to the Financial Services User Group between 2013 and 2016 supported this study. In February 2017 a [Call for applicants for new members was published](#).

Zusammenfassung

- **Ziel der Studie:** Das Ziel der Studie war es, verschiedene Auszahlungsformen betrieblicher und privater Altersversorgung zu analysieren. Sie betrachtete dazu die Auszahlphase in vier Ländern (Großbritannien, Niederlande, Deutschland und Polen). Die Angemessenheit der Entscheidungen, die Begünstigte getroffen haben, sollte analysiert werden. Aus unserer Perspektive erfüllt die Studie ihren eigenen Anspruch jedoch nicht: Für Deutschland beschränkt sie sich im Wesentlichen auf private Riester-Renten, Rürup-Renten und private Rentenversicherungen und bleibt mit ihren Beschreibungen oberflächlich.
- **Umfang und Schwerpunkt der Studie:** Titel und Rahmen der Studie legen nahe, dass die betriebliche Altersversorgung in die Studie einbezogen wird. Für Deutschland ist dies allerdings nicht der Fall. Es wird auch nicht erklärt, warum die betriebliche Altersversorgung mit rund 20 Mio. aktiven Anwartschaften im Hauptteil der Studie unter den Tisch fällt. Darüber hinaus liegt der Schwerpunkt der Studie auf dem britischen System, was nach dem Votum der Briten, die EU zu verlassen, verwundert.
- **Qualität der Studie:** Die betriebliche und private Altersversorgung in Deutschland werden teilweise missverständlich und unklar dargestellt. In der Studie werden weder deutsche Gesetzestexte noch Fachliteratur zitiert.
- **Kapitalzahlung und Altersversorgung:** Aus sozialpolitischer Sicht sind gewisse Einschränkungen und/oder Anreize in der Auszahlphase sinnvoll, um eine lebenslange Absicherung der Menschen zu erreichen. Vor diesem Hintergrund überrascht es, dass die Studie diese Einschränkungen für die untersuchten Länder nicht klar auflistet und Kapitalzahlungen positiv wertet. Diese positive Darstellung von Kapitalzahlungen sollte daher keinen Einfluss auf den erwarteten legislativen Vorschlag der EU-Kommission zu PEPP (Pan-European Personal Pension Product)² haben.
- **Fazit:** Die Ausführungen zur betrieblichen und privaten Altersversorgung in Deutschland sind teilweise missverständlich und von unzureichender Qualität. Sie sollten daher nicht als Grundlage für Politikempfehlungen oder gar Entscheidungen dienen. Falls es nicht bereits der Fall ist, sollte die EU-Kommission vertraglich festlegen, dass internationale Berater ihre jeweils nationalen Experten für Projekte dieser Art auch nutzen.

Für Rückfragen stehen Ihnen gern zur Verfügung:

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² Mehr Informationen zum PEPP: [aba Website](#)

I Objective of the study

The study on decumulation practices was published in October 2016 by the European Commission (DG Financial Stability, Financial Services and Capital Markets Union). The aim of the study is to analyse the decumulation practices in four EU countries (UK, Netherlands, Germany and Poland) with a focus on consumer choice and the adequacy of the options chosen.³ To better understand the consumers' perspective, issues such as information, advice, market structure and regulation trends are being considered.

The title of the study („...pension decumulation practice...“) suggests that the study covers supplementary pensions, i.e. both occupational and personal pensions. The introduction states that the study will look at decumulation products that are offered through Pillar II and Pillar III DC schemes. For Germany, Riester, Rürup and pension insurance contracts are mentioned in the report. Occupational pensions are mentioned where the national debates are outlined, and they appear in the annex. The study does not explicitly explain why German occupational pensions are not considered in the main part.

The study is rather descriptive and does not make concrete policy recommendations. However, certain practices are emphasised as positive, e.g. shopping around, and lump sum payments providing better value for money (see detailed comment on that below) and are therefore implicitly recommended.

Neither the study nor the tender state any relation to the development of a pan-European Personal Pensions Product (PEPP). However, issues around decumulation have been discussed in that context and it is likely that the insights provided by the study will be used.⁴ With this in mind we are surprised that only four countries were analysed (the tender suggested 7), and that one of the countries chosen is the UK: after the Referendum to leave the EU, the importance of the UK for EU matters is declining. For a potential PEPP the situation in the UK is becoming less and less relevant – this should have at least been acknowledged in the study. We also note that both in terms of quantity of text and sources analysed (see the List of References in Annex 4) the study shows a bias towards the UK.

We do not think that the study actually achieves its objective of an analysis of decumulation practices. For Germany it neglects the existence of the second pillar in the main part, and is overall relatively superficial. We discuss both points in detail below. Before we turn to the conclusions, we briefly comment on the study's assessment of lump sum payments.

II Scope of the study

The title of the study („... pension decumulation practices ...“) as well as the objective quoted above suggest that the study looks at all supplementary pension systems, that is both the second and third pillar. This impression that occupational pensions are included in the study is reinforced by the Glossary, where concepts only relevant in the second pillar (defined benefit and defined contribution pensions) are explained. In addition, the outline of national debates contain references to occupational pensions. Regarding the scope of the report, the introduction states „...the decumulation products considered in this study are those offered through Pillar II and Pillar III DC schemes.“ (p. 11)

³ The study is also intended to cover issues the EIOPA report „[EIOPA's fact finding report on decumulation phase practices](#)“ (October 2014) did not cover. For the objective, see also the [Tender for the study](#).

⁴ It is expected that the Commission will publish a legislative proposal regarding the PEPP in the second quarter of 2017.

From our perspective it is not clear to the reader what this means for Germany: Which types of pensions are analysed in this report (Riester and Rürup pensions are named, as are pension insurance contracts)? Does this mean that for Germany only the third pillar is included? Are occupational pensions only covered in the context of current national debates and in the Annex because they are all DB?⁵

In addition to being considered DB or DB hybrid, German occupational pensions in most cases comprise both the accumulation and the decumulation phase. At the point of retirement, there is almost no consumer choice and therefore some of the issues mentioned in the report (information, advice, shopping around) do not apply here. If these were the reason for excluding German occupational pensions from the analysis, this should be stated clearly and the reasons should be explained. As it currently stands, the study paints a misleading picture for German supplementary pensions.

Overall, while the title and other aspects of the study suggest that occupational pensions are included, for Germany this is not the case, and it is not explicitly explained why they were left out.

III Quality of the study

We would expect from the European Commission as well as from a company like Ernst & Young that a certain level of quality is ensured. However, we find that the study falls short of quality in several areas, it contains misrepresentations of the German pension system and in some areas lack clarity.

From our perspective the study does not live up to a certain **standard of quality** for a number of reasons:

- It seems that the authors were relatively new to the German supplementary pensions system. This manifests itself in a lack of references to legal texts or official sources – rather, a website for expats in Germany is quoted as reference on Rürup pensions (www.howtogermany.com). Considering in addition the list of references, it doesn't look as if the authors had truly analysed the German supplementary pension system.
- The German experts listed in the Annex have a background in insurance / the third pillar. While this is fine if the focus is on the third pillar, this is not sufficient if the study is intended to cover the second pillar as well.
- As a mirror of the analysis conducted, the list of references is dominated by sources on the UK (ABI, FCA, HM Treasury, House of Commons), neglecting the other countries in the study.
- Throughout the study responses of the interviewed experts are shown. Particularly where this is done in a quantitative manner, the number of respondents should be clearly stated.

⁵ Background: In Germany the pension promise can take three forms: traditional DB, contribution oriented DB with an annual minimum return guarantee (beitragsorientierte Leistungszusage) or contribution oriented with minimum guarantee of sum of nominal contributions at retirement (Beitragszusage mit Mindestleistung). All of these include guarantees, a pure DC scheme would not qualify as an occupational pension in Germany. Currently a reform which is set to introduce a pure DC pension promise within a specific framework is under way. The conditions of the framework are still being discussed.

In addition, the **Germany pension system is misrepresented** in several areas:

- Figure 1 (p.11) does not show any supplementary pension income in Germany. While it is right that only the first pillar is legally mandatory, this figure presents a skewed picture of income in old age in Germany.
- Box „Description of pension schemes in Poland and Germany“ (p. 21): In Germany there are not only Riester, Rürup and pension insurance contracts. In 2015, there were 20.4m active occupational pension scheme memberships.⁶ Under the headline “Description of pension schemes” we would expect these scheme memberships to be considered.
- National debate in Germany (p. 62): Here the focus for the first time is on the German occupational pension system. Disregarding the fact that this does not fit the previous analysis of Riester, Rürup and pension insurance contracts, it does not reflect the current national debate in Germany adequately. While it is right that a social partner model was being discussed back in October 2016 (and is currently in the process of being adopted), the mention of auto-enrolment is misleading. The law is intended to make it legally watertight for the tariff partners to use auto-enrolment, however, it was not seriously considered to be introduced nation-wide (the text does not state this explicitly, but with the UK in mind, “introduction of auto-enrolment” suggests a nation-wide roll-out).
- Appendix 1: Countries profile states on the second pillar in Germany: “Employees typically have 2 decumulation options: a lifetime annuity or a lump sum payment.” From our perspective a right to choose is not typical in this area, and even if beneficiaries have the right choose, the tax framework steers them away from lump sum payments.⁷

The study is in places **not clear** about what certain findings refer to or what is included in the data presented:

- Table 1 (p. 28): „Most common decumulation products“: For Germany, what does this table refer to? It looks like it only refers to the third pillar, if that is correct, it should be clearly stated.
- Box on p. 46: 80% of respondents said that in Germany consumers are not informed about the overall costs /fees they pay. Again, it is not clear what this refers to – exclusively to the third pillar? How many responses were there for this question?
- Section 3.2.1 Availability of advice: the terminology for Germany is unclear here, what does “pension administrator” refer to?

⁶ Bundesministerium für Arbeit und Soziales (2016): Ergänzender Bericht der Bundesregierung zum Rentenversicherungsbericht 2016 ([Alterssicherungsbericht 2016](#)), p. 131.

⁷ Until 2005, Pensionskassen and Direktversicherungen could offer memberships under Art. 40b EStG (TEE taxation). The insurers used to offer choices concerning the pay-out of Direktversicherungen. Therefore it was possible / attractive to take a lump sum payment at retirement. In 2005 the taxation of pension (state, occupational and personal) was reformed and the EET system became standard for occupational pensions. It is still possible to contribute to the contracts of Pensionskassen and Direktversicherungen made before 2005 under Art. 40b, but all new contracts fall under Art. 3.63 (EET taxation), which includes measures which steer beneficiaries towards a life-long pension. A recent judgement ([Urteil vom 20.9.2016, X R 23/15](#)) of the Bundesfinanzhof (Federal Fiscal Court) ruled that lump sums in contracts based on 3.63 taxation will be taxed as income in the year they are taken out, making lump sums very unattractive.

Considering that Ernst & Young is already carrying out a feasibility study of a European Personal Pension Framework for the Commission and are likely to carry out many other studies in the future, care should be taken to ensure a certain level of quality.

On a positive note, we welcome that in many parts the report lists the limitations of the data available / the conducted analysis (in the boxes labelled “Data concerns”).

IV Lump sum payments and pensions

In some countries, one decumulation option is to take a lump sum payment. Beneficiaries are free to decide what they want to do with the received lump sum: some might pay off a mortgage, invest it in shares, annuitise parts of it later or spend it all straight away. In other countries, the tax relief which is granted on contributions made to a supplementary pension comes with strings attached: sometimes it is only possible to take out a small amount as a lump sum, sometimes it might not be possible at all. In other systems, it is not directly forbidden to take out a lump sum, but the tax framework is designed in a way to strongly discourage beneficiaries from using this option.

Particularly with a view to the structural reforms of the first pillar taking place in many countries, there are good reasons for these restrictions from a social policy perspective. While it might be attractive for beneficiaries to take out a lump sum, they might run out of money in the course of their retirement and fall back on social assistance. This is neither desirable for the recipient nor for the tax payer who ultimately has to foot the bill. We therefore welcome certain restrictions and/or incentives to steer individuals in their decision making in the decumulation process away from lump sum payments.

On this background we are surprised about the positive stance the study takes towards lump sum payments. The figure in the Box on p. 22 shows that the majority of experts asked considers taking a lump sum „not expensive“, while annuity products are considered „expensive“ by 39% of respondents and „not expensive“ by 61% of respondents. What is the message the figure is supposed to convey? That taking a lump sum is a better deal because it is considered less expensive by experts? Later on the report discusses this issue (in relation to the money’s worth ratio, p. 25 - We very much agree with the caveat inserted in the box on p. 25. If you are aware of these problems, why are you making the comparison?), and states that an annuity covers longevity risk while a lump sum of course does not, making a comparison based on returns difficult – we wonder why this figure was included if the authors were aware of the caveats of the comparison?

V Conclusion

Overall, we are disappointed that the study did not live up to its potential and – at least for Germany – did not provide any deeper insights into the decumulation practices of supplementary pensions. Not mentioning 20.4m occupational pension scheme memberships paints a misleading picture of German supplementary pensions.

We would like to caution the European Commission to use the positive description of lump sum payments for the design of a potential future PEPP, because this would not be desirable from a social policy perspective. As the part on Germany is misleading and lacks quality, it should not be used as a basis for any policy-making.

If it is not already the case, the European Commission should in the future contractually require international consultancies to make use of their national experts in different jurisdictions.

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