Arbeitsgemeinschaft
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Assessment of the proposal for a directive on improving the portability of supplementary pension rights

As the association responsible for all questions relating to occupational pensions in both the private and public sectors and held by its constitution to even-handedly promote occupational pensions in Germany, we have grave concerns about the proposed legislation to improve the portability of occupational pension rights. We fear that the positive developments in recent years could be undone. Today, around 40% of workers are still without any occupational pension rights in Germany. The planned EU directive would sharply reduce their chances of receiving an occupational pension at all. It must also be assumed that the directive would have a negative effect on workers in possession of pension rights over the course of time, as employers would adjust the existing schemes to counteract the additional cost impact.

The European Commission presented its proposals for a directive on 20 October 2005. The declared aim is to reduce obstacles to mobility. Both national and cross-border job changes of employees will be affected.

In principle, we welcome the proper resolution of the issue of portability. The aba played a constructive role in satisfactorily resolving this issue in Germany with effect from 1 January 2005.

We believe it to be counterproductive that, in addition to regulating transferability itself, minimum conditions are to be introduced (maximum vesting period of two years, minimum age of 21 years, maximum qualifying period of one year) and vaguely worded regulations for indexation of vested rights introduced. There is no justification for linking these different elements. The proposals make it unnecessarily expensive to run occupational pension schemes, even if the addi-

tional cost were tax-deductible. Permitting such deductibility is unlikely, since this would lead to a substantial loss of tax revenue in Germany.

The cost of providing indexation to vested leavers alone would increase the previously relevant cost of final salary schemes by 20 to 30%. The additional cost of reducing the vesting periods from five to two years would, depending on the rate in a company, turnover range between 1 and 20%. If these additional costs are not simply absorbed by employers, the level of benefits will be correspondingly reduced. It is obvious, that the extent of coverage of employer-financed new commitments will decrease in such a climate.

The proposed directive is based on the Treaty establishing the European Community, particularly on Articles 42 and 94. To have the proposal passed into law, the Council of Ministers must therefore adopt it by unanimous resolution.

The following person will be pleased to answer any questions:

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Content

I. Basic remarks on the proposed "portability" directive

A. Cross-border mobility is to be improved — requirements to accomplish this:

In light of the increasing role of occupational pension and the flexibilisation of national and European labour markets, aba deems it necessary to improve cross-border portability (in its classical definition) of occupational pension in the EU.

- The obstacles to national and cross-border transfers of pension entitlements and the respective values are not only caused by labour law, but are also due to wage tax and social security insurance law. The issue of insolvency protection insurance must also be clarified with respect to cross-border portability.

B. European regulatory efforts encounter great diversity and nearly only voluntary occupational pension schemes

In light of the great diversity of the occupational pension schemes in the EU, which is conditioned *inter alia* by their different role within the three pillars of retirement pension and the various traditions, the proposed portability directive would have varied effects in the various member states. For example, the needs for adjustment will only be low in states whose occupational pension schemes are exclusively externally funded, whose defined contribution schemes (already) play a significance role and where occupational pension is of a purely compensatory nature.

- A good impression of this diversity is provided by the two overviews from the EU Commission in its Impact Assessment (pp. 49 ff. and 64 ff.), which it prepared for the proposed directive.

In nearly all EU member states, occupational pension in private industry is a voluntary, basically collective and capital-backed scheme. It therefore differs fundamentally from the first pillar, but also from private retirement pension. These differences also constitute the strength of occupational pension.[1] These differences should be preserved and taken into account with respect to reforms.

- Occupational pension stands between statutory pension insurance and private retirement pension. The second pillar should not be made into the first or the third pillar.

- Occupational pension depends, due to its voluntary nature, on attractive tax and social-law framework conditions and on problem-free administration. Employers in particular will react to cost-increasing changes and to the labour-law regulations foreseen by the proposed directive.

- For employers, the foreseen "conditions governing acquisition of pension rights" and the foreseen "preservation of dormant pension rights" will lead to significant cost in-

[1] Also see the current aba brochure: http://www.aba-online.de/seiten/Broschuere__Die_Betriebsrente_.pdf

creases (cf. Annex 2: aba cost estimates). It can therefore be assumed that this proposed directive will counteract the urgently needed expansion of occupational pension.

C. Social and political environment for occupational pension and its current development in Germany

The aim or subject of the proposed directive is "to facilitate the exercise of the right of workers to freedom of movement and of the right to occupational mobility within the same Member State, by reducing the obstacles created by certain rules governing occupational pension schemes in the Member States" (Article 1 of the proposed directive).

- From the viewpoint of workers, the foreseen regulations in principle improve quality, particularly in relation to the conditions for the acquisition of pension rights and the dynamisation of dormant pension rights, but will increase costs for employers. It can therefore be assumed that the proposed directive counteracts the urgently needed expansion of occupational pension.

- The proposed regulations do not bring loyal workers an improvement in quality; only "disloyal" workers will profit from the new minimum standards. From the viewpoint of personnel policy, this is highly problematic in our opinion.

In light of the cuts in statutory pension insurance necessary as a result of demographic development, the framework conditions in tax, social security and labour law have been fundamentally improved in Germany since 2001. The first successes have also meanwhile become visible. This was confirmed *inter alia* by the study presented at the end of October 2005 entitled, "Situation and development of occupational pension in private industry and public service from 2001 to 2004" issued by TNS Infratest Sozialforschung.[2] The results show that since the pension reform in 2001 a lot has been achieved, though Germany still has a long way to go to reach the goal of nationwide occupational pension:

- share of workers subject to social security insurance with occupational pension promises in private industry: 46% (30 June 2004 as compared to 38% as of 31 December 2001);

- share of workers subject to social security insurance with occupational pension promises in private industry and public service: 60% (30 June 2004).

  - The actual social policy objective in our opinion should be to increase the percentage of workers who are entitled to occupational pension promises.

[2] The study (unfortunately only in German) can be found as Research Report 345 at: http://www.bmas.bund.de/

- The overview in the Impact Assessment (pp. 50 ff.) shows that Germany lies in the middle of the pack in Europe in terms of the degree of dissemination of occupational pension. Therefore, the foreseen EU quality requirements appear to some as a luxury.

- Even a glance at the annual survey presented on 9 November 2005 entitled, "Take advance of the opportunities: Make brave progress in reform" issued by the German Council of Economic Experts shows where the real political and socio-political problems are in Germany. In the sociopolitical sphere, the challenges consist of the high unemployment rate and the reform of health and health care insurance. In the area of retirement pension, an accurate, basic course has been set in recent years.

D. What does the EU Commission understand by "portability" or is it a Trojan horse from Brussels?

The EU Commission does not construe "portability" to mean the transfer of pension entitlements and the respective values, but as "the option open to workers of acquiring and retaining pension rights when exercising their right to freedom of movement or occupational mobility" (Article 3g of the proposed directive).

- The effort to facilitate and protect the acquisition of pension rights is a goal beyond this proposed directive, which has nothing to do with actual portability.

- The EU Commission is in our opinion using the alleged obstacles to mobility through occupational pension and the related topic of "portability in terms of transferability" as a pretext for new minimum standards for occupational pension.

E. Questionable reform approach: no indications of notable cross-border mobility of workers

The available statistical material regarding current obstacles to mobility through occupational pension and the number of affected workers is insufficient and does not allow for any clear conclusions. The figures currently do not appear to indicate any notable cross-border mobility of workers. This is not surprising in our opinion in light of language differences, which exist between Member States.

The EU Commission itself mentions in its Impact Assessment the following figures on geographic mobility (p. 12f.): Between 2001 and 2002 0.2% of the EU population (other estimates assume even lower values) moved from one member state to another. Mobility was somewhat greater seen in relation to the employed population. In 1999 approx. 1.4% of the employed population changed EU member states.

The only notable mobility within Europe takes place in multinational companies. Normally the delegate workers stay in their home country pension scheme due to their limited cross border employment. With respect to permanent transfers to another Member State, years of service in

the transferring company are normally graduated by the receiving company. Hence, solutions have already been found where notable mobility is taking place.

F. Many things are desirable, yet quality has its price: high costs for everybody

The national occupational pension schemes have developed historically over time, are complex and finely balanced systems. European regulations on "improving the quality" of occupational pension, as foreseen above all in Articles 4 and 5 of the proposed directive, therefore allow us to expect not only direct consequences for employers and workers, but also substantial consequences for tax revenue:

- Employers: The proposed regulations would lead to a substantial extension of the costs of occupational pension schemes. Based on the already high level of added wage costs, it can be expected that employers will react with adjustment measures aimed at long-term cost neutrality.
- Workers: At a first glance, the foreseen regulations, which are in part being promoted by unions, would lead to an improvement in the quality of occupational pension. In the medium term, however, all workers would bear the increasing costs of occupational pension, above all in the form of lower pensions. The quality of occupational pension for loyal workers will thus be reduced in favour of expanding the quality of retirement pension for disloyal workers.

  In addition, the foreseen reduction of the vesting period and the planned dynamisation requirement for vested rights will above all affect defined benefit schemes. The directive would therefore strengthen the trend towards defined contribution schemes.
- Tax revenue: Though the proposed directive would not have any effects on the EU Community budget (cf. p. 6 of the proposed directive), it would in all cases affect the national budgets, for the proposed labour-law measures will lead to a massive loss of tax revenue as a result of the necessary changes in tax legislation. In Germany, this should in our opinion be considered in light of the limits in Article 115 of the Basic Law and the specifications in the Maastricht Treaty.

  - The national implementation of the directive will go far beyond changes in occupational pension law.
  - Incomprehensible in our opinion is also that the EU Commission did not have to involve any experts in such a complex issue (cf. p. 4 of the proposed directive).
  - The EU Commission argues in the explanatory memorandum exclusively from the viewpoint of workers. This is incomprehensible in our opinion, as employers and external financing vehicles regularly belong to occupational pension schemes.

G. Breach of the principle of subsidiarity through intervention in national labour-law provisions?

The member states have "supreme authority" over the structure of social systems. The EU Commission can therefore in our opinion not prescribe provisions that affect the labour-law struc-

ture of occupational pension systems. Yet the Commission would do precisely this through the foreseen regulations in Articles 4 and 5 of the proposed directive.

- In accordance with Article 42 of the EC Treaty, the Council may adopt measures in the field of social security which are necessary to produce the freedom of movement of workers. The proposed directive should be restricted with respect to occupational pension as well to the reduction of obstacles to mobility in the case of cross-border changes of employers.

II. The proposed directive in detail

A. Legal bases for the proposed directive: Articles 42 and 94 of the EC Treaty

The EU Commission has based the proposed directive on Articles 42 and 94 of the Treaty establishing the European Community. The procedure is determined in accordance with Article 251 of the EC Treaty (Annex 1: Article 42, Article 94 and Article 251 EC Treaty).

- The Council must adopt a unanimous resolution within the framework of the legislative proceedings.

B. Scope (Article 2)

Analogous to Directive 98/49 (Directive 98/49/EG of 29 June 1998 on safeguarding the supplementary pension rights of employed and self-employed persons moving within the Community), the proposed directive provides for a very wide scope of application.

- From a German point of view, this means that the proposed directive will affect all financing vehicles: direct pension promises (Direktzusagen), support funds (Unterstützungskassen), Pensionskassen, direct insurances (Direktversicherungen) and German pension funds (Pensionsfonds). Affected will therefore be both pension promises financed via book-reserves, which constitute by far the most important vehicle for financing occupational pension in Germany, and pay-as-you-go or partial capital-backed occupational pension schemes.

C. Definitions (Article 3)

Part of the terms defined in Article 3 of the proposed directive is already in Directive 98/49. A reconciliation of the translations still appears to be necessary in this regard. New in the proposed directive are *inter alia* the terms "portability" (Article 3 (g)) and "transfer" (Article 3 (j)):

"Portability":

With respect to the term "portability", many would first think of the Latin word "*portare*" (to carry, bring) and would imagine in relation to occupational pension that it concerns transferring previously acquired occupational pension rights or their values from a former to a new employer. Portability issues would thus only be discussed if a value existed which could be transferred (across borders if possible).

The EU Commission, in contrast, construes portability to mean "the option open to workers of acquiring and retaining pension rights when exercising their right to freedom of movement or occupational mobility." This understanding of portability relates not only to leaving acquired rights with the old employer or taking the occupational pension entitlement or its value to a new employer when changing employers, but also encompasses questions of the prerequisites under which rights are acquired and how the rights left with an old employer develop after the withdrawal. The term "portability" is thus extended very far beyond its actual meaning.

- In this way, circumventing the competence of the Member State, new minimum labour-law standards are being introduced for occupational pension.

This definition also appears to be relatively new for the EU Commission. The questionnaire of the EU Commission entitled "Improving the portability of occupational pension rights in the EU" (deadline: 30 June 2004), which served to prepare the proposed directive, only used the term "transfer".[3]

The term "transfer" is also recognized by German legislators. The labour-law arrangement for transfers is in § 4 German Act for the Improvement of Occupational Pension (the "Act"). This arrangement relates exclusively to transfers within Germany, not to cross-border transfers.

- The new definition of "portability" thus goes far beyond the original approach and must be rejected. We therefore propose the following wording for Article 3 (g): "the option open to workers of transferring the value of the vested right to occupational pension acquired by workers when exercising their right to freedom of movement or occupational mobility."

"Transfer":

According to the definition in Article 3 (j) of the proposed directive, this term concerns "the payment by a supplementary pension scheme of a capital sum representing all or part of the pension

[3] The former definition of the term "transfer" read: “surrender by a pension scheme of a capital representing (part of) the vested pension entitlement acquired under that scheme. The capital may be surrendered to a new scheme or to the early leaver.”

rights acquired under the scheme, with the possibility of transferring this sum to a new supplementary pension scheme or another financial institution which provides pension rights."

- Incomprehensible for us is that upon the "transfer" part of the principal sum can apparently remain in the pension scheme of the former employer. If part of the acquired value stays with the old employer, the goal of bundling rights pursued with portability cannot be achieved. Partial transfers must therefore be rejected and we recommend a corresponding change.

Article 3 (j) assumes that upon a change of employer either a transfer to the occupational pension scheme of the new employer or a transfer to the third pillar (this is what is meant by a transfer to "another financial institution which provides pension rights") can occur.

In order to avert the administration of miniscule claims, it should be possible to transfer vested rights. Transfers to the third pillar upon a change of employer should in our opinion be avoided not only based on the related problems in tax and social security contributions law. Occupational pension should also remain occupational pension even in the case of a change of employers.

- Upon a change of employers, the value of the past service benefits should be transferred to the new employer or its pension scheme.

D. Conditions governing acquisition (Article 4)

The proposed directive prescribes measures to facilitate acquisition for workers. These include a reduction of the statutory vesting period for occupational pension rights to two years and the introduction of a minimum age of 21 years for participation in an occupational pension scheme. Also to be introduced is a maximum statutory qualifying period, i.e. a worker is to become a member of the occupational pension scheme after a maximum length of employment of one year.

In order to illustrate the changes that would arise in Germany through Article 4 of the proposed directive, we will provide a short overview of the material conditions for acquisition in German occupational pension law:

- An employer-financed right becomes vested by law if the employment relation ends upon reaching 30 years of age and the statutory vesting period of five years has been fulfilled (§ 1b(1) of the Act); through the 2001 pension reform, the minimum age was reduced from 35 to 30 years and the vesting period from 10 to five years.

- In the case of worker-financed occupational pension schemes (deferred compensation), rights become immediately vested by law (§ 1b(5) of the Act).

- The pension right normally also encompasses pension rights related to employment periods below the minimum age. Decisive is the date of the occupational pension commitment.

- For employer-financed pension with an effect on income taxes (though not for the labour-law claim), the minimum age is currently 28 years in accordance with § 6a(2)1 of the German Income Tax Act (pension book reserves) and § 4d(1)1b), Sentence 2 thereof (support funds).

- No statutory regulations exist in Germany concerning qualifying periods.

Article 4a):

Article 4a) of the proposed directive is difficult for us to understand. It is therefore unclear what significance this regulation would have for Germany.

What are "contributions paid by, or on behalf of, the outgoing worker"? Does this only refer to deferred compensation contributions or also to employer contributions paid to the pension scheme? The following sentence in the explanatory memorandum on the proposed directive speaks in favour of assuming that only deferred compensation contributions are intended: "A worker who has not yet built up any acquired rights within the supplementary pension scheme but who has already paid contributions should not lose them. Accordingly, contributions should be reimbursed or transferred in full" (p. 7 of the proposed directive). Should employer contributions also be meant, in our opinion this would be equivalent to a cancellation of the vesting arrangement.

- ➢ The meaning of the expression "all the contributions paid by, or on behalf of, the outgoing worker" should be clarified.

If no pension rights have yet been established upon the termination date, this can only mean that no vested rights exist yet.

- ➢ Given that only vested rights are to be transferred through the proposed directive, the words "or transferred" should be deleted in Article 4a).

Article 4a) of the proposed directive demands a reimbursement or transfer of *all* the contributions. It should be noted that costs might already have arisen upon the termination date of the employment relation, which might make a general, full reimbursement of paid contributions appear unacceptable. In our opinion, the costs of mobility should also be borne by the mobile workers—and not by loyal workers or employers.

- A general, full reimbursement of paid contributions at the expense of loyal workers and employers must be rejected.

Article 4b): minimum age of 21

Article 4b) sets the age from which a worker must be allowed to participate in a pension scheme. This provision does not correspond in our opinion to any additional prerequisite for the vesting of occupational pension rights (e.g. the age limit of 30 in Germany), but will cause a further reduction of the minimum age for vesting in Germany: For if a worker has a right to be accepted in the plan at age 21 and if the vesting period would still be two years, in our opinion the current age limit of 30 years for vesting would also have to be adjusted.

This reduction would be associated with substantial costs for employers and the state:

- A reduction of the minimum age would make employer-financed occupational pension more expensive due to the turnover in the group of persons who have not yet turned 30 years of age.

- A reduction of the minimum vesting age in labour law would have substantial tax consequences for employer-financed occupational pension—for all financing vehicles.

When making cross-border comparisons of occupational pension schemes, it must be taken into account that in the rest of the EU only the time of scheme membership counts for the vesting period and, in contrast to the German arrangement for occupational pension law, the period of service from the entry into the employment relation is completely irrelevant.

Article 4c): qualifying period/waiting period

The period during which a worker does not acquire pension rights should not exceed one year according to the proposed directive.

- The EU Commission rests on one year so that the "schemes thus maintain in particular the possibility of linking the waiting period to the qualifying period (which generally does not exceed one year)" (cf. p. 7 of the proposed directive). In our opinion, the question of limited employment relations nonetheless arises in this context. In Germany, there are meanwhile also employment relations with a two-year qualifying period.

- The EU Commission appears to have a different understanding of a waiting period than is common in Germany. In the explanatory memorandum on the proposed directive, the EU Commission uses the term "waiting period" (cf. p. 7 of the proposed directive). Normally,

when a waiting period is foreseen, then a person must belong to an occupational pension scheme for a particular amount of time in order to be able to claim benefits. Nevertheless, in contrast to a qualifying period, rights are already accrued during this period. The difference between a waiting and a qualifying period therefore also has consequences for the fulfilment of vesting prerequisites.

- It should be made clear in our opinion that a qualifying period is meant in the proposed directive.

Article 4d): vesting period

Article 4d) of the proposed directive requires workers to acquire a pension right after a maximum membership period of two years. For Germany this would carry a further reduction in the vesting period for employer-financed occupational pension as a consequence.

Article 9(2) of the proposed directive gives the Member States the option of an extended implementation period (additional 60 months) to reduce the vesting period to two years (Article 4 (d)).

- aba cost estimates show that by reducing the vesting period from five to two years additional costs of 1 to 5% of the current costs could be expected in the case of "stable employee populations (cf. Annex 2). Sharply higher cost increases can be expected in the case of "unstable employee populations" (up to 20% of the current costs).

  This is problematic from the viewpoint of companies in light of the fact that a reduction of the statutory vesting period from 10 to 5 years just occurred through the 2001 pension reform. Deferred compensation is immediately vested.

- The special effect that would arise for Germany if the EU sets the vesting period is also seen by the EU Commission: "These costs would be higher if the maximum vesting period would be set at two years and moreover have important implications for the costs of occupational pension provision in Germany (where vesting periods are five years)." (Impact Assessment, p. 36).

- Apparently not discussed to date, however, are the consequences for insolvency protection insurance in Germany (cf. § 7 of the Act). With the reduction of the vesting period, the number of rights subject to pension guarantee fund (PSV) guarantees would increase. In this context as well, employer-financed occupational pension would become substantially more expensive.

- In our opinion, the basic question arises for Article 4 as to whether these regulations do not breach the principle of subsidiarity (cf. Item I G).

E. Preservation of dormant pension rights (Article 5)

The most expensive changes for occupational pension are concealed in Article 5(1) of the proposed directive, which stipulates that "Member States shall adopt the measures they deem necessary in order to ensure a fair adjustment of dormant pension rights so as to avoid that outgoing workers are penalised."

- The Member States are basically supposed to assure for a "fair" adjustment of dormant rights in favour of withdrawn workers. But what is a "fair" adjustment?

- Does the German version of the proposed directive actually have the same content as the English version (German: "Die Mitgliedstaaten nehmen die Maßnahmen die ihnen notwendig erscheinen um eine faire Anpassung der ruhenden Rentenansprüche sicher zu stellen und damit zu gewährleisten, dass ausscheidende Arbeitnehmer nicht benachteiligt werden"; English: "Member States shall adopt the measures they deem necessary in order to ensure a fair adjustment of dormant pension rights so as to avoid that outgoing workers are penalized")?

- The required dynamisation of the rights of withdrawn workers would be associated with extremely high costs. Article 5(1) of the proposed directive is therefore particularly problematic. aba cost estimates show that cost increase of up to over 30% of the current costs could be associated with this (cf. Annex 2).

  Under social policy perspective, the question arises why one would want to impose such high costs on employers for outgoing workers, when the employers would ultimately have to pay a lower and presumably qualitatively worse pension for loyal workers over the medium term.

- This adjustment requirement should also be problematic in Germany above all for classical employer-financed occupational pension. Flat rate promises, final salary promises, “Eckwert” schemes and promises integrated with social security benefits would be affected.

- The dynamisation of rights in deferment period corresponds to the contribution plan structure for fixed amount commitments and for average salary schemes without any appreciation for accrued rights, which are widely disseminated in Germany.

- In order to preserve trust, any dynamisation requirement should at least be restricted to newly hired persons.

- The foreseen dynamisation obligation would require a sharp change in the structure of the German occupational pension schemes. This would be associated with significant consequences in tax law, requiring long transition periods. Only through such long

transition periods could the cost-related effects of such an obligation to dynamise vested rights be kept under control.

- Last but not least, the basic question also arises here in our opinion as to whether this provision does not breach the principle of subsidiarity (cf. I G of the comments).

Article 5(1) of the proposed directive must be read together with Consideration (7), which reads: "Steps must also be taken to ensure a fair adjustment of dormant rights so as to avoid that outgoing workers are penalised. This objective could be achieved by adjusting dormant rights in line with a variety of reference measures, including inflation, wage levels, or pension contributions which are in the course of being paid, or the rate of return on assets under the supplementary pension scheme."

- Obligatory dynamisation regulations for dormant pension rights are currently hardly prevalent in the EU Member States. This is also illustrated by an overview from the EU Commission (cf. p. 49 of the Impact Assessment). A restricted linkage to an inflation index exists in Ireland (max. 4%) and in Great Britain (max. 5%). In the Netherlands, an adjustment of dormant rights exists in accordance with any increase in occupational pension, whereby normally the adjustment is only made if sufficient financial resources are available for the adjustment. An "unconditional" obligation to make an adjustment is not recognized there.

  Otherwise, the regulations on indexing vested rights in Great Britain and Ireland must be viewed in light of the history of relativly high inflation. Because Germany has realized a policy of low inflation in the past and this is now also being continued by the European Central Bank for the EU as a whole, there is not a lot of need to protect vested rights against devaluation by inflation.

- At a European level, when assessing whether dynamisation of occupational rights is necessary or not, the entire period of the benefit under one occupational pension scheme should be taken into consideration, i.e. both the active time and the retirement period. If the vested right is either dynamised during the active time or the pension benefit adjusted during the inactive phase, then this should be able to be taken into account in a low inflation context as sufficient for a "fair" adjustment of the commitment.

Article 5(2) of the proposed directive:

Alternative to the dynamisation of the pension rights of withdrawn workers, the Member States can permit with respect to supplementary pension schemes, within certain limits, pension rights to be transferred or the principal sum corresponding to the rights to be paid out.

- Without modifying the Act, the foreseen option of paying out "a capital sum representing the acquired rights" should hardly play any role in Germany. Based on the very narrow limits for indemnity payments (§ 3 of the Act), which are intended to ensure that the previously implemented capital will continue to be used to increase occupational retirement pension despite the change of employers, only the options of dynamisation or transfer remain in Germany.

F. Transferability (Article 6)

By way of Article 6 of the proposed directive, the EU Commission pursues the following objective: "An outgoing worker opting for a transfer of his rights should not be penalised by calculations of the value of the rights transferred made by the two schemes involved in the transfer, or by excessive administrative charges" (p. 8 of the proposed directive).

- A labour-law claim to transfer will alone not satisfy this objective. If the transferability is not accompanied by changes in tax and social security insurance law, the claim would lose a lot of its value.

Article 6(1) in principle provides for a transfer claim on the part of workers, even across borders.

- Article 6(1) rests on the transfer of the acquired pension rights. It is unclear, at least as worded, if only a transfer of pension entitlements or a tranfer of the respective values is possible too. In our opinion, Article 6 of the proposed directive must aime at the transfer of the computed principal sum—and not at the transfer of rights. Many years of experience have shown that the assumption of third-party pension promises hardly works in practice.

- The transfer claim relates to "all the acquired pension rights". In order not to jeopardize occupational pension institutions through portability claims and to make a long-term investment strategy possible for them in the future, the transfer claim of workers should be limited to small and medium-sized sums. German legislators, for example, have restricted the transfer claim to values not exceeding the contribution limit in the general pension insurance system (§ 4(3)2 of the Act). The claim foreseen in the proposed directive also might contradict Article 3(j) of the proposed directive, in which a payment of a principal sum is foreseen "representing all or part of the pension rights acquired under the scheme".

- In Article 6 of the proposed directive (also with reference to Article 5(2)), it would have to be stipulated that the sum must be transferred to the new employer.

- Absolutely necessary in our opinion is a clarification in the EU proposed directive that the transfer exonerates the debt of the issuing employer.

Pursuant to Article 6(2) of the proposed directive, when calculating the value of the acquired rights to be transferred, the actuarial and interest-rate assumptions should "not penalise the outgoing worker".

- During the transfer, the transfer value must be computed in accordance with the rules and assumptions of the transferring employer and the transfer value must be integrated into the pension plan of the new employer in accordance with the latter's rules and assumptions.

- The question of insolvency protection insurance arises with respect to the transfer. In our opinion, it is problematic that the proposed directive ignores the problem of insolvency protection insurance with respect to cross-border transfers.

The provision in Article 6(3) of the proposed directive is not clear in our opinion. It requires the occupational pension scheme to which the rights are transferred to guarantee the preservation of the transferred rights "at least to the same extent as dormant rights in accordance with Article 5(1)".

We are assuming that the rules of the absorbing scheme are relevant to the transfer and that no distinctions may be made here between the workers accepted into the scheme and withdrawn workers, whose rights are preserved.

Article 6(3) of the proposed directive could be construed, however, to mean that employers are required to make a reconciliation with the occupational pension scheme from which the worker is coming. Comparative European calculations by the new employers or the absorping pension scheme are in our opinion inconceviable, particularly since the form of benefit can be completely different: lump-sum payment, term annuity, life annuity with or without survivor annuities and with or without pension adjustments. Yet biometric and financial bases of calculation can be very different as well.

- This is not possible for an employer to whom an occupational pension is transferred or an external pension scheme that must accept rights. Solely the rules of the absorbing occupational pension schemes should be relevant for the transfer.

According to Article 6 (4) the administrative costs as a consequence of the transfer may not be "disproportionate to the length of time the outgoing worker has been a scheme member".

Costs are incurred through the transfer or the changing worker. The proposed directive demands a far-reaching "socialisiation of costs". In our opinion, it should be asked who should bear the costs of mobility—the employer to the benefit of a former worker? Loyal workers or the instigator?

- Why should loyal workers and companies pay the costs of mobility for withdrawn colleagues or workers? Loyal workers should in our opinion not be penalized. The portability costs should therefore be borne by the mobile workers instigating them.

- It is not clear what the EU Commission understands by the term "administrative costs". For example, it is not clear whether the Commission subsumes consulting costs under the term "administrative costs". The cost problems sometimes arising during transfers relate more to one-time consulting costs than ongoing administrative costs. A corresponding clarification is therefore absolutely necessary in our opinion.

G. Transfer right of workers: Time-limited special rule upon implementation

In relation to the portability claim to acquired pension rights upon a change of employers (Article 6(1) of the proposed directive), Member States have the option to exempt pay-as-you-go schemes, support funds and book reserve schemes (Article 9(3) of the proposed directive).

With respect to book reserve financed occupational retirement pension schemes, a portability claim to acquired pension rights upon a change of employers would force employers to capitalise reserves tied up in the company in order to be able to provide the workers the capital. If a portability claim existed, substantial problems could also be expected with respect to support funds which cannot be fully funded for tax reasons and to the benefits of which workers have no legal claim.

- Direct pension promises, support funds and pay-as-you-go schemes are of substantial importance in Germany as chosen financing vehicle. According to a recent study entitled "Situation and development of occupational pension schemes in private industry and public service from 2001 to 2004" by TNS Infratest Sozialforschung, 4.123 million workers in the social security insurance system were assured with direct pension commitments and support fund commitments, while 5.372 million workers in the social security insurance system were assured via a public occupational pension scheme (30 June 2004).

- Contrary to the tenor of the press release of the EU Commission on 20 October 2005 concerning the presentation of the proposed directive book reserve schemes do not only exist in Germany. The following countries are mentioned in a report from the

Commission on the implementation of Council Directive 98/49/EC of 29 June 1998 on safeguarding the supplementary pension rights of employed and self-employed persons moving within the Community (page 4): Austria, Belgium, Denmark, Germany, Italy, Luxembourg, Portugal, Spain, Sweden, the United Kingdom and Norway.

The special provision in Article 9(3) must be viewed in connection with Article 10(2) of the proposed directive, however. Only in this way does it become clear that this is supposed to be a time-limited arrangement from the viewpoint of the EU Commission.

- In relation to the future significance of direct pension promises in Germany, we do not share the EU Commission's view, which assumes a phase-out model based on IAS and altered tax provisions (p. 54f. of the Impact Assessment). In contrast, we see the risk that the legal claim to a transfer of past service benefits basically required by the EU Commission could give the deathblow to occupational pension systems financed via book reserves and thus the most widely used form of occupational pension in Germany.

- Likewise, the conversion of (partial) pay-as-you-go schemes in public service to capital-backed schemes within 10 years is unrealistic.

- aba is therefore against a portability claim of workers with respect to these forms of occupational pension—for an indefinite period of time.

H. Information (Article 7)

Article 7 of the proposed directive is aimed to give "every potentially outgoing worker […] information on how terminating an employment relationship could affect his supplementary pension rights."

The information duties foreseen here vis-à-vis workers go far beyond the obligations pursuant to Article 11 of the so-called "Pension Fund Directive" (Directive 2003/41/EC). Article 7 of the proposed directive would likewise represent a clear accentuation of workers' claims to information in German law (§ 4a of the Act).

Claims for information "in a comprehensible form", as foreseen in Article 7 (4) of the proposed directive, would increase the liability risks of employers considerably.

- Liability risks for employers should be ruled out through clear and unequivocal provisions.

These extended information duties must also be viewed in connection with the foreseen changes in the terms and conditions of acquisition. In particular, the reduction of the vesting period to two years and frequent changes of employers in young years will sharply increase the burden of em-

ployers and pension schemes as a result of the foreseen information duties. If requested by a withdrawn worker, the dynamisation duty (Article 5(1) of the proposed directive) could even lead to a duty to provide regular information.

- aba is against further information duties for employers and pension institutions which present high risks in terms of liability. Such a right to information should only exist where there is a legitimate interest.

Article 7(2d) of the proposed directive provides an explanation of the conditions governing the transfer of acquired rights. What counts as a condition—even the tax consequences?

- A duty of the employer or pension scheme to provide information about the amount of the transfer value is in our opinion fully sufficient, as foreseen in German law under § 4a(1)1 of the Act.

I. Implementation and reporting (Articles 9 and 10)

The Member States would in principle be obliged to implement the directive prior to July 2008 (Article 9 (1) of the proposed directive). In Article 9, Paragraphs 2 and 3, however, there are special regulations for the transfer claim of workers (cf. limitation in Article 10 (2) of the proposed directive) and the reduction of the vesting period.

- The foreseen implementation period appears extremely short to us and unrealistic based on the necessary tax regulations.

- Because in our view, in contrast to the EU Commission's estimation, neither direct pension promises nor support funds will be phased out over the long term, we request unlimited application of Article 9(3) of the proposed directive.

Annex 1: Legal basis of the proposal for a directive on improving the portability of supplementary pension rights and the legislative proceedings

***Article 42* OF THE TREATY ESTABLISHING THE EUROPEAN COMMUNITY**

The Council shall, acting in accordance with the procedure referred to in Article 251, adopt such measures in the field of social security as are necessary to provide freedom of movement for workers; to this end, it shall make arrangements to secure for migrant workers and their dependants:

(a) aggregation, for the purpose of acquiring and retaining the right to benefit and of calculating the amount of benefit, of all periods taken into account under the laws of the several countries;

(b) payment of benefits to persons resident in the territories of Member States.

The Council shall act unanimously throughout the procedure referred to in Article 251.

***Article 94* OF THE TREATY ESTABLISHING THE EUROPEAN COMMUNITY**

The Council shall, acting unanimously on a proposal from the Commission and after consulting the European Parliament and the Economic and Social Committee, issue directives for the approximation of such laws, regulations or administrative provisions of the Member States as directly affect the establishment or functioning of the common market.

Article 251 OF THE TREATY ESTABLISHING THE EUROPEAN COMMUNITY

1. Where reference is made in this Treaty to this Article for the adoption of an act, the following procedure shall apply.

2. The Commission shall submit a proposal to the European Parliament and the Council.

The Council, acting by a qualified majority after obtaining the opinion of the European Parliament:

- if it approves all the amendments contained in the European Parliament's opinion, may adopt the proposed act thus amended,

- if the European Parliament does not propose any amendments, may adopt the proposed act,

- shall otherwise adopt a common position and communicate it to the European Parliament. The Council shall inform the European Parliament fully of the reasons which led it to adopt its common position. The Commission shall inform the European Parliament fully of its position.

If, within three months of such communication, the European Parliament:

(a) approves the common position or has not taken a decision, the act in question shall be

deemed to have been adopted in accordance with that common position;

(b) rejects, by an absolute majority of its component members, the common position, the proposed act shall be deemed not to have been adopted;

(c) proposes amendments to the common position by an absolute majority of its component members, the amended text shall be forwarded to the Council and to the Commission, which shall deliver an opinion on those amendments.

3. If, within three months of the matter being referred to it, the Council, acting by a qualified majority, approves all the amendments of the European Parliament, the act in question shall be deemed to have been adopted in the form of the common position thus amended; however, the Council shall act unanimously on the amendments on which the Commission has delivered a negative opinion. If the Council does not approve all the amendments, the President of the Council, in agreement with the President of the European Parliament, shall within six weeks convene a meeting of the Conciliation Committee.

4. The Conciliation Committee, which shall be composed of the Members of the Council or their representatives and an equal number of representatives of the European Parliament, shall have the task of reaching agreement on a joint text, by a qualified majority of the Members of the Council or their representatives and by a majority of the representatives of the European Parliament. The Commission shall take part in the Conciliation Committee's proceedings and shall take all the necessary initiatives with a view to reconciling the positions of the European Parliament and the Council. In fulfilling this task, the Conciliation Committee shall address the common position on the basis of the amendments proposed by the European Parliament.

5. If, within six weeks of its being convened, the Conciliation Committee approves a joint text, the European Parliament, acting by an absolute majority of the votes cast, and the Council, acting by a qualified majority, shall each have a period of six weeks from that approval in which to adopt the act in question in accordance with the joint text. If either of the two institutions fails to approve the proposed act within that period, it shall be deemed not to have been adopted.

6. Where the Conciliation Committee does not approve a joint text, the proposed act shall be deemed not to have been adopted.

7. The periods of three months and six weeks referred to in this Article shall be extended by a maximum of one month and two weeks respectively at the initiative of the European Parliament or the Council.

Annex 2: Estimated Impact of the prpopsed EU Portability Directive

The German Association for Occupational Pensions (Arbeitsgemeinschaft für Betriebliche Altersversorgung e.V. - aba -) has estimated the cost effect of

(i) the reduction of the vesting requirement from 5 to 3 years and
(ii) the indexation of vested pension entitlements of early leavers in deferment

on typical occupational pension schemes in Germany.

Assumptions

In performing the estimates the following assumptions were used:

1. employee population with balanced age structure
2. decreasing turnover as service (and age) increases using the service-related turnover rates below:

up to 1 year of service:	20 %
between 1 and 5 years of service:	15 %
between 5 and 10 years of service:	10 %
between 10 and 20 years of service:	5 %
from 20 years of service:	1 %

and variations thereof

3. Discount rate: 5 % p.a.

For determining the cost of item (ii) above, the following additional assumptions were made:

4. type of scheme:	final pay
5. general salary increase:	2 % p.a.
6. merit increase:	1 % p.a.
7. indexation in deferment:	in line with full salary increase

Reduction of the vesting requirement from 5 to 3 years

<u>Results:</u>

(i) Current or regular cost is estimated to increase by between 1 and 5 % for “stable” employee populations;
(ii) and by up to 15 % to 20 % for “unstable” employee populations.
(iii) In addition to an increase in current or regular cost there will be past service-related cost; the effect of which should be marginal if spread over future service (US-GAP) and noticeable in the first year if expensed immediately (IAS 19).

The estimated additional cost can be expected to be – more or less – independent of the type of pension scheme.

Indexation of vested pension entitlements of early leavers in deferment

Results:

(i) current cost is estimated to increase by between 20 % and 30 %.
(ii) In addition to an increase in current or regular cost there will be past service-related cost; the effect of such cost is significant, whether spread over future service (US-GAP) or if expensed immediately (IAS 19). Under the former, we would expect an additional 2 to 5 percentage points, i.e. leading to a longer term additional cost of 22 % to 35 %; under the latter a one-time additional cost impact of 20 to 50% can be expected, i.e. an initial additional cost impact of 40 to 80%, followed by a longer term additional cost of 20 to 30% of current or regular cost.

The quoted cost increases relate to final pay-related pension schemes and assume that indexation in deferment is at the full salary increase rate.