



## Netspar Research and Innovation Agenda 2011-2014

In this document you will find a description of the Netspar research and innovation agenda for the 2011-2014 period. This agenda comprises seven Pension Innovation Labs (PIL):

1. Risk management during working life
2. Risk management during retirement years
3. The art of choosing
4. Supervision of fully funded pensions: solvency and transparency
5. Risk sharing and distribution among generations: full funding, pay-as-you-go, taxation
6. The labor market
7. Heterogeneity within generations and the position of senior citizens

You will find a description of each PIL below.

PILs 1, 2 and 3 fall under the Innovation Program for Retirement Management (IRM), which is subsidized by the Ministry of Economic Affairs, Agriculture and Innovation. PILs 4, 5, 6 and 7 fall under the Renewal of the Dutch Pension System Program (RDP), which is subsidized by the Ministry of Social Affairs and Employment.

Next, a brief explanation of the terminology applied in the descriptions of PILs 1, 2 and 3. In each of these descriptions you will find a brief outline of the subject, followed by an identification of *components* plus an indication of *products* that might ultimately be developed by applying the knowledge that has been acquired within the related PIL. The idea behind these *components* and *products* is the following:

- For an innovation program it is essential to clearly identify in concrete terms what output the program is going to deliver. For the Retirement Management program it has been decided to refer to this output as *components* (read: building blocks) for new or renewed pension and insurance products. These components represent the “precompetitive output” of the overall innovation program. This in turn serves as input for the market and product development activities of the individual partners in the pension insurance industry.
- The *products* are the products that are ultimately developed by the industrial organizations themselves for their own customers and markets. They fall outside the scope of the innovation program.

# PIL 1: Risk management during working life (IRM)

## Background

The financial crisis has demonstrated and further enhanced the importance of pension risk management. There is considerable expertise in the Netherlands in the field of pension risk management, owing to the long tradition with asset-liability management. In traditional pension plans – based on defined benefits, where investment risks were borne mainly by the employer – the non-value-based risks were limited and the value-based risks were optimized in favor of the employers. As risks increasingly come to lie with the participants in pension plans, risk management has grown in importance: no longer to protect against employer risks, but to protect pension fund members against risks and to allow them to benefit fully from risk premiums. Pension ambitions and the desired pension guarantees serve as the starting point; a reverse calculation is then made to determine the premium and investment levels that are required to achieve these. It is important to develop the necessary asset-liability techniques for both domestic and foreign use.

A key question is; what makes a pension contract efficient? What commitments should a pension fund or insurance company make, and how do these commitments relate to uncertain developments? Managing a pension product on the basis of the desired pension benefits does not necessarily mean that the benefits need to be guaranteed. Instead of hard guarantees, it is also possible to work with softer ambitions, which partially depend on uncertain future developments. Finding a new balance between guarantees and ambitions can play a major role in exporting pension products abroad, with the pension product being managed with a view to the ultimate pension benefit for the participants.

The issue is therefore how the risks can be divided best over the various stakeholders. That calls for development of pension concepts that transcend the traditional dichotomy between defined benefit and defined contribution systems and that combine and further develop elements of these traditional pension concepts.

## Output of innovation program: precompetitive components

### *Component 1-1: Consequences of variations in composition of portfolio assets involving risk*

Investments in financial assets involving risk are essential when it comes to keeping pension products affordable. Many different types of assets that involve risk are available, not just stocks and bonds, but also private equity, commodities, real estate, and infrastructure. Investment for pension benefit purposes involves the long term, and that has great impact when deciding on the mix of investments. Also the question to what extent a liquidity premium offsets the disadvantage of limited liquidity is quite relevant. Evidence will be provided of the consequences of variations in the composition of an asset portfolio involving risk for the characteristics of the resulting pension product.

*Component 1-2: Characteristics of investment policy for optimal management of interest and inflation risks*

Interest and inflation risks threaten the purchasing power of pension benefits during the accrual phase. On the one hand, a sufficient investment return must be achieved; on the other hand, low nominal or real interest levels will lead to low pension benefits. Evidence will be presented as to how investment policy can be effectively applied to manage interest and inflation risks optimally.

*Component 1-3: Determining factors for variations in optimal risk allocation*

The capacity to absorb financial risk differs between participants. In many countries the pension product is based on the assumption that young people with a permanent job must accept greater risk in their pension assets portfolio. The determinants for variations in optimal risk allocation will be identified, and also to what extent intergenerational solidarity can improve the balance between risk and return.

*Component 1-4: Forms of survivor's pensions that link better with new role patterns and a flexible labor market*

Life insurance policies and survivor's pensions that are incorporated in pension plans often cover the risk of death during working life. Provisions for survivors are under pressure in many countries nowadays since more and more women are economically independent nowadays. However, if survivor's pensions are insured until the employee retires rather than being based on capital funding, survivors will incur considerable risk in case of death of the principal earner. Evidence will be presented on forms of survivor's pension that link well with new role patterns in a flexible labor market.

**Products that can be developed using the components**

*Product 1-1: Pension contracts for group pension products that are offered to employers for their staff*

Dutch pension providers have considerable experience in group pension products. This means opportunities for Dutch providers to offer their expertise regarding group pensions to foreign employers who seek a less costly alternative to the traditional defined benefit pension. When an employer or a group of employers offers a collective scheme, this will reduce marketing expenses. The competition for clients is then at wholesale rather than at retail level.

Another benefit of a group pension plan is that the process of selecting members can be simplified. Group schemes also provide other scale benefits. For example, they enhance the purchasing power of the member group as a whole. A proper balance must always be found between guarantees ('hard' rights) and ambitions ('soft' rights), involving investment in high-risk assets and management of interest and inflation risks. The products must match the specific features of the employer involved, the related employee base, and the legal and regulatory framework of the country involved.

*Product 1-2: Pension products for individual consumers*

This involves products for self-employed workers, for example. These products must feature considerable flexibility during the accrual phase because of the often irregular earnings pattern of self-employed persons. In addition, individual pension products must provide a hedge against the conversion risk during the accrual phase. This calls for products that not only aim for capital accumulation, but that are also managed during the accrual phase to generate income during the benefit payout phase. Major risks in this regard are a low interest rate and the likelihood of high inflation at the moment when capital is converted into an annuity. Due to the defined benefit tradition, Dutch providers have considerable experience in integrating the accrual and benefit payout phases of pension products and can thus cope better with these risks.

*Product 1-3: ALM analyses for the corporate market*

This involves ALM analyses for new pension products to be developed, where a major part of the risks lies with the participants. The market value of these products can be determined fairly accurately with these analyses.

*Product 1-4: New instruments for the commercial trade of financial risks*

This involves financial instruments available to pension insurance providers for commercial exchange of financial risks. Pension insurance companies can thus limit their solvency risks and optimize the risk distribution between and within generations. Due to the ageing of the population, it is becoming increasingly difficult to provide guarantees to retirees in work-related pensions by – as occurred in the past – absorbing risks in the form of fluctuations in past-service premiums (where those paying premiums guarantee the pension entitlements of the elderly if investment earnings are low). The management of systematic risks thus calls for product innovation.

## **PIL 2: Risk management during retirement years (IRM)**

### **Subtheme 2-A: Longevity risk**

#### **Background**

A major risk for pension insurers is the longevity risk. Relevant questions are: how great is this risk, how should it be reflected in price, and how can this risk be estimated better so that capital requirements can be kept to a minimum?

Another key question is what differences there are in life expectancy between people with differing characteristics. How differences in life expectancy should be reflected in the pension claims of participants is asking: what constitutes the optimal pension contract? In more and more countries state pension entitlements shift during the accrual phase in line with life expectancy, so that the systematic longevity risk stays with the related cohort until the retirement date. The question is: at what age can the longevity risk best be hedged through public-private schemes?

A related question is: when is it wise to convert collectively accrued capital into individual (deferred) lifetime annuities? Individuals who know that they will continue to live for many years will seek an annuity, causing the insurance to become too expensive for others. Preventing such selection would call for early conversion into a deferred annuity. However, limitation of the risk premium (since the average life expectancy of a cohort is still uncertain) would plead for later conversion. This too requires product innovation.

#### **Output of innovation program: precompetitive components**

*Component 2-A-1: Insight into the possibilities of estimating the longevity risk and into the limitation of current methodologies*

To estimate the effects of longevity risk, it is essential to estimate the longevity of a given population accurately. The recent discussion regarding the longevity tables of the Actuarial Association shows that this is no trivial matter. Similar discussions are going on in other countries. Evidence will be presented of how the longevity risk of a population can be calculated and of the limitations of current methodologies. The combination of actuarial techniques with medical information will also be examined.

*Component 2-A-2: Models for linking actuarial pivotal age to developments in life expectancy*

Uncertainty regarding retirement benefits due to developments in life expectancy can be managed by linking the actuarial age at which a guaranteed or desired benefit takes effect to developments in the life expectancy of the population involved. Models will be worked out to shape this, linking these to the suggestions in the EU Green Paper on the subject.

*Component 2-A-3: Concepts to reduce the limitations of current marketable longevity risk contracts*

Marketability of financial instruments in regulated markets would contribute to transparency and efficient price setting and lower transaction costs. At this time it is still hardly possible to trade longevity risk in regulated markets, in part because the basic risk per institution is too great. Evidence will be presented on how to design products that reduce the limitations of current marketable longevity contracts.

**Products that can be developed using the components**

*Product 2-A-1: Contracts that enable marketing of longevity risk*

Contracts that enable pension insurance companies to trade longevity risk with each other (over the counter) and contracts to market longevity risk on the open market (longevity swaps, q-forwards).

*Product 2-A-2: Pension contracts for the corporate market that enable optimal distribution of longevity risk among different stakeholders.*

*Product 2-A-3: Pension contracts for the retail market, where the effective date of pension benefits is linked to developments in life expectancy.*

## **Subtheme 2-B: How should retirement benefits be paid?**

### **Background**

A key issue in designing a pension system is the decumulation (payment) of accrued pensions and the importance of customization. What risks can a retiree afford, and how do these depend on such factors as housing situation, health insurance, and personal health?

Innovations in this field become increasingly important as more senior citizens are homeowners and take greater responsibility for all sorts of personal services around the home when their health declines. This may involve mixed lease-purchase arrangements, where insurers repurchase homes from senior citizens, who choose to convert the equity in their home into income. Where health services, health insurance, housing, and retirement benefits come together, all sorts of innovations are conceivable.

Dutch pension insurance companies possess much experience with annuity systems and can profile themselves with this in the global market. Annuity products are attractive since a lifelong benefit prevents having considerably less to spend at a later age. But these products mean less flexibility and liquidity. For a senior citizen who is faced with an uninsurable health risk it may therefore be better not to convert a part of personal savings into an annuity but to keep it directly accessible so as to be able to cover health risks and the related extra costs. In addition, it is important that annuities are index-linked so that they cover the inflation risk. Equity in the personal home can also play a role in covering old-age risks. Pension products can therefore not be viewed apart from the housing market (home ownership versus rent, role of housing associations), health insurance, and tax issues.

### **Output of innovation program: precompetitive components**

*Component 2-B-1: Insight into innovative concepts to improve the mutual exchange between risk-taking and a higher return*

The mutual exchange between risk-taking and a higher return during retirement is exposed. The role that innovative concepts can play (e.g. escalating annuities) to improve this exchange will be analyzed: how can risk premiums be benefited from, while the related risk is optimally managed?

*Component 2-B-2: Insight into the relationship between the need for cash and the need for insurance*

Annuity payments cannot be commuted since the insured party possesses asymmetrical information about his or her life expectancy. This means that annuity-based products need to be designed such that an unexpected need for direct cash can be met. The need for liquidity during the payment phase will be made visible and compared against the need for insurance. In this context, various ways will be developed to avoid selection as much as possible as senior citizens get more choice of freedom during retirement.

*Component 2-B-3: Solutions to bottlenecks in the conversion of equity in the personal home into a constant income flow*

The bottlenecks in converting equity in the personal home into a regular income flow will be examined. Potential solutions will be identified.

*Component 2-B-4: Insight into the benefits and drawbacks of the link of retirement benefits with health insurance*

The benefits and drawbacks of the link of retirement benefits with health insurance and other in-kind benefits will be identified. The insurability of various old-age risks will be covered, such as the risk of inflation of the cost of personal care.

*Component 2-B-5: Methods for covering old-age risks in developing countries*

In many developing countries there are no financial instruments or reliable data about death rates to allow annuities to be offered. The various possibilities for these countries to cover old age risks will be identified.

### **Products that can be developed using the components**

*Product 2-B-1: Annuities for the individual consumer market.*

...that are attractively priced, that prevent selection but at the same time enable consumers to cover their longevity risk as much as possible, such as deferred annuities.

*Product 2-B-2: Products that convert equity in the personal home into retirement income.*

*Product 2-B-3: Products that cover the risk of rising home and care expenses during old age.*

This may involve a pension in kind, for example in the form of sheltered housing. It may also involve products that pay out when a person loses the ability to perform activities of daily living (ADLs). At issue here is the insurability of the various risks. Also to be investigated are contract forms where financial institutions act as confidential advisors and assist senior citizens in managing their financial affairs and the purchase of diverse services.

*Product 2-B-4: New annuity products*

...whereby people can continue to run a certain amount of investment risk and thus continue to benefit from risk premiums. There is also the issue of whether a certain level of liquidity and flexibility can be offered that matches with the various distinct phases that can be identified within the payment period.

*Product 2-B-5: New financial instruments*

...that pension insurance companies and health insurance providers with different groups of participants and solidarity circles can use to trade risks. In that way pension insurers can limit their solvency risks and optimize the distribution of risk between and within generations.

*Product 2-B-6: Micro-pension products.*

This involves products that cater to the fast growing desire in developing countries to become less dependent during old age on traditional family ties.

## **PIL 3: The art of choosing (IRM)**

### **Subtheme 3-A: Pension communication**

#### **Background**

Pension communication is getting increasingly important as pension plan members take on greater risks. Furthermore, as more and more women enter the labor market takes, which thereby becomes increasingly flexible, citizens experience more transitions (“life events”) that have major consequences for their retirement situation, This can involve, for example, the transition from full-time to part-time work, or from employment to entrepreneurship, but also changes in personal relations and thus the composition of the household, or a long-term stay abroad. People are also increasingly being confronted with all sorts of choices in the pension area (money put in, investment mix, value transfer, conversion of survivor’s pension, combination of pension and part-time work, decumulation method). Responsible choices call for accessible and comprehensible information. The demand for knowledge plays a role here, meaning how pension information can best be communicated to the various categories of participants. There is also the question to what extent this information must be standardized to keep products transparent.

As elsewhere in the world, the pension accord between the Dutch trade unions and employers’ organizations calls for transparency of pension products. In line with this, the recent Green Paper of the European Commission emphasizes the importance of transparency. On the one hand, the products must be easy to understand; on the other hand, pension plans must be implementable at low cost. In the Netherlands, information regarding personal pension accrual is made available as from 2011 via the pension register. This provides opportunities for innovation of products that can also be exported later.

#### **Output of innovation program: precompetitive components**

*Component 3-A-1: Insight into ways to effectively inform members about the consequences of life events, such as marriage, divorce, or change of job.*

*Component 3-A-2: Insight into ways to clearly communicate the risks that are inherent to pension results for various product types*

It is important in this regard to indicate whether the targeted pension goals will be sufficiently achieved or that adjustments are required. This pertains both to systematic risks (e.g. the risk in the financial markets) and idiosyncratic risks (such as unemployment and disability from work).

## **Products that can be developed using components**

### *Product 3-A-1: Clear communication*

...to a specific group of collective contract participants, where these participants have little choice. Adequate communication can be expected to become a key competitive factor and is essential to gain support for group contracts.

### *Product 3-A-2: Communication regarding an individual retirement product, where people can make various personal choices.*

For individual pension products, the possibility for the consumer to assess during the accrual and decumulation period whether the product will generate the desired outcome becomes an important sales factor.

### *Product 3-A-3: Internet applications, such as the Dutch pension register.*

Analogous to the electronic patient record in the medical sector, every citizen can be the owner of his or her personal financial planning record. Financial institutions (including pension administrators) can gain access in this way, following authorization by the customer, to data regarding financial products that individuals have purchased. This puts providers in a better position to offer integrated financial advice and to develop products that match better with the customer's personal situation.

## **Subtheme 3-B: Selection behavior of pension clients**

### **Background**

Due to the growing heterogeneity of pension clients (in terms of household situation, employment contract, personal health, home ownership, human capital), customization in pension solutions is becoming increasingly important. This is a key argument for more consumer sovereignty. However, pension clients are hardly prepared and able to make well-considered pension choices. The credit crisis and the ensuing financial turbulence have shown this in many countries. Structuring choices wisely is therefore of great importance for any pension product.

Recent literature in behavioral economics and psychology provide points of reference for product innovation in this area. Research, for example, points out that standards (or defaults) heavily determine the selection behavior of people, especially when it comes to pensions. These standards determine what happens if no conscious choice is made. Standards are so powerful because many people are financially illiterate and regard the default as an implicit recommendation for a product that they do not understand and for which they – still – have little interest. These standards can, for example, relate to the minimum amount paid in, the way pensions are paid (e.g. lump sum or annuity), or the investments (and thus the investment risks that participants run). Defaults can also be attuned to the characteristics of an individual or a group.

In the Netherlands the possibilities to deviate from the default are often quite limited. In countries with a different tradition or culture this is often quite different. The challenge for Dutch pension providers is to adapt group products that have been developed for Dutch clients to the situation in countries where personal freedom of choice weighs more heavily, without imperiling the benefits of those products. Such product innovations require good insight into how people make choices, and into how they can best be supported in taking decisions regarding their retirement provision.

### **Output of innovation program: precompetitive components**

#### *Component 3-B-1: Insight into factors that determine selection behavior regarding pensions*

This deals with the impact of communication, defaults, labeling, financial incentives, etc. on specific choices (e.g. the choice of the age at which benefits are to start, conversion of survivor's pension into old-age pension, amount paid in, investment behavior, choice of risk, etc.) by a number of clearly delineated groups with defined characteristics.

## **Products that can be developed using the components**

### *Product 3-B-1: Group pension products for the corporate market*

...that offer limited freedom of choice as to investments, amounts paid in, benefits, and related supplementary insurance. It deals with optimization of the choice architecture for individual employees, depending on the characteristics of the employee base and local laws and regulations.

### *Product 3-B-2: Pension products for individual clients*

This involves products that provide the client with the desired measure of freedom of choice regarding periodic amounts paid in, the level of investment risk to be taken, and the way pension benefits are paid. This may, for example, involve periodic contributions that depend on income level, or products where the defaults for investment mix and contribution are adjusted to the amount accrued and age of the employee.

## **Subtheme 3-C: Governance and pension vehicles**

### **Background**

Whoever lacks the knowledge to put together a good pension product should delegate this task to a specialist. But that often presents the problem that commercial providers of pension products do not act strictly in the interest of the client – especially when the client has insufficient knowledge to assess the quality of the product. In other words, clients run the risk of obtaining products that do not cater to their needs, but that yield a high profit margin for the provider.

The demand for knowledge implies the need for a good governance structure behind pension products. Trust plays a major role in group pension plans, which require a group decision-making process regarding defaults and the purchase of financial products and expertise. Decisions regarding this must be taken by people with sufficient expertise, who attend to the interests of the participants. This calls for a governance structure for pension plans, where the decision-makers possess sufficient expertise and at the same time commit themselves to the interests of the participants (instead of extra profit for the providers of financial products).

There is much experience in the Netherlands with group pension plans. In the Dutch setting, employers and employees, in coordination with the pension fund board, establish a specific premium level for supplementary pensions (second pillar), while the pension fund board determines the investment mix and purchases financial products from commercial providers. It is necessary to perfect these governance structures and, when it comes to export, to adapt these to the specific foreign environment. This also involves finding the right pension vehicles (premium pension institution or PPI, general pension institution or API).

### **Output of innovation program: precompetitive components**

*Component 3-C-1: Insight into the success factors that have led to successful pension products and pension choices internationally*

This especially involves analysis of the respective roles of employers, employees, financial product providers, and supervisory authorities.

*Component 3-C-2: Models for good governance structures*

This involves the design of good governance structures for group pension products that link up with the local environment in a given country, as well as the characteristics of the related solidarity circle

*Component 3-C-3: Insight into the selection behavior of managers who put together group pension contracts and take investment decisions on behalf of participants.*

## **Products that can be developed using the components**

*Product 3-C-1: Pension vehicles for the foreign market (API, PPI)*

...that link up with the European directive governing Institutions for Occupational Retirement Provisions (IORP), that match the specific labor market legislation of a specific country, and that correspond with the wishes of participants. These pension vehicles will become important pension product providers in the European market.

*Product 3-C-2: Group pension products for employers with a governance structure that is in keeping with local institutions.*

## **PIL 4: Supervision of fully funded pensions: solvency and transparency (RDP)**

### **The Dutch discussion on renewed supervision**

Following on from the Goudswaard Committee, the social partners (trade unions and employers' organizations) have in the recent pension accord expressed the need of shock-resistant pension contracts, where 'soft' rights adjust to developments in the financial markets. This calls for forms of supervision, to examine whether the way pension funds are funded corresponds with the level of security promised.

New forms of supervision of the solvency of pension insurance companies are required, ensuring that they hold sufficient cash to meet their hard and soft obligations.

The recent cabinet evaluation already identified various bottlenecks around the Financial Control Framework for pension funds, and the social partners too call in their pension accord for a renewed framework, in conjunction with the renewal of collective pension contracts with modifiable rights that they seek. Also, the requirements to make premiums cost-effective must be revisited. Choices regarding parameter values in the supervisory sphere (e.g. the risk premium on shares) must be based insofar as possible on the latest scientific insights. In addition, new requirements are needed with regard to the communication of pension risks and the related transparency now that participants in group pension plans are confronted with greater risk. This calls for market conduct supervision.

### **European discussion or supervisory harmonization**

The credit crisis has given new impulse to the European discussion around the harmonization of national legislation. Dutch supervisory regulations (such as in the context of a new Financial Control Framework) will need to match closely with the European rules (e.g. in Solvency II), or if they differ then with solid motivation. In the supervisory sphere, the Netherlands can play a central role in the European debate. It is important in this regard that the European rules on supervision take into account the regulations around group pensions that this country has. Also, the playing field for different pension administrators – with different nationalities and governance structures – needs to be as level as possible. Lastly, the supervisory approach to group pensions must link up well with that for individual pension products.

## **PIL 5: Risk sharing and distribution among generations: full funding, pay-as-you-go, taxation (RDP)**

### **Pay-as-you-go and traditional capital funding under pressure**

In many countries, austerity is the word when it comes to pensions that are financed on a pay-as-you-go basis. Corporate pension plans that are fully funded, where the employer takes all risks, are also under pressure. After all, companies run the risk through their pension plan of increasingly ending up in an insurance role, where the risks of pension liabilities are becoming dominant compared to their standard business risks. In addition, new bookkeeping rules are requiring companies to report the growing risks related to their pension plans by recording their pension liabilities and related risks on the balance sheet.

### **New split of public and private responsibilities in intergenerational risk sharing**

The credit crisis, together with the ageing of the population, stimulates the private funding of old-age risks now that the government finances of many countries are in a sorry state. Many governments therefore seek to cut the growing costs of state pensions that are financed on a pay-as-you-go basis. All of this intensifies the search for new combinations of private and public responsibilities to cover old-age risks and the related sharing and reallocation of risks between and within generations. How can risks best be divided between generations, and what is the role of government and the private sector in this? One question in this regard is whether governments can play a role in the coverage of risks within private fully-funded systems, for example by issuing new financial instruments or through insurance arrangements. In that way governments would make it easier for the private sector to take on more responsibility for pension facilities.

### **Tax treatment of fully funded pensions and other capital accumulation**

Another knowledge requirement is the tax treatment of capital accumulation in general and of pension savings and pension insurance in particular. Should the tax authorities distinguish between different types of equity (liquid assets, illiquid pension savings, equity in owner-occupied homes) and between collective pension (second pillar) and personal pension savings (third pillar)? Or should we aim for a pension framework that is neutral as to the shape of labor? What consequences does the choice for a specific tax system have on intergenerational risk sharing and international mobility?

### **Measurement of claims by and against national governments**

The knowledge demand focuses here on how the pension liabilities of a government and the tax claim on private tax savings can best be measured – also in the context of European supervision of national budgets and transparent information on budgets for financial markets. A related question is how the budgeted costs of guarantees to the pension sector (e.g. insurance of defined-benefit pensions) can best be made visible. The debate regarding sharpened European supervision and the greater disciplinary impact of financial markets on national budgetary policy enhances the relevance of this question. Is it possible to perform an ALM analysis on a government balance sheet, which takes the

great level of uncertainty into account? Is it possible to reach international agreement regarding the underlying parameters that is based on recent scientific research? International standardization of information on pension systems appears essential in this context.

## **PIL 6: The labor market (RDP)**

### **Higher retirement age and the labor market for senior citizens**

The correlation between pension facilities and the labor market is getting increasingly important and calls for analysis. The credit crisis underscores the importance of a smoothly functioning job market for older people. Senior citizens will want to stay employed longer in order to keep their pension at a desired level, since pension facilities everywhere are being cut back. However, the stimulus to continue working longer fully brings to light the weak position of senior citizens in the job market. Reforms are needed that keep senior citizens productive in positions where their talents are optimally utilized.

### **Labor supply**

The need to cherish human talent also calls for a pension system that encourages people to stay active longer, for example through part-time pension or by supplementing income from work with pension benefits. This requires an answer to the question what factors have most impact on whether someone decides to keep working longer or not. Should continuing to work be made more attractive financially, should work be structured differently, should we work especially on better health of senior citizens, or are social and cultural norms the prime factor?

To cherish human capital, it is also necessary to develop products and regulations to optimally insure human capital and at the same time to keep the related cost as low as possible. This applies, for example, to insurance of occupational disability and of illness.

The extent to which individuals run the risk of dropping out of the labor market, or experience a quicker or instead slower career development than expected, also heavily determines what makes a pension product appropriate. Research is needed to determine which groups of employees and self-employed workers are especially exposed to these risks, what the greatest risks are, and how these risks extend into income from work and the structure of pension products. Other issues in this respect are optimal transferability of pension rights between jobs, different types of employment contracts, and countries.

### **Labor demand and job mobility**

Another important link between the way the labor market operates and pension facilities is the growth in job mobility: within the Netherlands and internationally, between industries, between employee status and entrepreneurship. For example, the growth in this country of the number of self-employed workers without employees represents a challenge for the system of supplementary pensions, since this group largely falls outside the system. That raises the question how the pension system should respond to these and other developments in the labor market. Can the pension system offer greater flexibility and freedom of choice without spilling the benefits of collectivity and solidarity? Is there still a future for the average system, or should pension premiums be made more actuarially neutral so that the second and third pillars link better with each other? The Goudswaard Committee calls for a study

of the advantages and disadvantages of the average system and as to how a transition to a different accrual system might take shape.

## **PIL 7: Heterogeneity within generations and the position of senior citizens (RDP)**

There is great heterogeneity within the older generations in terms of income, wealth, health, life expectancy, work capacity, family situation, social networks, and activities. It is highly important to gain insight into this with a view to the required social policy. In this context the pension accrual of different groups (both pension rights already accrued and yet to accrue) is important to be able to determine whether much poverty can be expected among senior citizens in the future and whether people will need to adjust their living standard downward as they become older. In what respects are current and future senior citizens vulnerable?

This project combines various existing data sources to gain a better insight into the current and future position of senior citizens, with their differing characteristics as to income, financial and human capital, personal health, and social networks. This information is compared wherever possible with similar data abroad. It is important, in the context of European learning processes, that data regarding the position of senior citizens are comparable internationally. A contributing factor in this is that the budgetary sustainability of state pensions cannot be isolated from the income position of the elderly. Limited future public outlays for state pensions are only credible if senior citizens have sufficient other sources of income.

A key knowledge demand in this regard is how the living standard of senior citizens can best be maintained without discouraging savings, the search for work, and investments in human capital.