Netspar

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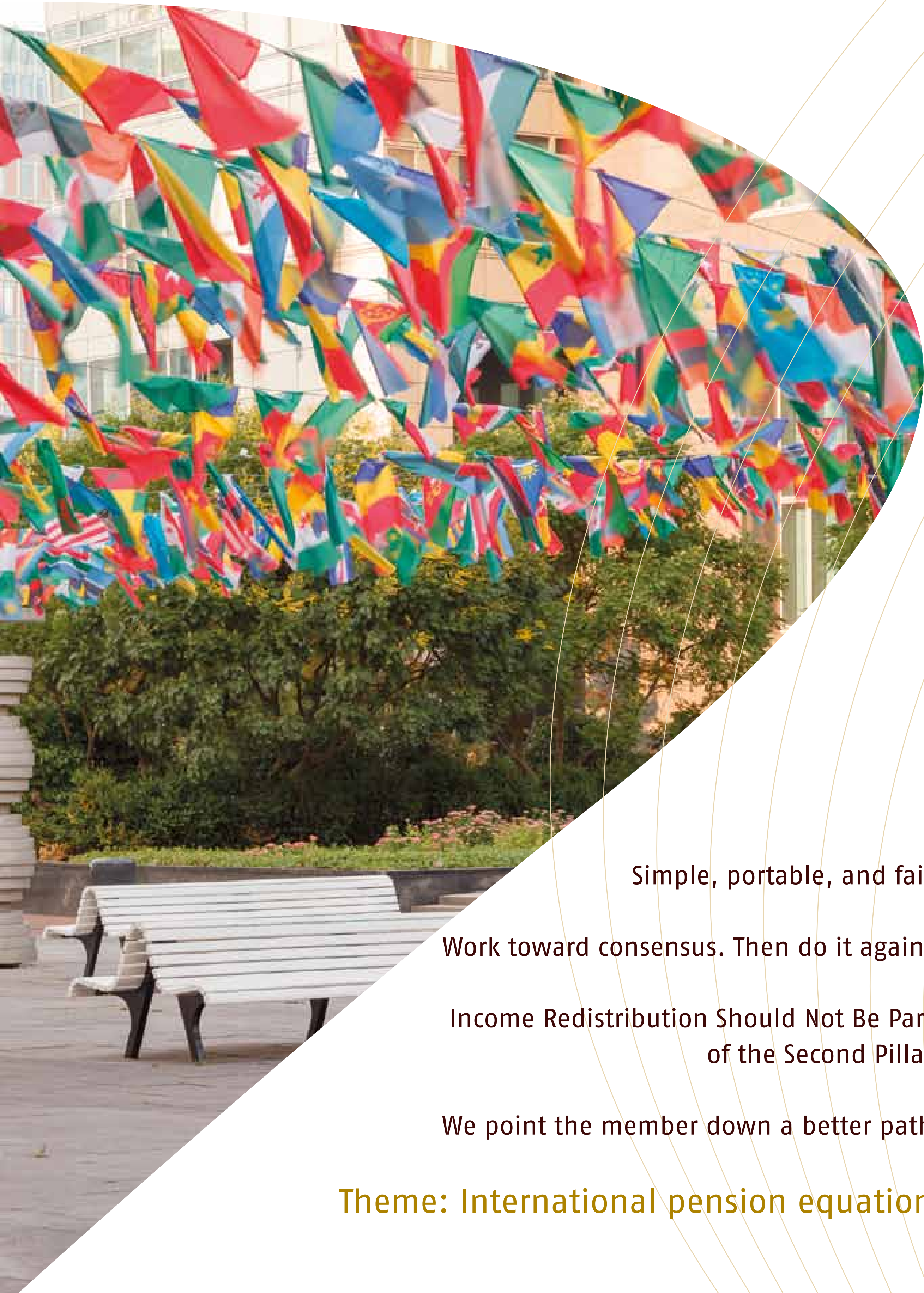

Simple, portable, and fair

Work toward consensus. Then do it again.

Income Redistribution Should Not Be Part of the Second Pillar

We point the member down a better path

Theme: International pension equation

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INTRODUCTION

Over five years since the outbreak of the financial crisis, State Secretary Klijnsma has finally signaled the start of a national dialogue on pensions. Of course, the past several years have already seen a great deal of talk, discussion, and even argument about many fundamental aspects of our pension system, including the discount rate, the mandatory nature, the uniform contribution rate, the retirement age, and the association with other portfolios such as housing and healthcare. The fact that a formal dialogue is being initiated suggests that the progress made to date has been insufficient, and maybe that's true.

There have, however, been some significant steps:

1 The buffers worked, for the most part, and beyond that, we have accepted that pensions can ultimately be cut. As a result, the pension contract is truly more comprehensive.
2 The eligibility age of 65 is no longer sacrosanct.
3 The efficiency of the industry has improved tremendously, due in part to the astonishing wave of consolidation.
4 Together with the new Improved Governance of Pension Funds Act (Wet Versterking Bestuur), this wave of consolidation has made boards stronger and more responsive.

Subsequent steps will need to go even farther: institute clear ownership rights, abolish the uniform contribution system, stop allowing rollovers among groups within funds... Only then will the system be future-proof. It is extremely helpful to occasionally share thoughts with foreign pension experts, because many of them would gladly take over our pension system, problems and all. For our part, we have more to learn from other countries than simply how things should not be done. At both the macro-level and the level of individual service providers in the pension world, we can learn a great deal from our colleagues in places such as Sweden, the United Kingdom, Canada, and Australia. The arrogance of thinking we always know better in the Netherlands when it comes to pensions is a thing of the past.

At a recent Netspar event at Erasmus University, a number of these lessons from abroad in the fields of legislation, communications, administration, and investment policy were shared with a wider public. It was extraordinarily inspiring and the audience then continued the conversation about the future of the system while enjoying a drink. You can find a report on the conference on the Netspar website, and we elaborate further on the theme in this issue of the magazine.

Onno Steenbeek
Erasmus University / APG

Keith Ambachtsheer

'SIMPLE, PORTABLE, AND FAIR'

Keith Ambachtsheer advises the Dutch to look northward. "The Danes are implementing some interesting concepts that could also be useful in the Netherlands," says the Canadian pension expert, who is now equally at home at the large Dutch funds.

Frank van Alphen

This is not the first time he has had to ponder the Dutch pension system, and it will not be the last. Over the past several years, he has often served as an oracle for the large Dutch pension funds and their providers. And his teachings stem not only from Canada, but also the U.S., the UK, Australia, and Denmark, where he sees many developments the Dutch can learn from. And it certainly cannot hurt to learn more about the new investment policy at PFZW/PGGM.

Because of his extensive expertise, in fact, Ambachtsheer is routinely asked to turn his attention to the Dutch pension system. At the invitation of the Dutch Royal Economy Society (Koninklijke Vereniging voor Staat-huishoudkunde, or KVS), he is currently writing a recommendation on pensions to be presented at the end of the year. Each year, the economists association issues a recommendation on some relevant topic. Here, he presents a sneak peek.

In the debate about the future of the system, Ambachtsheer believes it is essential to avoid getting stuck in a discussion about DC versus DB. "It is much more productive to think in terms of affordability and certainty," he says. "Those are the criteria that matter for all pension systems. Not until you get beyond the DC-DB dispute can you take the next step," he says. "In designing the second-pillar system, you have to weigh the variables of adequacy, affordability, and certainty. You simply cannot have everything. It is logical that the benefits of the first pillar be included in those considerations."

Ambachtsheer also thinks that a good pension system must meet a number of criteria that all of the stakeholders largely agree on. "The criteria that Thomas van Galen, Theo Kocken, and Stefan Lundbergh have outlined in the Fall 2014 issue of the Rotman International Journal of Pension Management this year are highly useful," he says. "These principles are aimed at revamping the system so that it is widely accepted; it is stable; and it is fair."

Participant Behavior

Those criteria fall into three categories. The first involves incorporating insights into participant behavior. "'Keep it simple' is an important principle," Ambachtsheer contends. "It is also essential that you limit the number of choices and offer a good default option for participants who do not want to have to choose. Finally, you have to take people's expectations into account: don't promise too much. That's what was wrong with the present system. Excessively high expectations were built that now cannot be met."

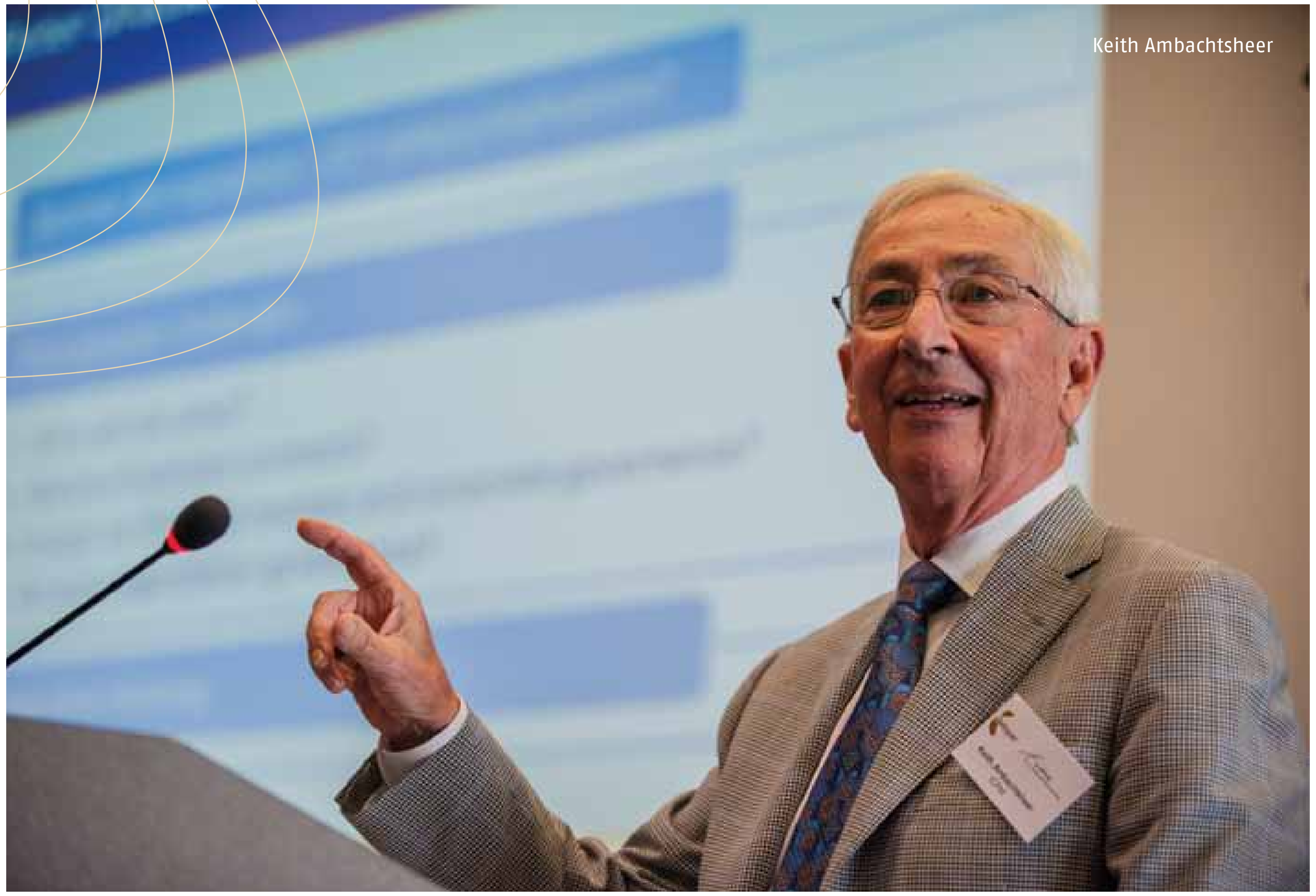
Portability

Portability is the second heading under which some of the new conditions fall. "Make sure the system can be adapted to external changes," Ambachtsheer says. "A precondition of that is to have clear ownership rights. That makes it easier to transfer pension savings to another fund. Of course, part of any portable system has to be objective valuation. And that means using market valuations as much as possible. Otherwise, you run the risk of participants thinking they are better off leaving the system."

Risk Distribution

The third matter parties need to reach agreement on is the thorny issue of risk distribution. "Avoid situations in which certain groups come out as winners, while others are the losers. Share the risks that can be pooled within groups. On the other hand, recognize that macro risks such as rising longevity for the whole group and future financial crises cannot be pooled, and must be borne by the group as a whole", Ambachtsheer says.

He feels that recent changes made to the Danish system meet the criteria listed above. The Danes already had a system that scored better on portability than the Dutch one but have also taken a couple of additional steps. "A pension based on 80 percent of the premiums will be guaranteed for a 15-year period starting next year," he explains. "The Danish pension provider ATP decided on this because long-term guarantees cannot be hedged in the financial markets. Moreover, this method offers better protection against inflation. The guaranties are adjusted every 15 years to reflect the prevailing interest rates and most recent mortality tables."


Keith Ambachtsheer

Split into Two Funds

There is another area in which the Danes are leading the way, according to Ambachtsheer. They draw a strict line between saving for a guaranteed annuity and investing for the purposes of indexing pensions. "This is in line with the principles of Jan Tinbergen," he says. He has great admiration for the Nobel Prize-winning Dutch economist, who argued that you should never use one instrument to accomplish two objectives.

Ambachtsheer's contention is that funds should be split into an earnings fund and an endowment fund: the first would aim to earn high yields (within a set risk tolerance), and the second would be able to guarantee the flow of payments. "The earnings fund can truly target the long term," he asserts. "That fund could focus more on a tenable flow of dividends or rent income instead of the daily rates. TIAA-CREF, the pension organization for American academics, has worked that way for decades and continues to meet expectations."

Interests of Investment Managers

In terms of investing, furthermore, it is important to be mindful of the somewhat opposing interests of investment managers and participants. "It needs to be structured in such a way that the investment managers have the same interests as the members," Ambachtsheer says. "Too often, investment managers are overly concerned with money-wasting beauty contests that are not in the best interests of members. They want to beat their competitors in the short term. The fund for teachers in Ontario is a good example of a truly long-term investor that is performing better than traditional investment managers."

In that regard, he thinks the developments at PGGM and PFZW are interesting. "After a thorough analysis prompted by the financial crisis," he continues, "they're establishing new criteria for their investment policy. Sustainability, limiting the number of investment categories, and dedicated long-term investing are important aspects of that policy. PFZW, for example, is no longer using financial benchmarks as a guide, but the fund's liabilities."

Transition

Ambachtsheer is the first to acknowledge that there is still a long way to go to get from today's system to the form of pension accrual he envisions. One of the greatest obstacles is the rights people have accrued. Those have to be incorporated into the new system; otherwise, you will end up having two pension systems. "Rights could, in theory, be converted based on the amount of contributions, but the uniform contribution rate makes that tricky, because accrual is not directly linked to deposits," he reasons. "The transition to another system will be disadvantageous for some groups. That can perhaps be fixed with an age-based bonus on top of the AOW (social security). In any event, a conversion protocol will need to be developed that meets all of the criteria we set for the entire system."

Involve the Participants

Ambachtsheer saves the toughest for last. The confidence participants have in the pension system is low and their involvement leaves much to be desired. Nevertheless, creating a base of support for the new system is vital. "Getting people involved in pension reform is probably the industry's biggest challenge," he says. "It takes time. Experts must take care not to get too technical. The trick is to use words that resonate with the experience of the average citizen. It has to be about more than just any cuts that may be necessary. The debate should be about a system both young and old can trust."

Keith Ambachtsheer

The 72-year-old Canadian, who recently relinquished the chairmanship of ICPM to Professor Rob Bauer, has written numerous authoritative books on pensions. He was introduced to the Dutch pension industry by Jean Frijns, former director of investments at ABP. Since then, he has been asked to provide advice on a regular basis. Ambachtsheer was born in Rotterdam and moved with his parents to Canada when he was 12.

Tim Jones, CEO of NEST:

'WORK TOWARD CONSENSUS. THEN DO IT AGAIN.'

"You have to take stock of the objections to a change well ahead of time," says Tim Jones, CEO of NEST in the UK. "That allows you to address those problems. Then you can prevent stakeholder groups from dropping out."

Frank van Alphen

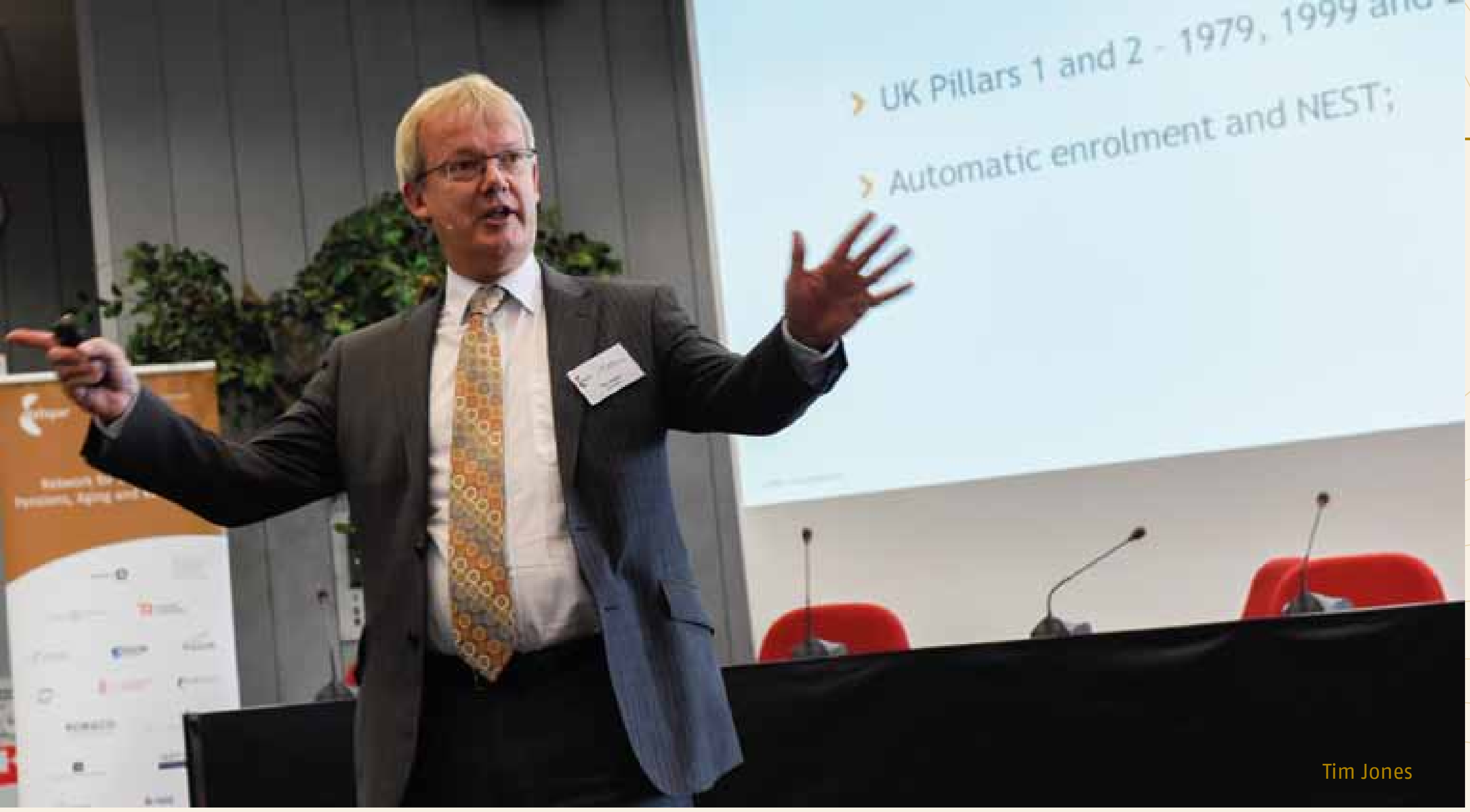
A former banker, Jones drew this conclusion based on his experience with setting up NEST (National Employment Savings Trust). The pension company was established by the British government fairly recently and is a critical component of the British pension reform now underway. Three years after its founding, NEST is still a relatively small player in the UK, but it has the potential to become a pension juggernaut. Within the next few years, it is expected that three to four million British workers will be saving their pension with NEST. Those members work for some half a million employers, from the corner pub to major corporations.

"We are a start-up totally devoted to becoming a large company, taking it one step at a time. At the moment, only employers with around sixty employees can sign up. In the next few years, we'll add smaller companies, too," says Jones (1955), who has vast experience with automated payment systems. The assets under management are thus expected to rise exponentially in coming decades.

Since current members (1.6 million workers employed by over 9,000 mid-size to large employers) have just started saving, NEST has only £ 232 million in its coffers. In 15 to 20 years, though, those assets could grow to a few hundred billion pounds, allowing NEST to join the ranks of the largest European pension funds. The pension fund, which was launched in July 2011, is a long way from that at the moment, however. "It was not until October 2012 that companies could subscribe," Jones points out. "We started with the large corporations. To get employers like McDonald's as a client, everything has to work perfectly – and you have to be able to prove it. Otherwise, they won't make the switch."

Inception of an Idea

Tony Blair and a few of his advisors were behind the inception of the NEST idea. "At the start of this century, some smart politicians recognized that pensions would not be adequate in the future. Too few employees were building a supplementary pension. Remember, that was before the pension problems arose, nor was it a topic that received much attention in the public domain.



Tim Jones

I was a banker at the time and absolutely unaware of any kind of pension debate," Jones points out.

The government formed a commission that was charged with analyzing the pension problems. According to Jones, the selection of the members of that committee, under Adair Turner's leadership, was brilliant. "These were people who had the right intellectual baggage and were also able to get all the parties to agree," he says. Nearly all of the recommendations of the Turner Commission were adopted by the government. "Simplifying the state pension was one of the recommendations. The current Minister of State for Pensions, Steve Webb, started working on that."

Compulsory Regulations

The commission was painfully aware of the British population's aversion to compulsory regulations. "It is very simple: anything that is compulsory is seen as a form of taxation," Jones explains. Turner solved this by turning to some of the latest findings from behavioral economics. "That was brave. Those findings were not yet generally accepted then," Jones continues. "Moreover, no one had tried them out."

The premise behind the NEST scheme is that "if you do nothing, you're in." "We knew from behavioral economics that most people will then choose the standard solution. To keep it from being too big of a shock, the premiums are still low. They will gradually rise to about 8 percent," says Jones.

The strategy was a big success: about 92 percent of the employees who join the scheme continue saving with it. "We do not exactly know why 8 percent drop out," Jones says, "but we do know that it's mostly older workers. I find that encouraging. Young people apparently see the benefits of saving for a pension."

The not-for-profit NEST does not have a monopoly. The British, after all, love the free market. Companies are required to offer their employees a pension scheme but do not have to use NEST's services for that. They can also go to market parties such as Scottish Widows, Aegon, or Friends Life, which also work through "automatic enrollment," like NEST does. As the only pension scheme with a public service obligation, NEST does have to accept all employers.

The British pension structure is not likely to be copied by the Netherlands anytime soon, in Jones's opinion. "Pension arrangements reflect society to some extent. British people want to know exactly how much money is in their pension pot. The Netherlands is more accustomed to collective schemes, where that is less obvious," he says. The most important lesson others can take away is about the quest for consensus. Despite multiple rounds of consultation and intensive deliberation, the original plan for NEST remained reasonably intact. "It is no camel," says Jones, r eferring to the saying "A camel is a horse designed by a committee."

"We held the consultation sessions to take stock of the objections. That allowed us to modify or explain things. One example is that businesses can only communicate with NEST electronically. You cannot send us a letter. Smaller companies in the country had their reservations about this, because they have less reliable internet connections. We explained that eventually the tax authorities were also only going to allow electronic communications, so we were not the only ones... That won that group of business owners over," he recalls.

Simplicity is another issue everyone in the pension industry should bear in mind. "Complexity is your enemy," Jones says. "NEST's design is elegant in its simplicity." Both employee and employer pay premiums and NEST invests the money. It is a DC scheme with some collective features. Everyone has their own savings pot of money, but the money is collectively invested for each age cohort. "Our investment policy is aimed at obtaining a stable yield," he continues. "We want to avoid having some cohorts achieve much poorer results than other age cohorts. In that sense, it is not the same as an individual DC pension."

Costs

One of the major objectives of NEST is to offer an excellent pension scheme at a low cost. NEST withholds 1.8 percent of the premium. In addition, NEST, which was established with a government loan, charges 30 basis points on the assets managed. "All told that amounts to about 50 basis points. That is a reasonable fee for our services," says Jones. He expects that the costs could even decrease in the long term, as more workers sign up. "It might take ten years before the costs shrink," he says. "That is why it is not something we emphasize much. That would just give the wrong impression."

Full Retirement No Longer Standard

As in the Netherlands, the pension landscape is undergoing transformation in Great Britain. "We will have to continually adapt to changes in the regulations," Jones says. One important change is that pensioners will have more choice in the payout phase. Now, you can withdraw one fourth of the money tax-free and have to use the rest to buy an annuity. That requirement is being overhauled, in part because full retirement is no longer the rule. "People want to work less, for example, instead of stopping completely," Jones explains. "That will require more flexible rules. This change has huge repercussions for our investment policy, which is based entirely on the compulsory purchase of annuities." This topic is relevant in the Netherlands, as well. Here, too, pension experts are calling for more freedom during the payout phase for individual DC schemes. If people were allowed to invest more in the stock market upon retirement, it might influence the existing life-cycle investments.

The changing rules are already forcing NEST to reexamine a number of issues. "We do not exactly know what a member is going to do under the new situation," Jones points out. "That means we have to develop a default that will work out best in most cases. We are in the midst of a round of consultations. We hope to have a proposal by next year. And here, too, we are once again seeking consensus."

The new freedom workers are being given demands a degree of guidance. The government is mulling over a system of offering guaranteed independent guidance to members to help them make decisions at retirement. "We do not know what the decision is going to be," says Jones. "Fortunately, we have time to prepare for the changes. Workers have only saved relatively small amounts with us."

Tim Jones (CEO of NEST)

Tim Jones (1955) originally worked in the bank industry, for Capital One Bank and as CEO of NatWest Bank. Jones was also closely involved in the modernization of the British payment systems. In addition to his work at NEST, Jones is the director of Investment Technology Group, an institutional broker dealer. He is also an unpaid member of the Board of Directors of the Rothman International Centre for Pension Management.

Stefan Lundbergh

'INCOME REDISTRIBUTION SHOULD NOT BE PART OF THE SECOND PILLAR'

Stefan Lundbergh knows all there is to know about the Swedish and Dutch systems. "More free market influence does not automatically mean it's going to be the 'wild west.' That's something the Netherlands can learn from Sweden's experience with controlled competition," he says.

Frank van Alphen

"Countries have a tendency to be complacent with their pension systems. You see that in the Netherlands, and in Sweden, as well. The drawback is that they look primarily only at their own system. It never occurs to people that other countries are dealing with the same problems and have found other solutions to them."

Lundbergh believes the Netherlands can learn a great deal from Sweden, because the two are so similar. "The mentality in the Netherlands is similar to that in Scandinavian countries," he points out. "We don't flaunt our riches or success, for example. We, too, value consensus and the collective good. In that regard, we both differ greatly from Anglo-Saxon countries. That's why I expect the British, Americans, and Australians can benefit more from sharing their experiences. Those countries are more concerned with the investment side of their pension systems. The Netherlands is not likely to adopt the British or American approach, because in the eyes of Dutch people, it's too focused on the individual."

Lundbergh has worked in the Netherlands for eight years. He started out at APG, before becoming head of innovation at Cardano a couple of years ago. In addition, he is a non-executive director for AP4, one of the buffer funds for the Swedish pension system. The Swedish pension system was set up in the fifties. "At the time, white color workers had reasonable work place pensions, but the blue color workers did not have a pension solution. There was a debate about the potential solutions. It basically came down to the left wanting a mandatory national pension run by the state and the right wanting a second-pillar solution with pension funds," he explains.

In the end, the choice was a compensation-based first pillar with buffers, with the government as custodian. The system was made robust with the Notional DC reforms in the mid 90s. Today, all Swedish citizens pay a contribution of 16 percent of their income to fund this first pillar (the income-based pension). The big difference with the Dutch social security system (AOW) is that the first pillar is subject to possible reduction in pension rights including pension in payment. This year, for instance, 1.2 million pensioners saw a 2.7 decrease in their state pensions. On top of the income-based pension in the first pillar, people also pay a "premium pension" contribution of 2.5 percent of their pensionable income. In the second pillar, they pay an additional 4.5 percent into DC plans. In total, most Swedes pay 23 percent of their income in pension contributions. There are no individual choices with regard to the income-based pension in the first pillar, but there is in the premium pension and the second pillar plans.

Lundbergh believes the Swedish system makes a clear distinction between government responsibilities and private pensions as a financial product. "Income redistribution is the domain of government. It can take concerted measures in that regard. And citizens can voice their preference for different kinds of incomes policies by voting," he says. The Swedes have a form of income redistribution built in to their first pillar. People in the higher income brackets also pay premiums on the top portion of their income, even though the pension rights issued in the first pillar has a ceiling. That means those with higher incomes are subsidizing people very low or even no income, say if they are unemployed. Lundbergh finds it strange that in the Dutch system, some of the income redistribution is also embedded in the second pillar. "Income redistribution is not the task of the social partners and their pension funds," he says. "A second pillar pension is actually deferred salary. It is a financial contract."

Lundbergh is also surprised by the general confusion in the Netherlands surrounding DC and DB plans. "In the pension system, participants bears the risk. Payouts are reduced when that becomes necessary. You call this a DB system. But the Dutch have to get used to the idea that they, too, have a DC system," he says. According to him, the issue is not the contrast between DC and DB. "In essence, all modern schemes are DC: premiums are collected and the benefits depend on the market developments and changes in life expectancy."

One major obstacle to innovation in the Netherlands, in Lundbergh's opinion, is the fiscal treatment of pensions. "My advice would be to start by tackling the tax regime," he argues. "It results in progressive rates for DC, which means older employees are more expensive than younger ones. That makes older workers less attractive on the job market. In Sweden, everyone pays the same percentage of the income in contributions." Another advantage of equal premiums is that they make the system much simpler than the Dutch system with its hundreds of different rules. "Equally important," Lundbergh continues, "is that costs for the workforce becomes predictable. Employers know exactly how much they will have to pay in pension costs in coming years."

Uniform Contribution Rate

Another Dutch phenomenon Lundbergh has serious doubts about is the uniform contribution rate, and he finds some of its effects hard to justify. "Early in your career, you are paying too much for the pension you're accruing," he points out. "That adversely affects anyone who leaves the system when they are, say, 45. This impacts not only older workers who decide to start working for themselves, but also poorly educated workers who become unemployed. The system is particularly unfair for a 55-year-old, poorly educated woman who loses her job. I don't understand why the social partners would want to maintain a system that hits the weaker members of society."

Lundbergh realizes that getting rid of the uniform contribution rate will take some efforts, but he is still in favor of transitioning to a system with a fixed contribution amount for everyone who works. "There will always be winners and losers in any transition," he admits, "but that is no excuse for not changing things. Under the present system, you also have some participants who benefit, while others bear the costs. Eventually, we need to find an acceptable compromise."

Providers

One of the major focuses in the Netherlands has been the issue of which party can best administer a scheme. The trade unions are generally opposed to commercial parties such as insurers: they prefer the pension funds and their captive providers, because they do not have any profit motives. Lundbergh thinks this debate about providers misses an essential point. "The more important issue is the scheme's features," he says. "What portion is guaranteed? How is the longevity risk dealt with? How are other risks distributed? Only after you know that can you go looking for the best provider."

In Sweden, the social partners choose the providers, which can be either non-profits or commercial parties. The social partners use their purchasing power in selecting pension providers, which allows them to negotiate low fees for their participants.
"Participants have the legal right to exchange their provider for another party," says Lundbergh. "In practice, though, few workers ever do. But the fact that customers can walk away keeps the providers on their toes."

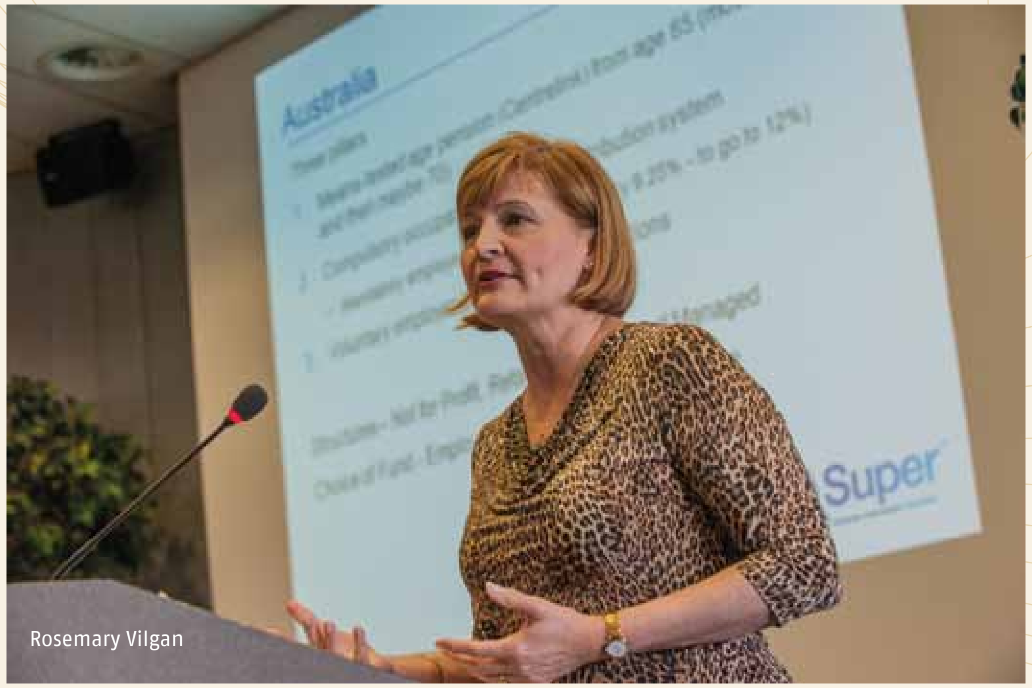
According to Lundbergh, the Swedish model shows that giving participants more freedom of choice does not mean there is no longer a role for the social partners. "The privatization here has not led to the 'wild west' scenarios that were feared," he says. "In fact, the controlled competition leads to lower costs. In Sweden, costs are considerably lower than in the Netherlands." The asset management costs at the largest Swedish pension investors, for instance, are between 0.1 and 0.23 percent in the second pillar.

Too Many Options

Of course, not everything goes right in Sweden. "You could also learn from the things that went wrong for us. For one thing, we discovered that you should never offer too many choices," Lundbergh says. This was a problem with the so-called premium pension under the first pillar. Participants were allowed to choose which investment fund to put their money into. "Participants could choose from about 800 funds. That didn't work. Worse yet, consultants started popping up who tried to get a piece of the pie by getting people to switch to other funds so they could make a commission. Fortunately, plans are underway to reform this part of the pension system, and most Swedes choose the default anyway."

Not that everything in the Netherlands needs to be overturned. "Two elements of the Dutch system should absolutely remain intact: the high premium level and the fact that nearly everyone contributes," Lundbergh says. "That is the foundation for a good system. Countries with disappointing pension results generally have a much lower premium level and lower degree of participation."

Stefan Lundbergh
Economist Stefan Lundbergh is the head of innovation for Cardano Risk Management. He is also a non-executive director at AP4, one of the Swedish buffer funds for the first pillar. Lundbergh was formerly employed by APG and Skandia, a Swedish insurance company.



Rosemary Vilgan

Rosemary Vilgan, CEO of QSuper:

'WE POINT THE MEMBER DOWN A BETTER PATH'

QSuper – one of Australia's largest pension funds, representing over half a million Queensland government employees – plans to start providing more personal advice. "The members expect us to use our information to send them in the right direction," says CEO Rosemary Vilgan, who has held the reins there for over 15 years.

Frank van Alphen

She anticipates that pension funds will have no choice but to start treating their members more as individuals. "Other providers of financial products have also started sending out more personalized letters based on knowing your age and how much you've saved," she says.

Compulsory pension saving was introduced in Australia in the early nineties. The schemes are under the control of the trustee, being either non-profit organisations, such as QSuper, and profit motivated financial institutions. "The decision as to who administers the pension scheme depends primarily on the industry," Vilgan says. "In industries with trade unions that have lots of members, non-profits were chosen. The trustee will comprise of representatives from unions and employers to run these funds. In that sense they are like Dutch funds." Large companies generally bring in a financial institution to administer the pension scheme.

This second-pillar DC pension is on top of a generous, for an Anglo-Saxon country, first-pillar pension. The level is comparable to that of Dutch social security (AOW). The big difference with the Netherlands is that the Australian government pension payment is dependent on income and assets. It can be decreased if a person has income from, say, his or her second-pillar pension. Because the first-pillar pension is for life, it is also the de facto insurance against longevity risk. "That is not a risk that members can cover through us," Vilgan says. "They receive a regular sum until their capital is gone.

The big difference with the Netherlands is that the Australian government pension payment is dependent on income and assets.

Once the pension pot from the second-pillar pension is empty, the Australian government pension goes back up." In her opinion, the Government's age pension is sufficient to afford life's necessity's but not much more.

The percentage employers pay into the pension pot has gradually increased since the current system was first introduced. In early 1992, it was 3 percent of the salary, but it has since tripled. By 2025, it is expected to have risen to 12 percent. The contributions are invested in the default life-cycle fund of QSuper, which manages over $50 billion Australian dollars (+/- € 34.5 billion) in assets. "Members can choose not to be in the default option," Vilgan says, and indeed one in less than four takes over investing their own funds. "Especially members who are older and have saved a considerable sum do that, usually after they have consulted a financial planner, who will also look at their other assets."

Members can even fully manage their own pension savings. "Only people who have accrued considerable capital do that. You have to fill out quite a few documents before you can take that step," says Vilgan. She cautions that members who call their own shots tend to follow the market. "We see them make all the classic mistakes of private investors. They buy when prices are high and sell when they are low. That doesn't happen if you stick to a predetermined investment mix."

This summer, there was criticism of the fees charged by some of the superannuation funds, as they are called in Australia. It was alleged that private third-parties, in particular, were charging excessively to manage assets. QSuper claims that it is among one of the least expensive providers in the industry. The administration costs are 22 basis points (but capped) and asset management fees are between 7 and 46 basis points, depending on the selected investment mix. Those costs are in line with those of the large Dutch DB schemes.

Several of the problems the Dutch pension industry is wrestling with – e.g., the uniform contribution rate, the lack of pension savings among the self-employed and the irksome issue of rollovers – are not an issue in Australia. The main reason for that is that workers in Australia accrue their own pension pot. "Members who go work in another industry can continue to save their pension with us. The same is true for members who decide to work for themselves," Vilgan says.

This is not to say that the Australians feel that their pension system is finished. "We are exploring, for instance, whether there is some way to provide more certainty in cases where that might be desired," says Vilgan. She also thinks DC schemes could learn something from how DB schemes communicate. "With a DB scheme, the emphasis is on the final benefits. That is what the members care about. We can learn from that."

Providing Advice

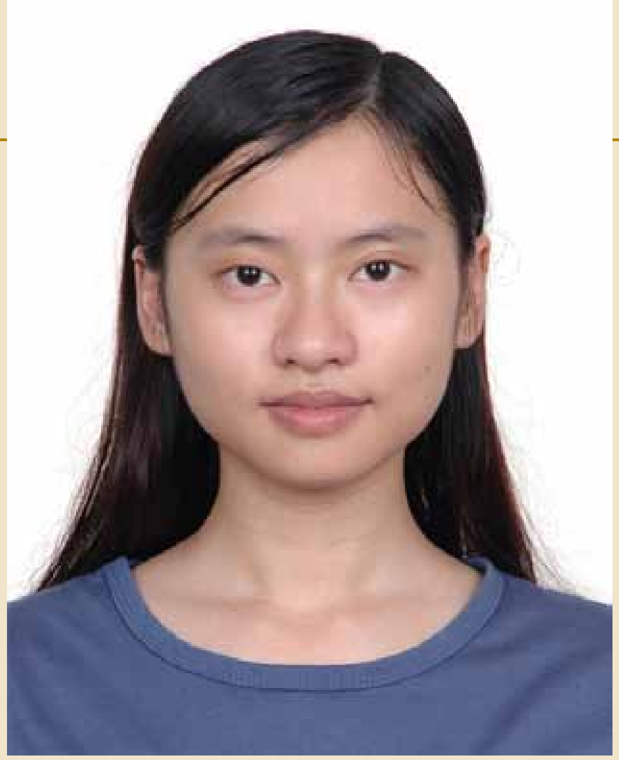
Vilgan thinks providing education and advice will become increasingly important. "We already have a related company where members can turn for advice," she says. "Some members are probably unlikely to consult an adviser. These are people who think it's scary or complicated. But we want to be able to provide a more personalized communication and advice offering to those members, too. We can do that because we have amassed an enormous amount of data over time." The automated provision of advice will be increasingly customized for the individual through the tailoring of the investment mix of their life-cycle funds. "This is linked to the amount saved and we also take age into account. And so we can add another variable each time," says the QSuper CEO.

Longevity Risk

Longevity risk is a topic everyone is putting great thought into. A government advisory committee led by David Murray suggests that second-pillar pensions should also account for this risk. One possibility is that, upon retirement, members would be required to put a portion of their money into a life annuity. As it stands now, members have a great deal of freedom. In that sense, the Australian situation is the opposite of the

Rosemary Vilgan

Rosemary Vilgan became the CEO of QSuper in 1998, at age 33. She has worked for the large pension fund for government and former government employees and their spouses in Queensland (Australia) since 1990. In her time at the helm, she has implemented great changes. In 2013, she was named the Telstra Australian business woman of the year. In addition to her work at QSuper, Vilgan is affiliated with Queensland University of Technology and the Australian Council of Superannuation Investors.



CHINESE NETSPAR STUDENT DELVES INTO THE UFR

Danqin Jiang heard about Netspar from her cousin Ting while she was a student studying Quantitative Finance. She got in touch and was able to come to Tilburg for a year, where she compared various methods for setting the UFR. Professor Bas Werker was her supervisor.

What do you think of the Dutch system?
"I think distancing pension funds from companies is a good model. The participants are not at risk then if their employer goes bankrupt. Another advantage is that the assets are professionally managed. The managers use advanced methods to control the risks. But there are also underlying threats, such as incomplete contracts and rising life expectancy. The people at Netspar know a great many details about the Dutch system. It struck me, for instance, that the staff often knew how many assets a given pension fund was managing."

How did you like it at Netspar?
"It was a pleasant experience. I learned a great deal because there were so many different people with different opinions. The contact with the insurers and funds was instructive."

Why did you compare European UFR methods?
"I am interested in the way these kinds of discount rates are determined. What's more, the discussion about how the UFR should be set under Solvency II is still ongoing. That rate is extremely important for determining the liabilities for both insurers and pension funds. My research showed that the different methods used in Sweden, France, and the Netherlands produced varying results."

To what extent is this information applicable in China?
"More in the general sense that risk management is valuable in the Chinese context. But you need to remember that the situation in China cannot be compared to that in Europe. In China, for instance, there are no mandatory annuities because the insurance market is still under development. People there still bear many risks they cannot insure themselves against."

You are now back in China. What are your plans?
"I'm still figuring out my plans. I am looking for a job. I don't know if I can use what I learned about the UFR here."

RECENTLY PUBLISHED PAPERS

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outline the implications of new developments in the academic literature for policy questions faced by Netspar's partners. The PPs are meant for professionals in the pension and insurance sectors and are discussed twice a year during one-day panel meetings. Representatives from academic and private sector partners, as well as international academics, act as discussants. The papers are published in a special PP booklet series.

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Gradual retirement. A pathway with a future?
Bloemen, Hans, Stefan Hochguertel and Jochem Zweerink
Panel Paper 41 - Juni 2014
Project: Pensions, savings and retirement decisions II

Reinventing international risk sharing
Bonenkamp, Jan, Lex Meijdam, Eduard Ponds and Ed Westerhout
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Project: Multi-pillar pension schemes and macroeconomic performance

Asset accumulation and decumulation over the life cycle. The role of financial literacy
Borella, Margherita and Mariacristina Rossi
Panel Paper 39 - April 2014
Project: Financial literacy

Emerging equity markets in a globalizing world
Bekaert, Geert and Campbell Harvey
Panel Paper 38 - Maart 2014
Project: Portfolio strategies

Pensioenbewustzijn
Soest, Arthur van and Henriëtte Prast
Panel Paper 37 - Maart 2014

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describe and motivate the position of the author on a policy-relevant topic. In contrast to the PPs, these papers contain strong statements. Although Netspar as such is impartial, individual researchers of Netspar may very well have (and express) a personal opinion. Netspar simply offers a forum for in-depth discussion. The authors present the NEA Papers at meetings and discuss them with the audience.

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Fouarge, Didier and Andries de Grip
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Project: Human capital and aging

Sociale interacties van invloed op de arbeidsparticipatie van ouderen
Rooij, Maarten van, Niels Vermeer and Daniel van Vuuren
NEA Paper 53 - Mei 2014

Waarom mensen de pensioenvoorbereiding uitstellen en wat daar tegen te doen is
Krijnen, Job, Seger Breugelmans and Marcel Zeelenberg
NEA Paper 52 - Mei 2014

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discuss the design of a component of a pension system or product. It analyzes the goals of the component and the possibilities of improving its function. A Netspar Design Paper is well accessible by specialists in the industry, responsible for designing these components. The Netspar Design Paper is to be printed, and both digitally and as a printed booklet available.

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Brounen, Dirk and Ronald Mahieu
Design Paper 29 - Februari 2014

EIOPA: bevoegdheden en rechtsbescherming
Witte, Ivor
Design Paper 28 - Februari 2014

Illiquiditeit voor pensioenfondsen en verzekeraars. Rendement versus risico
Driessen, Joost
Design Paper 26 - Februari 2014

De doorsneesystematiek in aanvullende pensioenregelingen: Effecten, alternatieven en transitiepaden
Bonenkamp, Jan, Ryanne Cox and Marcel Lever
Design Paper 27 - Februari 2014
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Colofon

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Netspar, Network for Studies on Pensions, Aging and Retirement is a 'think tank' and knowledge network. Netspar is dedicated to promoting a wider understanding of the economic and social implications of pensions, aging and retirement. Expertise from scientific research is used to transfer knowledge through publications, events and education. With that Netspar actively contributes to the social dialogue between policy makers, scientist and the pension and insurance practitioners.

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