

Being Prepared for Retirement Netspar Research Agenda, 2015–2019

Background

In 2014, we presented a research plan to our private partners that was based on the evaluations performed in the lead-up to the new funding term for 2015 to 2019. This framework plan was then further delineated in meetings with the government regarding the funding for the pension research agenda (Dutch Ministries of SZW and EZ) and the housing–healthcare–retirement research agenda (Dutch Ministries of VWS and BZK). All of the various parts of the work plan have been integrated into a comprehensive whole and categorized under five programs in the agenda presented here. The lines of enquiry will remain primarily economic, but now other disciplines such as sociology, psychology, law, and communications will be incorporated into the program more than before.

Netspar pursues this research agenda by launching targeted, large-scale, three-year research projects every year, based on an open competition. This is complemented with short-term projects, called “topicality projects,” chosen in consultation with the partners, which address pressing issues. The final research agenda is determined annually in consultation with the partners.

Research Agenda Comprised of Five Programs

The new Netspar agenda adopts an integrated approach to studying pensions and retirement from the perspective of the individual. One of the priorities is thus to gain a greater understanding of how people tackle the complex decisions surrounding old age; central to this are behavioral and communication aspects and decision analysis (how choices are presented). Moreover, this area of study ventures expressly into disciplines other than economics, such as law, sociology, psychology, and communications. The comprehensive approach means looking at retirement in conjunction with other essential concerns in old age: housing, healthcare, and work.

In addition to the micro issues at the individual level, Netspar will, of course, continue to address the macro issues related to the pension system as a whole and the reforms aimed at strengthening its resilience for the future. This will involve renewing our focus on pensions and paying greater attention to the issues of ownership rights, choice, and obligation, along with the question of how pensions can contribute to the financial stability of the economy as a whole. The research agenda has been broken down into five programs.

1. *Wellbeing and Welfare of Older People*

Research can help us understand the wide range of income and wealth situations and general welfare of people in their old age. Previous Netspar research by Alessie, Knoef, Goudswaard, and others indicates significant differences in the financial standing of elderly individuals. Recent studies have significantly improved our understanding of income levels and income differences during the payout phase of retirement savings, thanks in part to the availability of detailed data on income and pensions. However, our attempts at comprehending the big picture remain in their infancy. This will involve taking a more comprehensive approach that examines such aspects as consumption patterns and needs, living situations, healthcare expenses, and the possible role played by social networks and informal care, as well as linking all this to the sense of well-being among older people. Special attention should be paid to heterogeneity and at-risk groups (the formerly self-employed, widows, divorced people, people with social security shortfalls, etc.). The availability of information from new databases has provided a great opportunity to increase our insight in these areas, whereby we will seek to partner with other parties (e.g., CBS, DNB, RIVM, CPB, and Nibud).

Having insight into the lifestyles and living conditions of elderly people is essential for all policymaking related to old age. The central question is how the pension system can contribute, in conjunction with healthcare, housing, and employment, to securing a living standard for the elderly that approximates their pre-retirement living standard. The first and second pillars (i.e., social security and employment-based retirement plans) form the basis for post-retirement income but no longer guaranty a financially carefree retirement for everyone in the future. Accordingly, there is a need for research into the repercussions of both existing and future pension and income policies on the welfare of the elderly.

2. *Communications and Choice*

As citizens have become more vocal on social issues, they are demanding transparency and greater control over their pensions. Evidence shows, however, that consumers do not always make decisions that are in their best interest, particularly when it comes to complicated decisions with long-term implications and risks that are difficult to foresee—essentially, any decisions related to ageing. Many people lack the knowledge, financial literacy, and engagement required to absorb the information available to them and use it to take action as needed. Behavioral economics and psychological factors play a big role in this.

Sound choice architecture can help people make the right decisions. There is a deficiency of knowledge, however, about how it affects pension communications and the pension products offered and the respective roles of the pension provider, employer, and government in providing pension advice. Which decisions should be left up to the individual (and which should not)? What can we learn from other countries that offer “guided” freedom of choice through such things as defaults and opting out? Should there be a distinction between the accrual and payout phases? Together with research into the use of existing options and targeted

experiments, comparative international research can provide insight into the question of how best to supply information and design the choice architecture.

3. *Work, Retirement, Housing, and Healthcare*

Retirement cannot be viewed separately from the other underpinnings of old age: healthcare, housing, and employment. Many people build assets not only through their pensions, but also through their own home, and often these two forms of wealth creation are poorly coordinated. Moreover, the level of assets needed for retirement is directly related to elder care. The new emphasis on investment and self-reliance raises a host of new questions about the confluence of employment, healthcare, and full- or part-time retirement. Health issues also play a significant role. Advantages could be gained by better coordinating the various domains, and there are specific questions in need of investigation in certain areas.

In terms of housing, the issue is how to better coordinate wealth accrual through pensions and home ownership. Should newcomers to the housing market, for instance, be allowed to divert some of their pension or pension contributions to home financing? And how can the equity older people have in their homes be better converted to liquid assets, such as through reverse mortgages?

In terms of long-term care, the question is how personal savings could play a greater role in the future. Faced with an aging of the population, the government is under increasing pressure in this area and shifting more of the responsibility to individual households. What are the implications for retirement income and the associated uncertainties? Could healthcare savings plans or greater flexibility in pensions provide a solution? Is there a need for new forms of insurance and schemes for long-term care and could these ease the strain on the collective services? Other countries have voluntary insurance for long-term care—albeit on a limited scale—but it is a difficult market due, in part, to adverse selection. We can gain an estimation of possible developments in the Netherlands by studying the experience of those other countries.

Finally, there are some critical questions that need to be addressed about the transition from employment to retirement. With the increase in the retirement age, people are under pressure to work longer. However, not all workers are able to reach retirement age without physical problems. Part-time retirement can help make the transition from work to retirement smoother and thus also mitigate the differences in health between low- and high-education personnel. Greater flexibility could also help people in balancing employment and informal care. Information from new databases (stream, PIAK) will provide better insight into the connection between informal care and labor market participation.

4. *Savings, Investments, and Insurance*

One of the primary functions of the pension system is dealing with risk. Every individual faces a host of risks throughout their lifetime, such as those related to income, investments, health, family, and so forth. The pension system—along with the government and social services—ensures that these risks are managed and distributed efficiently. Netspar has invested heavily these past few years in improving our knowledge of financial risk, but important research questions remain to be addressed.

Risk management is a key task of pension funds and insurers. One of the new questions in this domain involves the role of illiquid investments. Investment in a home is not liquid for people, and mortgage financing is also tied up for long periods of time. There is a growing interest among insurers and pension funds in these illiquid assets. That could benefit the housing market, while also helping the banks' balance sheets. However, as insurers and pension funds grow their mortgage portfolios, new questions arise with regard to their asset management. This has been a major theme in the recent academic literature about illiquid investments. Applying this to the Dutch context could provide insight into the future demand for illiquid investments, the associated shortcomings, and the policy options for alleviating those shortcomings.

A second topic in this program concerns the future development of existing pension contracts. Variable annuities in individual contracts ("smart DC" plans) allow people to take risks even in the payout phase as a way of decreasing costs. And greater individual differentiation in collective contracts could contribute to a better distribution of risk across all life stages. Many countries offer people flexibility in terms of how their pension is paid out. This might take the form of receiving part of it as a lump sum or choosing between different forms of pension. Could offering greater flexibility provide better alignment with people's individual situations and preferences? What lessons are there to be learned from the experiences of other countries? And could experiments in the Netherlands provide better insight into their applicability?

Greater pension flexibility could help in terms of better harmonizing cuts and payouts with individual circumstances. Under this line of thinking, pension contract design is directly aligned with such themes as freedom of choice, housing–healthcare–retirement, and employment. Providing flexibility in the savings stage, by allowing pension contributions to be substituted by home financing contributions, for instance, could help families make better use of their financial resources in "expensive times." Meanwhile, flexibility in the payout phase could help people adapt their living situation to their needs in old age (e.g., installing a stair lift) or make provisions for costly long-term care. The main research question involves which decisions could be allowed a certain degree of freedom without leading to deleterious effects in terms of faulty individual decision-making, undesirable risk selection, and the undermining of solidarity. In other words, how can the pension system be *realistically* modified to allow greater customization and choice?

Any modification of the pension contract will inevitably meet with transition problems, especially where the uniform contribution system is concerned. By quantifying alternative scenarios, we can provide insight into the scope of the transition problems and any potential solutions or compensatory measures.

5. *Institutions, Governance, and Solidarity*

The final program focuses on the institutional aspects of pensions and other old age provisions. In the area of pensions, especially, because of their long-term nature, reliable institutions are an indispensable part of making the contracts possible. Pension governance is one of the key themes. Current benefits agreements provide considerable room for discretionary decision-making on the part of pension fund boards. This “social contract” has the benefit of allowing the funds to respond agilely to unforeseen developments. It also provides the capacity for distributing risks that cannot be dealt with through the market. However, the attendant requirements in terms of trust and solidarity among participants are high. At the opposite end of the spectrum is the “financial contract” that prescribes near complete ownership rights. Research is needed (e.g., contract theory, sociological–institutional analysis) to provide further insight into the tenability of both contracts.

The questions surrounding tenability, governance, and regulatory supervision apply equally to individual contracts supplied through the market. The greater number of options and rise of choice architecture design have placed the issues of information provision, advice, and fiduciary duty at the top of the agenda, including questions about the regulation of the various parties. To what extent are the various players able or willing to be responsible for the fiduciary duty associated with these complex issues? On top of all this are questions about the role pension funds, insurers, and corporations might play in the domain of healthcare and housing.

The emphasis in this program is on the cohesion within the system as a whole. The government establishes frameworks with tax policies, legislation, and regulatory bodies. These frameworks are not fixed, but must rather be constantly adapted to the changing social environment, including an aging population, increasingly vocal citizenry, and fluctuating labor market and labor relations. Comparative international research and scenario analysis—along with historical research—can serve to place the problems associated with retirement in the Netherlands within a broader context.