The regional and local impact of EU pension system reform

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Executive Summary

The **ageing of the workforce** is a widely recognised challenge which has been given considerable political emphasis in both national and EU policies. As the Stockholm strategy highlighted as early as 2001, a significant, well-documented increase in demographic dependency ratios poses particular challenges for both the adequacy and the sustainability of pension structures. The **financial and economic crisis**, along with the consequent increases in national debt levels and the setback to public budgets, financial stability and employment, has increased the urgency of dealing with pension structures. In view of the new **Europe 2020** strategy adopted by the Council in June 2010, there is now a particular demand for policy that helps Member States ensure **adequate income support**. Fiscal consolidation and **long-term financial sustainability** also feature strongly in Europe 2020. In this context, the Green Paper on Pensions highlights a number of shared challenges for Member States, on which it is clear that the Commission sees an increased role for the EU.

At a high level, the Green Paper remains focused on four main issues. First, the paper raises issues around the **work / retirement balance,** particularly with a view to **adequate pensions** and **sustainable pension structures**. Responses to these challenges are likely to include pressures to enforce national regulatory changes by raising pensionable age or possibly employer contributions, as we have already seen, for instance, in the Greek response to its budget deficit. In theory, this could have a considerable effect on local and regional authorities (LRAs). Increasing the retirement age would affect LRAs, since employer contributions to both first and second pillar schemes would increase and would affect recruitment at the other end. Since the public sector in general has a considerably higher proportion of female employees, it is fair to assume that the impact will be greater for LRAs than for the private sector, for example. It is worth noting, however, that for schemes such as the Local Government Pension Scheme in the UK the impact is expected to be limited, as pension age is already set at 65 (unlike statutory public schemes). From this perspective, other sectors are more likely to be affected than LRAs.

Secondly, harmonisation of local legislation relevant to **cross-border activities** could lead to regulatory changes as well as administrative costs. Since legislative changes may require revised pension products, this may ultimately also have a financial impact on LRAs. Where LRAs play a role in financing supplementary non-mandatory schemes at regional level, this could also increase their financial costs. Similarly, **introducing minimum standards,** e.g. on vesting periods, may have a regulatory impact on pension products offered to employees of LRAs, which may in turn have a financial impact on local government as a bearer of financial risk. Increased standardisation of second pillar pension schemes could in turn impact on the attractiveness of local government as an employer. However, mobility of pension schemes is likely to be more relevant for the private sector than for public sector agencies. The actual impact on LRAs may therefore be limited. Moreover, policy reforms in this area are likely to have a greater impact on the regional economy than on LRAs as employers. From an SME perspective, there is a risk of discouraging rather than encouraging cross-border activity by introducing more legislation to improve transferability of pension rights.

Thirdly, the Commission sees a role for employers in **sharing the risks** of occupational pension schemes, e.g. through a solvency regime. This carries obvious financial implications for LRAs, as it may require the sponsoring undertaking to increase contributions in the case of underfunding. Requirements to tie up funds in solvency capital will ultimately prevent employers from spending such funds on addressing short-term needs and could, for example, prevent recruitment. One would assume that solvency capital requirements for LRAs as employers could lead to a reduced level of service due to lower expenditure budgets. They could also have a clear regulatory impact on LRAs, due in particular to their responsibilities for managing the risks of public pension funds. However, solvency requirements for LRAs should take account of the fact that the public sector generally has a much **longer deficit recovery period** than the private sector. In this sense, LRAs have a sort of ‘institutional permanence', where liabilities would always be passed on to the successor.

Fourthly, alongside developing **default options on participation and investment** choices, ensuring that there are **minimum information disclosure requirements** could have an impact on the pension products offered to LRA employees. At the same time, this would improve the transparency and availability both of additional private schemes for individual employees, and of comparative advantages in LRA benefit packages (as part of pay and reward schemes).

With these impacts in mind, it is worth noting that there is an **obvious lack of attention to the role of SMEs in pension structures**, and consequently to their role in meeting challenges such as an ageing population and fragile pension structures. SMEs could, for instance, play a significant role in allowing longer working lives through more flexible working conditions in self-employment, which would clearly impact on pension contributions. It is quite clear that the Green Paper does not pay enough attention to these issues. Furthermore, there is **limited attention to the gender dimension** in the Green Paper. This is an issue which is particularly important to LRAs, as women dominate many local and regional public sector domains such as healthcare, social work, education and public administration. Moreover, care responsibilities and the lack of quality care for older people place additional pressures on women and often force them into early retirement. Consequently, the EU pension reforms currently under discussion are likely to affect women much more directly than men.

1. Introduction

The publication of the Commission Green Paper on pensions in July this year represents the culmination of recent EU policy developments in the field of pensions. With particular attention having been given to pension reform in view of the ageing EU population, and more recently the financial and economic crisis, pension reform is high on the political agenda. And although many Member States have reformed national pension systems in recent years, the Green Paper makes clear that the Commission sees a more developed role for the EU in meeting those challenges.

By and large, the main focus of this briefing note is on employer contributions to first pillar schemes and second pillar, employer-sponsored occupational pension schemes, along with regional supplementary pension funds for those not covered by mandatory pension funds that are partially or fully funded by public budgets. A distinction is made between first pillar schemes (state pensions) and second pillar schemes such as occupational schemes (which are often mandatory funded schemes), both of which generally benefit from employer contributions.

This briefing note focuses on changes to pension structures as a result of EU intervention, which may affect both employee pension regulations and the financial cost to local and regional authorities, particularly through employer contributions to first and second pillar schemes, and as a result possibly their service delivery. The note also looks at their role in promoting regional and local development, and particularly in support of SMEs.

The purpose of this briefing note is to serve as a background document for an outlook opinion that is to be drafted by the Rapporteur for the Committee of the Regions. It aims to:

- identify the main elements of current pension system reform plans at EU level that may have an impact on local and regional authorities;

- identify the impact of these policy plans on local and regional authorities, with particular attention to LRAs both as public sector employers and as providers of supplementary pension funds for e.g. self-employed individuals; and

- propose policy positions for local and regional authorities in the EU debate.

2. Current EU pension system reform plans

This section follows a three-step approach based on an impact assessment logic. The first subsection summarises the main issues that reform plans aim to address, and is followed by an examination of current EU legislation in the field of pensions and its relevance to LRAs. The final subsection summarises current reform plans with a view to identifying the main areas of impact for LRAs.

2.1 Main issues

The Green Paper on Pensions stresses a number of common challenges addressed across the range of European pension systems and the history of national pension structures.

First, there is a particular need to achieve an appropriate **balance between work and retirement** and, since people today generally live longer, to facilitate a longer active life. This could either mean raising the retirement age or encouraging earlier or more flexible pension contributions. The gender dimension features heavily in this context, since average retirement age for women is generally lower than for men. In Greece, for example, reforming the pensionable age, and more particularly raising women's retirement age from 60 to 65, features prominently in efforts to deal with the public finance crisis.

As noted in the Green Paper, this requires additional efforts to maintain the employability of older workers, e.g. by offering appropriate retraining opportunities and flexible working arrangements. More specifically, this would include increased access to both training and disability adjustments, preferably coupled with financial incentives, e.g. through tax rules.

This interlinks with two other common themes in the field of pensions. The Green Paper points to how ensuring **adequate pension** incomes necessitates sufficient opportunities for complementary entitlements, e.g. by compensatory crediting for periods of unemployment, sickness and caring duties, or increased coverage for vulnerable groups such as those on short-term contracts and atypical workers. At a structural level, this further requires, for example, stimulating labour supply to support the **sustainability of pension structures** (i.e. ensuring an adequate labour force that can support the costs of the pension system) particularly with a view to maintaining long-term financial stability. Achieving higher employment levels among older workers features centrally in this context.

Thirdly, the Green Paper refers to considerable barriers to **cross-border activities**, particularly in relation to occupational retirement provision and the internal market for life assurance products. For example, different local legal definitions represent a particular barrier to cross-border activities. A related issue is the **mobility of pensions across Europe**, in respect of which it is recognised that there is a need to coordinate recent legislative and policy changes in order to improve mobile workers' access to supplementary pension rights within and between Member States. It is the latter issue that is of most relevance to LRAs, whose pension systems may need to be adapted to allow employees or those supported by supplementary pensions through regional initiatives to move within the EU, while maintaining accrued pension rights.

Finally, the Commission calls for safer and more transparent pensions, e.g. through managing the **risks and volatility of private and funded pensions**. This could, for instance, include increased collective risk-sharing through hybrid schemes guaranteeing a minimum return. Similarly, the Commission raises a potential need to ensure a certain level of **pension benefit guarantee** by looking explicitly at insolvency and the protection of workers' rights, in line with protection systems in other financial markets such as bank deposits, investment products and insurance policies. This could also include compensation for excessive losses in Defined Contribution (DC) schemes, which are dependent on external factors such as the cost of purchasing pension income at retirement. For local public pension scheme providers, which are often associated with, but are ideally legally separate from LRAs, this could mean carrying an increased risk for pension provision for employees. For example, in the UK local authorities bear the responsibility for providing adequate pension payouts for their employees, while the funding for this relies on the investment returns of public pension funds.

Under the heading of transparency, the paper also draws attention to **information disclosure requirements**, to ensure comparable information in view of developments showing a general shift from Defined Benefit to Defined Contribution schemes. For LRAs, complicated and widely different information is likely to make the tendering and selection processes costly and possibly less systematic than could be the case.

2.2 Current EU legislation and policies

Since pension policies remain within the national competences of the Member States, the main EU tools include measures such as surveillance, coordination and facilitation of mutual learning, e.g. through the Open Method of Coordination. Moreover, commitments such as the Jobs and Growth Strategy of the Lisbon process and the multilateral budgetary surveillance inherent in the

Stability and Growth Pact (SGP) in the context of fiscal policy have placed considerable emphasis on policy coordination. More recently, Europe 2020 has allowed for greater political focus on integrated policy responses to the challenges identified. However, in accordance with the EU competences laid out in the TEU, attention has remained focused on ‘a framework for policy learning with common objectives conducive to the planning, implementation and assessment of such reforms’[1].

That said, there are a number of directives in place to support common aims, while respecting national competences in the design of pension structures. The following table provides an overview of the legislation currently in place related to pension systems and its relevance to local and regional authorities.

Table 1: Current EU pension-related legislation and relevance to LRAs[2]

EU legislation	Relevance to LRAs
Directive 2003/41/EC on occupational retirement provision (IORP)	LRAs are leading stakeholders in second pillar funded schemes for their employees. The directive requires, for example, legal separation between scheme and LRA, a requirement that has been called into question[3]. LRAs also bear responsibilities to ensure that pension funds are kept in line with requirements set out in the directive.
Directive 98/49/EC on mobility and portability	LRAs are required to provide adequate information on the pension rights and choices available to scheme members when they move to another Member State.
Directive 2009/65/EC on single market for retail funds	Applies to LRAs as ‘collective’ investors in funded schemes, which consequently bear risks e.g. where investor protection is limited.
Directive 2006/54/EC on employment and occupation	Covers all pension schemes, including second pillar public sector schemes. Requires LRAs to ensure equal opportunities and equal treatment of men and women in provision of pension benefits or contributions.

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1 European Commission, EPC / SPC (2010): ‘Interim EPC – SPC Joint report on Pensions, 28.05.2010.

2 With the exception of the internal market rules, the structure of the table is based on the publication European Commission (2010): ‘Commission Staff Working Document, EU legislation, coverage and related initiatives – accompanying document to the Green Paper towards adequate, sustainable and safe European pension systems’, SEC(2010) 830 final.

3 See Unison’s response to UK implementation of the IORP directive (www.unison.org.uk/pensions/governance.asp).

EU legislation	Relevance to LRAs
Internal market rules – e.g. Directive 2006/123/EC on services in the internal market	A recent ECJ ruling concluded that local authorities of a certain size – with more than 2 042 employees in 2006-07 – breached EU rules on free trade in services by not tendering mandates for occupational pension provision[4].
Directive 2002/83/EC on internal market of life insurance, 2009/138/EC on solvency and Directive 73/239/EEC on non-life insurance	Not applicable - these are third pillar issues, and apply to the business of individual additional policies for life assurance, direct insurance and reinsurance.
Directive 2008/94/EC on insolvency	Not applicable – this applies to private sector employers.
Directive 79/7/EEC on equal treatment	Not applicable – covers statutory pensions, which is a first pillar issue, and set out in national legislation.
Directive 2004/113/EC on discrimination in access to and supply of goods and services	Not applicable - this is a third pillar issue that covers private / individual pension products.

2.3 EU reform plans

In view of the new Europe 2020 strategy adopted by the Council in June 2010, there is now a particular demand for policy that builds on 'the many interlinkages between labour markets, social protection systems, financial market policies, and migration policies and develops the synergies necessary to deliver pensions that are adequate and sustainable'[5]. In this context, the strategy highlights the importance of Member States ensuring adequate income support and of the EU supporting Member States in providing evidence on the adequacy

[4] Investments and Pensions Europe, 20.07.10: 'EC ruling forces German Local authorities to tender pension services'.
[5] European Commission, EPC / SPC (2010): 'Interim EPC – SPC Joint report on Pensions', p63

and sustainability of pension systems. Moreover, fiscal consolidation and long-term financial sustainability feature strongly in Europe 2020, e.g. in relation to promoting the internal market for pension products.

The Green Paper on Pensions picks up on issues raised in Europe 2020, and highlights a number of areas for potential EU intervention. The table below provides an overview of the issues identified, the current status of policy developments in each domain, their relevance to LRAs and the specific questions raised by the Commission.

Table 2: Issues identified, current status, relevance to LRAs and specific questions raised by the Commission

Issues identified	Current status[6]	Relevance to LRAs	Questions raised
Balance between work and retirement, pension adequacy and sustainability of pension structures	Europe 2020 follows up on targets set at the Barcelona Council in 2002 to raise average retirement age by five years. With the new strategy, however, there has been a shift away from explicit targets, which is more in line with the subsidiarity principle.	Employer contributions to first and second pillar schemes Costs and benefits of flexible working conditions Contributions to regional supplementary non-mandatory pension schemes (e.g. self-employed)	Should the EU seek to define better what an adequate retirement income might entail?
			How can higher effective retirement ages best be achieved and how could increases in pensionable ages contribute?
			How can the implementation of the Europe 2020 strategy be used to promote longer employment and its benefits to business and to address age discrimination in the labour market?
			Should automatic adjustment mechanisms related to demographic changes be introduced in pension systems in order to balance the time spent in work and in retirement?

[6] European Commission (2010): 'Commission Staff Working Document, EU legislation, coverage and related initiatives – accompanying document to the Green Paper towards adequate, sustainable and safe European pension systems', SEC(2010) 830 final.

Cross border activities and mobility of pensions	Live proposal on minimum standards for the acquisition, preservation and transferability of supplementary pension rights, applying to people moving both within and between EU countries. A revised 2007 version omitted the transferability element and placed emphasis on timely acquisition of pension rights and their subsequent preservation.	Compliance by (legally independent) local public sector occupational pension schemes and regional non-mandatory supplementary funds Compliance by LRAs as employers (e.g. providing employees with information on options)	In which way should the IORP Directive be amended to improve the conditions for cross-border activity? What should be the scope of schemes covered by EU-level action on removing obstacles to mobility? Should the EU look again at the issue of transfers or would minimum standards on acquisition and preservation plus a tracking service for all types of pension rights be a better solution?
Risk management and pension benefit guarantees	With the aim of improving the sustainability of financial institutions (and hence pension providers which may be used by LRAs), the Commission is also looking at amending the IORP directive in order to allow for similar solvency requirements for pensions as for individual insurance products.	Bearers of risk through administration of funds, employer commitment to pension guarantee	What should an equivalent solvency regime for pension funds look like? Should the protection provided by EU legislation in the case of the insolvency of pension-sponsoring employers be enhanced and, if so, how?

Information disclosure requirements	The Commission Communication of 30 April 2009[7] emphasised the need for a horizontal approach to regulation of sales and pre-contractual disclosures of products with a view to effective consumer protection. It is expected that this will be followed by specific legislative proposals in 2011.	Compliance by LRAs in providing options in line with disclosure requirements	Is there a case for modernising the current minimum information disclosure requirements for pension products (e.g. in terms of comparability, standardisation and clarity)? Should the EU develop a common approach for default options about participation and investment choice?
EU governance		Possible reporting requirements to national government	Should the policy coordination framework at EU level be strengthened? If so, which elements need strengthening in order to improve the design and implementation of pension policy through an integrated approach? Could the creation of a platform for monitoring all aspects of pension policy in an integrated manner be part of the way forward?

[7] Communication from the Commission on Packaged Retail Investment Products, 30.4.2009, COM(2009) 204

3. Impact of policy reforms on LRAs

3.1 General considerations

As an initial point, it is worth looking at the types of issue raised in the Green Paper. From a local and regional perspective, there is, for example, an obvious lack of attention to the role of SMEs in providing pension structures for their employees, and consequently their role in meeting challenges such as an ageing population and fragile pension structures. SMEs could, for instance, play a significant role in allowing longer working lives through more flexible working conditions in self-employment, which would clearly impact on pension contributions. It is quite clear that the Green Paper does not pay enough attention to these issues.

Moreover, there is limited attention to the gender dimension in the Green Paper. This is an issue which is particularly important to LRAs, since women dominate many local and regional public sector fields such as healthcare, social work, education and public administration[8]. In the UK, for example, there are twice as many women as men working in the public sector in general, a tendency that has increased in the period 1997-2006[9]. Moreover, as noted by the AGE Platform, the lack of quality care for older people or provision for other care responsibilities places additional pressures on women, often forcing them into early retirement. Consequently, as AGE further highlights in its response to the Green Paper, the EU pension reforms currently being discussed are likely to have a greater effect on women than on men[10].

Greece provides an illustration, where the Civil and Military Pensions Code provides for a considerably lower retirement age for female public sector workers (e.g. 5-10 years less for mothers than for fathers)[11]. A Greek draft bill providing for an increase in the female retirement age to 65 will result in women having to work an estimated 5-17 years longer before retiring. More importantly in this context, since women dominate certain local government sectors, reforms are also likely to have a greater effect on LRAs.

Ebbinghaus applies a useful distinction between the different governance modes of supplementary pensions. Three modes are identified: (1) collectively

[8] Eurostat (2008): 'The Life of Men and Women in Europe – a statistical portrait'.
[9] Millard et al for UK Office for National Statistics (2007): 'Characteristics of Public Sector Workers', Economic & Labour Market Review Vol 1: No 5, May 2007.
[10] Euractiv 04.06.10: 'EU pension proposal will hit women much harder than men' (www.euractiv.com/en/experts-eu-pension-proposal-will-hit-women-much-harder-men-news-494853).
[11] EIRonline 15.03.10: 'Public sector to bring in parallel retirement age for men and women (www.eurofound.europa.eu/eiro/2009/10/articles/gr0910029i.htm).

negotiated occupational pension schemes; (2) voluntary employer-sponsored pension commitments; and (3) individual retirement saving decisions. The first category further highlights the importance of recognising how social partners remain a key stakeholder in the field of pensions, and as such will influence both the policy process and, for example, the feasibility of implementing standards at national and local level.

The EFRP emphasises this point in its response to the 2004 Commission proposal on improving portability of occupational pension rights in the EU, pointing to how 'harmonising occupational pensions benefit design reduces the social partners' negotiation margin for wages, and if relevant, for occupational pensions'[12]. This dimension is, for example, particularly relevant in situations where local authority pension schemes are based on collective agreements, as in Germany, where a recent ECJ ruling has put pressure on the union representing public employees and the association of local authorities to change their collective agreement to include a tendering process for occupational pension provision.

3.2 Work / retirement balance and adequate and sustainable pension structures

Maintaining adequate pensions remains a key challenge, particularly as several countries have implemented pension reforms that make public pension systems less generous[13]. Although this remains within the national competences of the Member States, it is quite clear that the EU is putting considerable pressure on Member States to make appropriate legislative changes, for example to deal with budget deficits, as in the case of Greece. Policy discussions in this area imply national regulatory changes that will ultimately have a considerable impact on LRAs.

The fact that average exit age is generally lower than statutory retirement age in the majority of Member States further aggravates the challenge of an ageing population[14]. The Green Paper looks explicitly at **increasing pensionable age**, or extending active working life in general. This could have major regulatory

[12] EFRP (2004): 'Improving portability of occupational pension rights in the EU – EFRP response', 16.07.2004

[13] European Commission, Economic and Financial Affairs DG: '2009 Ageing Report: Economic and budgetary projections for the EU-27 Member States (2008-2060)', European Economy 2:2009.

[14] European Commission, Economic and Financial Affairs DG: '2009 Ageing Report: Economic and budgetary projections for the EU-27 Member States (2008-2060)': An increase of the employment rates of older workers by 5 percentage points compared to the baseline would reduce the decrease in pension expenditure as a share of GDP by -0.1 p.p. over 2007-2060. In earnings-related systems, there are counteracting effects: a decrease in the number of pensioners (due to the postponement of the retirement age) in the short term and a resulting increase in the average pension in the long term (due to larger accumulated rights) and a reduction in the average number of pension drawing years..

and financial implications for LRAs, in those cases where pensionable age is not already at an acceptable level.

It is particularly interesting in this regard to look at some of the key characteristics of LRA employees or, in the absence of such specific data, of public sector employees more generally. Data from the UK, for example, show that the proportion of public sector workers increases with age, particularly for those over 50[15]. Moreover, cross-European data show that there are considerably more women in the public sector[16]. Consequently, increasing the retirement age will have a clear impact on LRAs in terms of employer contributions to both first and second pillar schemes, and it is fair to assume that the impact will be larger for LRAs than e.g. for the private sector. This could in turn impact on future recruitment.

Evidence has shown that that the likelihood of being restricted in the ability to work as a result of a long-standing health problem or disability increases markedly with age[17]. Extending active working age will put additional pressures on employers to facilitate flexible working arrangements and provide support to employees, including opportunities for retraining and lifelong learning. Women are more likely to suffer from long-term chronic illness or conditions and are more likely to report a work restriction than men[18]. This places additional pressures on LRAs compared to other sectors. On the other hand, women in positions in public administration are more likely to benefit from flexible working conditions than in other economic sectors, and the evidence shows that part-time working also increases with age, and that this is particularly common in the public sector[19]. LRAs seem to have a particularly important role to play in providing flexible employment opportunities.

Flexible working can also be promoted by making regulatory changes to legislation on self-employment. Many countries today place considerable restrictions on the flexibility to combine pension income with self-employment. Local and regional authorities can be seen has having particular responsibilities to promote such opportunities and support entrepreneurship (including social entrepreneurship) among the older generations. Although this would involve certain costs through the use of public services and, where relevant, the provision of opportunities to continue to accrue pension rights through regional

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[15] Millard et al for UK Office for National Statistics (2007): 'Characteristics of Public Sector Workers', Economic & Labour Market Review Vol 1: No 5, May 2007.
[16] Eurostat (2008): 'The Life of Men and Women in Europe – a statistical portrait'.
[17] Applica, CESEP, and Alphametrics (2007), 'Men and women with disabilities in the EU: Statistical analysis of the LFS ad hoc module and the EU-SILC'.
[18] Ibid.
[19] Eurostat (2008): 'The Life of Men and Women in Europe – a statistical portrait'.

non-mandatory supplementary pension schemes, it would at the same time contribute to local and regional economic development.

An important issue is the impact that extended working lives would have on employer expenditure on sickness absenteeism. As research has shown that absenteeism increases with age[20], increasing the retirement age is also likely to increase average absence rates. Moreover, data suggests that absenteeism is more prevalent in the public sector than in the private sector, for example in Finland, the Netherlands and Sweden[21]. With public sector age characteristics in mind, this supports the argument that raising the retirement age is likely to have a higher impact on LRAs than on the private sector. It is worth noting that evidence suggests that these impacts would be more significant in Central and Northern European countries, where sickness absence is comparably higher than in Southern Europe[22].

For individual retirement income to be more adequate could imply **increased employer contributions** in first and / or second pillar schemes. This would have an obvious financial impact on LRAs as employers. In Germany, for example, where nearly 63% of pensioners in the Länder and local authorities are former civil servants[23], increasing employer contributions would have a significant financial impact on regional and local budgets, possibly preventing further employment as resources are reduced. Without an increase in regional budgets for pension-related expenditure, this could impact on service delivery by local and regional authorities, and budgets in other sectors would have to compensate for the increased costs of employer contributions. However, it is worth noting that the UK has introduced a cap on employer contributions, demanding that employees carry the responsibility for increasing their own pension rights.

In this context, public sector employment in general and local government employment in particular seem to have increased in a number of Member States, such as in the UK, where the local government workforce increased by 21.3% between 1998 and 2005[24]. In Poland, research has shown that downsizing employment in the public sector was associated with employment growth in public and state administration in the 1990-2006 period[25].

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[20] See e.g. EWCO 19.05.10: 'Incidence of absenteeism due to illness and accidents'.
[21] Eurofound (2010): 'Absence from work'.
[22] Gimeno et al (2004): 'Distribution of sickness absence in the European Union Countries', Occup Environ Med 2004;61:867–869.
[23] Freibert (2006): 'Public Sector Pensions in Germany', prepared from seminar on 'Social Rights and Pensions for Civil Servants in some EU Member States', Vilnius 2006.
[24] Livesey et al (2006) for UK Office for National Statistics: 'Public sector employment 2006: seasonally adjusted series and recent trends', Labour Market Trends, vol 114, no 12, pp 419-438.
[25] Zawojska (2008): 'Public Versus Private Sector Employment and Remuneration: Objective and Subjective Empirical Evidence from Poland', Socialiniai tyrimai / Social Research. 2008. Nr. 3 (13), 186–196.

It is important to note that LRAs bear different levels of responsibility and costs in different Member States. For example, the federal structure in Germany clearly differs from the centralised model in France, with the German Länder carrying the direct costs of pension schemes for employees along with statutory pension payments for citizens in general[26]. While increasing pensionable age will clearly impact on employer contributions to both first and second pillar pension funds, in Germany these regional and local costs could be directly balanced against reduced expenditure on the number of first pillar pension payments.

In other countries, the link may not be as obvious, and reduced public expenditure as a result of increased working age could more easily be allocated to other areas of expenditure. It is likely that increasing regional and local pension budgets would be more sensitive to political processes than in countries where those budgets are managed at the same administrative level. In such cases, there is consequently a higher risk to LRAs that regulatory changes will lead to budget pressures.

There could also be changes to national regulation on compensatory provisions for gaps in employment. In the context of LRAs, this has a clear gender dimension. Women tend to have more care responsibilities, and as has been noted in Greece, for example, those responsibilities can lead to early retirement[27]. If regulatory changes are made at national level to pension contributions for periods of employment gaps due to e.g. care responsibilities, that could have a clear financial impact on LRAs if employers are to bear the cost of those changes. It is essential that such discussions take cost allocation into account.

Measuring impact on LRAs:

- Demographic changes to LRA labour force
- Calculating increased employer contributions to first and second pillar schemes
- Costs and benefits of flexible working for the target group
- Calculating increased contributions to regional supplementary non-mandatory pension schemes for e.g. self-employed
- Budget reductions in other expenditure areas

[26] Freibert (2006): 'Public Sector Pensions in Germany', prepared from seminar on 'Social Rights and Pensions for Civil Servants in som EU Member States', Vilnius 2006, p2.
[27] Angelaki (2010): 'Reforming the Greek Pension System in the Age of Crisis', Work in Progress, prepared for the Annual ESPAnet Conference "Social policy and the global crisis: consequences and responses", Budapest, 2-4 September 2010.

3.3 Cross-border activities and mobility of pensions

First, the Commission proposes to examine the IORP[28] Directive to improve cross-border activities. Although the directive currently allows pension providers to manage funds for entities established in other Member States, there is a clear awareness of the barriers to full realisation of an internal market for pension schemes, related in particular to fiscal differences between Member States and the transferability of pension rights. Although the amended Commission proposal excluded the transferability element, it is quite clear that this is still recognised as an important aim in order to fully realise the internal market in the field of pensions[29].

CEIOPS noted in its review of the IORP Directive that definitions of 'cross-border activity' and related concepts in local legislation are generally not clear-cut and the understanding of the concept of cross-border activity differs quite significantly, resulting in different notification practices and legal requirements[30]. Harmonisation of local legislation in this area would consequently carry considerable administrative costs. However, as stakeholders have noted, mobility is less frequent among LRA employees than in the private sector, and the impact would consequently be less for LRAs than for the private sector.

From an SME perspective, there is a risk of discouraging rather than encouraging cross-border activity by introducing legislative changes to improve transferability of pension rights. For instance, complying with the notification requirements under Article 11 of the Directive commits institutions to providing detailed information about benefits on cessation of employment and arrangements for transfer of pension rights. As UEAPME emphasised in its 2003 response, this could have 'the opposite effect and discourage employers (...) from offering voluntary pension schemes (...)'[31]. Where LRAs play a role in financing supplementary non-mandatory schemes at regional level, this could increase their financial costs. Where this is the case, one would expect budget reallocations, thus reducing expenditure for other public services.

Linked to these issues, the Green Paper addresses the discussion about ensuring mobility of pensions for EU citizens by setting minimum standards. That could mean minimum standards on vesting periods (the crystallisation of pension

[28] Institutions for Occupational Retirement Provision.
[29] European Commission, DG Employment, Social Affairs and Equal Opportunities - press release: 'Pension proposal on track to improve workers' mobility', P/07/1461 09.10.2007.
[30] CEIOPS (2008): 'Initial review of key aspects of the implementation of the IORP directive', OP-03-08.
[31] UEAPME (2006): 'UEAPME position paper on the proposal for a directive on improving the portability of supplementary pension rights', 02.02.2006.

rights). Even if this complies with the subsidiarity principle, it may still have a regulatory impact on the development of pension products offered to employees of LRAs and a financial impact on local government as a bearer of financial risk. Setting minimum standards may also place requirements on LRAs to ensure compliance through their selection of pension products where this is fully external to the authorities. However, the likelihood of these changes taking place is questionable. The actual impact on LRAs would therefore probably be limited.

At a more systemic level, this may impact on the comparative attractiveness of local and regional public sector pension schemes offered by LRAs. In the UK system, for example, where favourable supplementary pension rights are often seen as compensating for lower public sector wages, increased standardisation of second pillar pension schemes could in turn impact on the attractiveness of local government as an employer.

Finally, the Green Paper raises the question of what the scope should be of schemes covered by EU-level action on removing obstacles to mobility. From a regional perspective, the fact that regional supplementary funds for people not covered by mandatory supplementary schemes are not consistently applied in the EU raises a particular challenge.

Measuring impact on LRAs:

- Regulatory changes as a result of a revised IORP directive
- Changes to pension products and their financial impact
- Existence of voluntary pension schemes offered by employers at regional level and possible increases in LRA contributions to non-mandatory supplementary schemes
- Comparative attractiveness of the full remuneration package (incl. pensions) of LRAs

3.4 Risk management and pension benefit guarantees

First, it is essential to recognise that not only LRAs but the public sector in general play very different roles in pension structures across Europe. For example, in the UK, second pillar employer contribution (defined contribution) schemes are much more common than in other European countries. As the state pension scheme is 'considerably less generous'[32], the UK system is more vulnerable to market fluctuation than to an ageing population. The funded local government pension schemes depend on investment returns, while local authorities carry the ultimate responsibility for providing pensions to employees. In France, on the other hand, pay-as-you-go public sector schemes form part of the first pillar of unfunded state pensions, while second pillar occupational schemes are considerably less common[33]. Consequently, pension funds are more exposed to demographic challenges than to market fluctuations, and LRAs play a less prominent role in managing these risks.

In a 2005 study, the OECD looked explicitly at risks for the public sector with regard to pension funds[34]. For instance, the study pointed to a public sector investment mismanagement risk (which would include LRAs), where authorities are 'often required to, directly or indirectly, finance infrastructure, social projects or allocate resources on investments not necessarily linked to retirement income objectives'. Moreover, the study pointed to how governments can influence pension funds' investment policies to achieve specific capital market and financial goals. At the same time, the study points to the fact that it is taxpayers who ultimately bear the burden of unfunded liabilities with public sector pension contributions.

As such, one can assume that a solvency regime for pension funds would directly affect LRAs by stipulating how those risks should be managed. It could also change the relationship between LRAs and supervisory institutions in Member States, as the latter may have an increased role to play. As several studies have identified a shift from public to private pensions through statutorily-funded, privately-managed schemes, it seems to be relevant to discuss more directly what role public pension funds should play in ensuring financial stability in their relationship with private schemes. However, as noted by stakeholders consulted for this paper, there is an important distinction between the private and public sector in this context, which would influence the solvency risks of public pension funds. LRAs have what has been referred to as 'institutional permanence', where liabilities will always be transferred to a successor. The deficit recovery period is thus much longer for the public sector.

On the assumption that EU policy reforms would imply increased risk-sharing between stakeholders, including LRAs as employers, it is likely that changes will have a financial impact on LRAs. Requirements to tie up funds in solvency

[32] Mayhew (2001): 'A Comparative Analysis of the UK Pension System Including the Views of Ten Pension Experts', p2.
[33] Stakeholder consultation.
[34] Pinheiro, Vinicius for OECD Directorate for Financial and Enterprise Affairs: 'Pension funds for government workers in OECD countries', Financial Market Trends No. 89, November 2005.

capital will ultimately prevent employers from spending those funds on addressing short-term needs and could, for example, prevent recruitment. As such, one could assume that solvency capital requirements for LRAs as employers could lead to reduced service delivery due to lower expenditure budgets.

It is worth noting that there is a lack of systematic assessment of the risks borne by sponsors[35], which is of direct relevance to LRAs. A literature review undertaken for this briefing report has also uncovered a lack of data on the risks borne by employers in this regard. As such, one could argue that introducing risk management measures at European level should account for different types and levels of risk for different stakeholders, including local and regional authorities.

Measuring impact on LRAs:

- Financial impact of solvency requirements (e.g. increased contributions due to underfunding)
- Regulatory changes to risk management approach
- Budget reallocation due to financial impact and changes in service delivery due to budget reallocation, financial impact on the taxpayer

3.5 Information disclosure requirements

Although EU standards on minimum information disclosure requirements for pension products will first and foremost have a direct impact on local public sector pension funds and not LRAs directly, LRAs bear responsibilities in this respect to ensure that the information disclosed meets the relevant requirements.

It is important to recognise that there are considerable differences in the role that LRAs or associated (but legally separate) public entities play in pension provision. In Finland, for example, the Local Government Pensions Institution is responsible for providing and financing employment pensions for local government employees, whereas in Sweden *Pensionsvalet* handles the administration of the choice of pension provider, while the employees themselves are responsible for choosing the insurance company that will actually provide the pension.

[35] European Commission, Internal Market and Services DG: 'Consultation on the Harmonisation of Solvency Rules Applicable to Institutions for Occupational Retirement Provisions (IORPs) covered by Article 17 of the IORP directive and IORPs operating on a cross-country basis', Ares (08) 14767 (2008).

Together with developing default options on participation and investment choices, ensuring minimum information disclosure requirements could have an impact on the pension products offered to LRA employees. At the same time, this would improve the transparency and availability both of additional private schemes for individual employees, and of the comparative advantages of LRA benefit packages (as part of pay and reward schemes). As pension benefits could be considered a comparative advantage of LRA employment as compared to private sector employment, this could in turn improve the attractiveness of LRAs as employers. However, if LRA pension schemes are not competitive enough, this could ultimately reduce the attractiveness of LRAs as employers.

Measuring impact on LRAs:

- Impact on pension products offered to employees
- Financial impact of changes to pension products
- Impact on attractiveness of the full remuneration package (incl. pensions) of LRAs compared to e.g. private sector

3.6 Improving EU governance structures

An important feature of the discussions around improving policy coordination at EU level is often the focus on improving the availability of monitoring data. It is fairly safe to assume that detailed LRA reporting requirements are unlikely to be implemented, including in the field of pensions. However, there is a chance that initiatives aimed at improving EU governance structures will lead to pressures to improve data availability and comparability, with some of those responsibilities possibly being left to LRAs. That would of course imply certain administrative costs, but at the same time LRAs could benefit from access to comparative data for their own policy decisions. In this context, it seems imperative to highlight the role that CEIOPS could play. As noted in its response to the Green Paper, CEIOPS is already contributing with direct evidence and findings on financial stability matters related to the occupational pensions sector and also stands ready to assist further on these matters[36].

Measuring impact on LRAs:

- Regulatory changes to monitoring requirements
- Administrative burden of complying with monitoring requirements

[36] CEIOPS (2010): 'CEIOPS welcomes the European Commission Green Paper on Pensions', 02.08.2010.

4. Recommendations for LRA policy positions

There is an **obvious lack of attention to the role of SMEs in pension structures**, and consequently to their role in meeting challenges such as an ageing population and fragile pension structures. SMEs could, for instance, play a significant role in allowing longer working lives through more flexible working conditions in self-employment, which would clearly impact on pension contributions. It is quite clear that the Green Paper does not pay enough attention to these issues.

There is also **limited attention to the gender dimension** in the Green Paper. This is an issue which is particularly important to LRAs, as women dominate many local and regional public sector fields such as healthcare, social work, education and public administration. Moreover, the lack of e.g. quality care for older people places additional pressures or other care responsibilities on women, often forcing them into early retirement. Consequently, the EU pension reforms currently being discussed are likely to affect women much more than men.

It is imperative to look at the **full picture of pension provision** and allow for the fact that many people may be recipients of several types of pension. In clarifying the role and responsibilities of LRAs to contribute to adequate pensions for employees and possibly those outside the scope of mandatory supplementary schemes, the overall balance should be considered. More importantly, under the heading of creating transparency, increasing comparability through standardisation would allow individual beneficiaries to make informed decisions.

Vastly different pension systems present a particular challenge to the feasibility of some of the European measures under discussion, particularly related to issues like standardisation and portability. Addressing these issues as barriers to the internal market seems to be an important aim for the Commission. However, this would require considerable regulatory changes to national legislation on pension rights and could ultimately be counterproductive for local and regional economies by discouraging employers from offering voluntary pension schemes to employees.

In the context of improving the basis for decisions by individuals, there should also be a discussion on what role LRAs should play in the **financial education of the public**. Frontline services across the public sector could play a role here in helping people make informed decisions about their future pensions.

There is a lack of **systematic assessment of the risks borne by sponsors**. Introducing risk management measures at European level should account for the different types and levels of risks involved, including those assumed by local and regional authorities.

Solvency requirements for LRAs should account for the fact that the public sector has in general a much **longer deficit recovery period** than the private sector. In this sense, LRAs have a sort of ‘institutional permanence’, where liabilities would always be passed on to the successor.

5. Literature

Methodology for the identifying the literature

This briefing paper is by and large based on review of policy and academic literature on EU pension system reform and local and regional authorities. In addition to a literature review, the note is also based on informal discussions with a limited number of stakeholders, such as representatives of the European Association of Public Sector Institutions.

The literature review attempted to identify relevant material through a multi-step approach. The first step was to review relevant policy publications on pensions with particular attention to the role of LRAs, which included resources available through the Commission. A first scoping phase set the parameters of the review, mapping the relevant issues and current legislation in place relevant for the topic.

The second step looked explicitly at both policy and academic literature in order to explore the existing evidence base in mapping possible impacts on local and regional authorities of identified policy changes. This included keyword-based searches across a series of relevant web sites and in a number of academic databases.

The search of the literature was based on the use of a range of keywords that focused on the role of local and regional authorities in pension provision, in conjunction with reference to the identified issues addressed in the Green Paper (e.g. work / retirement balance, pension adequacy, sustainability of pension structures, cross-border activities and mobility of pensions and information disclosure requirements). Particular attention was paid to identifying any baseline data on labour force characteristics.

As anticipated, these searches were generally disappointing in their results. Dialogue with relevant stakeholders, such as the ASISP network (Analytical Support on the Socio-Economic Impact of Social Protection Reforms), confirmed this finding. Consequently, emphasis was placed on reviewing policy documents available from Commission web sites, supplemented by searches of web sites of European think tanks, local and regional representative associations and business organisations.

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