



# EURO PENSION BULLETIN

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## EDITORIAL

“Free collective bargaining – a danger for the single market?” – is the title of an abstract on the infringement procedure instituted by the Commission against the Federal Republic of Germany. The subject of the procedure is a collective agreement in the public sector pertaining to a deferred compensation. The agreement stipulates that the salary foregone facility must be taken up either with a public sector supplementary pension institution, or with companies belonging to the savings bank financial group or local government insurers. The European Commission considers that local government authorities and their establishments are not entitled to enter into service contracts on occupational pensions with institutions referred to directly in the collective agreement, and that a Europe-wide call for tenders should have been organised beforehand. Given that the German government does not share this view, the Commission has instituted an infringement procedure before the European Court of Justice.

Although this matter, that concerns only 100,000 contracts for the whole of Germany, does not fall within the scope of the general interest, it draws attention to an essential point of conflict in Europe, namely the issue of whether priority is given to a Europe of free competition or to a social Europe. Whilst there is no doubt that opening markets has contributed to prosperity within the European Union, the success of collective agreements in terms of occupational pensions, in order to ensure that the standard of living of employees is maintained after they retire, is equally undeniable. In view of the cuts implemented by most states with respect to the first pillar, it is to be expected that the significance of occupational pensions will continue to increase in the years to come.

Hagen Hügelschäffer  
Original language: French

## Joint Conference of EAPSPI and AEIP on portability of occupational pensions

EAPSPI and AEIP (European Association of Paritarian Institutions of Social Protection) organised a joint conference on April 18, 2007 in Brussels, on the topic: “Portability of Occupational Pension Rights – a threat or an instrument to promote mobility?” For the organisers, the key issue of the Conference was not so much the political aspect of the steps to be taken within the October 2005 Draft Directive of the European Commission on the portability of occupational pension rights, as a focus on exchanging views on “A technical approach to portability and experiences at European level”, hence the subtitle of the event.

The purpose of the event was to identify the major challenges linked to cross-border portability of occupational pensions within the European Union and to highlight existing experiences. In his opening address, Hagen Hügelschäffer, the Secretary General of the EAPSPI, started the Conference with the following words: “Portability of occupational pension rights is a very complex issue, in particular in cross-border cases. The Draft European Directive on portability can at least be credited with highlighting that within Europe, there are different concepts of the term portability”. Financing methods and tax legislation also differ from one Member State to another, which complicates the introduction of standard rules at European level.

In his welcome address, Gerd Andres, Secretary of State at the German Ministry of Labour and Social Affairs, emphasised that the theme is a very current

issue: "You could not have chosen a better time for your Conference. Germany started its EU Presidency with the objective of achieving agreement on the Directive within the Council by the end of May." Whilst acknowledging that this was a rather ambitious target, he emphasised that "it is only with ambitious aims that you achieve a result at the end of the day". The Secretary of State added that "in principle, Germany is in favour of the idea of portability of occupational pension rights. We share the view of the Commission that we need to improve the rights of workers with respect to free movement and professional mobility. We therefore entirely reformed the portability of occupational pension rights at national level in Germany at the beginning of 2005, including the related tax regulations." He then pointed out that such reforms always involve a risk of increasing the cost of occupational pensions for employers, who may choose to withdraw from their occupational pension commitments. He therefore stated that he was in favour of removing portability in the restrictive sense of the term, a compromise put forward by the Finnish Presidency in its modified Directive proposal.



Georg Fischer, from the Directorate-General for Employment, Social Affairs and Equal Opportunities expressed a different view, regretting that transferability would no longer be the subject of the future Directive, given that "the portability directive was intended to reduce the obstacles to free movement within the EU. The remaining measures, namely conditions for the accrual and preservation of dormant pension rights, are still adequate tools to achieve flexibility of labour markets."

We know that no agreement has been reached concerning the draft directive in the meantime. The Netherlands vetoed the proposal, deemed to be too "watered-down". They criticised the many excep-

tions and are, moreover, concerned that the current directive text may create legal uncertainties that will need to be clarified by the European Court of Justice. Vladimír Špidla, the competent Commissioner, has already announced that he will be presenting a revised draft directive.

During the conference, Professor Yves Jorens from the University of Ghent presented a study conducted in the construction trade, traditionally characterised by the presence of very mobile workers. At the request of the social partners of the construction sector, and with the support of AEIP, he analysed the impact of the portability directive on this sector. He reached the conclusion that most of the existing occupational pension schemes in this sector are already in line with the draft directive, but came out in favour of exceptions for social partners.

EAPSPI presented its portability report, explaining the practical consequences of cross-border transfers of occupational pensions, by means of an in-depth legal and actuarial analysis. The study of different transfer situations showed that this transfer of rights does not always have positive results for the migrant worker, given that all occupational pension schemes are based on different parameters, regarding, for example, indexation or mortality tables. It is therefore crucial that the migrant worker benefit from adequate information to decide whether he wishes to transfer his occupational pension rights or whether he prefers to maintain them in his previous scheme.

With respect to the transfer of occupational pensions, tax legislation plays a significant role, which is why EAPSPI presented another study entitled: "Fiscal Rules and Portability: have all tax obstacles been removed?" The study shows that most of the member States have not yet made a final decision on the issue of whether cross-border transfers should benefit from the same treatment, fiscally speaking, as transfers within the country. There is a great deal of confusion, in particular in countries where portability has been introduced only recently and where there is no long-standing experience in this field. It is likely that the European Court of Justice, that has already contributed to increasingly harmonised tax legislation by means of its recent case law, will continue to do so in coming years.

The Conference also organised a round table discussion, during which participants actively debated the issue of portability in practice, and reported on experiences in Germany, the Netherlands, Italy and Ireland. Speaker contributions and the press file are

available on the internet at [www.eapspi.eu](http://www.eapspi.eu) in the "current issues" section.

Eva Kiwit  
Original language: German

## Social Security Fund

The apparently generous nature of the Spanish public Pension system and the negative demographic forecasts were at the origin of an extensive reflection on the future of public pensions. As a result, through the so-called Toledo Pact in 1995, the Spanish parliament agreed for the first time that it would "maintain the Social Security System and undertake the necessary reforms to make this commitment a reality".

The agreement included 15 recommendations. The first recommendation referred to the separation and clarification of the social welfare system's financing accounts, as part of a gradual process to be completed by the year 2000 and with the purpose of the contributory payments being financed by social contributions, and the non-contributory payments being financed by State contributions, dispensing with the previous situation whereby the Social Security payments financed part of the Public Health System.

The second recommendation involved the creation of a Reserve Fund. On clarifying the sources of its financing, the contributory system was to present a balanced budget and tend towards creating reserves whose role could be anti-cyclical.

There were various legal references to the Reserve Fund from 1995, but it was regulated by the Law of 29 September 2003, when the fund contained contributions of 5,979 million euros, corresponding to the years 2000, 2001 and 2002.

The law stated that the fund was to be endowed with the budget surplus from the operations that finance the contributory payments.

Returns would automatically be paid into the fund.

The fund's withdrawals would be earmarked for financing contributory pensions and other expenses necessary for its management in structural deficit situations arising due to non-financial operations of the Social Security system.

Both the contributions and the withdrawals were to be agreed on by the Council of Ministers.

The following bodies were created for its management:

- Fund Management Committee,
- Investment Advisory Commission,
- Monitoring Commission.

This last commission was participated in by trade unions and business organisations.

In accordance with Article 5, the investments have to be made in securities issued by public legal entities with optimum credit quality, issued in Euros and exchange-traded.

The Fund's accounts are the property of the General Social Security Treasury.

The significant growth of the Spanish economy has favoured the endowment of the reserve fund, up to a total amount of 32,740 million euros at the close of 2006 which, added to the returns of 3,140 million euros, yields a total of 35,880 million euros. 55.12% of this amount is invested in Spanish public assets and the remaining 47,88% in other European countries, therefrom

- 38.65% in the Public Debt of Germany,
- 37.09% in the Public Debt of France,
- 24.26% in the Public Debt of the Netherlands.

A significant increase in external investment was observed in the year 2006. The annualised profitability obtained was 4.21%.

In 2007, including the contribution agreed on 12 July of 4,300 million euros, the Fund attained the figure of 45,046 million euros, some 5% of the Spanish GDP and representing 8 months of pension payment.

Backed by the unions and business organisations, the Government has presented a preliminary draft law dated 12 July 2007 for Regulating the Social Security Reserve Fund, and intends it to be passed by the end of the year. The government considers that the increase in endowments and the likelihood of this trend continuing will mean certain amendments will need to be made to the Fund's present regulation, with a view to greater efficiency in its compliance with its ends.

The significant amendments regard the investment policy, which must conform to the principles of Security, Profitability, Risk Diversification, adaptation to the Fund's time frame and social, financial and environmental Responsibility in investment selection.

As regards suitable assets for the current situation, it allows investment to be made in all types of assets: shares, fixed interest, derivatives, collective investment institutions and others, without excluding any issuer, providing the assets are exchange-traded and comply with certain liquidity requirements.

To guarantee the principles of Security and diversification by law, the government will establish maximum share investment limits, Fixed Interest, assets issued in currencies other than euros and in derivatives. The maximum percentage of voting rights corresponding to the Social Security fund with respect to the total voting rights of one single issuer will be established.

Part of the Fund's management may be externalised, with the maximum externalisable percentage subsequently being fixed.

The decree also refers to aspects such as the Fund's management and organisation. It prevents access to the fund for management costs, and it eliminates the classification as Structural as regards deficits.

While the preliminary project was being drawn up, the political parties harshly criticised the possibility of the Fund's management being partly externalised and the investment in Equity.

José Carlos Garay

Original language: English

## Almost There! – Reforms and Changes to Pension Schemes Completed

After four years of public service pension review, we are almost in sight of the finishing tape.

Reforms to our Schemes for Police, Fire and Teachers are already in place and now we have reached an important stage in the reforms for National Health Service staff and Local Government staff.

### National Health Service

By the time this article is published (barring accidents anyway) we will have finalised the changes to pension arrangements. Basically the existing Scheme, with some adjustments, will remain for current staff, and with a pension age of 60. For new staff a new Scheme will commence on 1 April 2008 but with a pension age of 65. The new Scheme will have improvements to the pension package. Members in the existing Scheme will get the option to switch, without penalty, in 2009. Both the existing scheme and the new scheme will remain as defined benefit, final salary arrangements.

A summary of the main comparisons between what we have now and the reformed arrangements is shown below:

	Existing NHS Pension Scheme	Improvements to the existing Scheme (closed to new entrants from 1 April 2008)		NHS Pension scheme for new entrants (from 1 April 2008)	
<b>Normal pension age</b>	▪ 60 (or 55 for special classes)	▪ 60 (or 55 for special classes)		▪ 65	
<b>Minimum pension age</b>	▪ 50	▪ 50		▪ 55	
<b>Contribution rate on pay</b>	5% and 6%	up to £ 19,165	5%	up to £19,165	5%
		£ 19,166 - £ 63,416	6.5%	£ 19,166 - £ 63,416	6.5%
		£ 63,417- £ 99,999	7.5%	£ 63,417- £ 99,999	7.5%
		£ 100,000 plus	8.5%	£ 100,000 plus	8.5%
<b>Membership limits</b>	▪ From age 16 to 70 ▪ 40 years at age 60 and 45 years overall	▪ From age 16 to 75 ▪ Limit of 45 years service		▪ From age 16 to 75 ▪ Limit of 45 years service	
<b>Accrual rate (the way you earn your pension)</b>	▪ 1/80 <sup>th</sup> final salary scheme ▪ Career Average Re-valued Earnings Scheme for practitioners (CARE) accrual rate of 1.4%	▪ 1/80 <sup>th</sup> final salary scheme ▪ CARE for practitioners accrual rate of 1.4%		▪ 1/60 <sup>th</sup> final salary scheme ▪ CARE for practitioners, accrual rate of 1.87%	
<b>Retirement Lump sum (x means multiplied by)</b>	▪ Fixed tax- free lump sum of 3/80ths x service x pensionable pay ▪ Fixed tax- free lump sum of 3 x pension for practitioners	▪ Automatic tax free lump sum of 3/80ths x service x pensionable pay (or 4.2%) plus the ability to give up part of pension for an increased tax free lump sum up to 25% of pension value		▪ Total flexibility to give up part of pension for a tax free lump of up to 25% of pension value or keep all as pension	
<b>Flexible retirement</b>	▪ No pensionable re-employment except ill-health and return to the NHS under age 50 ▪ Pension payable on retirement only	▪ <b>Step down</b> - pension protection where pay is reduced on taking a less demanding job; ▪ No pensionable re-employment except ill-health and return to the NHS under age 50 ▪ Pension payable on retirement only		▪ <b>Step down</b> - pension protection where pay is reduced on taking a less demanding job; ▪ <b>Draw down</b> – taking part of pension whilst continuing in employment ▪ <b>Pensionable re-employment</b> return to work after retirement and re-join the scheme	
<b>Late Retirement Factors</b>	▪ no enhancement where pension taken later than NPA60	▪ no enhancement where pension taken later than NPA 60		▪ enhancement to pension if taken later than NPA 65	
<b>Increased pension saving opportunities</b>	▪ Purchase of Added Years ▪ Money Purchase Added Voluntary Contributions (MPAVCs)	▪ Members (or employers on their behalf) can buy additional annual pension of up to £ 5,000 a year		▪ Members (or employers on their behalf) can buy additional annual pension of up to £5,000 a year	
<b>Survivor Benefits</b>	▪ Partners lose pension on re-marriage ▪ For legal spouse only and for same sex registered civil partnerships from 2006 (backdated until 1988)	▪ All qualifying partners eligible for pension backdated to 1988 ▪ All qualifying partners keep survivor pension even when re-marry or co-habit		▪ All partners eligible for all service ▪ All partners keep survivor pension even when re-marry or co-habit	
<b>Death in Service</b>	▪ Death in service lump sum twice annual pensionable pay	▪ Death in service lump sum twice annual pensionable pay		▪ Death in service lump sum twice annual pensionable pay	

### Local Government Pension Scheme

Following a review of the Scheme by employers, unions and Scottish Government, agreement has

now been reached on a set of proposals to put to members. The consultation is now underway. The changes are scheduled to be implemented in 2009 and a summary is detailed below:

Scheme Feature	Existing LGPS(S) as of 6 October 2006	New LGPS(S) Proposals by 1 April 2009
Type of scheme	Defined benefit final salary scheme, with a normal retirement age of 65.	Defined benefit final salary scheme, with a normal retirement age of 65.
Accrual rates	1/80 <sup>th</sup> plus lump sum (3/80 <sup>ths</sup> )	1/60 <sup>th</sup> with option to commute up to 25% of fund value into lump sum.
Death in service arrangements	A lump sum death grant of 2 times final pay.	A lump sum death grant of 3 times final pay.
Partner pensions	Dependants benefits payable in respect of widows, widowers and civil partners at a rate of 1/160 <sup>th</sup>	Dependants' benefits payable in respect of widows, widowers, civil partners, plus unmarried partners who cohabit, at rate of 1/160 <sup>th</sup>
Flexible arrangements in the run-up to retirement	From age 50 with consent, member can reduce hours or move to a lower grade and, with consent, elect to draw the pension benefits already built up whilst still drawing salary for reduced hours/grade.  Members can continue paying into the scheme to build up further benefits in the scheme. No limit on the amount of contributions, however tax relief only given on contributions up to 100% of taxable earnings.	Current provisions for flexible retirement to be retained as feature of the new Scottish LGPS.  Increased flexibility through being able to draw all or part of occupational pension benefits without having to retire completely, a provision to buy additional pension benefit, and cost-neutral uplift factors for benefits accrued beyond age 65 at no cost to the employer.  In case of flexible retirement, employer consent required to reduce hours or lower grade, but employer consent to access benefits only required in respect of those under age 60.
Minimum Pension Age (MPA)	In line with the Finance Act 2004, the MPA will change from 50 to 55 years on 6/4/2010.	All new members to have MPA of 55 years. All current members will have MPA of 55 from 6/4/2010.
Contribution rates for scheme members	General contribution rate of 6% except some existing manual employees (5%).	An increase in the employee contribution rate to an average of 6.3%.  Employee contribution rate set at tiered variable rates, linked to basic salary. Potential options outlined, including a range of bands and contribution rates.
Contribution rates for employers	Employer rate varies as determined by 3-year actuarial valuations.	Contributions rates for employers and scheme members to move towards a 2:1 ratio to ensure new scheme affordable.  Overall average new scheme costs estimated at 19.6%, with employee contributions at average of 6.3%. Employer contributions to make up the difference.  Commitment to principle of cost sharing to ensure continuity of scheme over the long term.

The year 2009 will therefore bring to an end six years of pension reform and change. A very difficult time for everyone. Hopefully things will settle down for a while but who knows?

Ian M. Clapperton  
Original language: English

## Belgium – New system of Wage Related Indexation

### Concept of wage related indexation

In addition to indexation of pensions to the Consumer Price Index, some pension schemes make provision for mechanisms intended to guarantee purchasing power by indexation of pensions to the salaries of active members.

In the Belgian public service, wage related indexation is defined as the mechanism linking current pensions to changes in remunerations of active members.

### System used prior to 1 January 2007

Before 1 January 2007, wage related indexation of pensions paid to members who retired at a specific grade was triggered when an increase in the maximum of the salary scale linked to that grade occurred.

Wage related indexation was undertaken by multiplying the new maximum of the salary scale by the wage related indexation coefficient which had been set at the time the member retired. This coefficient was the ratio of, on the one hand, the nominal rate of the pension at the time the member retired, to, on the other hand, the maximum of the salary scale of the last grade held by the member at that time.

Wage related indexation did not constitute, so to speak, an “individual right” but rather a “category right”, as the increase of the individual pension of a member who held a certain grade upon retirement was linked to the salaries of the “category” including active members holding that grade. Wage related indexation was automatically implemented without the member having to apply and was immediate, meaning that it came into effect on the date the salaries of active members increased.

### Shortcomings of the system prior to 1 January 2007

In practice, a wage related indexation was only implemented when the new maximum of the salary scale was automatically applied to active members holding the same grade, and if it could be assumed that the pensioner would have benefited from this advantage had he still been active.

To avoid wage related indexation from having a budgetary impact, various systems had been devised, in particular setting entirely formal conditions (for instance attending a conference), introducing quotas, creating salary supplements, etc.. These created substantial inequalities as some pensioners received substantial wage related indexations while others received nothing. This led to a breakdown in the solidarity which existed between pensioners and could ultimately have led to gradual impoverishment of some pensioners.

Due to the obligation to keep track of changes in multiple and different salary scales, in particular after the reform of the State, the operational management of the system became extremely difficult for public pension management organizations. In addition, it became so complicated that it was no longer transparent for the pensioner who was experiencing tremendous difficulties in knowing whether he was going to benefit from a wage related indexation or not.

### New system in force since 1 January 2007

The new system aims at preventing the implementation of mechanisms devised to avoid wage related indexation and therefore promotes more solidarity.

Wage related indexation remains an “automatic linkage of pensions to salary increases of active members”. Contrary to the adaptation of welfare applicable to pensions of salaried workers, wage related indexation is not subject to a decision by the Minister of Pensions.

The new system is clearer and more transparent as wage related indexation is implemented at a fixed frequency of every two years.

The “immediate implementation” feature which existed in the previous system is attenuated as

wage related indexation is only implemented every second year. This “delayed effect” has been accepted by the trade unions and has permitted budgetary savings for the years 2007 and 2008.

#### **Wage related indexation by category**

The legislation makes provision for a new system whereby wage related indexation is no longer linked to the individual grade of the member but is implemented by “categories”. The different categories, 15 in all, are linked to different sectors of the public service.

All retirement and survivor pensions are linked to a specific category and all the pensions of the same category benefit from wage related indexation by the same percentage every second year. A pensioner can therefore benefit from wage related indexation even when the maximum of the salary scale linked to the grade he held when he retired has not changed.

Every retirement and survivor pension is linked to a specific wage related indexation category.

Retirement pensions are linked to the wage related indexation category applicable to the sector in which the member ended his / her career;

Survivor pensions are linked to the wage related indexation category applicable to the sector in which the scheme member ended his / her career.

#### **Determination of categories**

Each category is constituted on the basis of retirement pensions which started during the 4 years prior to the reference period, the beneficiaries of which ended their careers in the sector concerned in the same time period. The reference category therefore consists of pensioners and no longer of active members.

Only the most representative salary scales are taken into account, that is to say those for which a minimum number of pensions has been granted.

#### **Date of wage related indexation – reference period**

Wage related indexation takes place at the end of each “two year reference period”. The first wage related indexation according to the new system will take place on 1 January 2009 and will be based on the changes in remunerations in each category during the first reference period, i.e. from 1 January 2007 to 31 December 2008, inclusive. An increase in salary granted in January 2009 will be taken into account for the wage related indexation which will take effect on 1 January 2011.

#### **Wage related indexation amount**

The nominal rate which must be taken into account for the wage related indexation is the nominal rate in force on the last day of the reference period, regardless of the date of onset of the pension.

The wage related indexation percentage of the category is equal to the percentage increase in the global remuneration at the end of the reference period, compared to the global remuneration on 31 December of the year preceding the reference period. This percentage is calculated to the fourth decimal.

#### **Global remuneration**

The “global remuneration” is calculated, for each category, at the beginning and the end of each reference period.

The percentage increase of the category is calculated on the basis of the increases in the global remuneration, which occurred during the reference period, linked to the most representative retirement pensions (only) of the category which started during the four years preceding the reference period.

Global remuneration includes the following:

- the maximum of the salary scale linked to the last grade of the pension recipient,
- the holiday allowance and the end-of-year allowance corresponding to the maximum of the salary scale linked to the last grade of the pension recipient,

- salary supplements taken into account for calculation of the pension,
- some salary supplements not taken into account for calculation of the pension but which will be included in a list fixed by royal decree.

### Annual instalments

If the wage related indexation for a specific sector exceeds 5 percent, the King may grant the wage related indexation in successive annual instalments of a maximum of 5 percent each. This postpones to some extent the full impact of exceptionally high wage related indexations. This arrangement already existed in the previous system. It will be significantly less often used in the future.

### Financial status applicable to the calculation of new pensions

As a result of the new wage related indexation system, the method of calculating new pensions which started after 31 December 31 had to be adapted, specifically in order to avoid situations where the amount of a survivor pension could be higher than the amount of the retirement pension granted.

Philippe Nys

Original language: French

### Free collective bargaining: A danger for the Single Market?

Occupational pensions are governed by collective agreements in many of the Member States of the European Union. This is specifically the case in Germany. At the end of June, the Commission of the European Communities decided to initiate an infringement procedure against Germany before the European Court of Justice (ECJ), with respect to a public sector collective agreement on deferred compensation. According to the Commission, this collective agreement constitutes an infringement of the European Law governing the award of contracts.

### History: Reform of pension schemes and supplementary pensions in Germany

As in other European states, Germany has in recent years implemented measures to render pensions durable and financially sustainable in the long term. To that effect, the "Law on the reform of the statutory pension scheme and the promotion of funded retirement pensions" was passed by parliament in May 2001 and came into effect in January 2002. This law makes it possible to compensate for the predictable decrease in benefits of the statutory scheme (first pillar) by giving each citizen the possibility to augment his/her own pension, with State aid. Concomitantly, the state encourages, in a targeted manner, by direct subsidies and tax allowances,<sup>1</sup> the establishment of funded supplementary pensions.

Almost concurrently with the reform of the statutory pension scheme, the social partners of the public sector redefined the basis of occupational, supplementary pensions for the public sector. The details of the rights to benefits and the principles of financing are governed by two identical collective agreements, one of which applies to the Federal State and the Länder (German regions), and the other to local government. The key point of this restructuring is the winding up of the former top up scheme and the creation of a points system aimed at ensuring transition to a funded scheme. Collective agreements give employees the possibility to increase their old age benefits through own contributions within the scope of a voluntary insurance.<sup>2</sup> To encourage this increased contribution, employees may benefit from State subsidies provided for by the law of May 2001 ("Riester Pension") or from old age insurance linked to a fund if their supplementary pension scheme offers such a product. In addition, local government employees can benefit from deferred compensation<sup>3</sup> negotiated as part of a collective agreement of 2003. Since last year, an identical collective agreement has been negotiated at Länder level.

The collective agreement concerning the deferred compensation constitutes the stumbling block for the Commission. It makes provision for a deferred

<sup>1</sup> More details can be found in the contribution of Hügelschäffer, Reform of the general scheme of pension insurance, in EPB 10, August 2001, page 1 et seq.

<sup>2</sup> Cf. Hügelschäffer, The new public service supplementary pension, in EPB 12, April 2002, page 1 et seq.

<sup>3</sup> Collective agreement relating to deferred compensation for local government employees (TV-Entgeltumwandlung/VKA).

compensation option by local Government employees which is, as a rule, made within public occupation pension institutions, but the employer can also have the objective of this deferred compensation reached through the saving banks or local government insurers. If needed, different arrangements can be made by collective agreement at Länder level. In the opinion of the Commission, this type of collective agreement is improper. The commission sees an infringement of European regulations relating to the award of public contracts in the definition of certain arrangements by means of collective agreement.

### Legal regulations governing occupational pensions in Germany

In Germany, the legal basis for occupational pensions is the Law on the improvement of occupational pensions (BetrAVG). Section 1 of the law makes provision for different ways to implement occupational pensions, the transformation of a portion of the employee's remuneration into a right to equivalent pension benefits (deferred compensation) being one of them. Section 1a(1)(2) of the law stipulates that the implementation of the deferred compensation will be governed by agreements. According to this provision of the law, the employer can nominate a pension scheme or a pension fund. That means that one, and only one, institution of that kind (and not only the choice of the "pension scheme" or the "pension fund" kind) must be nominated by the employer. The same applies in the case of direct insurance through an insurance company. When such a choice is made, it becomes an integral part of the corresponding deferred compensation agreement.

If the nomination of a pension fund is compatible with labour law at individual level, it is even more so in the case of a collective agreement. In addition, legislation on occupational pensions stipulates that all terms of deferred compensation, thus both "if" and "how", are placed under reservation of collective agreement (Section 17(3)(1) BetrAVG), including the decision of whether or not to establish a provision and how it is to be established. This also includes the nomination of the pension institution. One could object that this restricts the freedom of choice of the employer. But this objection is unfounded because such a restriction is the very nature of collective agreements and this type of objection could also be

applicable to all the other issues governed by collective agreements.

If remuneration of employees is based on collective agreement, German legislation moves another step forward towards giving more scope for free collective bargaining. In such a case, as in the public sector, deferred compensation can be implemented only if allowed by collective agreement (Section 17(5) of BetrAVG). In the absence of collective agreement in this respect, employees of a sector do not even have the possibility of deferred compensations. The legal framework defined by the legislation on old age pensions is transposed only by virtue of a collective agreement on deferred compensations.

This legal framework reflects social evolution throughout Europe. In view of diminishing old age benefits of the first pillar, the socio-political importance of occupational pensions is increasing. Considering that occupational pensions are linked to existing employment conditions, the possibility of and responsibility for shaping occupational pension schemes rest with social partners. The action of social partners is not limited to essentially tariff issues such as the amount of remuneration or the number of hours worked. Moreover, the ECJ also considers that occupational pension rights must be regarded as a component of salary. This means that social partners have full authority to regulate the issue of occupational pensions. German legislation takes this principle into account and grants them regulatory powers corresponding to their level of autonomy. Social partners made good use of this possibility. Presently, there are in Germany more than 400 collective agreements governing occupational pension schemes.

### Criticism from the Commission

According to the opinion of the Commission, the relevant employers of local Government are acting as contracting entities. Considering that they award contracts in order to provide occupational pensions, the contracts are, according to the Commission, public contracts for paid services which must be subject to a tender procedure before being awarded. The fact that employers and employees settle labour relations by mutual agreement, through such collective agreements, is not in opposition to this approach, according to the Commission. The Commission considers that

the legal obligation of inviting tenders is a priority. This opinion, however, is up against some objections.

Local authorities do not have the function of public contracting entities when acting as employers in the framework of negotiations on collective agreements and when implemented deferred compensation accordingly. This conclusion is based on a functional interpretation of the notion of contracting entity respecting domains reserved to social partners and their autonomy.

The ECJ has not yet, in any of its rulings, questioned the acceptability of this functional interpretation of the notion of contracting entity, which respects the domains reserved to social partners and their autonomy. Local authorities, in particular, do not have any possibility to intervene as public authorities which could lead to the award of contracts outside the rules of competition (therefore leading to discrimination against pension funds in the Community). The outcome of collective negotiations is obtained by mutual agreement with employee representatives and constitutes the expression of the interests of each of the parties. This means that there is no autonomous and unilateral expression of the will of local governments which could lead to the materialization of the risk of effective discrimination against tenders on grounds of their nationality.

An agreement on the implementation of deferred compensation, as provided for by the BetrAVG law, along with the collective agreement concerning deferred compensation for local government employees (TV-Eumw/VKA), between a public entity and a pension institution does not constitute a service contract falling within the provisions of directive EEC 92/50 or EC 2004/18, because such an implementation agreement constitutes the materialization of a work contract between employer and employees, which does not fall within the scope of application of directives EEC 92/50 and EC 2004/18. Functionally, the legal link between the employer and the pension institution does not constitute a public contract.

An agreement on the organisation of an occupational pension scheme and its terms do not give the public employer and the pension institution any margin for action, which is defined by collective agreement and is implemented only by individual agreement on the deferred compensation. The legal link concerning implementation is initi-

ated by an individual agreement, governed by labour law, entered into between the employee and the employer.

The conclusion of an implementation agreement depends on the prior conclusion of an agreement between employer and employees relating to a deferred compensation option. The insurance link arises only due to the existence of such an agreement, as part of the work contract; the form thereof (amount of transferred sums) depends upon this element of the work contract. There is therefore really no intervention by public authorities.

### The European social model

It is difficult to understand the refusal attitude of the Commission, considering the European social model the Commission promotes.

From the end of 2001, the first proposals in the field of pensions were formulated in a joint report of the commissions for social and economic affairs under the term "European Social Model". In this report, the adequacy of pensions, the financing of schemes and their modernisation in view of economic and demographic changes were considered as the most important objectives. In its communication "The future evolution of social protection from a long-term point of view: safe and sustainable pensions",<sup>4</sup> the Commission stated as a principle, among others, the maintenance of a sufficient pension level. The three pillars of old age pension, by interaction in a combination which can be decided upon by every Member State, should allow citizens to maintain, upon retirement, the standard of living they acquired during their working life.

In its communication "European values in a globalised world",<sup>5</sup> the Commission deals with the subject of an ageing society and the consequences thereof. It stresses therein that the continuity of social welfare must be pursued by suitable measures. Consequently, this means that Member States must have the possibility to respond with flexibility. In most Member States, the steps taken indicate that they seek to compensate the diminishing benefits of the first pillar of the old age pension by developing occupational pensions. As a general rule, occupational pen-

<sup>4</sup> COM (2000) 622 of 11.10.2000.

<sup>5</sup> COM (2005) 525 of 20.10.2005.

sions are implemented on the basis of agreements between social partners. Thus, a report of the Council of Ministers of the European Union highlights the fact that it is precisely occupational pensions based on collective agreements that make it possible to ensure sound supplementary pension income for the majority of the active population. The report also states that, wherever social partners play a major part in the implementation of occupational pension schemes, management costs are significantly lower than in other schemes.<sup>6</sup> Thus the positive role of social partners in the creation of occupational pension schemes is recognised at European level.

### The principle of free collective bargaining

The Commission itself values the role of social partners. Thus, upstream of the proposal for a directive on improving the portability of supplementary pension rights, it asked the social partners to first make use of the regulating possibility offered to them. In this specific case, it addressed the social partners before addressing the Member States because matters of an occupational nature were involved (in this case, the portability of occupational pension rights). This approach is a good reflection of the legal background.

At national as well as community level, the freedom of collective agreement and the right of negotiation between social partners are protected. In Germany, article 9(3) of the constitution deals with freedom of associations of employers and employees and empowers them in the role they play for the protection and development of economic life and labour conditions. In particular this includes also the possibility for the conclusion of collective agreements. In the opinion of the German Constitutional Court, this article is the constitutional basis of free collective bargaining. Whenever free collective bargaining is operative, the state has decreased its legislating powers on employment and economic matters to the benefit of social partners. In other Member States, freedom of association is protected by the constitution, too. This is clearly in evidence in the constitution of Belgium (article 23(3) no. 1: "Collective bargaining"), of Finland (Sect. 13(2)(3): "Freedom of association for trade unions"), of France (para. 6 of the preamble of the constitution: "Freedom of association for trade unions"), of Greece (article

22(2 – 3), article 23: "Free collective bargaining and freedom of association") of Italy (article 39: "Freedom of association for trade unions"), of Luxemburg (article 11(4) "Trade union freedoms"), of Portugal (article 55 et seq.: "Freedom of association for trade unions, free collective bargaining") and of Spain (article 7: "Freedom of association for trade unions").

Protection of free collective bargaining is also experienced at Community level. Thus, it is precisely the aim of article 136 et seq. ECT. The European Social Charter, the Community Charter of the Fundamental Social Rights of Workers and the Charter of Fundamental Rights of the European Union include complementary protection. Article 6 of the European Social Charter affirms the right of collective bargaining. Nos. 12 to 14 of the Community Charter of the Fundamental Social Rights of Workers of 9 December 1989 include the right to collective bargaining and to collective measures in case of conflict of interest in the framework of freedom of association. Article 28 of the Charter of Fundamental Rights deals with the right of collective bargaining. The project for the EC Treaty made provision unequivocally in article 1 – 48(1): "The European Union recognises and promotes the role of the social partners at Union level, taking into account the diversity of national systems; it shall facilitate dialogue between the social partners, respecting their autonomy."

It is not difficult to note the acknowledgement, at European level, of the existence of the Community law principle of free collective bargaining.

### Jurisdiction of the European Court of Justice

A review of the rulings of the European Court of Justice (ECJ) shows that, for the time being, the Court has not yet clarified the issue of whether the legislation on public contracts must be applied to agreements between social partners in the framework of collective bargaining. On the other hand, the relationship between free collective bargaining and competition law was on several occasions the subject of ECJ rulings. On the whole, regarding collective agreements, the ECJ recognised in this respect an exception to the provisions of competition law. The cases of "Albany", "Brentjens" and "Maatschappij Drijvende Bokken"<sup>7</sup>

<sup>6</sup> Council of the EU, 28.2.2005, "Privately managed pension provision", Report by the Social Protection Committee.

<sup>7</sup> ECJ, case C-67/96 („Albany“), case C-115/97 à C-117/S7 („Brentjens“), case C-219/97 („Maatschappij“).

dealt with the compulsory membership of employers and employees of occupational pension schemes. Some employers disputed such a membership, arguing that this would deprive them of the possibility to become a member of another occupational pension scheme. In its ruling, the Court emphasised, on the one hand, the mission of the Commission to promote a close collaboration between Member States in the social sphere, especially in matters concerning right of association and collective bargaining between employers and workers to implement the social policy laid down in the EC Treaty. It also emphasised that agreements entered into between social partners by means of collective agreements aimed at reaching these objectives, do not, by virtue of their nature and aim, fall within the scope of article 85, para. 1 of the ECT.<sup>8</sup> During the same procedure, the findings of Advocate General Jacobs were even clearer. He explained that “by encouraging the conclusion of collective agreements between social partners, the EC Treaty acknowledges the possibility of an exception to the general presumption relating to the consequences of agreements between private operators, on grounds that, normally, this particular type of agreement serves the public interest”. This position is corroborated by national laws as well as by the approach adopted by competition authorities and Courts in Member States which consider that collective bargaining normally fulfils a social function. To consider collective bargaining as subject to the rules of competition would in fact be a step backwards in the practice generally adopted in the Member States. Such an approach would lead not only to demand the notification of these agreements in the framework of Community law and/or national competition law, but also to their submission for assessment in court.<sup>9</sup>

This case law is corroborated by the Court in the “Hendrik van der Woude” case. In this ruling, the Court establishes that the clauses of a collective agreement on health insurance, stipulating that the portion of the insurance premium paid by the employer will be paid only to the insurer nominated in the collective agreement, are compatible with European law. In this context, the European Court of Justice emphasises in particular: “Otherwise, the freedom of social partners would be unjustifiably restricted, given that when they enter into agreement on one of the aspects of the con-

ditions of employment, they must also be able to agree on the creation of a distinct organization to implement the agreement and that this organization can go to another insurer.”<sup>10</sup> In the same proceedings, Advocate General Fennelly explains it very clearly in the findings by expressly rejecting the process of invitation to tender: “A limitation to this point of the applicability of the exclusion of collective bargaining from the prohibition as per article 85 of the EC Treaty would necessarily restrict the freedom of social partners to attempt to reach consensus on conditions of employment by means of agreements entered into for that purpose. In addition, it would undermine the solidarity which is inherent to collective bargaining ...”<sup>11</sup> and he went on “... would amount to negation of the autonomy of the parties involved in the collective agreement procedure. That is why we do not agree with Mr. Van der Woude when he maintains that Community law requires that such contracts be subjected to invitations to tender.”

#### **Deferred compensation does not involve public funds**

The procedure to award public contracts is based on the premise of ensuring that public authorities get “best value for public money”. It is therefore a matter of protection of public funds. In the case of deferred compensation, only portions of employee remuneration, therefore private funds, are transferred. Deferred compensation, with its legal consequences and economic effects, fall within the scope of remuneration. Through the deferred compensation, the employee forfeits a portion of his/her salary and the employer provides for pension rights of an equivalent amount. Based on the agreement reached with the employee, the public employer enters into a contract with a pension institution and pays in the employee’s contributions arising from the conversion of a portion of the salary. In this process, only economic assets of the employee are involved. Only the employee decides whether or not, and for how long, he/she makes use of deferred compensation.

<sup>8</sup> Cf. ECJ, case C-67/96, marginal number 54 ss., 59 s.

<sup>9</sup> Petition of Advocate General Jacobs case 67/96 and others, marginal number 185.

<sup>10</sup> ECJ case C-222/98, marginal number 26.

<sup>11</sup> Petition of Advocate general Fennelly case 222/98, marginal number 32.

### Threat to the position of workers

In view of limited or reduced state pension benefits, the promotion of individual old age pension supported by tax relief compensates for the fact that workers forfeit a portion of their salary to take personal responsibility for building up their own old-age pension. Because of the importance of deferred compensation for the old age pension of workers and because of the contractual nature of the amounts allocated to deferred compensation by public service employees, the terms of this facility and the implementation thereof fall within the reserved domain of sectoral collective agreements.

Reservation for sectoral collective agreements confers to worker unions power of co-decision with respect to occupational pensions which, according to the opinion of the ECJ, represents an integral part of salary. This means that the interests of workers must be taken into account when selecting the occupational pension scheme. Workers do not have to accept a short listing of institutions made by employers, but have the right to participate in the organisation of their scheme. This right of participation, arising from the reservation affirming the priority of sectoral collective agreements, guarantees specific protection for the interests of workers.

Occupational pension is pegged to the worker's salary as a direct element of the remuneration of his/her work. It is intended to improve the terms of employment of workers. Financial security of workers after they retire is a basic element of the terms of employment, as is expressly acknowledged by the ECJ in the case of occupational pension funds.<sup>12</sup>

The invitation to tender for old age pension benefits offered by the employers of local Government as part of deferred compensation, as required by the Commission, would eventually diminish the rights of workers. Binding a public employer, in his capacity as a social partner, to the outcome of an invitation to tender, would significantly limit the bargaining capacity of unions and therefore of employees, thereby even negating free collective bargaining. Deferred compensation is an unquestionable expression of the protection of worker interests because, due to the principle of reservation, unions have power of co-decision. The invi-

tation to tender process would deprive social partners of the possibility to reach agreement on various institutions meeting their requirements, from which the workers could choose.

The principle of reservation is precisely what gives worker unions power of co-decision in employment matters. The obligation to make use of invitations to tender would significantly reduce this power of the unions and would not be in the interest of workers. The principle of reservation is precisely intended to protect the economic situation of workers. The obligation to invite tenders would limit the rights of workers.

### The situation in other Member States

Pension schemes based on collective agreements exist in many Member States of the European Union. Thus, compulsory membership of an occupational pension fund is widespread in the **Netherlands**, where 90 to 95% of employees have access to occupational pensions. If requested by social partners, the relevant ministry or minister may impose membership of an occupational pension fund on all the employees of a sector. Pension insurance is then compulsory for the whole sector, the employer being forced to participate in the occupational pension funds of the sector. In 2003, there were 86 occupational pension funds including 76 compulsory funds. The structure of these funds is stipulated by collective agreements.

In **Sweden**, about 90% of employees benefit from occupational pensions organised by collective agreements. For employees whose salaries do not exceed the ceiling for contributions to the State pension (about 330,000 Swedish Krona in 2006), occupational pension organised by collective agreements constitutes a supplement to state pension and represents about 10 to 15% of the total amount of the pension of employees after thirty to forty years of membership. Regarding higher salaries, occupational pension could represent 65 to 70% of the total pension. Schemes established by collective agreement may offer other types of benefits such as survivor pension or benefits in case of illness.

In **Denmark**, the pension scheme for public service employees is also based on collective agreements entered into between employer associations and unions. Since 1990, there have been

<sup>12</sup> ECJ, joint case C-67/96 and others – „Albany“.

specific collective agreements involving old age pensions.

In **Austria**, occupational pension, as a supplement to the general old-age insurance scheme, experienced increasing importance in recent years. Thus legislation introduced a new product in 2005 to reinforce the second pillar of pension: an occupational group insurance. The terms of organisation of the new model can be governed by collective agreement.

All these agreements represent the transposition in practice of free collective bargaining and the right to collective bargaining, as guaranteed by constitutions and Community law. They are the living expression of the European social model at Member State level. In this era of change, they show that social partners are ready to take responsibility with respect to social policy and to constructively participate in a functional welfare State.

### Conclusions

Free collective bargaining is based on the understanding that only social partners, and no one else, are in the best position to define the terms governing labour relations. To impose preconditions for their autonomous decisions such as procedures to formally invite tenders would be in contradiction to this principle. Social partners who conduct collective bargaining and organise deferred compensation in the framework of collective agreements are setting the clauses of employment contracts and are not public contracting entities.

The position of the Commission would excessively limit the freedom of social partners to negotiate matters concerning conditions of employment which also include the transfer by employees of a portion of their salary.

One must retain the possibility for employers and employees to enter into collective agreements on some aspects of employment conditions, such as the granting of occupational pensions. It would be regrettable if an example of economic governance were made in this case to the detriment of German social partners. Among over 400 collective agreements which organise occupational pensions in Germany (frequently by deferred compensation), only one, that is to say the one concerning the public sector, would be measured by Community law. This would involve the risk of a "two-class society" as far as conventional labour law is concerned. It would not be appropriate to misuse Community law governing the award of public contracts by using it as a weapon in matters of economic governance.

It is precisely in the field of collective labour relations that, based on articles 136 and 137 ECT, Community law expressly acknowledges the diversity of legal systems in the Member States. Respecting the diversity of traditions in the different Member States should enable the resolution of the apparent contradiction between the obligations linked to the award of public contracts and free collective bargaining. Nothing justifies the application of purely academic economic governance. To the contrary, social structures developed over the years in Member States deserve consideration. In the "Albany" case, the ECJ rightly separated competition law and conventional collective decisions concerning membership of a pension scheme, because "the objectives of social policy pursued by such agreements would be seriously compromised".<sup>13</sup> One can only agree with this approach.

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<sup>13</sup> ECJ, case C-67/96; marginal number 59.

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