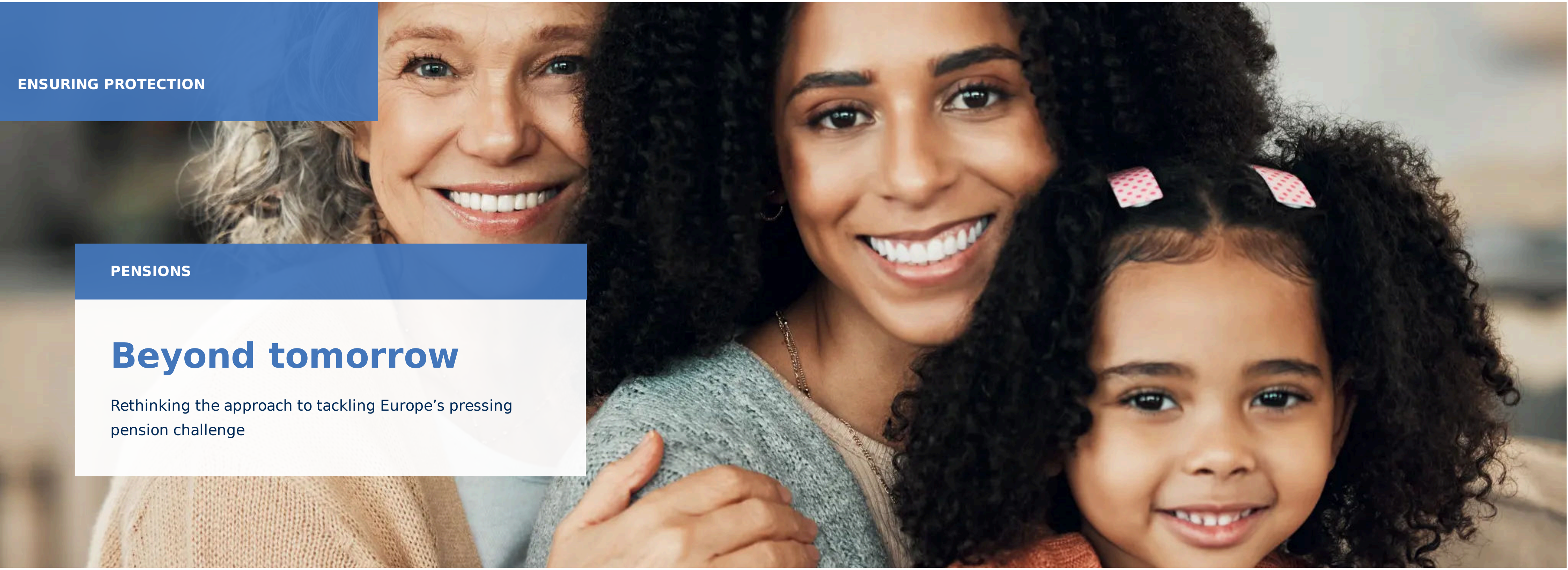
ENSURING PROTECTION

PENSIONS

Beyond tomorrow

Rethinking the approach to tackling Europe’s pressing pension challenge



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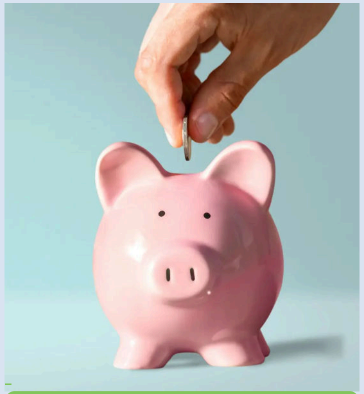
Insurance Europe's third Pan-European Pension Survey (November 2023) confirmed that over a third of Europeans are not setting aside money for their retirement. This is concerning, because, without sufficient savings, individuals may face financial insecurity during their retirement years, and this may result in reduced quality of life or an inability to afford healthcare costs. An excessive reliance on social welfare may put undue pressure on public finances, especially during a time of increasing 'age dependency ratio'. Standing on the brink of a new European Commission assuming office, now is an appropriate time for a critical reflection on how Europe can contribute to addressing the situation.

The pension challenge has reached a critical juncture. In addition to demographic changes and the dwindling ratio of active population to retirees, the labour market is undergoing profound changes. Non-linear careers are becoming more frequent, linked to the clear shift towards more service-oriented economies and new types of employment. The demographic changes in combination with evolving labour market realities are having a strong impact on both pension contributions and the stability of funding sources.

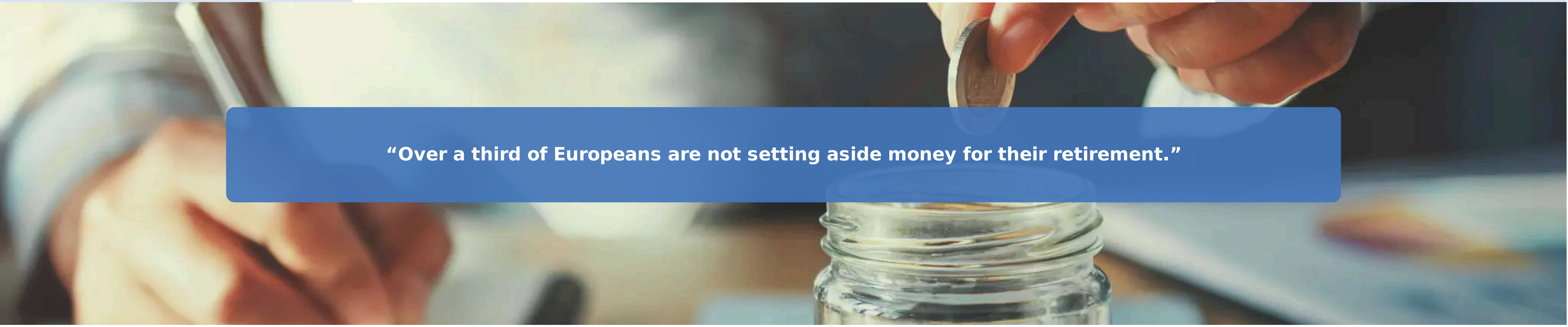
There is no silver bullet to solving the pension challenge, and so the approach to solving it can only consist of a range of different measures. One thing is clear, however, and that is that people will need to save more in order to maintain a comfortable living standard after retiring. The insurance industry can contribute to this objective through the role life insurers play as major providers of both occupational and personal pensions, thereby complementing state-funded pensions.

A unique element of insurance pension products is that they often offer future pensioners a minimum return guarantee, providing individuals with a sense of security and peace of mind about their financial future. This is key, because safety and security are the most important priority for many pensions savers, as confirmed by Insurance Europe's third Pan-European Pension Survey, showing that this is the case for 44% of the respondents. This result is fully in line with the previous surveys, conducted in 2019 and 2021.



How to increase the number of people saving for retirement?

Insurance Europe's recommendations to policymakers



"Over a third of Europeans are not setting aside money for their retirement."

Insurers' role extends beyond mere product offerings, however. For instance, many insurers are involved in awareness raising and educational campaigns, such as targeted communication efforts and workplace seminars about the risks of delayed action and the benefits of early retirement savings. Such efforts are pivotal, as Insurance Europe's survey results indicated that 14% of the respondents are interested in saving but would need more information to get started.

Digitalisation also offers interesting perspectives. For instance, digital tools and user-friendly applications increasingly offered by insurers can encourage saving by helping policyholders assess and forecast their financial situation, set realistic retirement goals, and create a personalised savings plan.

IORP II Directive

Report by former Italian prime minister Enrico Letta on the future of the Single Market

While all these are interesting steps insurers can and should take, addressing the pension challenge also requires action by public authorities at both national and European levels. This is the case notably in three areas: awareness raising, auto-enrollment, and tax incentives. Awareness raising is particularly important. Here, the goal should be to ensure that all over Europe, citizens have access to accurate and easy to understand information about their future pension entitlements, helping them make the right choices, in line with their own circumstances. This is already the case in a few countries, but, unfortunately, not everywhere. The European Commission has a role to play, notably by pointing to good practices and encouraging all member states to move forward.

Second, member states should consider implementing automatic enrollment schemes for employees, when this is not yet the case. Indeed, there is evidence demonstrating that individuals are more likely to participate in pension savings schemes when they are automatically enrolled, with a possibility to opt out if they so wish. Of course, the introduction of such schemes has to be envisaged giving due consideration to the realities of national pension systems.

Finally, there is no doubt that most people need to be encouraged to save for their retirement, and that adequate, targeted tax incentives (in the form of tax deductions or credits) can go a long way in achieving this goal. Member States should thus be urged to make sure that they have the right fiscal incentives in place to encourage all citizens, whatever their personal circumstances, to save for their old age.

A recent GFIA survey on protection gaps, which assessed insurance protection gaps in four areas (pensions, natural catastrophes, cyber and pensions) concluded that the gap is the highest in the pension area, with an estimated USD 1.0trn per year additional saving required globally. This staggering figure means that the challenge will only be met by having all stakeholders – citizens, pension providers, public authorities – joining forces and taking appropriate measures. From a European perspective, while member states will continue to play an important role in the pensions area, it is very clear that the European level also has a key role to play. Insurance Europe looks forward to engaging with the new Commission, EIOPA and other EU institutions to jointly identify the best solutions to one of the biggest challenges of our times.

IORP II Directive

The IORP Directive, adopted in 2003, had the objective to create the conditions for a future EU-wide market for occupational pension funds, and to ensure that they invest prudently, prioritising their beneficiaries' best interests. The Directive was revised 2016 to improve the governance, risk management, transparency, and information provided by occupational pension plans. It also aimed to make it easier for these plans to operate across borders within the EU.

A review of the functioning of the Directive is expected in 2024, building on a technical advice provided by EIOPA at the end of 2023. This review is important for the insurance sector as well, because while insurers fall under Solvency II for their occupational pension activities, many aspects of the IORP II directive have an impact on insurers as well.

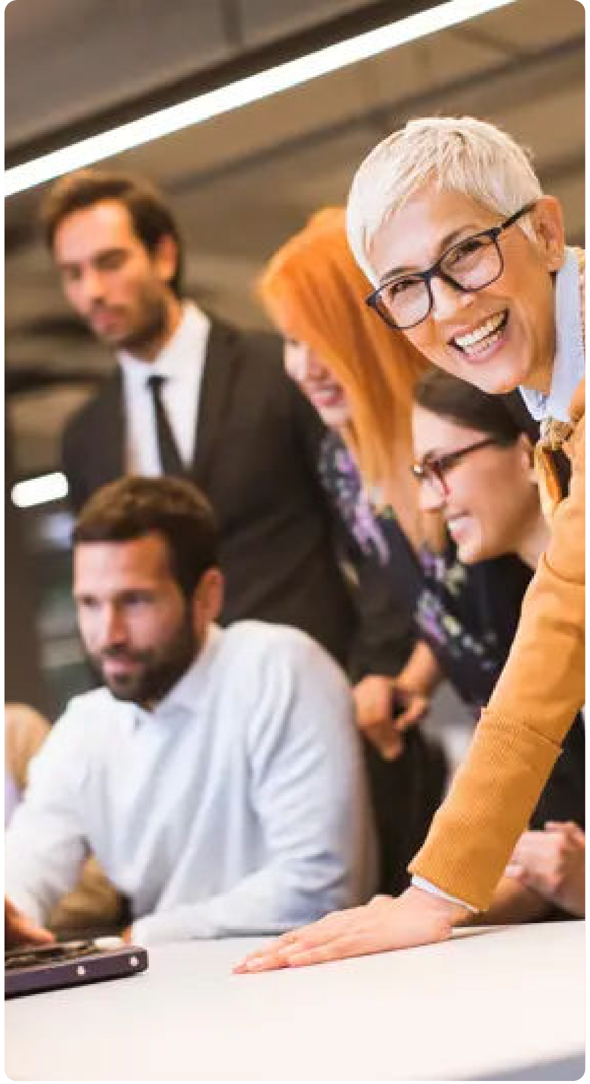
For instance, there is the question of ensuring a level playing field for pension funds and insurers, when they are involving in similar activities.

Also, insurers sometimes manage the investment portfolio of pension funds, and, in this activity, they might be influenced by requirements included in the IORP II Directive.

In our response to EIOPA's consultation which led to its advice to the Commission, Insurance Europe emphasised the need for a "minimum harmonisation" approach that respects the often very unique features of the national pension characteristics, including the role of social partners and national labour, social security, and tax laws. The harmonised framework, with the relevant national adds-on, would then be fit to cover more effectively the financial needs in retirement of European pensioners.

From an industry perspective, it is moreover key that the framework focuses on the actual risks posed by IORPs, rather than solely on their size and structure. This would avoid overburdening companies and permit them to operate in an efficient manner, and so allowing them to pursue their valuable function for European retirees.

Insurance Europe recognises the importance of fostering investments in sustainable assets and favoring an inclusive governance and workplace. Nevertheless, the insurance industry suggested addressing matters related to sustainability and diversity and inclusion through separate initiatives. This would allow the IORP II Directive to focus on its raison d'être, which pertains to governing IORPs' core prudential and governance aspects.



Enrico Letta's report on the future of the Single Market

The report by former Italian prime minister Enrico Letta, "*Much more than a market – speed, security, solidarity. Empowering the Single Market to deliver a sustainable future and prosperity for all EU citizens*", issued on 17 April 2024, touches upon several important issues for the insurance industry. Noteworthy among its proposals is the establishment of an "auto-enrolment EU Long-Term Savings Product". Moreover, the report addresses the "underwhelming" performance of the Pan-European Pension Product (PEPP) and advocates for its simplification and enhancement.

The fact that, since the implementation of the PEPP Regulation over two years ago, just one provider has put PEPPs on the EU market in a limited number of member states, confirms the concerns raised by the industry about the practical feasibility of the PEPP Regulation. The industry therefore urges policymakers to be realistic about the potential of the PEPP as a way to channel savings across Europe. What this means is that, to see the PEPP come to fruition, substantial reforms will be necessary, touching on many aspects of the regulation. Among those aspects, crucial ones include: the much-debated 1% fee cap, which makes it difficult for companies to offer PEPPs, especially considering the many requirements providers have to fulfil. Additionally, the requirement for PEPPs to outperform inflation over a 40-year timeframe is practically impossible to guarantee. Likewise, the lack of clear and consistent national tax decisions on PEPPs creates uncertainty regarding the potential national tax incentives offered. The insurance industry is keen to take part in such a dialogue with policymakers and other stakeholders in this regard, with the objective of increasing pension adequacy for all.

How to increase the number of people saving for retirement?

Insurance Europe's recommendations to policymakers

Policymakers should help to further develop multi-pillar pension systems

- Not everyone is aware of the need to save for retirement. Awareness-raising efforts therefore need to continue, as well as efforts to improve levels of financial literacy so that individuals can make the most appropriate decisions for their own circumstances.
- The development and uptake of pension tracking systems should be enhanced to improve citizens' awareness of their future entitlements and help them make the best choices.
- It is important to make sure that no undue regulatory burdens and obstacles are placed on supplementary pension products that prevent insurers — as key providers of second- and third-pillar pensions — from continuing to offer supplementary pensions. For example, it is vital to avoid the regulatory framework lengthening the distribution process with additional questionnaires, tests, assessments and disclosures.
- Auto-enrolment should also be considered as a way to incentivise people to save, but this decision should be made at national level, based on national realities.

Regulation should enable insurers to keep playing their fundamental role of protection

- There is a clear appetite for the protection offered by the financial guarantees, annuities and biometric coverage traditionally offered by insurers. It is crucial that regulation, and in particular the Solvency II Directive and the new Retail Investment Strategy, do not prevent or discourage insurers from fulfilling their important role in offering protection.
- National circumstances require country-specific solutions. The survey confirms the diversity inherent in retirement saving across Europe. Pensions come in a variety of forms and are influenced by a broad range of factors. As a result, there is no one-size-fits-all approach to tackling all the challenges.

Pension policies need to be consumer-centric

- Policies should be based on evidence of users' demands and needs, so any initiatives should always be subject to extensive consumer-testing.

Disclosure requirements need to be simpler and more targeted to avoid overloading consumers with information

- When defining the information requirements for pension products, policymakers should consider what information respondents consider relevant. For instance, with respect to the Pension Benefit Statement, the survey indicates that benefit projections are not considered a fundamental piece of information either before buying the product or after. Regulators should avoid overburdening consumers with excessive information, which — far from providing clarity — contributes to confusion.

Pensions should be brought into the digital era

- As the survey reveals a strong preference for receiving information in a digital format by default (71%), rather than on paper by default, policymakers should take steps to ensure that this reality is reflected in the regulatory framework.