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Welcoming Remarks

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Opening Presentation

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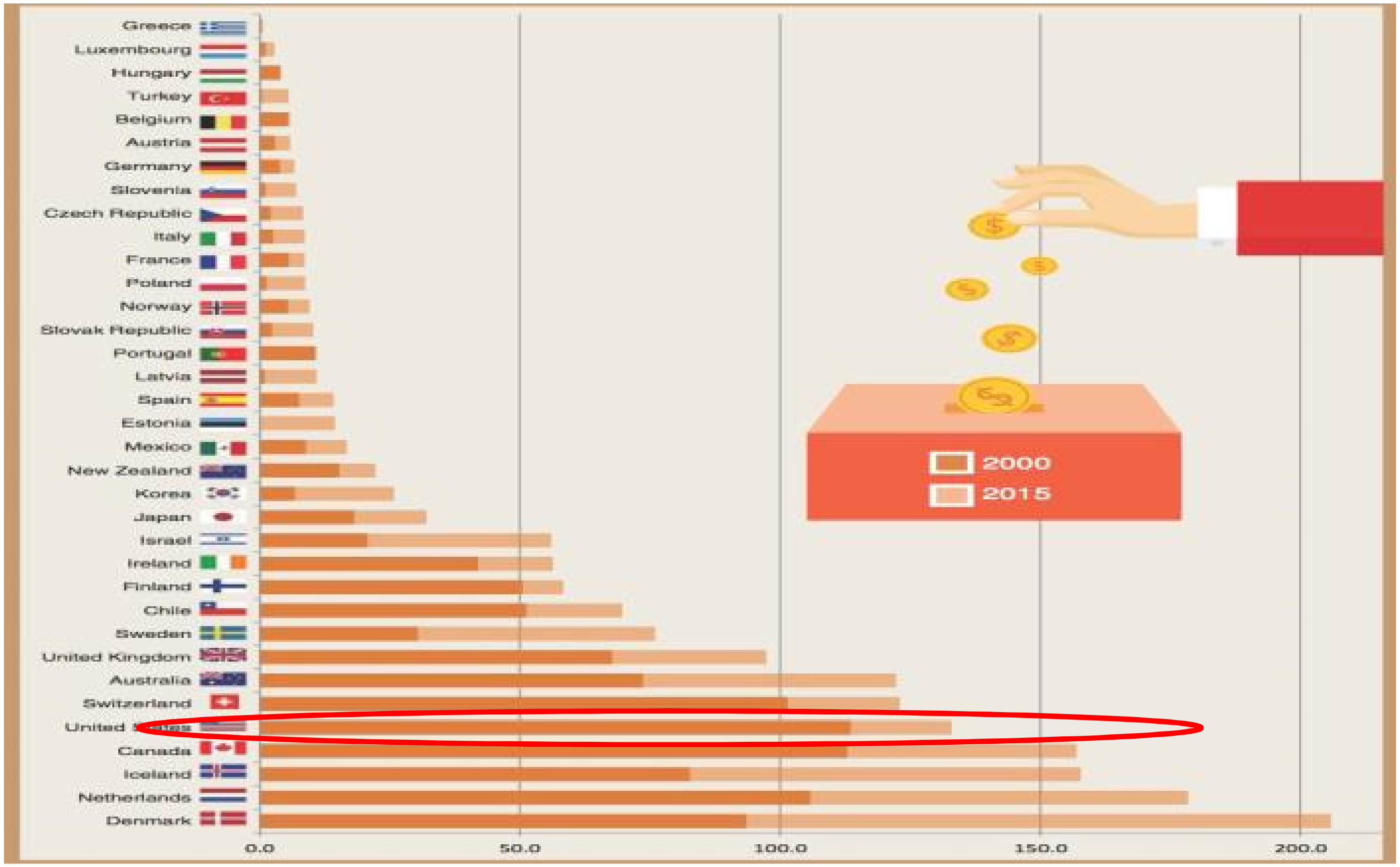
OECD PENSIONS OUTLOOK 2016

OECD
BETTER POLICIES FOR BETTER LIVES

Changing pensions landscape: more diverse and balanced

- Changing pensions landscape as a result of
  - ageing populations,
  - the fallout from the financial and economic crisis,
  - the current environment of low economic growth and low returns.
- Increased role of funded pensions: pension arrangements in which asset back pension benefits
- In line with OECD long standing policy messages:
  - Diversification of the sources to finance retirement
  - Funded pensions complement PAYG public pensions

The growing importance of funded pension arrangements (assets as % GDP)



13 countries more than 50% of GDP, up from 10 in 2000

7 countries more than 100% of GDP, up from 4 in 2000

DCs are here to stay, have advantages, but their design needs to be improved

- The growth in funded pension arrangements comes mainly from arrangements in which there is a direct and straightforward link between contributions, assets accumulated and pension benefits (DC pensions)
- Advantages (direct link) and disadvantages
- They put more of the risks of saving for retirement (e.g. investment and longevity risk) and decision making on the hands of individuals.
- Improve design => OECD Roadmap Good Design of DC Pension Plans

We need to improve the design of DC pension arrangements

- Incentives: Does the tax treatment of retirement savings provide an advantage to save for retirement? *Chapter 2*
- Growing individual responsibility heightens the need for policy measures to improve the quality of financial advice for retirement: *Chapter 3*
- Partial annuitisation protects individuals from longevity risk, preserving choice (drawdown - deferred life annuity). Need for life annuity products: *Chapter 4*
- Growing individual responsibility heightens the role of financial education in supporting decision making for retirement: *Chapter 5*
- Civil service and private sector pensions should be aligned to facilitate mobility and efficiency => *Chapter 6*.

OECD Pensions Outlook 2016

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Chapter 2
Does the tax treatment of retirement savings provide an advantage when people save for retirement?

Goal of the chapter: tax advantage

- Assess whether the tax treatment of retirement savings in different OECD countries provides an advantage when people save for retirement
- Calculate the tax advantage that individuals saving into funded private pension plans may enjoy over their lifetime
- The overall tax advantage is the amount that an individual would save in taxes paid during their working and retirement years by contributing the same pre-tax amount to a private pension plan instead of to a benchmark savings vehicle

Tax Treatment of Retirement Savings: EET is the most common

EET

Canada, Chile, Estonia, Finland, Germany, Greece, Iceland, Ireland, Japan, Latvia, Netherlands, Norway, Poland, Slovenia, Spain, Switzerland, United Kingdom, United States

EEE

Slovak Republic

TET

Austria, Belgium, France, Israel, Korea, Portugal

TEE

Czech Republic, Hungary, Luxembourg, Mexico

ETT

Denmark, Italy, Sweden

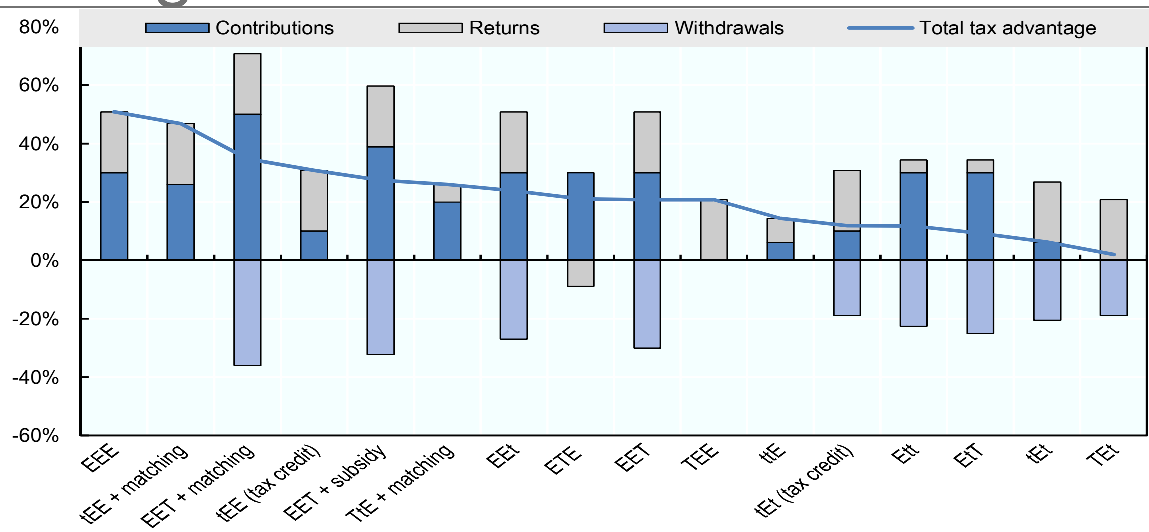
TTE

Australia, New Zealand, Turkey

Measuring the overall Tax Advantage

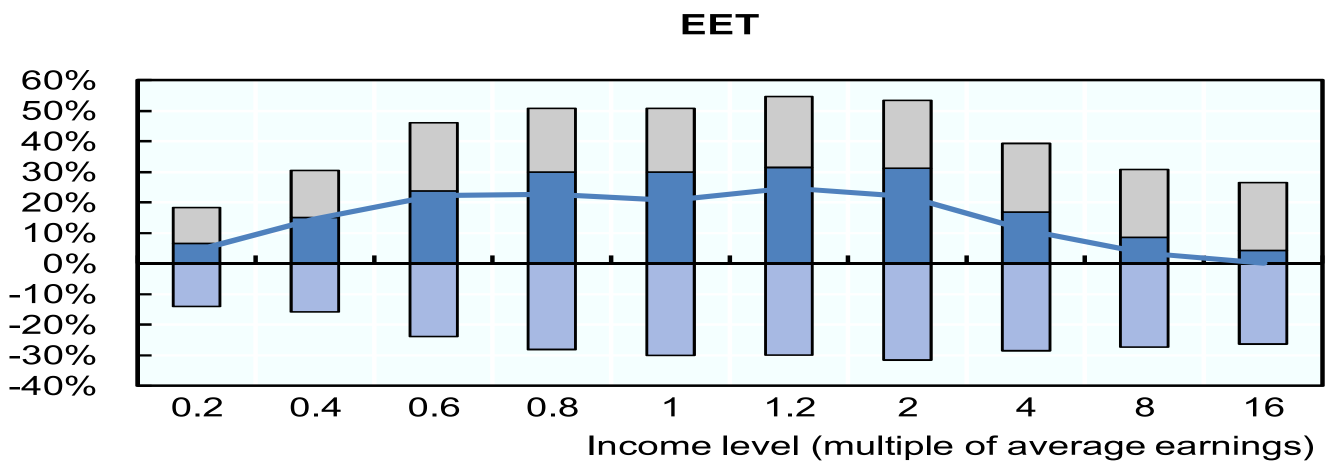
- The tax advantage is measured with respect to a benchmark savings vehicle
- **Overall tax advantage** = (PV of total tax paid for benchmark – PV of total tax paid for private pension) = amount that an individual would save in taxes paid during their lifetime when contributing the same pre-tax amount to a private pension plan instead of to a benchmark savings vehicle
- Only personal income tax (not social security contributions)
- State matching contributions and flat-rate subsidies considered as refundable tax credits

Different regimes provide different tax advantages: EET is in the middle



- The preferential tax treatment for contributions and returns on investment: tax exemptions/ deductions, tax credits, lower tax rates and state financial incentives (flat-rate subsidies and matching contributions)
- …is not offset by the potential taxation of benefits

The tax advantage increases with income but …

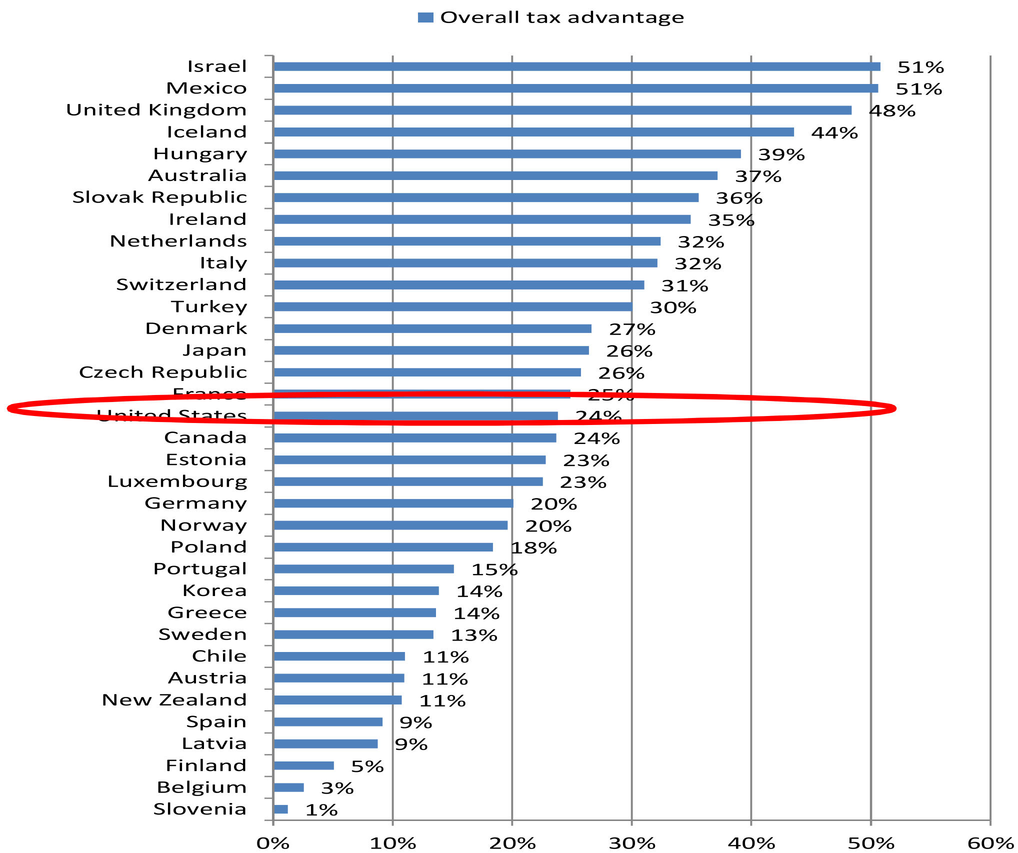


- The higher the income the higher the tax marginal rate and thus the higher the tax advantage.
- Tax-deductibility limits reduces the tax advantage when income increases

The tax advantage can also made income neutral by …

- Flat-rate state subsidies paid into private pension plans change the profile of the tax advantage with respect to income as they target the tax advantage at low-income individuals
- Tax credits on personal income tax and state matching contributions paid into private pension plans can be used to smooth out the tax advantage across income groups.
  - Caps lower the tax advantage for high-income individuals
  - Low-income individuals, who pay little or no income tax, benefit less from non-refundable tax credits

Size of the overall tax advantage in OECD countries (average earner)



- Country-specific parameters
- Variability across countries due to:
  - Tax regime applied to pension plans and benchmark savings vehicles
  - Characteristics of the personal income tax system (i.e. the tax brackets and the tax rates)

Main messages

- EET is the most common tax treatment of retirement savings across OECD countries
- The tax advantage comes from the exempting from tax returns on investment
- In most OECD countries, the tax treatment of retirement savings provides a tax advantage when people save for retirement
- Using tax credits and matching contributions can make the tax advantage income neutral

Chapter 3

Policy measures to improve the quality of financial advice for retirement

Goal of the chapter

- It looks at policy measures to help ensure that consumers receive appropriate financial advice for retirement and thus improve consumer outcomes.
- The measures include
  - Mitigation of conflicts of interest
    - Duty of care standards
    - Disclosure requirements
    - Remuneration limits
  - Qualification standards to ensure that advisors are competent
  - Dispute resolution mechanisms
- Challenge: potential advice gap
  - Drivers
  - Closing the advice gap
  - Technology-based advice

Mitigating conflicts of interest:

- Duty of care standards
  - Due diligence for personalised advice
    - Suitability vs best interest: trend towards uniform best interest standard
  - Dealing with conflicts of interest
    - Management or avoidance: trend towards written conflicts of interest policy
  - However:
    - Increased compliance costs: improve clarity of regulation
- Disclosure standards
  - Disclose coi, nature and amount of remuneration
  - Disclose nature of support: personalised or general
  - Trend toward simplified presentation

Mitigating conflicts of interest:

- However:
- Limits on remuneration
  - Compliance costs, poor disclosure practices, effectiveness (consumers understanding)
- Caps (hard or soft)
- Bans (certain channels or structures)
- Structural requirements: time limits to pay fee-based advice
- However:
  - Changes incentives
  - Appropriate limits depend on problems observed in the market and the effectiveness of the other policies to mitigate conflicts

Key challenge of those measures: Potential advice gap

- The above measures to improve quality of advice can lead to problems of suitability and affordability, especially for people with small pots of assets, which may create an advice gap
- Drives of advice gap
  - Reduction in the supply of advice
    - Uncertainty around regulatory liability
  - Increased cost of advice
    - Increased due diligence, increased administrative costs, increased legal liability
  - Consumer reluctance to pay for advice
    - Transparency of cost from disclosure requirement
    - Transparency of cost from limits on more opaque commission structures

Closing the advice gap

- Supply of advice
  - Uniformity of regulation
  - Clarity of regulation
- Cost of advice
  - Clarity of regulation
  - Streamlined processes
- Consumer reluctance to pay for advice
  - Flexibility in fee structure
  - Promote and support technology-based advice (e.g. robo-advice):
    - Potential to increase the accessibility and affordability of advice
    - Challenge: regulatory framework, consumer protection

Main messages

- Measures are needed to address conflicts of interest in financial advice and improve the quality of financial advice
- Such measures can potentially lead to an advice gap, reducing the availability and affordability of advice, particularly for consumers with low to moderate retirement wealth
- The scope and definitions used by the regulation need to be clear in order to minimise the impact of these measures on the advice gap
- Technology-based advice has the potential to increase the accessibility and affordability of financial advice (regulation in place?)

Chapter 4
Policy considerations for life annuity products

Goal of the chapter

- Annuity products can play an important role in helping individuals mitigate investment and longevity risk (outliving their resources to finance retirement).
- OECD Roadmap Good Design of DC Pensions: Combine drawdowns with deferred life annuities (e.g. age 85). Strikes balance between flexibility, choice and protection from the tail risk of longevity
- Annuity products and their associated guarantees present challenges. This chapter and associated monograph examine those challenges and provide policy guidance.

Defining a common language

- Scope
  - Distinguish between annuity income and annuity products
- Definition
  - Distinguish between pension products and annuity products
- Terminology
  - Define a common terminology to aid in data collection and policy discussions

Classification of annuity products

- Fixed payment annuities: payments defined in advance
- Indexed payment annuities: payments vary depending on an index
- Retirement savings with guaranteed income option
  - Individual retains access to underlying capital, and has the future option to receive annuity payments at a guaranteed rate

Designing a coherent framework

- Life annuity products fit in the overall structure of the pension system
- Ensure products can be used
  - Rules relating to accumulation and drawdown of pensions need to accommodate the use of annuity products
- Ensure products are designed to be useful and sustainable
- Ensure products are used in practice
  - Ensure that limits on market segmentation do not exclude certain populations from the annuity market
  - One-size-fits-all mandate not appropriate for all segments
  - Carefully designed default
  - Fiscal incentives can encourage use of products

Keeping up with innovation

- Ensure sustainability given increased flexibility
  - Capital and reserving requirements need to adapt to changing product features and risks posed by consumer behaviour
  - Approaches based on principle more flexible than requirements based on static formulas
- Ensure suitability given increased risk-sharing
  - Product disclosures need to clearly communicate product features, risks and costs
  - Role of financial advice to help consumers find suitable products is increasingly important

Encouraging appropriate risk management

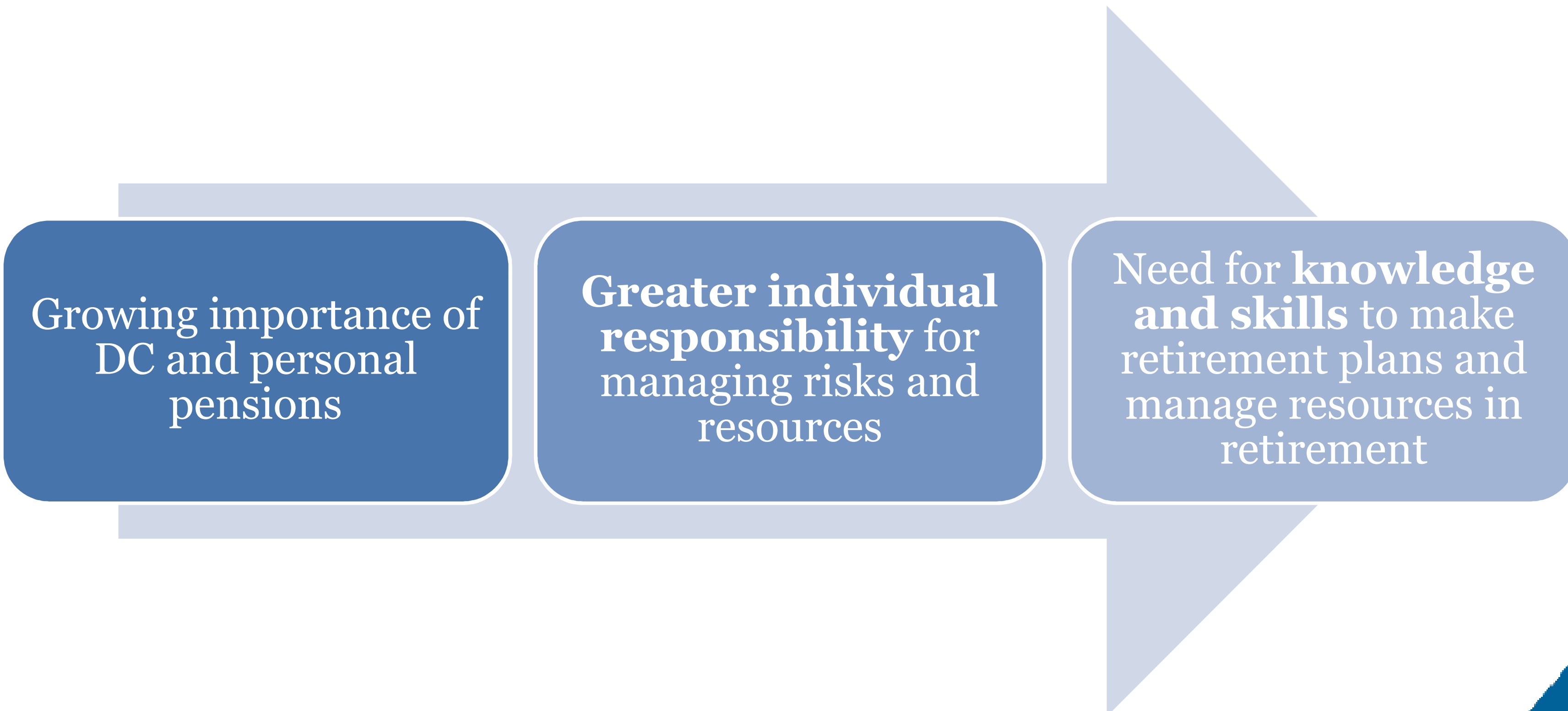
- Implications of accounting measures should be understood
- Effective risk mitigating actions should be available
- Risk-reducing measures should be recognised
  - Capital and reserving requirements should be reactive to measures taken to reduce risk

Main messages

- Defining a common language
  - Need for ability to compare and have coherent discussions
- Designing a coherent framework
  - Pension system needs to accommodate and facilitate the desired role of annuity products
- Keeping up with innovation
  - Ensuring sustainability and suitability in an evolving annuities landscape
- Encouraging appropriate risk management
  - Align risk measures and incentives to manage the risk

Chapter 5
The role of financial education in supporting decision-making for retirement

Increasing need for financial skills to take retirement-related decisions



Decision-making challenges about retirement get compounded

- Challenges: planning and estimating retirement needs, assessing risks, and understanding retirement product
- Compounded because of
  - Limited general financial literacy
  - Limited pension specific knowledge
  - Behavioural biases
    - Aversion to plan ahead
    - Status quo bias
    - Over-confidence / over-optimism

Decision-making challenges vary with the features of a pension system

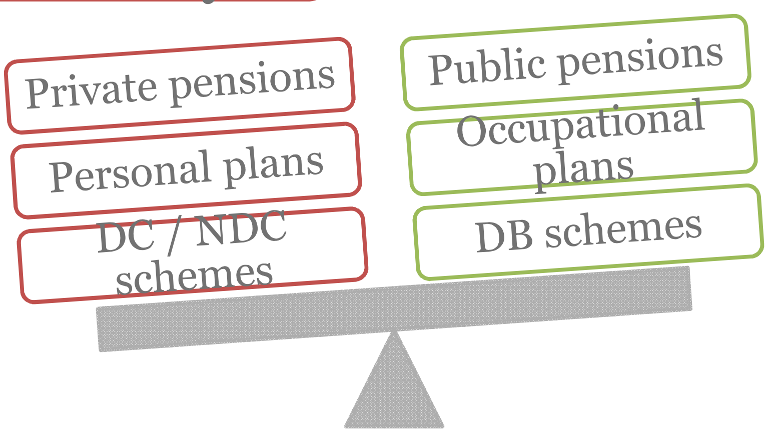
Depending on the structure and features of a pension system,

- what people need to know, and
- what they should be able to do

…is likely to vary

More difficult and requiring greater financial literacy…

Relatively less difficult…



Different financial education tools can address different needs

		What these tools can do
Generalised information	• Websites, regular and one-off communication campaign, comparison tools	• Provide information on rules and risks • Raise awareness • Lower cost of information
Personalised information	• pension statements, personal information online, retirement calculators, simulators	• Lower cost of planning and estimate needs • (May) explain risks and uncertainty • Make long-term needs more salient
Training	• Instruction and training in the workplace or elsewhere	• Provide general information • Explain what do to and how to do it • Make long-term needs more salient
Generic advice	• about pensions and retirement	• Provide general information • Support decision making

Policy guidance

Taking into account national circumstances and the extent of retirement planning challenges due to the features of the pension systems and of the financial environment

Provide general financial skills within a national strategy for financial education

Information should be clear, comparable, comprehensive, complemented by calculators/simulators

Provide not only information but also training to foster skills to act upon information

Provide unbiased advice about all pension sources, especially when the system is particularly complex

Practical tools to help policy makers identify needs and solutions

- A matrix of financial education needs and tools
- A checklist on financial education for retirement

Chapter 6
Civil service pensions

Goal of the chapter

- Examine the pension system for public sector workers in OECD countries
  - USA: Federal (FRSE), not State or local civil servants
- The chapter compares the key pension parameters of public-sector and private sector pensions,
- and calculates their replacement rates

After 20 years of reforms

- Four countries have entirely separate schemes (BEL, FRA, DEU, KOR)
- Eight countries have fully aligned their schemes in the last 15 years, with half of OECD countries now "fully integrated".
- Four more countries have similar benefits, with ten others having a top-up for civil servants.

Main messages

- Most OECD countries have been aligning the pension system for civil servants and private sector workers
- Civil servants should be covered under the general public pension scheme to improve:
  - Equity – comparability and transparency of benefits
  - Efficiency – economies of scale with one system and improve cross sector mobility

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