

Location, location...

Conference Report

The Competence Centre for Pension Research of Tilburg University and the Dutch Circle for Pension Specialists organised a debate to determine the best location for pan-European pension funds. Peter Schonewille reports

The competition for market share on the pan-European pension fund market is limited. In practice, only Belgium, the Netherlands, Luxembourg and Ireland have shown the political will to attract Institutions for Occupational Retirement Provision (IORPs) providing pensions across borders. Why such limited competition? Attracting pension business brings high-level employment for administrators, actuaries, accountants, tax advisers, consultants, supervisors and others. On the other hand, it may be necessary to offer solutions that are different from the ones provided currently on the domestic market, which may also prove hard to ring-fence.

Vehicles offered

Lut Sommerijns, secretary general of the Belgian Association of Pension Funds, told conference attendees that Belgium offers a vehicle for pan-European pension funds, the OFP (Organism for Financing Pensions), that can cover both defined contribution (DC) and defined benefit (DB) plans.

The Luxembourg pension sector was represented by Gerd Gebhard, director of PECOMA, a pension consultancy. Luxembourg offers three vehicles. A SEPICAV (pension investment company), can only be used for DC plans. The ASSEP (pension fund) is the best vehicle for international pension funds as it is suited for both DC and DB. Luxembourg also has the CAA (pension insurance fund), which is regulated by the insurance supervisory authority. Brendan Kennedy, chief executive of the Irish Pensions Board, noted that Ireland uses trusts to offer pan-European solutions. Ireland did not create a special legal vehicle to implement the IORP Directive (2003/41/EC).

Robin Fransman, of Holland Financial Centre, a lobby group, explained that the Netherlands hoped to be able to offer the PPI (premium pension institution) vehicle later this year. The legislative proposal for the PPI had been sent to parliament on 13 March 2009. A PPI could only deal with DC but it is claimed that a PPI can do everything an Irish trust can. Later this year, a proposal for a law establishing a general pension institution (API) should be tabled which will be able to deal with both DC and DB plans.

Solvency requirements

All participants in the debate took the politically correct position that there was no competition regarding solvency requirements. But such competition is possible, since the IORP Directive did not harmonise the solvency requirements. Ton Daniels of Ernst & Young presented a new study, Pan-European Pension Funds in a Future World, which compares the solvency requirements in Belgium, the Netherlands and the United Kingdom. Under the assumptions of the

Comparison of solvency requirements

	UK	Belgium	Netherlands
Discount rate	4.5%/6.5%	4%/6%	2.5%/4%
Technical provision (€m)	11.8	14.5	28.5
Regulatory own funds (€m)	3.2	1.5	
Coverage ratio	100%	122%	105%
Required assets	11.8	17.7	30.0
Comparison of required assets	100%	150%	254%

Source: Ernst & Young

study (a pension scheme with 500 employees at age 40, 40% allocated to equities, 60% to bonds), a Dutch fund would require 154% more assets than a UK fund and considerably more than a Belgian fund (see table). As Jacqueline Lommen of Hewitt Associates noted, the required solvency requirement is not the whole story. For instance, in Belgium the employer is obliged to cover any deficits, whereas this is not the case in other countries.

Daniels proposed that to harmonise, an update of the IORP Directive could provide that the European Central Bank would regularly publish the appropriate discount rate, for instance, the market rate for a package of high quality corporate bonds. He also noted that while a multinational company would save cash if it were to establish its pan-European fund in a jurisdiction with low solvency requirements, it would still have to report any deficits in the various national accounts of the sponsoring companies under IAS19. One participant remarked that in the present market conditions, companies would be happy to report any deficit, as long as they could save cash.

Solvency requirements

For direct taxation the position of the four contenders is similar. They all exempt the investment income of their pension vehicles. Ireland and the Netherlands have full exemption of their pension funds. Belgium and Luxembourg, however, subject their pension vehicles to corporation tax, but at a low rate. The aim is to bring pension vehicles under the scope of their tax treaties. A number of tax treaties is applicable on condition that the pension fund is subject to tax. This is only relevant for withholding taxes on dividends and interest paid from debtors outside the EU/EEA. For intra EU/EEA dividend and interest payments the source-states need to give national treatment on the basis of the EC Treaty. This means that if they exempt their own pension funds (as most member states do), they should also exempt foreign pension funds. Dividend and interest payments from countries outside the EU/EEA do not fall under the scope of the EC treaty. For these, the limited tax base for pension funds might help

them to pass the 'subject to tax' test, leading to a reduction of withholding taxes.

Remarkably, harmonised VAT causes the biggest distortion. Asset management fees charged to a (pan-European) pension fund are subject to VAT in Ireland and the Netherlands, but are exempt in Belgium and Luxembourg.

Political climate/local experience

The political support for pan-European pension funds is strongest in Ireland. Brian Cowen, the Irish prime minister, has established a committee directly reporting to him to foster pan-European pension developments. In terms of occupational pensions experience, the Netherlands scores best, with five pension funds in the top 30 biggest pension funds in the EU, according to the annual IPE Top 1000 Pension Funds study. There are no funds from Ireland, Belgium or Luxembourg in that top 30.

On the other hand, as Paul Kelly of Towers Perrin explained, Ireland hosts one of the first cross-border IORPs with more than two sections. As presented at the International Employee Benefits Association conference earlier this year, Intel has set up shop in Dublin, with sections for Ireland, the UK, Poland, Hungary already in place and sections for Turkey, Egypt and Russia being put in place. The sections for Turkey, Egypt and Russia prove the point that when competing for market share on the pan-European pension fund market, the market is in fact bigger than the EU. Once a multinational has experience in setting up a number of sections for EU member states in an IORP, it is relatively easy to include the pension liabilities of expats working outside the EU.

Votes

During the debate a number of votes were organised among the 160 participants of the debate. Governance scored highest (33%) as a criterion for choosing the location of a pan-European pension fund, although the debate did not go into the details of the differences in governance between the member states.

It is also interesting to note the participants' votes on the best location from the employee's and from the employer's perspective. Given that most participants were Dutch, the high number of votes for the Netherlands from the employee's perspective does not come as a surprise (58%). Belgium scored the highest (56%) when asked from the employer's perspective. This may be influenced by the results of the Ernst & Young study, which showed that with comparable liabilities, a Dutch solution would require considerably more cash than a Belgian solution.

Conclusion

There may not be a uniform answer to the question about the best location for a pan-European pension fund. A company with an Anglo-Saxon background may feel more comfortable in a trust environment, while continental companies may feel more comfortable staying on the continent with their pan-European solution. With a momentum building up in only four member states, the next few years will be decisive in the battle for market share on the pan-European pension fund market.

The Ernst & Young study, Pan-European Pension Funds in a Future World, will be available via www.europeanpensiondebate.com, as are the slides of all the presentations at the conference.

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