BENEFITS PASSPORT

Updates and Information on International Benefits

AMERICAN BENEFITS INSTITUTE

The American Benefits Institute is the education and research affiliate of the American Benefits Council. The Institute conducts research on both domestic and global employee benefits policy matters to enable public policy officials and other stakeholders make informed decisions. The Institute also serves as a conduit for global companies to share information about retirement, health and compensation plan issues.

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Highlights from the Summer 2016 Meeting Of the OECD Working Party on Private Pensions

The Organization for Economic Cooperation and Development (OECD) Working Party on Private Pensions (WPPP) held its summer meeting this past June at the OECD headquarters in Paris, France. The American Benefits Institute (Institute), the education and research affiliate of the American Benefits Council (Council), serves as a private sector advisor to the U.S. government delegation to the OECD. Richard Hinz, Senior Advisor to the Council (and former Chairman of the OECD's Working Party on Private Pensions when he served in the U.S. Department of Labor (DOL)), attended the meeting on our behalf.

As has become customary, the WPPP meeting was held in conjunction with a meeting of the International Organization of Pension Supervisors (IOPS), for which the OECD serves as the secretariat. (Note: the joint meeting was followed by a conference, "Challenges for Global Pensions: Trends and Heterogeneity". Immediately following that conference an event was held to launch the second edition of the new OECD publication series "OECD Business and Finance Outlook." A report on the IOPS conference and the new OECD publication will be covered in the next Benefits Passport.)

Below is a summary of the main topics addressed at the WPPP meeting and includes links to the relevant documents and presentations for each topic. While the content of these documents and OECD documents may be of a highly academic nature, they often serve as a basis for standards that are adopted by OECD – and its member nations.

Consequently, the findings and recommendations set forth can have important practical implications for both plan sponsors and service providers conducting business in OECD countries.

Following each WPPP meeting, the OECD requests comments on the documents presented at the session from each member government delegation. As we have done the past few years, we prepared draft comments that were then distributed to a working group of interested Council members for review and suggestions prior to submitting the comments to the U.S. Department of Labor (which is the U.S. government's official representative to the WPPP). Our comments were then used by DOL in developing its formal comments submitted to the OECD.

Our comments on the various papers are included in the links following each summary description. Broader participation in this review process is encouraged and any Council members interested in participating should contact Richard Hinz to be added to the distribution list. There will also be the opportunity for one or two Council members that have been engaged in commentary on these products to attend the OECD meetings as part of the U.S. delegation beginning with the December 2016 meeting that is scheduled for December 5-6, 2016, in Paris.

WHAT IS THE WORKING PARTY ON PRIVATE PENSIONS (WPPP)?

The *Working Party on Private Pensions* is a sub-group of the *Committee on Insurance and Private Pensions* that was established in 1999 under the auspices of the OECD's *Directorate on Financial and Enterprise Affairs.* It provides a venue to plan and review OECD's work that is directed to the development and regulation of private pension funds. Although originally primarily oriented to employer sponsored plans ("occupational funds" in the European vernacular) the group has extended its activities to address individual retirement savings arrangements (also referred to as "personal pensions") in recent years.

The WPPP holds two meetings each year in June and December at the OECD's headquarters in Paris and sponsors research and policy analysis conferences at other locations as part of the OECD's outreach effort to non-member countries. The WPPP undertakes its activities in close cooperation with the International Organization of Pension Supervisors (IOPS), which receives administrative and staff support from the OECD and holds its annual meeting in the days following the OECD's June meeting. The general distinction between the two groups is that the OECD body focuses on legislative and regulatory policy issues for its member countries, and the IOPS is oriented to the actual conduct of supervision within its much broader membership.

The program of work and other initiatives related to private pensions now underway at the OECD is wide ranging and ambitious. It is based on four broader OECD priorities to undertake projects directed to: (1) Enhancing financial stability by addressing systemic risks (particularly solvency issues) of financial institutions, (2) developing common and integrated core regulatory systems, (3) addressing the pressures of demographic changes and population aging through enhancement of private sources of retirement income and (4) supporting growth and security through financial literacy. Not coincidently, these are also priorities that underlie the current activities of the G20, a policy and information sharing forum of developed nations whose membership overlaps with that of the OECD.

SUMMARY OF THE MAIN TOPICS AND DOCUMENTS

Please note: The agenda and all of the documents from the meeting have been placed on the Council's website. Many of these, however, are not yet in the public domain so access is password-protected for Council members only. Members are welcome to read and use the documents but are requested not to distribute them. Those in the public domain are available on the OECD website as noted.

Core Principles for Private Pension Regulation

The **final version of the proposed revisions** to the "Core Principles for Private Pension Regulation" was presented at a session of the meeting that was closed to the private-sector observers. This represents the product of a two-year effort with multiple rounds of consultation and comments to update the principles and adopted by the OECD in 1999 and extend them to cover individual retirement savings arrangements.

The American Benefits Institute, through its role in advising the DOL delegation, provided extensive comments on the principles and some revisions have been made in response to these comments. . The final principles have now completed the review and comment process and now need to be accepted by the OECD's Council which is its final review body.

The OECD staff provided **a PowerPoint presentation of the revisions made** in response to the final round of comments received.

Policy Measures to Improve the Quality of Financial Advice for Retirement

This paper is the third component of an effort by the WPPP to examine issues related to regulation of the way in which financial advice is provided to the members of private pension funds. The work was initiated at the suggestion of DOL as it undertook the development of the recent regulatory project to update and extend fiduciary standards under ERISA. As we reported in the April 6 *Benefits Byte*, the DOL's new rule broadly expands the definition of "investment advice" by extending fiduciary status to a wide array of relationships.

The first two elements of the OECD's work in this area were **an overview report on the issues** and a roundtable discussion of the experience of several countries that had undertaken initiatives to prohibit or limit advice involving commission-based transactions that were presented at the 2014 and 2015 meetings. This report is intended to be published in the forthcoming edition of the OECD's *Pensions Outlook* publication series in December 2016.

The paper begins with a broad review of the regulatory developments involving investment advice in several countries. These include the banning of all commissions in Australia (since rescinded) and the United Kingdom, the European Union (EU) proposed rules in the new Financial Markets Directive and a series of provisions in U.S. law (including the recent DOL regulations) directly affecting private pensions. The paper proceeds to offer a review of the issues that are raised in these different initiatives and identifies different ways to establish a comprehensive policy framework that includes standards to mitigate conflicts of interest, qualification standards for advisors, regulation of new technology and procedures for dispute resolution. The document concludes by offering a discussion of the policy implications of the various regulatory regimes in an effort to develop a comprehensive approach to addressing these issues.

OECD staff also provided **a PowerPoint presentation** summarizing the paper.

The Institute provided **written comments to DOL** for submission to the OECD.

The Shift from Defined Benefit to Defined Contribution Pension Plans

The report was initiated by OECD to provide some analysis of the continuing trend from defined benefit (DB) to defined contribution (DC) plans. It is mostly based on a review of the database on private pension systems that has been developed by the OECD beginning in 1995, since the inception of the WPPP. The report is also intended to be a chapter in the forthcoming *Pension Outlook* publication to be released in December 2016.

The report begins with a partial review of the literature documenting the shift from DB to DC plans in a number of high-income economies. It follows with a review of the data the OECD has compiled in its database to document trends in private pension plans across a range of member countries. This review focuses on the longitudinal data on asset levels.

The report then proceeds to a discussion of the factors that are associated with the observed changes. This review indicates that the shift is associated with changes in the legal and regulatory environment, although a limited number of other factors are discussed. The document then attempts to document differences between DC and DB plans and offer some observations about factors that may have contributed to the observed changes. The discussion of the issues is relatively narrow and in **written comments to the DOL** the Institute suggested that it be broadened to consider the interaction of both supply and demand issues behind this 40-year process.

OECD staff also provided **a PowerPoint presentation** summarizing the paper.

Policy Considerations for Annuity Products

This document is the final element of a multi-year project on Annuity Markets that has been sponsored primarily by Prudential Financial, Inc., beginning in 2012. The first phase of the project provided an overview of the various types of annuity products that are now available in OECD countries and developed a classification framework based on features and guarantees. The second stage examined several of the key regulatory and structural factors; to consider their potential impact on the development of annuity markets and the availability and use of annuity products for retirement income. The third component examined the risks associated with annuity products and how annuity providers manage these risks. The final element, a product undertaken by the OECD staff utilizing internal resources is an effort to distill lessons and policy observations about how annuity markets have developed and implications for policy, regulation and supervision.

The latest version of the document is a shorter and more policy-focused version of the draft summary report than was distributed at the December 2015 meetings. This less technical version of the previous draft is better suited to publication as a chapter in the OECD's publication series *Pension Outlook*. The Institute provided **comments to DOL** for submission to the OECD.

The draft chapter is organized around four main sets of policy recommendations:

(1) The need to establish a consistent terminology that is applied to annuity type products that will facilitate comparative analysis and a common regulatory framework.

(2) Designing a coherent regulatory framework that is consistent with the broader regulation and supervision of retirement systems and integrates pension plan regulation with the control and oversight of insurance products.

(3) Updating regulation and making it sufficiently flexible to enable and accommodate innovation in the product markets.

(4) Ensure appropriate risk management in the management of annuity products.

OECD staff also provided **a PowerPoint presentation** summarizing the paper.

Investment Governance and the Integration of ESG factors

This report seeks to provide an overview of the issues and regulatory consideration that arise in relation to incorporating Environmental, Social and Governance (ESG) factors in the investment practices of pension funds. It is the result of a directive received from the office of the OECD's Secretary General in response to a request from the French Government in conjunction with, the proposed climate change agreement developed at the United Nations conference in Paris in December 2015 that is now under consideration for approval by the signatory countries (including the United States). The report was intended to provide input for a broader report prepared for the Green Finance Study Group of the G20 for discussion at its Finance Ministers meeting, that was held in July, and as the basis for a report focused on private pension funds to be presented at the December 2016 WPPP meetings.

The report represents a convergence of two strands of thinking about (1) the role of institutional investors in facilitating macroeconomic stability following the 2008 Global Financial Crisis and, (2) their potential role in mitigating global warming. Both of these focus on pension funds as potential "long-term investors" that can have an important role in both of these areas. The report should be considered in the context of efforts by the G20 and other bodies to develop policy and regulatory frameworks that facilitate investment in long term areas such as infrastructure that can enhance stability and growth or investments that are consistent with managing climate change. Ideas that have been considered include mandates for such investments and minimizing perceived barriers. The Institute provided **comments to DOL** for submission to the OECD.

The report begins with an overview of the existing legal and regulatory frameworks that govern the management and investment of pension fund assets and a discussion of how these may be perceived to be an impediment to "green" investing or pursuing what may be deemed as desirable social or long-term economic benefits. In this context it suggests the potential development and acceptance of what is termed a "universal owner" concept that would enable the expansion of the traditional "exclusive purpose" fiduciary framework to consider long term economic growth as an element in investment strategies that would be permissible in a standard prudence framework.

The report suggests a framework for evaluating investors' duties within a broader framework that is more conducive to social and environmental considerations. It follows this theoretical discussion with a review of the research on investment outcomes that it interpreted to suggest that there is no diminution of returns when secondary and potentially non-financial objectives are included in the investment strategy.

The report concludes with a discussion of the various strategies that investors might take in incorporating ESG considerations in investment decisions, a discussion of how these have been implemented and a review of the perceived obstacles.

OECD staff also provided **a PowerPoint presentation** summarizing the paper.

Aligning Funded Private Pensions with Public Pensions

This document is the first draft of a study proposed by the OECD Secretariat and approved at the December 2015 meeting of the WPPP. It is an effort to provide a broad overview of the design and policy issues relevant to the integration of public pension systems with funded private pensions. As with several other documents presented at the recent summer meeting, the intention is to develop this report into a chapter for the forthcoming *Pensions Outlook* publication.

The document suggests a framework of analysis that is largely derived from the multi-pillar analytical model that was developed in the early 1990's and is now used in many EU, OECD and World Bank publications in a variety of forms. This model considers pension systems to be comprised, ideally, of between three and five distinct elements that are designed to complement each other by achieving income replacement, poverty alleviation and risk management objectives. These elements and their overall outcomes are then evaluated:

(1) To the degree that they are robust, equitable, and sustainable in providing retirement income.
(2) To the degree of redistribution that results from their design.
(3) To the extent that they may contribute to economic stability and growth.

The Institute provided **comments to DOL** for submission to the OECD.

This report is focused on the way in which publicly financed basic (what are sometimes called "citizens" or "zero pillar") pensions and earnings-based social security systems are implicitly or explicitly integrated with private pensions to achieve poverty alleviation, income replacement and redistribution objectives. It provides an initial and somewhat novel analytical framework organized largely around evaluating how systems manage several categories of risks (labor market, longevity, social, macroeconomic, management and political) and reviews the design of six country systems (Australia, Chile, Netherlands, Denmark, Sweden and the United States) to evaluate how the individual element and overall system addresses these risks. The paper concludes with some initial observations about how the different countries seek to achieve "complementarity" to achieve the broader objectives.

OECD staff also provided **a PowerPoint presentation** summarizing the paper.

CONCLUSION

The OECD's documents can often be of a highly academic nature. But as a basis for standards that are adopted by OECD – and its member nations – the findings and recommendations set forth can have important practical implications for both plan sponsors and service providers conducting business in OECD countries. Council members are encouraged to provide input on the issues under consideration and to provide guidance to the Institute in our role as a private sector advisor to the U.S. government delegation to OECD.

FUTURE MEETINGS

The next meeting of the OECD and WPPP is scheduled for December 5-6, 2016, in Paris.