AMERICAN BENEFITS COUNCIL

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Report from the OECD– Working Party on Private Pensions Meeting

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The Working Party on Private Pensions (WPPP), a part of the Insurance and Private Pensions Committee (IPPC) of the Organization for Economic Cooperation and Development (OECD), met recently for their annual December meeting at their headquarters in Paris. (Note: The Council is a private sector advisor to the U.S. government's delegation to the Pension and Insurance Committee of the OECD.)

The WPPP reviews private pension systems in member countries, analyzes policy and technical issues, formulates policy recommendations and promotes policy dialogue with non-OECD countries. In conjunction with the International Organization of Pension Supervisors (IOPS), the WPPP recently completed the working papers Good Practices on Pension Funds' Use of Alternative Investments and Derivatives and Good Practices for Pension Funds' Risk Management Systems. The Working Party separately issued an OECD Roadmap for the Good Design of Defined Contribution Pension Plans earlier this year.

Though no new draft guidelines were introduced at the recent meetings, it was evident that the WPPP has begun to work in new areas, including longevity risk and investment by large pension funds, particularly infrastructure investment. Other features of this meeting were an explanation of the pension systems of selected countries, and a number of presentations made by various business and labor interests. This led to an active discussion on the possible rethinking of risk sharing in pensions between employees in employers in light of the shift from defined benefit to defined contribution plans and the effect of the recent financial crisis on retirement plans of all kinds.

Country Presentations

Country presentations on pensions were provided by both Columbia and Finland. The representative of Columbia spoke of that country's minimum pension guarantee, but also the problem of low pension coverage, which was attributed to the informal employment market. The representative from Finland explained the TyEL plan, which is mandatory for all private sector employees. Currently, TyEL represents 50% of Finnish GDP.

TyEL is a defined benefit plan with a fixed accrual rate based on salary. An employer can choose to contribute to a private pension insurer under the plan, in which case it is accounted for as a defined contribution plan under the International Accounting Standards Board's IAS19, *Employee Benefits*, or to its own fund, in which case it is accounted for by the employer as though it were a defined benefit plan. It was noted that this illustrates how defined benefit and defined contribution concepts may mean different things in different contexts and countries.

The Russia delegation made a private presentation on its new pension reform proposal, the details of which are still being determined. Generally, it is to be effective in 2014, and provide that current required contributions to the mandatory private pensions will be decreased from 6% to 2%, with 4% of contributions going to the public pension system, which is a pay-as-you-go program. It was reported that there is to be a progressive replacement of the mandatory private pension component in conjunction with the development of voluntary occupational private pension schemes and increased effectiveness of financial institutions. However, many details remain uncertain. The Russian delegation is expected to make a further presentation on the changes at the June WPPP meeting.

Among the other presentations at the WPPP was a study on pension accumulations at retirement among different countries; in this case Chile, Netherlands and the United States. While it is very difficult to compare pensions between and among different countries, the study indicated that higher employment, more voluntary pension contributions and delaying retirement have a major positive impact. Another interesting conclusion of the study was that as economic conditions worsen, pensions become more redistributive.

Business and Labor Presentations

Both the Business Industry Advisory Committee (BIAC) and the Trade Union Advisory Committee (TUAC), longstanding representatives to the OECD, made presentations to the WPPP. BIAC noted the surge in defined contribution plans and the decline of defined benefit plans, recommending in particular that stakeholders should seek a redefinition of the "pension promise" through risk sharing, which could lead to better governance, increased flexibility in funding and accounting rules, and improved financial literacy by employees.

The TUAC followed with a presentation on the need for more long term, responsible investing by pension funds, and argued that there has been ineffective monitoring by pension fund investors in the past. Such concepts have previously had a receptive hearing at the OECD, as evidenced by the existing pension governance guideline that a pension governing body may be required to disclose publicly if, and if so how, environmental, social, and governance considerations are taken into account in the fund's investment policy, contained in the OECD's Guidelines for Pension Fund Governance. In particular, the TUAC called for board accountability and shareholder activism, and advocated for further pension investment in "climate related" assets such as green funds, green bonds, and clean energy infrastructure. The TUAC also announced that it has prepared a paper on what pension plans can do when a complaint against a company is filed under the OECD Guidelines for Multinational Enterprises.

A number of presentations were made by private sector representatives. Stefan Lundbergh, of the Netherlands pension administrator and advisor APG, spoke on the need for a "third way" between traditional defined benefit and defined contribution plans, referring to the Netherlands experience with risk sharing between employers and employees and the use of collective pension arrangements. He called for regulators to allow the regulatory framework to accommodate new such pension arrangements. A representative from British Telecom spoke on the trend toward more direct investment by pension funds and advocated that institutional investors such as pension funds should invest for a low-carbon economy and provide more infrastructure investment to align long-term assets with long-term liabilities.

A representative of the EU spoke on the upcoming Institution for Occupational Retirement Provision II (IORP II), which is expected to deal with European cross-border pensions and funding. They expect an economic, social and environmental impact assessment of the regulation to be completed in 2013.

Infrastructure Investment

The WPPP recently completed a report on Infrastructure Investment in New Markets: Challenges and Opportunities for Pension Funds (Working Paper No, 26, Oct. 2012). At the December meeting, infrastructure investment trends were the subject of a presentation by the Canadian Pension Fund. Much of the discussion of infrastructure investment is related to the concepts of both socially responsible investment and investing for long term liabilities.

As part of the discussions of re-defining risk sharing between employees and employers and social investing, a representative of the United Kingdom Department of Work and Pensions noted that the government had issued a consultation last month on redefining pension risk and hybrid schemes. The UK experience indicated that plans could balance fiduciary duties and socially responsible investing.

Final Observations

With this meeting, there appears to be greater coordination between the WPPP and the Working Party on Social Policy, which may start meeting in conjunction with the WPPP. OECD's Working Party on Social Policy has become particularly interested in pension sustainability. It seems likely, therefore, that meetings could see more focus on pension investment practices and social issues in the future, though there remains a strong undercurrent of interest in the question of risk sharing between employers and employees as well.