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PENSION REFORM IN THE NETHERLANDS – 'WET TOEKOMST PENSIOENEN'

Following almost fifteen years of debate, the Dutch Senate has now given the go-ahead for the largest-ever pension reform in the Netherlands, known as the Future of Pensions Act '***Wet toekomst pensioenen' (Wtp)***[1], requiring a switch from defined benefit (DB) pensions to a defined contribution (DC) system.

The Wtp entered into force on 1 July 2023 and a transition period means that social partners[2], employers and pension providers will have until 1 January 2028 to amend pension schemes.

The aim of the Wtp is to make corporate pensions more sustainable and workers with a company pension scheme will no longer face certainty in how much pension they will receive, as members will pay into individual accounts, with income levels more dependent on investment returns and individual contributions.

Funds can also offer collective DC arrangements, which aim to smooth out investment volatility for individual pension holders.

In common with many other European countries, the Dutch pension system has for a long time consisted of three pillars: the state pension (AOW), the supplementary collective pensions and the private individual pension products that each person can arrange for themselves.

However, the Netherlands, like other jurisdictions, face challenges resulting from an aging population, hence the new Wtp.

What does the Wtp mean in practice?

To help simplify what these changes mean in practice, the Dutch Government has launched an information campaign to provide reliable information about what will remain the same and what will change in the new system. This consists of general information about the new system and personal information about the own pension provision by the pension providers.

This information campaign link then provides further details at: https://www.onsnieuwepensioen.nl/.

Overview of the Wtp

Who will be impacted by the New Pension Act?

- Employers;
- Employees;
- Self-employed persons;
- Pension providers and their administrative organisations; and
- Asset managers.

For the most part, in this article, we focus on pension providers and asset managers.

What will stay the same?

The Wtp has been designed to keep elements of the present system. For example, continuing to save up for a lifetime pension and sharing the risks of old age, death and occupational disability collectively.

Pension schemes will also continue to be administered collectively, and pension providers will continue to apply a collective investment policy to limit the costs for their members. Compulsory employment-related pension build-up will also stay, which means many people will be part of the system.

What's changing?

The introduction of the Wtp will mean a transition from pension entitlements to personal pension pots, where the current defined benefits schemes will get replaced by defined contribution schemes.

Defined Benefit Scheme

- A certain fixed amount of pension benefits guaranteed to participants.

Defined Contribution (DC) Scheme

- A fixed pension premium that participants (and employers) pay, with which a personal pension capital is accrued, for the individual (in a 'personal pension depot').
- There are three variations of the DC scheme to choose from:
- (a) The solidarity DC scheme;
- (b) The flexible DC scheme; and
- (c) The DC capital scheme.

Transition plans

Employers, together with the pension funds, should produce a 'transition plan,' which forms the basis for the transition to a new pension scheme in the form of the DC scheme.

The transition plan should make clear which defined contribution scheme will be chosen and elaborate on how to deal with the conversion of current pension entitlements to the new scheme.

> *"...The new system is defined contribution based. It is a misconception that defined contribution does not match with including illiquid investments in the investment portfolio. We have researched this in depth and found that, also in the new schemes, there is room (and a need) for illiquid investments..."*
>
> **Karin Roeloffs, Head of Fiduciary Management, Aegon**

According to the Wtp, the transition (including the conversion) must be 'balanced.' This is still an undefined standard, which the social partners, pension funds and employers involved can interpret differently.

Other changes

Other changes introduced by the Wtp include, but are not limited to the following:

Abolition of the uniform premium: The premium contribution in the new defined contribution schemes will become age independent. Each participant, regardless of age, will receive the same premium percentage (a flat-rate premium).

The maximum premium is 30% of the pensionable salary.

Transitional arrangement for current age-dependent premiums: Employers who already have a defined contribution arrangement with an age-dependent premium before 1 July 2023, can use a transitional arrangement.

The employer can however continue the existing pension scheme for participants who are employed before 1 January 2027.

Minimum entry age: The statutory minimum entry age for the pension scheme will lower from 21 to 18 years, as of 1 January 2024.

Switching from one large pension fund to multiple individual funds: The Netherlands will transition from having one centralised pension fund at each pension provider – shared amongst all customers – to having individual pension pots for each participant.

This will help ensure that workers can access more personalised information about their pension accrual.

Differences between groups – Under the current rules, all workers pay the same premiums – into one collective fund – regardless of their age.

In the new scheme, pension providers should be able to take the differences between groups of members more into account when investing contributions. For example, younger groups are still far away from retirement and are able to pay contributions for years to come. This means a pension fund can take higher risks on their behalf.

Older groups have fewer opportunities to recover from lower returns and therefore need more security. Therefore, a pension fund will take less risk on their behalf.

Individual pension capital: Under the new scheme, each member's pension contribution is allocated to their individual pension capital. This is aimed at preventing people from building up too much or too little pension in relation to the contributions paid.

Pensions which are more personal – This approach makes pensions more personal. In the new system, employers and employees can also decide to set apart a specific share of the collective pension capital as a buffer for setbacks.

The rules for this buffer must be laid down in advance, so that both parties can see how it is built up, for example by setting apart a share of the pension contributions or by using a share of the investment returns.

It should also be clear when money from the collective part is moved to the personal pension assets.

Age-related defined contribution schemes:These are no longer allowed and need to be amended in flat rate defined contribution schemes. Exceptions apply for voluntary top-up and net pension schemes as well as:

- Age-based defined contribution schemes existing on 30 June 2023.
- Defined benefit plans (administrated with an insurance company) existing on 30 June 2023 which will be amended in an age-based defined contribution plan prior to the end of the transition period.

Maximum tax allowed pension contribution: The maximum tax allowed pension contribution amounts to 30% of the pensionable salary minus franchise (excluding administration costs and contributions for risk-based coverage).

- During a transition period until 1 January 2037, the maximum tax allowed pension contribution will amount to 33% for compensation purposes.[3]

Definition of partner pension: This will be made uniform.

- Partner pensions paid out upon death prior to retirement will all become risk-based and capped at 50% of the pensionable salary (regardless of years of service).
- Partner pensions which are paid out upon death after retirement will be capped at 70% of the retirement benefits.

The definition of 'partner' contained within the Wtp is: a) husband; b) registered partner; or c) partner within the meaning of the pension agreement, being the person of age who runs a joint household with the employee or former employee, unless it concerns a blood relative in the first degree, a blood relative in the second degree in the direct line, an adult stepchild or adult former foster child.

Whilst a partner's pension is defined as a monetary payment, which is fixed or variable, for the partner or former partner due to the death of the employee or former employee.

> *"Catalyzed by the shift to a defined contribution pension system, we expect millions of Dutch citizens to be more engaged with their pension savings. Therefore, it is important for Dutch pension funds to adopt investment solutions that align with the identity of their participants. This transition also presents challenges and opportunities for asset managers in areas such as communication and regulation."*
>
> Martijn Scholten, CEO Investment Management at MN

Transitional dates and next steps

Wtp provides for transitional phases, split into three areas:

By 1 January 2025 at the latest: The employment benefit phase – where social partners or the individual employer make agreements on the new pension scheme and drawing up of a transition plan.

By 1 July 2025: The accommodation phase – where pension providers must prepare an implementation plan.

By 1 January 2028: The implementation phase – where pension accrual can only take place in a DC scheme with an age-independent 'flat' contribution.

2028 may seem like a long way off, but given the substantial changes involved and approximately 70% of all employees in the Netherlands currently participating in a DB plan, there will be a lot to consider. See below for further details.

"...Even though the assets of each pension fund will continue to be managed collectively, the new pension system requires an even closer cooperation between the service providers of each pension fund: pension administrator, fiduciary manager and custodian. There will be a substantial increase in the amount of information shared between these parties in the new system to allocate to the pension pots and communicate adequately with the participants of the plans..."

Karin Roeloffs, Head of Fiduciary Management, Aegon

Pension providers and asset managers – will need to consider matters such as:

Pension providers

Changes in collective character: Which means a shift from a collective to a more individual character of the pension system. Pension providers will be required to create individual pension pots, with each participant managing their own accrued assets.

Investment policy adjustments: The Wtp gives participants more choice when investing their pension assets, depending on the type of pension agreement.

Pension providers will therefore need to offer different investment profiles and ensure there is sufficient flexibility to meet participants' individual preferences and risk profiles.

Changing role: There will be a greater emphasis on transparency and governance within the pension sector.

Pension providers will become responsible for providing clear information to participants about their pension schemes, costs and returns and the risks involved in investing.

Asset managers

Asset managers need to go through a transition together with pension funds and their pension administrators. They should prepare for things such as new IT infrastructure and an adjusted investment policy.

Analysis will need to be undertaken of existing documentation, outsourcing arrangements and how data will be exchanged.

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1. https://www.rijksoverheid.nl/actueel/nieuws/2023/07/01/wet-toekomst-pensioenen-in-werking
2. Examples of social partners include employers, employees, trade unions, and governments.
3. The 30% contribution is subject to future economic circumstances (interest and expected yield) and could be amended every five years based on a statutory adjustment mechanism.

Please contact for further details:

David Morrison
Global Head of Trustee and Fiduciary Services
david.m.morrison@citi.com
+44 (0) 20 7500 8021

Ann-Marie Roddie
Head of Product Development Fiduciary Services
annmarie.roddie@citi.com
+44 (1534) 60-8201

Amanda Hale
Head of Regulatory Services
amanda.jayne.hale@citi.com
+44 (0)20 7508 0178

Caroline Chan
APAC Head of Fiduciary Business
caroline.mary.chan@citi.com
+852 2868 7973

Shane Baily
EMEA Head of Trustee and Fiduciary Services
UK, Ireland and Luxembourg
shane.baily@citi.com
+353 (1) 622 6297

Jan-Olov Nord
EMEA Head of Fiduciary Services
Netherlands and Sweden
janolov.nord@citi.com
+31 20 651 4313

www.citibank.com/mss

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