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### Letter from Minister Donner regarding broad-scale approach towards issues surrounding pensions

In a letter to the Lower House of the Dutch Parliament on 25 May, Minister Donner explained the details of the investigations that he will undertake in the coming months into the issue of pensions in an effort to learn lessons from the current crisis.

A committee consisting of Mr. Don, Mr. Van Ewijk, Mr. Knot, Mr. Van Popta and Mr. Driessen will issue a recommendation prior to 1 September 2009 with regard to the renewed arrangement of Financial Assessment Framework (FTK) parameters.

On the basis of the findings of De Nederlandsche Bank (DNB) an investigation will take place before the end of the year into the investment policy and risk management of pension funds.

Later this year, the Minister will also draw up a memorandum in consultation with DNB in order to evaluate the FTK. This memorandum will address subjects including the volatility of coverage as a result of the market value, the issue of whether a nominal framework is hindering genuine ambitions and whether a moderation in the setting of premiums would be welcomed. The conclusion drawn from this memorandum and the specific recommendations of the Committee will be addressed when the Minister, the Labour Foundation (Stichting van de Arbeid), associations of pension providers and supervisory bodies meet in the spring of 2010.

Finally, an investigation will be conducted into the possibility of streamlining the current structure in relation to governance. This will be based on the findings of the first inventorisation of the principles of good pension fund governance.

### Progress of Phase 1 of Project IAS 19

During April of this year, the IAS Board met in order to continue discussions regarding the Phase 1 Project relating to the conceptual changes to IAS19 in the future.

The Board had taken a number of provisional decisions at an earlier stage, including direct inclusion of the profits and losses in each year. The use of Other Comprehensive Income (OCI) or the Statement of Recognised Income and Expense (SoRIE account) will no longer be permitted.

Furthermore, the pension expense must be divided into three components, namely employment cost (service cost), financing cost (interest cost) and 'other'. This last component will be shown after deduction of tax.

The Board confirmed at the most recent meeting that all results in terms of obligations and profits must be included. As far as the pension provision is concerned, it has been decided that the administration costs relating to the entitlements accrued must be included in the provision and the investment costs must be included in the expected return. This will bring an end to the current flexible arrangement in which companies are able to make their own choice with regard to the incorporation of the administration costs. This decision will not be welcomed by all parties as this will result in a further increase in the provision, at least for companies that do not yet include administration costs in the provision.

What was surprising was the decision taken by the Board not to provide further guidelines for the selection of a discount rate. A possible need for a different approach for the discount rate in deep or shallow markets was not addressed either.

### Successful implementation of risk management

On 3 March, Minister Bos gave a speech at the Eumedion Congress on the financial crisis and the level of confidence in financial institutions. In this speech, the Minister also devoted the necessary attention to the subject of risk management. "To begin with, the financial institutions must pay more attention to good governance, this being a stable governance structure with independent and professional officers/non-executives, while devoting considerable attention to risk management." The Minister's speech emphasised the importance of risk management within financial institutions. Risk management is also appearing ever higher on the agenda as far as pension funds are concerned. The question this raises, however, is how pension funds can implement risk management. There are three aspects that are essential if risk management is to be implemented successfully, namely structure, culture and information provision.

#### Structure

Risk management is not a one-off action, but is a continuous process. It should therefore be well-embedded into the organisational structure. This embedding can be achieved by making a clear distinction in responsibilities and the distribution of roles. Management is ultimately responsible for integral risk management.

#### Culture

Successful risk management requires commitment and involvement on the part of everyone within the organisation. This means that a culture must exist within the organisation in which all parties are aware of risks and how to manage those risks.

#### Information provision

Risks can only be managed effectively if all parties involved are provided with the information that is relevant to them. Such information could be included in policy documents or handbooks, for example. Management responsible for integral risk management must also be informed with regard to the status of the various risks and how these can be managed. As a provider of Pension Risk Control, Watson Wyatt provides pension funds with (permanent) support with regard to the implementation of risk management. Pension Risk Control focuses on all of the aspects referred to above.

### **Sending Uniform Pension Overviews on time**

The Netherlands Authority for the Financial Markets (Autoriteit Financiële Markten – AFM) has observed in the past year that administrators have differing views of the ‘on time’ standard in sending out the Uniform Pension Overview (UPO). In its Consultation document entitled ‘Issuing UPOs on time’, the AFM stated that it deemed it to be in the interests of participants that the UPO is issued on time and for this reason, it has provided a definition of the ‘on time’ standard. The AFM believes that by sending out UPOs on time, the provision of outdated information is avoided. In the Consultation document, it also states that in 2009, UPOs must be issued by 30 September at the latest. From 2010, a UPO will be deemed as being issued on time if the UPO is sent out no later than 30 June of every calendar year. In the event of unusual circumstances, the issuing of the UPO could be delayed, according to the AFM.

The standard of ‘on time’ has since been partially laid down by the AFM in the form of a policy regulation dated 14 April 2009. This document states that a pension administrator has fulfilled the statutory obligation to issue the annual UPO on time if the participant has received his/her UPO by 30 September at the latest.

Pension administrators will already have to take this into account as of this year by moving the issue date forward, if their UPOs are normally issued later than this date.

### **Reclaiming dividend tax on pension funds**

Until now, most European countries still treat foreign pension funds less favourably than their own pension funds as far as their tax systems are concerned. Pension funds are able to reclaim dividend tax that has been deducted from income from investments in their own country, yet the same facility is not open to pension funds registered in a different country within the EU.

However, it seems that recent European legal precedents are set to change that.

At the end of 2006, the European Court of Justice ruled that unequal treatment of cross-border dividends within the European Union is not permissible. On the basis of this ruling, the Netherlands amended the Dividend Withholding Tax Act 1965 [*Wet op de dividendbelasting*] with effect from 1 January 2007.

The Dutch Tax and Customs Administration [*Belastingdienst*] announced that it will change its system to allow repayment of dividend tax deducted from investments in the Netherlands to pension providers registered in other EU countries in the years 2003 to 2006 inclusive. It has since emerged that the Dutch Tax and Customs Administration has changed its system to allow repayment of approximately €100 million in dividend tax to British pension funds that hold investments in the Netherlands. A refund request with regard to pension funds in Germany is also pending.

The financial interest in this regard for foreign pension funds is therefore quite considerable.

Legal proceedings with regard to this issue are also in progress in other EU Member States, and as a result it will also be possible now or in the near future for pension funds registered in the Netherlands to reclaim dividend tax on investments in other EU countries. The French Supreme Court has recently ruled that a Dutch pension fund is eligible to fully reclaim dividend tax deducted in France. The Austrian Tax Office has also recently made an informal statement that it will change its system to allow full reclamation of dividend tax from EU pension funds that are eligible to do so.

By submitting a claim on time, both Dutch and foreign pension funds are able to make optimum use of the existing entitlement to reclaim, including for the years preceding 2007. In some EU countries, claims may be made for the repayment of tax paid up to 5 years ago. As already mentioned, there are considerable financial interests at stake here.

### **Z-scores 2008**

Each year, the Dutch Association of Industry-Wide Pension Funds (VB) publishes the legally prescribed ‘Z-score’. In calculating the Z-score, the five-year average of the performance of a compulsory industry-wide pension fund is compared with the return of a pre-determined benchmark. The list recently published by the VB on its website showed that 14 of the 59 compulsory sector-specific pension funds had not achieved this standard. The result of this is that participation in these pension funds is temporarily not mandatory. Companies affiliated with these sector-specific pension funds have a period of one year in which to place a pension scheme of at least the equivalent value with a different pension provider or to set up a new pension provider. The transfer of pensions already accrued will be more problematic in view of the current situation.

#### **Further information**

For more information on the matters covered in this issue of the Watson Wyatt Update, please contact Wichert Hoekert (Letter from Minister Donner regarding broad-scale approach towards issues surrounding pensions), Linda Kleynscheldt (Progress of Phase 1 of Project IAS 19), Rianne de Vos (Successful implementation of risk management), Ingeborg Agema (Sending Uniform Pension Overviews on time), Eric Heemskerk (Reclaiming dividend tax on pension funds) or Paul de Koning (Z-scores 2008).