# Looking down under

**With one of the mostly highly ranked pensions systems in the world, Natalie Tuck takes a look at how Australia's retirement benefit system operates**

Australia, it may be down-under but when it comes to pensions it's on top of the world. In the 2017 Melbourne Mercer Global Pension Index its pension system was given a B+, the highest mark achieved, putting it in joint first place with Denmark and the Netherlands.

The country's retirement provision works on a three-pillar pension system that includes the age pension, a mandatory superannuation system, and a voluntary superannuation system.

Australia's age pension, equivalent to the UK's state pension, is a means-tested benefit with a maximum amount payable of $826.20 (£461) for a single person every two weeks. The amount they receive is reduced by 50 cent (28p) for each dollar of income they receive every fortnight over $172 (£96), and become ineligible if they have an income over $1987.20 (£1109) every fortnight.

As is the case in the UK, the age at which you can claim the benefit is increasing. From 1 July 2017, the eligible age increased to 65 years and six months, and from that date it will increase by six months every two years, until it reaches 67 on 1 July 2023.

Unlike the UK, however, Australia is way ahead of the game when it comes to occupational pensions, having had a mandatory superannuation system since 1992. According to the Association of Superannuation Funds Australia (ASFA), as of 31 March 2018, the country's superannuation assets totalled $2.6trn (£1.45trn). Over the 12 months from March 2017 there was a 6.8 per cent increase in total superannuation assets.

Australia has also seen a big shift in the number of defined benefit schemes relative to the number of defined contribution schemes. In 1982/83, around 80 per cent of schemes were defined benefit, but by the millennium this had dropped to 13 per cent, and is now below 10 per cent, according to ASFA.

Unlike the UK's automatic enrolment policy, the superannuation guarantee is mandatory in that all employers must pay eligible employees 9.5 per cent of their salary; employee contributions, however, are voluntary. Under current plans the rate is expected to be in place until June 2021, and then increased by 0.5 per cent each year until it reaches 12 per cent.

Employees are however encouraged to contribute more to their funds and can do either through salary sacrifice or after tax, which makes up the third pillar in the pension system. Most Australians are also given the option to select which accumulation fund they use, rather than have their employer choose, but a default fund exists called MySuper. According to ASFA, the average superannuation balance at the time of retirement (assumed to be age 60 to 64) in 2015-16 was $270,710 for men and $157,050 for women.

Despite performing well on the Melbourne Mercer Global Retirement Index, the country's 2017 score fell slightly year-on-year from 77.9 to 77.1. One suggestion to improve the country's score was to introduce a requirement to take part of the benefit as an income stream. Savers can access their super between the ages of 55 and 65 depending on their birth date and when they retire, but do not have to purchase an annuity.

With annuity sales low in Australia, the government extended the tax-free superannuation status to a range of long-term annuity products, in an attempt to boost their popularity. The Australian Prudential Regulation Authority (APRA) reported that the annuity market hit $18.4bn in 2016, up 7.6 per cent on the previous year. It said that while annuities only account for 14 per cent of superannuation products over the 12 months to June 2016, the data shows an upward trend.

**Written by Natalie Tuck**

# Oh Canada...

**Amongst its peers, Canada fairs well when it comes to its pension system, but still the government is taking steps to improve it. Natalie Tuck takes a look**

The most recent OECD report on Canada's pension system reveals the country's future net replacement rate for retirees will be 53 per cent, but is that enough loonie to live on?

Canada has a three-tier pension system, with two of those being part of the public pension system, and third consisting of occupational and private pension schemes. The country's basic state pension is known as the Old Age Security (OAS) pension, which Gowling WLG partner Daniel Hayhurst notes is available to everyone at the age of 65.

It is provided to citizens regardless of their work history, and can be claimed whilst people are still working. However there is also the option to defer the pension for up to five years in order to receive a higher amount. Eligibility and the amount people receive are based on an individual's residency in Canada; the maximum benefit for a single person is $891.18 (£511.82) a month.

Alongside the OAS, all workers across Canada, including the self-employed, are enrolled in the Canada Pension Plan (CPP), except for those in Quebec, which have the Quebec Pension Plan, however both serve the same purpose. Benefits are based on a person's work history and their contributions, with the average monthly amount for new beneficiaries in March 2018 being $666.56 (£382.82) a month; the maximum payment possible for 2018 is $1134.17 (£651.38).

The government has recently made reforms to the CPP, which will enhance the benefits of the plan. They are set to increase from 25 per cent to 33 per cent of a worker's average monthly pensionable earnings between 2019 and 2025. The standard age to claim the CPP is 65. However, it can be taken early for a reduction (0.6 per cent for each month before 65), or deferred, which would see the monthly payment increase by 0.7 per cent for each month it is deferred.

In addition to the OAS and CPP, many employers also offer occupational pension schemes for employees to join, which Hayhurst notes are becoming increasingly defined contribution schemes. Canadians can also save privately for a pension through a retirement savings plan. Registered Retirement Savings Plans are available for savers to build up private pension savings, and they are usually tax-exempt in the accumulation phase, but subject to tax on withdrawal.

In the Melbourne Mercer Global Pension Index 2017 Canada fared well, with the country given a B ranking, for a system that has a sound structure, but has some areas for improvement. The index suggests increasing the coverage of employees in occupational pension schemes by developing a product for those without an employer-sponsored scheme.

Furthermore, the OECD's *Pensions at a Glance 2017* for Canada notes that increasing coverage of voluntary schemes is a priority for pension policy in Canada. Over the past two years, five provinces, including Ontario, implemented the Pooled Registered Pension Plans (PRPP) Act, providing a legal framework for creating and operating voluntary, low-cost, defined contribution pension plans for employed and self-employed persons who do not have access to a workplace pension.

**Written by Natalie Tuck**

# Land of the rising pension

**Japan is home to the largest pension fund in the world, but does not rank so highly for its retirement provision. Natalie Tuck explores the provisions it has in place**

Japan's Government Pension Investment Fund is the largest pension fund in the world, with assets of YEN 156,383.2bn (£1052.19bn), yet the country's pension system doesn't reach the heights of Mount Fuji.

Japan was given a D grade in the most recent Melbourne Mercer Global Pension Index, with a score of 43.5. It was the lowest grade handed out by the index, for systems that have some desirable features but major weaknesses that need to be addressed.

The Japanese pension system consists of a flat-rate basic pension, an earnings-related pension and voluntary supplementary pension plans. Japan's Nenkin (national pension) is a public pension system, in which everyone between the ages of 20 and 59 participates in. At the age of 65, participants can claim the basic old-age pension as long as they have at least 10 qualifying years, recently reduced from 25. The full benefit based on 40 years' service is YEN 779,300 (£5243.37) each year.

As well as the National Pension, public sector workers and private sector employees must join an employees' pension scheme (Kousei-nenkin) which means they will receive a pension in addition to the national pension, in proportion to their salary. Contributions for both employers and employers are tax-exempt.

The Kousei-nenkin is part of the National Pension and not classed as an occupational pension. It is not compulsory, but common for employers to offer supplementary pension schemes as well, with almost half of employees members. A national supplementary pension scheme is available to individuals and companies. There are also defined contribution schemes, based on the US' 401(k) fund, defined benefit schemes, and the National Pension Fund – aimed at those who are unemployed or not entitled to join the Employees' Pension Insurance Scheme, such as the self-employed.

The Melbourne Mercer Global Pension Index suggests that Japan could improve its score by raising the level of household saving, increasing the level of pension coverage and introducing a requirement that part of the retirement benefit must be taken as an income stream.

The index also suggests announcing a further increase to the state pension age as life expectancy continues to increase. A big issue for the country is its ageing population. It has the highest life expectancy, and the highest old-age dependency ratio among OECD countries; in 2015 there were 46 individuals aged 65 and over for every 100 people working, compared to 13 in 1975. The OECD notes that the retirement age in Japan is set to remain at 65, despite other countries in the OECD increasing the age from 64 to about 66 by 2060.

In Japan, people can choose to work longer with higher deferred pensions, to retire early and take a pension penalty or combine work and a pension after the normal retirement age. However, working and deferring the pension increases pension levels significantly, and the large bonuses are costly for the pension system, according to the OECD. In Japan, both the basic and earnings-related components are increased by 8.4 per cent for each year of deferral; adding in the effect of extra contributions and indexation of pension in payments results in an overall increase of around 11.5 per cent, which is the highest among OECD countries.

On the other hand, retiring before the retirement age has a negative impact on annual total benefits of around 8 per cent, more in line with actuarial neutrality. These bonus-penalty schemes provide large incentives for older workers to work longer in Japan. However, for those that want to continue working whilst also taking their pension, there is an obstacle; if older workers earn beyond a certain amount, the pension benefit is reduced.

**Written by Natalie Tuck**

# Going Dutch

**Theo Andrew explores the Netherlands pension market, its long road to consolidation and what makes it the envy of European pensions systems**

The sweetheart of European pensions, as many would have you believe, is the Netherlands. It is without doubt the envy of Europe, even if it doesn't see it that way.

Comprised of two pillars, the first, the state pay-as-you-go compulsory system; and the second, occupational pension funds, many of which are collective across different industries.

In order to qualify for a full state pension, you must have lived in the Netherlands for at least 50 years, from the ages 15 to 65. If you would like to retire early, then you'll be looking at a deduction of 2 per cent for every year before the age of 65. The retirement age is set to rise to 66 in 2020 and 67 in 2025.

The second pillar, which is effectively compulsory, is made up primarily of defined benefit schemes, where employees usually pay in as much as 4-8 per cent of their salary. For defined contribution schemes however, employer contributions tend to be double that of the employees.

The political hot potato in the Dutch market has been the long road to consolidation.

The number of schemes has fallen from 700 a decade ago, and now sits roughly below 250.

Willis Towers Watson senior consultant Wichert Hoekert says that he expects the number of schemes to continue to fall, whether it be through buyout arrangement with insurers, or through joining the Algemeen Pensioenfonds (APF), a vehicle that can manage funds collectively, while ring-fencing individual pension funds.

According to State Street Global Advisor senior pensions strategist for Northern Europe Jaqueline Lommen, reforms are underway to change €1.8 trillion of defined benefit liabilities into defined contribution.

Currently, DB is by far and away the largest market in the Netherlands, with a market share of 94 per cent, compared to 6 per cent defined contribution.

However, reforms ahead are looking to tilt the balance towards DC, all be it with a different design format to that we are used to in the UK.

"Our DC plans are more collective than other DC plans, as the solutions has to be a life-long payout in the Netherlands, so we came up with all kinds of creative solutions to share longevity risks … that is something where the Netherlands is ahead of other countries," Lommen says.

According to a Willis Towers Watson *Global pension asset study 2018*, the Dutch market totalled $1.6 trillion at end 2017, and out of all of the developed nations, the Netherlands has the highest pensions to gross domestic product ratio at a staggering 194 per cent, increasing by 68 per cent over the past 10 years.

A wider trend that has been developing across the European pensions market is that of factor investing, led, in part, by the Dutch and the Nordics.

Mercer global director of strategic research Phil Edwards puts this down to the fact that the large Dutch pension schemes that wield influence over their smaller counterparts.

Overall however, the Netherlands take a more conservative approach to investment strategies, with 50 per cent allocated to bonds, 33 per cent to equities and 17 per cent to other, according to the Willis Towers Watson study.

With regards to technology, the Netherlands seem much more adept at modernising their system in order to prove member engagement.

The Dutch, in one form or another, have implemented a pensions dashboard, allowing citizens to log on to a website and see all of their pensions savings in one place. Having undertaken trials throughout 2016, members are now delivered monthly updates on their pots, offering something close to 'real-time' information.

It was introduced, much for the same reasons that the industry is asking for it in the UK, in order to generate engagement with pension saving through increasing individuals' awareness of their pension rights.

In many ways, they are where the UK wants to be.

**Written by Theo Andrew**

# Swiss precision

**Theo Andrew explores the ins and outs of the Swiss pension market, how they save and what you can expect in retirement**

Known for their efficiency and time management, the Swiss pension industry is often overlooked, but there is no doubt the country offers a high quality of life for those in retirement.

Made up of three pillars, the first, the state pension, known as old age and survivors insurance (OASI), the second, occupational pensions, with private pensions making up the third pillar.

To be eligible for the OASI a Swiss national must have contributed into their Alters- und Hinterlassenenversicherung (AHV) from the moment they turned 20, until they hit retirement age, which is 64 for women and 65 for men.

Last year the Swiss public rejected plans to raise the state pension age of women to 65.

Once there, depending on the level of contributions, the level of pension can be anything from CHF 1,175 (£893) to CHF 2,350 (£1,786). By law, the maximum pension can be no more than twice the minimum pension. According to Organisation for Economic Co-operation and Development (OECD), the median household disposable income for ages 65 and over was $43,621 at the end of 2013, compared to $23,019 in the UK and $30,960 in the US.

Last year, Switzerland was rated as second in the global finance retirement index, with an overall mark of 77 per cent, the same result as the year previously.

Switzerland was the only country to rank in the top 10 in all the indices of the report, which takes into account finances in retirement, material wellbeing, quality of life and health.

The country's occupational scheme is mandatory for all employees earning over CHF 21,150 (£16,000) a year, while both employers and employees are required to pay contributions, set by auto-escalation.

Interestingly, the Swiss market operates primarily in the defined contribution market, with 85 per cent of the pensions market weighted towards DC. Despite this, DC in Switzerland has many of the characteristics that we in the UK would associate more with defined benefit pension plans.

Official statistics released last year highlighted the disappearance of DB schemes, falling from 289 in 2005 to 58 in 2015, while 15 of those were public sector pension schemes.

Minimum saving rates into Swiss pillar two defined contribution pension plans are mandated by law to rise by age, with a basic-, standard- and top-option for every age bracket. Furthermore, employers are required to pay in at least the same minimum contributions as their employees.

When it comes to drawing down, 57 per cent of people chose to partially annuitise their pension pots in 2015, according to Schweizer Pensionkassenumfrage statistics.

In part, this is due to the fact that it is mandatory for a portion of savings to be annuitised, unless that specific pension fund allows 100 per cent of the funds to be withdrawn in a lump sum.

Geneva Association director of global aging research programme, Ronald Klein, adds: "Of course, mandating a minimum annuitisation rate comes with its own complications, as pension funds argue that paying something other than the actuarially determined rate is not financially sustainable."

According to the Willis Towers Watson report *Global Pensions Assets Survey 2018*, Switzerland has no pure DC assets, where members can traditionally make an investment choice and receive market returns on their funds, and instead, act more like defined benefit schemes.

Total assets under management of Swiss pension funds hit $906 billion at the end of 2017, equating to 133.1 per cent of gross domestic product, the report said.

On the investment front, Switzerland, much like the Netherlands, generally has a more conservative approach to investing, with 33 per cent invested in equities, 34 per cent in bonds, 28 per cent in other and just 4 per cent in cash.

In general, the Swiss are just good savers. A habit which means that the average worker now saves around 19 per cent of their disposible income, whether that be for personal or pension saving. This is compared to 6 per cent in the US and 0.2 per cent in the UK.

**Written by Theo Andrew**

# The American dream

**The US began the road from defined contribution to defined benefit long before the UK. Theo Andrew takes a look at the challenges facing the US market and what makes it unique**

When you hear the saying 'everything's bigger in America', it sure does account for their pensions too. Across the pond, things are done a little differently.

The American state pension system, officially named Old-Age, Survivors and Disability Insurance programme (OASDI), is primarily paid for by employee and employer contributions, topped up with social security beneficiaries and interest earned on accumulated trust fund reserves.

The retirement ages sits between 65 and 67, while Americans on the 401(k) plan have full access by the time they are 59 years and six months old.

Statistics from Pension Funds Online Wilmington Insight says that 60 per cent of Americans in the private sector have access to retirement plans.

While in the UK the defined contribution is growing, in the US the DC market has tipped the balance. According to the Willis Towers Watson *Global pension asset study 2018*, DC accounts for 60 per cent of the asset allocations, to 40 per cent of defined benefit.

The most well-known of these plans is the 401(k). The plan allows employees and employers to make tax-deferred contributions from their salaries to the scheme.

Interestingly, new regulations in the US means employees will be auto-enrolled into existing employer DC plans if they fail to make a decision, allowing inertia to take hold and letting the default option spring into action.

According to a report by the Geneva Association, *Annuitisation: Retirement Income That Lasts A Lifetime*, the average pot size for 55-64 year-olds in the 401(k) plan is $178,963, while for those 65 and over it totals $196,907.

Despite this, the switch from DB to DC in the late 80s and early 90s mean that it is clear that the risk is now "square on the shoulders of the employee".

Global Ageing research programme director, Ronald Klein, who conducted the research, says: "Economists will argue that a reduction in costs for employers will find its way back into the pockets of employees through the increase in other benefits or higher wages. Even if this were true, the risk once borne by the employer now rests squarely on the shoulders of the employee."

According to the Willis Towers Watson study, the US took a huge 61 per cent share of assets out of the P22, the 22 pension markets covered in the study with overall assets under management of $41.3 trillion, of this the US amounted to $25.4 trillion, a 12.7 per cent growth for the year.

Over the past 20 years, US assets have more than tripled from $7.9 trillion, meaning that the US assets to gross domestic product ratio is 131.2 per cent.

According to the latest figures from Nasdaq, the recent news that interest rates have risen means the US corporate pension plans are now 92.8 per cent funded, compared to 87.6 per cent at the start of the year, primarily down to the higher rate of yields.

On an investment level, the US market tends to allocate a majority of its investments to equites (50 per cent), bonds (21 per cent) and other (28 per cent) and cash (1 per cent).

Of course, the US market is not without its problems. The global financial crisis meant a fundamental shift away from riskier equity investments and into bonds, leading to inadequate returns for many.

**Written by Theo Andrew**