INVISIBLE PENSIONS IN BELGIUM.
AN INVESTIGATION OF THE NATURE, SCOPE AND DISTRIBUTION OF THE SECOND AND THIRD PENSION PILLARS.

(Summary of 10 pages, SO/01/006 'Onzichtbare pensioenen in België')

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INTRODUCTION

In 1986 Berghman talked about invisible social security to explain the fact that social security research was overlooking important aspects of social security, due to its limited vision of social security. This limited vision devoted adequate attention to public/group social security, while neglecting labour-related and private social security.

Invisible social security has received increasing attention over the past decade, primarily in the pension sector. According to recommendations by the OECD and the World Bank, savings at the level of statutory pensions should be offset by stimulating the second and third pension pillars, where the second pillar relates to the labour-related sector and the third to the private individual sector. What is notable here is that the pension issue is approached almost exclusively as a quest for an economically effective solution to the problem of ageing in a changing socio-demographic context.

Much less is known about the social consequences of the surge in the additional pension pillars. Nonetheless, various authors point to the potential dangers of a dual society of insiders and outsiders, where some have access to an extensive network of additional pension provisions, while others are excluded from participation and have to rely solely on a modest statutory pension.

This investigation forms part of the above discussion and attempts to make the “invisible” pensions in Belgium more visible. To this end, a definition of the various pension pillars is first formulated and a clear legal explanation is given of which rulings in Belgium apply to the various pillars. Then, we assess the evolution and scope of the additional pension sector. This involves analysing the macro data available. Part three attempts to make invisible pensions in Belgium more visible by placing them within their international context. Finally, the last section deals with the question of the distribution of additional pension benefits and the existing bottlenecks in additional pension provisions are highlighted.

1. PILLARS OF THE BELGIAN PENSION SYSTEM

The scant attention devoted to access to additional provisions in general and second and third pillar pensions in particular in part has to do with a misconception about the positioning of these benefits within social security. Additional benefits do not differ significantly from first pillar provisions either in objective or in effect on the disposable income of an individual. The fact that the additional provisions are nevertheless rarely seen as a component of social security probably has to do with the integration of these provisions into the private insurance system. The discussion being conducted about second and third pillar pensions is chiefly an insurance discussion. For this reason, it is essential that we first indicate how the additional provisions should be interpreted within the social security system as a whole and that a framework is then provided within which the investigation into additional benefits can be systematically conducted. We begin this chapter with a general definition of social security and of the various pillars that can be identified within social security.

Social security is a collection of redistributive arrangements intended to reach a situation of optimum protection against collectively recognised human damage. The first pillar consists of those regulations in which redistributive flows of finance are controlled by public institutions[1]*. The second and third pillars consist of social security regulations in which the redistributive flows of finance are controlled by private institutions. The second pillar is distinguished from the third pillar by its work-related character. This is expressed through the fact that such schemes are developed within an enterprise or an industrial sector, or within a professional category or group. Every individual, however, regardless of his professional status, is free to take part in the third pillar.*

Situating this definition theoretically within human damage theory allows us to make a distinction within the concept of social security, which is being studied, according to different causes of damage. In this study, we will, in principle, only look at old age pensions, or, to use human damage theory terminology, at the function of 'age'. We do not look at derived rights, nor do we deal with damage that is the result of a loss of income associated with the cost of living.

Applied to our general definition, the second pension pillar in Belgium encompasses various forms of pension provision. Within company pensions, a distinction is made between group company pensions and individual company pensions. What is common to both forms of additional pension is that, as a rule, they are provided on the basis of a unilateral decision by the employer. *Group company pensions* are aimed at a group of employees, the entire staff or a specific personnel category. The employer is, in principle, free to decide which personnel categories to include, but he may not make any unlawful distinctions. These pensions are financed via group insurance or a pension fund. *Individual company pensions* are not aimed at a group, but at one specific employee. They are only permitted on an occasional, rather than a systematic basis. In addition to company pensions, Belgium also has a number of *sector pensions*. Sector pensions are provided on the basis of a collective labour agreement within a joint committee or subcommittee. The employers in the sector are thus obliged to include all employees covered by the scope of the collective labour agreement in the sector pension.

Within the second pillar, the self-employed have the possibility of concluding a pension agreement within the context of the *Free Additional Pension*. The contributions for these pensions are tax deductible as professional expenses within defined limits. Participation in the system is free. The members of *certain liberal professions* also have the possibility of building up an individual pension with a pension fund, which has been set up for that specific professional group. Finally, some self-employed people are entitled to the additional pension for *self-employed company managers*.

[1] Public institutions refer to what the OECD calls 'general government'. This covers the central government, local governments and social security institutions.

Within the third pillar, Belgium has two important forms of additional pension provision. The first form is *individual life assurance*. The second form of pension provision within the third pillar is the *saving-based pension scheme*. In terms of concept, a saving-based pension scheme is very similar to life assurance. The difference relates mainly to tax aspects.

The scope of the second and third pillar pensions, as well as the extent to which these have developed since the early 1980s is explained below.

2. SCOPE AND DEVELOPMENT OF ADDITIONAL PENSION PROVISIONS

First, we look at the situation regarding the second pension pillar, then that of the third pillar. In each case, we first look at premium collection and reserves, then at the contributors and benefit recipients.

Reliable data are available from 1988 onwards for premium collection for second pillar pensions among employees and the self-employed. Expressed as a percentage of GDP, in 1988 an amount equal to 1.0% of GDP was contributed. In 2000, this was 1.4% of GDP. Of this, 85% are contributions to a group insurance, 13% contributions to a pension fund and 2% contributions to an additional pension for the self-employed. A comparable picture is obtained if we show the development in reserves as a percentage of GDP. The global reserve as a percentage of GDP doubled between 1988 (8.9%) and 1999 (15.5%).

The increased absolute importance of the additional pension provisions, however, says nothing about the importance of additional pensions within pension provision as a whole. The relative importance for employees can be examined by expressing the premiums collected for the group company pensions as a percentage of expenditure on the statutory employees' pension.[2] Whereas this percentage was around 20% in 1988, by 1998 it had risen to around 30%.

We then examine the number of participants[3] and benefit recipients within the second pension pillar. It is not possible to show a clear development in the number of participants, given the unreliability of the available data. Only for 1999 is any kind of reliable figure available. In that year, a maximum of 30% of employees participated in a group company pension or a sector pension, financed via group insurance or a pension fund. Better data are available about the number of benefit recipients. These show a clear increase between 1981 and 2000. While 6.9% of retired people received a second pillar pension in 1981, this figure had risen to 21.0% by 2000.

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[2] As far as statutory pensions are concerned, expenditure is used because the earnings of the pension sector are no longer fixed, since the introduction of the Global Finance Management System (Dutch: Globaal Beheer). However, since the statutory pension system for employees works on a redistributive basis, it can be assumed that the expenditure for a given year forms a mirror image of earnings for that year.

[3] Participation indicates that the employee contributes himself and/or that the employer pays an allowance.

As with second pillar pensions, we also observe an increase in premiums collected in the third pension pillar. This increase is much more pronounced than participation in the second pillar. Premiums collected as a percentage of GDP quadrupled between 1993 (1.1%) and 2000 (4.2%). This is primarily due to the increased importance of branch 23 individual life assurance.[4] Not only is the increase in premium collection much more pronounced than for second pillar pensions, but also the absolute importance of these provisions exceeds that of the second pillar. Premium collection as a percentage of GDP is four times higher in the third pillar than the second pillar for 2000. A comparable picture is obtained by illustrating the reserves as a percentage of GDP. The global reserve as a percentage of GDP quadrupled between 1990 and 1999, from 6.6% to 18.0%. Hence the importance of global reserve in the third pillar as a percentage of GDP (18.0%) exceeds that of the second pillar (15.5%).

In order to demonstrate the relative importance of the third pension pillar with respect to statutory pensions, premium collection for third pillar pensions is compared with total spending on statutory pensions among employees, the self-employed and civil servants. Here too, the sharp increase in the importance of the third pillar pensions over the past decade is obvious. Total expenditure on third pillar pensions expressed as a percentage of global spending for statutory pensions rose from barely 10% in 1989 to almost 50% in 2000.

In order to obtain a picture of the number of participants in a third pillar pension, samples of tax returns were analysed for the years between 1992 and 1999. Since the tax returns of married people are not requested separately, we have to make a distinction between unmarried and married people. In the sample, around 14% of unmarried people were contributing to pension saving schemes in 1998, 17% to life assurance and 25% to at least one of the two schemes. These figures are 34%, 43% and 58% respectively for married people. Moreover, it is clear from a longitudinal analysis that this represents an increase compared to 1992. No information is available about the number of benefit recipients within the third pension pillar.

The importance of additional pensions has therefore risen perceptibly over the past two decades, both in absolute terms and in relation to statutory pensions. This evolution has not come out of the blue. Various factors have contributed to it.

Firstly, we should bear in mind the evolution in statutory pensions. Over the past twenty years, the statutory pension system for employees has undergone a remarkable facelift. The statutory pension was originally conceived as a form of social security and an attempt to protect earnings from income following the termination of professional activities. Gradually, however, the statutory pension has increasingly reverted to offering a basic form of protection. As a result of the generalisation of income limits, the statutory pension took on the nature of a basic pension for many employees. This evolution was

[4] In branch 23 insurance, the premiums are converted into units in an investment fund and the value of the reserve evolves with the value of the investment fund. By contrast, in branch 21 insurance the insurer guarantees a pre-determined return.

further reinforced because, between 1982 and 1997, the income limit was not adjusted to the increase in wages, but only to the increase in prices. The need for additional forms of pension build-up has therefore increased as a result of restricted pension rights within the legal system.

The restriction of services within the statutory system was the result of a number of structural financial imbalances. These were the result of a combination of various factors, such as the increased labour participation of women, the policy of early retirement and the ageing of the population. From the point of view of the government, the development of additional pensions thus represented a means of counteracting the spending catastrophe within the statutory system. This type of policy was also strongly promoted by international organisations such as the OECD and the World Bank.

The need for additional pension build-up is also related to other social developments. For instance, reference should be made to increased life expectancy at retirement age and to the increased length of education, which means that only a few people can build up a full statutory pension. We should also bear in mind the reduced importance of family solidarity, with elderly people increasingly reliant on their own incomes.

One last explanation should be sought in increased wage flexibility within companies, where the basic wage is gradually making way for a highly diversified package of benefits (employee benefits), including meal vouchers, company cars, share options, profit-sharing, etc. Additional forms of social security, such as the additional pension, are an important element of this remuneration package. In this way, the need for additional pensions within companies has been picked up within the wage context. However, the risk of unequal access to the additional pensions then arises. After all, the risk is always present that additional pensions – as components of remuneration – are reserved as bonuses for better-paid employees.

3. ADDITIONAL PENSIONS IN AN INTERNATIONAL CONTEXT

The increased importance of additional pensions is not a purely Belgian phenomenon. The economic and demographic needs which formed a major incentive for pension reform were obvious not only in Belgium, but significantly influenced the pension debate and the resulting reforms in all industrialised countries. One constant in these reforms was a strengthening of the private elements of the pension system on top of, alongside or instead of the statutory system.

In virtually every industrialised country, a mixed pension system currently exists, based on a mixture of public and private pension provisions. The discussion which continued over a long period between advocates and opponents of a private contribution in this field of social protection has therefore been overtaken by events. The actual problem is now the issue of the best ingredients for this public/private mixture.

The mutual importance of public and private elements does after all differ fundamentally from one country to another.

Some countries, such as the Netherlands, France, Denmark and Sweden, have a very extensive network of additional pension provisions, covering a large proportion of the population. In these countries, additional pensions are often provided on the basis of joint consultation at inter-professional or sectoral level and participation in these systems is compulsory for employers and employees. In other countries, most people rely on statutory pensions and additional pensions maintain a relatively secluded existence. In these countries, the focus of additional pensions lies at the level of the company.

From an international perspective, Belgium currently belongs in this second group of countries. In Belgium too, the accent within the second pillar is on company pensions, with relatively limited coverage as a result. The new Additional Pensions Act attempts to change this situation. This act creates a legal framework within which the creation of sectoral additional pension systems is encouraged. In this way, an attempt is made to make the second pension pillar accessible to a larger group of employees. The key to generalisation of the second pillar is therefore currently in the hands of the social partners.

4. INVISIBLE PENSIONS: PARTICIPANTS VERSUS NON-PARTICIPANTS

The increased importance of additional pensions raises the question, more than ever before, of the distribution of these benefits. To this end, in this section we assess the determining factors for participation in additional pensions. Using data from the Panel Study of Belgian Households, we first analyse access to the second pension pillar.

Firstly, a multivariate logistic regression shows that executives participate more than office workers, who in turn participate more than labourers. In addition, employees with a permanent contract participate more than employees on fixed-term contracts and the likelihood of participation increases as income rises. These differences are in line with expectations. It is evident from the Colla Act and its corresponding circular that a distinction by labour status, type of contract and income level is permitted. The fact that these distinctions are also observed in practice has various explanations. The fact that executives participate more than office workers is undoubtedly linked to their desirable position on the labour market. The higher participation rate of office workers compared to labourers can be explained by their stronger tradition of organising a second pillar pension. The low participation of employees on a fixed-term contract can be explained by the relatively higher administrative cost price of introducing a pension scheme for temporary employees. Finally, the link between participation and level of income is probably an apparent link. The level of income possibly reflects a further-reaching distinction by labour status than the executive/office worker/labourer distinction used in the survey conducted.

The above links refer to varying participation levels between different categories of employees *within* one company. However, additional analysis shows that differences *between* companies are more decisive for the unequal distribution of access to the second pension pillar. Thus, the sector of employment and size of the company appear to be the most significant explanatory variables. The fact that not all sectors participate to the same level can be explained by the different financial space and/or expertise of companies within different sectors. The lower likelihood of participation among small companies can be explained by the relatively higher administrative cost price of introducing a pension plan.

So far, we have only looked at the differences between insiders and outsiders. However, we have said nothing yet about the varying extent to which insiders participate. The reality of this problem can be illustrated using fiscal data. These show that, out of a sample of benefit recipients in 1999, 80% of the total volume paid out goes to 20% of benefit recipients. The causes and exact methods of this insider/insider problem cannot be examined using existing data.

We now look at the deciding factors for participation in the third pension pillar. A multivariate logistic regression analysis performed on a sample of tax returns shows, first of all, that the likelihood of participation increases with increased income. A positive link also exists between participation and age. In addition, the self-employed participate more than the non self-employed and, finally, home-owners (with and without mortgages) participate more than non-owners. These effects can partly be explained by the higher need for additional pensions of certain population groups. For instance, the self-employed have a lower statutory pension than wage-earners and those on higher incomes receive a larger pension upon retirement than those on lower incomes. Furthermore, as a result of their imminent retirement, elderly people are more sensitive to the problems of loss of income upon retirement than younger people. However, other causes are most likely also at work. For instance, an additional analysis shows that employees who participate in the second pillar do not participate any less in the third pillar. Nevertheless, we can expect these employees to have less of a need for additional pension build-up within the third pillar than the non-participants. From an objective point of view, tenants also have more of a need for the third pillar than home-owners since, during their retirement, they will also have to pay rent from their benefits.

Many probably see the third pillar as a way of saving in a fiscally advantageous way, partly separate from the genuine need for additional pension build-up. Thus, the higher participation level of the higher income group is probably also linked to the fact that they can put more money aside and that investing this money via the third pillar is also very beneficial for them, given the progressive nature of the Belgian tax system. The fact that other factors probably also play their part, such as views and/or social background, can be deduced from the fact that home-owners with mortgages participate more than non-owners. Further research should provide more detailed results.

A longitudinal analysis of participation for the period 1992-1999 shows that pension saving schemes have become more accessible. In 1999 the lower income groups and lower age groups are involved more than in 1992. As far as participation in life assurance is concerned, this democratisation is not observed.

In contrast to second pillar pensions, where the extent of participation is important, in addition to whether or not participation is observed, the problems of pension saving schemes almost exclusively deal with participation versus non-participation. The same is not true of participation in life assurance. Here, we see that the deciding factors for participation also largely determine to what extent participation takes place.

5. RECOMMENDATIONS

Based on the above, several policy recommendations are formulated.

Firstly, better accessibility to administrative information for academic research is necessary, at the levels of contribution payment, reserve creation and payment. As far as the level of *contribution payment* is concerned, a change has to take place in the way in which parafiscal deductions are made for employers' allowances for a group company pension and for the benefits for an individual company pension. In this way, a detailed picture could be obtained of whether or not participation in the second pillar is taking place and of the extent of that participation. Moreover, it should thus be possible to link this information to relevant background information about the participants. This information should be supplemented by administrative information about *reserve creation*. The creation of a database of facts about acquired reserves is necessary and not unfeasible. The new laws regarding the second pension pillar for employees and the self-employed do after all oblige the pension institutions to provide each member with a pension statement showing the acquired reserves. Based on the statements, these details can be linked to a number of background variables, as well as to company features. Moreover, central registration offers the advantage that the reserves acquired by the individuals who have pension rights with various pension institutions can be globalised, so that account can also be taken of non-contributory contracts. Finally, *payments* from the second pillar are subject to a parafiscal contribution. As a result, a database already exists of information about both statutory and additional pensions, with the possibility of longitudinal research. The necessary resources should be provided as a matter of urgency for analysing this data source.

In addition, existing surveys still have a role to play. However, some questions need to be adapted. Firstly, benefits in capital should clearly be requested. In the past, this has not been the case. Given that the majority of Belgian additional pension payments are made in the form of capital, this means that so far it has not been possible to adequately examine the Belgian situation regarding additional pensions using surveys. Secondly, since an analysis of the survey material used shows that the content of the various products is not clear to all respondents, more attention should be devoted to clarifying the content of and the difference between the different second and third pillar pensions. Thirdly, the additional provisions for the self-employed should also be investigated.

Finally, permanent monitoring and evaluation of the consequences of the New Additional Pensions Act is needed. By encouraging sectoral pension systems in this act, the aim is to achieve a generalised second pillar. The effective interpretation of the new act, however, is a matter for the social partners at sectoral level. If a substantial proportion of the sectors do not have a sector pension within a reasonable period or if the sector pensions are too selective in describing their scope, some adjustment will be in order.

CONCLUSION

This study firstly makes it clear how, alongside the first-pillar pensions, second-pillar and third-pillar pensions also need to be considered in research into social security. This observation is becoming all the more important. One typical feature of these pensions is that the government provides a social benefit in the form of a tax exemption. As a result it is mainly people with higher incomes who enjoy these benefits. The question therefore arises as to whether, and to what extent, the increased importance of these types of pensions can be seen as socially fair.

To answer this question, supplementary pensions must be considered in comparison with statutory pensions. During recent decades we have observed a gradual evolution within the first pensions pillar from a Bismarckian wage-related pension towards a kind of basic pension. The rapid growth of the supplementary pension pillars can therefore be seen as a reaction from the private sector, encouraged by tax exemptions, seeking to make pensions more income-related. In view of the original aim of our social security system to guarantee a pay-related income guarantee, an increase in the supplementary pillars therefore does not have to constitute a social problem.

If, however, full and maximum access to these types of supplementary pensions is not available, the development outlined above should be seen in a different light. Our analysis of access to the second pillar revealed that we can by no means speak of full accessibility and that the likelihood of participation is not evenly distributed. The most important variables this concerning relate to the company where the worker is employed. For this reason, it is important to do something about opening up second pillar provisions to employees in all companies, without distinguishing by size and/or sector to which the company belongs. It remains to be seen to what extent the New Act on Supplementary Pensions can respond. Much will depend on the social partners.

However, the increased importance of the additional pension provisions, more than the emergence of the second pillar, seems to be attributable to the rise of the third pension pillar. The fact that these provisions are in theory accessible to all does not mean that they cannot be an object of social inequality. Formal access is not yet genuine access. In reality, those who participate are chiefly those on higher incomes, the elderly, the self-employed and home-owners. This higher participation cannot exclusively be explained by an objective need for additional pension creation. Moreover, provisions in the third pillar are in no way coordinated with the other two pillars. As a result, no supervision is exercised over the extent to which the build-up of a fiscally attractive additional pension within the third pillar is related to the actual loss of income upon retirement. Finally, the social objective of income preservation after retirement is difficult to reconcile with the fact that the majority of the third pillar provisions are paid out in the form of capital. These elements mean that, from a social policy angle, serious questions should be asked about giving tax benefits to third pillar pensions.