LESSONS FROM THE PAN-EUROPEAN PERSONAL PENSION PRODUCT (PEPP)

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1. INTRODUCTION

Europe, like most other continents, is ageing at a rapid pace. In 2060, there will be two people at a working age for every pensioner, in comparison with four people at a working age at the present time.[1] This puts the sustainability of the traditional pension systems across Europe under significant pressure, despite reforms that are currently underway in many European countries.

Some European Member States, like The Netherlands, have a large (mandatory) occupational second pillar, while the coverage of a second pillar in some Member States, such as France, is less significant.

Only 27 percent of all EU citizens presently have a personal pension product (third pillar).[2] There are only a limited number of third pillar pension product providers across Europe and the majority (83%) of retirement savings are currently built up with insurance companies.[3] In Eastern Europe, many employees simply do not have any pension arrangements at all.[4]

The EU therefore felt the need to solve the retirement security problem facing several European nations on a European scale. In this regard, the European Commission (which proposes EU legislation) of the EU published a proposal in 2017 for an EU regulation (a directly working and applicable EU Law) for Europe for a new individual pension product – the Pan European Pension Plan, or PEPP. The PEPP sought to introduce a portable individual retirement account that can be rolled out across the European Union (EU) and can also be offered to citizens worldwide.

EIOPA (the EU pensions supervisor) accordingly sketched the contours of the PEPP.[5] In early April 2019, the PEPP was adopted by the EU legislature and came into force in 2022. This was a remarkable achievement, especially considering that it concerns European pension legislation, a controversial subject in the EU.

[1] See for more detail : Commission proposal for a regulation on a pan-European personal pension product (PEPP), to be found at: https://finance.ec.europa.eu/publications/commission-proposal-regulation-pan-european-personal-pension-product-pepp_en#:~:text=The%20PEPP%2C%20one%20of%20the%20key%20measures%20of,regulation%20on%20a%20pan-European%20personal%20pension%20product%20%28PEPP%29.

[2] H. van Meerten, T.J.B. Hulshoff, 'PEPP: Catalyst for pension innovation?', SSRN 2022: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4278689

[3] H. van Meerten, T.J.B. Hulshoff, 'PEPP: Catalyst for pension innovation?', SSRN 2022: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4278689

[4] H. van Meerten, E. Schmidt, Compulsory Membership of Pension Schemes and the Free Movement of Services in the EU (June 25, 2017), European Journal of Social Security, 2017. Available at SSRN: https://ssrn.com/abstract=2992298 or http://dx.doi.org/10.2139/ssrn.2992298

[5] H. van Meerten, Een Europese Pensioenunie. Rotterdam, 2016. Available at (in Dutch): https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2689754.

By 2023 several PEPP providers are already active in the EU and the expectation is that the number of such providers and distributors will only increase.

1.1 The PEPP Overview

The PEPP will complement the current applicable rules at the EU and national levels by adding a portable, pan-European framework for pensions for (a collective of) individuals who want to use this additional retirement savings option. The PEPP is a European personal pension product, somewhat similar to 'bank savings'. It is a voluntary pension savings product that offers individuals a new pan-European option to save for retirement through investments, with or without the help of an employer.

The PEPP is a simple, transparent, and inexpensive pension product. It has a set of harmonized rules – except for the tax regimes - that are independent of the legal systems of the EU Member States. Difficulties that may arise with cross-border pension institutions (such as a difference in mortality rates) will hardly occur, if at all, with the PEPP.

The PEPP is also a welcome improvement in terms of the transferability of pension rights and ownership rights as conflicts about retirement savings and benefits usually arise due to lack of clarity on such issues.

The long-term expectation is that as the PEPP becomes more established, it will also help achieve the EU's capital market goals.[6] Furthermore, it will help to cope with the problems that Europe's huge aging population is creating for existing systems and for the public finances of Member States. The PEPP therefore is a top priority for the EU.

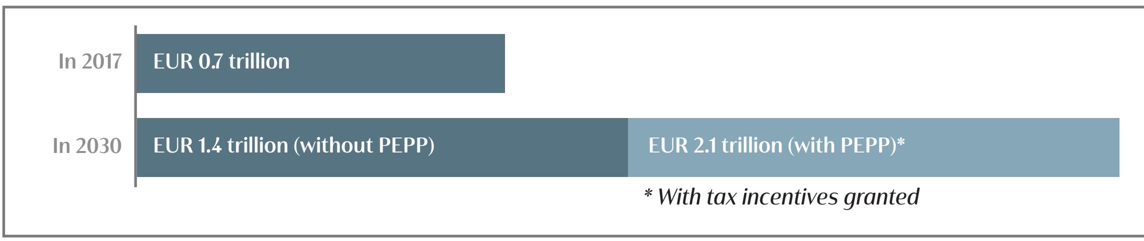
This chapter outlines the lessons from both design and the early efforts to implement the PEPP against the backdrop of political and legal difficulties. It also describes the PEPP architecture and the possible pitfalls that should be avoided by other regions that

[6] See for more information: H. van Meerten, J.J. van Zanden, 'Shaping the Future of Retirement: Aspects of Sustainability', European Journal of Social Security, 2021, 8 (online at: https://journals-sagepub-com.proxy.library.uu.nl/doi/full/10.1177/13882627211028246)

may contemplate a similar strategy. Subsequent sections describe the ‘EU (law) basics’, the PEPP product features, and key lessons for pension policy makers and regulators from other regions that are contemplating regionally portable pension solutions for overseas migrant workers.

This diagram[7] shows the potential additional retirement assets that the PEPP can help generate.

Personal Pension Product Assets Under Management in EU28



2. THE EU AND PENSION LAW BASICS[8]

The structure of the EU is necessary to put the PEPP into context.

2.1 General

The treaties on which the EU is based consist *grosso modo* of two parts: The Treaty on the European Union (TEU) and the Treaty on the Functioning of the European Union (TFEU).[9] Too little attention is paid to these important treaties in national pension discussions, despite the fact that we have known, since 1963, that these treaties are supranational and assume priority over national legislation.

The famous *Van Gend en Loos* (1962) Case cannot go without reference. In that case, the European Court of Justice (EU Court of Justice, the ECJ) held that European law constitutes its own autonomous legal order, with (so the ECJ held later) priority over conflicting national law.[10]

As a result, and over the course of time, a great number of European laws are directly or indirectly applicable to pensions,

[7] Source: European Commission

[8] See for more detail: H. van Meerten (et.al), ‘EU Pension Law’, Amsterdam University Press, 2019

[9] The protocols, addendums, etc., I leave aside.

[10] C-26/62, Van Gend & Loos, C-6/64, Costa/ENEL.

and these laws are based on the so-called 'EU free movement provisions'. Let me explain this further.

2.2 EU Laws

There are two main instruments under EU Laws.[11] The first is a 'regulation' that has general application, is binding in its entirety, and is therefore directly applicable in all Member States. The second is a 'directive', which is binding upon each Member State to which it is addressed, as to the result to be achieved, but leaves to the national authorities the choice of form and method. Therefore, a directive leaves much more room for Member States to add all kinds of national specificities ('gold plating'). Cross border activity between EU Member States is therefore harder to achieve because the legislation of the Member States differs, even though there is an EU legislation.

The PEPP is a regulation and hence gives much less leeway to the Member States, especially when the EU legislator specifies nearly every aspect in the regulation (except taxation as described below), such as investment strategy, costs, information, etc. Therefore, the PEPP is a special kind of regulation, a so-called 'second regime' that prevents Member States (as much as possible) from 'gold plating'.

EU regulations and directives are established in a complicated procedure. In principle, three institutions of the EU are involved in this legal process: the European Commission, the European Parliament, and the Council of the EU. The Commission submits a proposal, after which the Parliament and the Council must reach an agreement in order to adopt the legislative act. Furthermore, the Court of Justice of the EU ensures, among other things, that the EU law is followed and implemented correctly. The work of these four institutions is complemented by the work of another three EU institutions: the European Council, the European Central Bank, and the European Court of Auditors. These institutions are respectively responsible for the general political direction, the financial aspects, and the external audit aspects of the EU.

[11] *For more information on EU law: P. Craig, G. de Búrca, EU Law. Oxford, 2020.*

In the EU, there is in-principle free movement of workers, goods, capital, and services. Article 56 of the Treaty on the Functioning of the European Union (TFEU) plays an important role in this discussion as it provides that “services should be freely provided within the EU”. [12]

2.3 IORP Directives[13]

The IORP I Pensions Directive was the first attempt in 2003 to create an internal market for occupational pension provisions in which the occupational pension providers must be free to perform services and investments throughout the EU.[14]

The IORP I Directive regulates funded pension institutions that provide occupational pension schemes (i.e., Institutions for Occupational Retirement Provision, or IORP). A pension institution that qualifies as an IORP under the IORP Directive may, based on the supervision carried out in the Member State in which it is established, provide cross-border pension services (i.e. it has a IORP ‘Passport’). This means that when an IORP is established in Member State A, it can automatically offer pension services in Member State B.

The IORP I directive sets a number of general solvency and financing requirements, certain investment rules (based on the prudent person principle) and general administrative and governance requirements. These are just general rules which provide for minimum harmonization of pension entities, allowing Member States a considerable degree of freedom to elaborate the rules on the IORP in question at a national level.

The IORP II Directive replaced the IORP I in 2016 and contains much more detailed information.

In its Explanatory Memorandum, the European Commission set out four specific objectives in revising the IORP directive: (i) removing remaining prudential barriers for cross-border IORPs; (ii) setting requirements for good governance and risk management; (iii) providing clear and relevant information to members and

[12] *H. van Meerten & E. Schmidt, ‘Compulsory membership and the free movement of services in the EU’, European Journal of Social Security 2017, Vol 19(2).*

[13] *See for more detail: H. van Meerten (et.al), ‘EU Pension Law’, Amsterdam University Press, 2019.*

[14] *C-343/08, Commission/Czech Republic, para. 43. See also: C-678/11, Commission/Spain.*

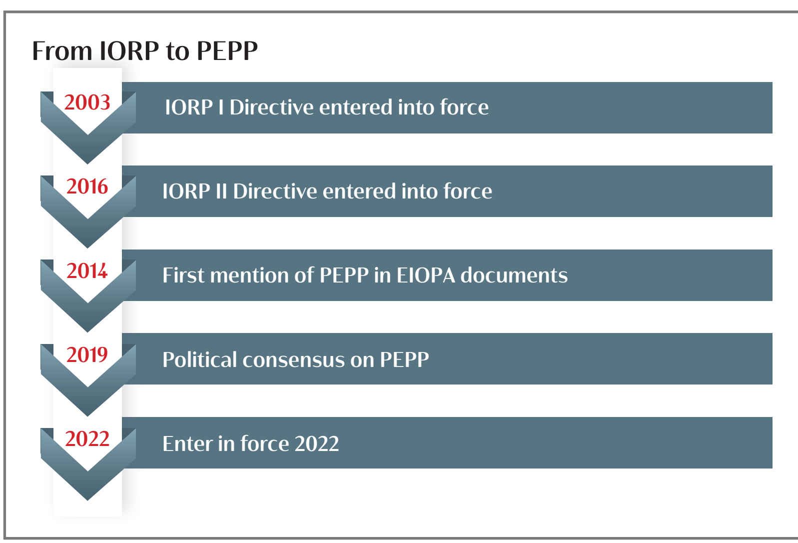
beneficiaries; and (iv) ensuring that supervisors have the necessary tools to effectively supervise IORPs.[15]

However, in 2023 we can conclude that the IORP II did not meet these goals. In fact, it is safe to say that IORP II makes cross-border activity harder, not easier.[16] The number of cross border pension providers is way below expectation[17] and the European market for pensions has still not been sufficiently developed, after numerous attempts.[18]

The differences among the national pension rules of the Member States form an obstacle in the context of developing simple, cross-border pension rules. The IORP directive did not take this away. This not only prevents, for example, a cost-efficient pension build-up by an employee working abroad, but the differences among national rules also restrict a local pension participant in choosing a pension fund established abroad.

EU regulations however, based on the 'free movement' provisions, can help break down these barriers. It is in this light that we need to view the PEPP.

The following diagram[19] shows the development of the European Pension market thus far.



[15] The Explanatory Memorandum to the IORP II Proposal, Detailed explanation of the proposal

[16] See: 'Position Paper on Possible Legal Inconsistency With EU Provisions on Cross Border Transfers of Pension Schemes With Regards to the Establishment of Excessive and Unjustified Majorities of Members and Beneficiaries Left to National Legislations (Art. 12, Paragraph 3 of the IORP II Directive)', https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3320500.

[17] '33 cross-border IORPs were active in the European Economic Area (EEA) at the end of 2020. This number represents a substantial drop compared to the 73 active undertakings in 2017, primarily reflecting the United Kingdom's departure from the European Union.': https://www.eiopa.europa.eu/eiopa-analyses-trends-cross-border-iorps-2021-12-03_en

[18] See for an overview, H. van Meerten, EU Pension Law, op. cit.

[19] Source: Hans van Meerten

3. THE PEPP[20]

3.1 General

The European Commission published a new proposal for a European regulation (a directly operative and applicable EU-law) for the Pan European Pension Plan (PEPP) in 2017. The proposal appeared at the beginning of April 2019 and the technical underlying legislation became public at the end of 2020. The PEPP was permitted to be offered since March 2022.

The PEPP is supplementing the rules both at an EU-level and at a national level by adding a pan-European framework for individuals who wish to voluntarily use a supplementary retirement saving option. The PEPP creates a label for a European personal pension product, somewhat similar to the tax-efficient blocked bank savings account or an annuity. It is a voluntary retirement savings product that offers individuals (including employees, self-employed persons and directors and major shareholders) a new pan-European option to save and invest for their future, with or without help from an employer. The PEPP does not contain opaque redistribution mechanisms. This can make PEPP a simple, transparent, and low-cost pension product. Importantly, although PEPP is an individual pension product, it can also be offered at a collective level, for example by an employer.[21]

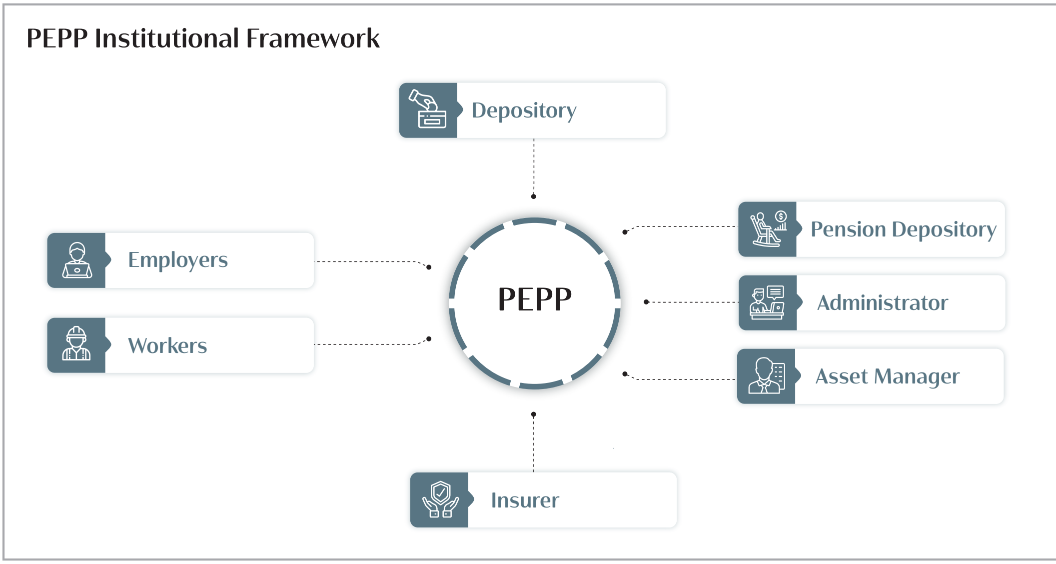
As mentioned above, the PEPP is in part harmonised in EU-regulations and is a so-called second regime: a regime that stands apart from the legal systems of the EU Member States. Difficulties that may arise with cross-border pension institutions (for example between the Netherlands and the UK), such as conflicts between the legal systems and social or employment law, will in principle hardly occur with the PEPP.

The PEPP is also a welcome improvement in terms of the transferability of pension rights and proprietary rights. The current conflicts between young and old about pension savings arise

[20] Some parts of this chapter appeared in Dutch: H. van Meerten, 'Het nieuwe pensioenakkoord: de PEPP', VBA, 2021.

[21] Idem.

because there is ambiguity about this matter. The diagram below[22] captures the PEPP at one glance:



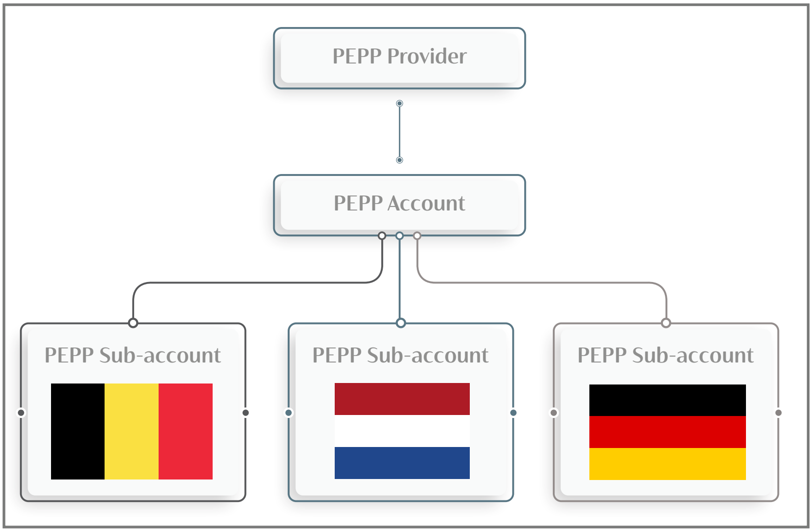
3.2 Transferability Service

PEPP-providers can offer a so called 'transferability service' to PEPP-savers with different national 'compartments'. Accumulated savings of a PEPP-saver can easily be transferred from one to another member State within the EU without having to switch savings to another State as the PEPP provider does not change. If the PEPP-saver moves to another member State, where the PEPP-provider does not have a 'compartment', the PEPP-saver has an option to switch to another PEPP-provider, without incurring any cost. Every PEPP-saver also has the right to change the provider on the retirement date. Obviously, this portability service can also be used within a member state, when a PEPP-saver changes jobs, for example. In this case, the new employer in the State can keep depositing contributions, if desired.

The PEPP only relates to the accumulation phase. Unless otherwise provided by PEPP-regulations, the conditions regarding

[22] *Source: Hans van Meerten*

the decumulation phase and payments to national sub accounts are determined by the Member States. This relates to a pension account that a PEPP subscriber may have in a particular country. Subscribers can opt for one or more of the following forms of benefit payments, depending on national tax laws governing pensions: (a) annuities; (b) lump sum withdrawals; (c) phased withdrawals; or (d) any combination of these forms. The following diagram[23] reflects the concept of compartments or (sub)-accounts.



3.3 PEPP Service Providers24

The following types of entities[25] are permitted to provide services under the PEPP:

a. Credit institutions (banks);

b. Insurance companies;

c. Institutions managing occupational retirement plans;

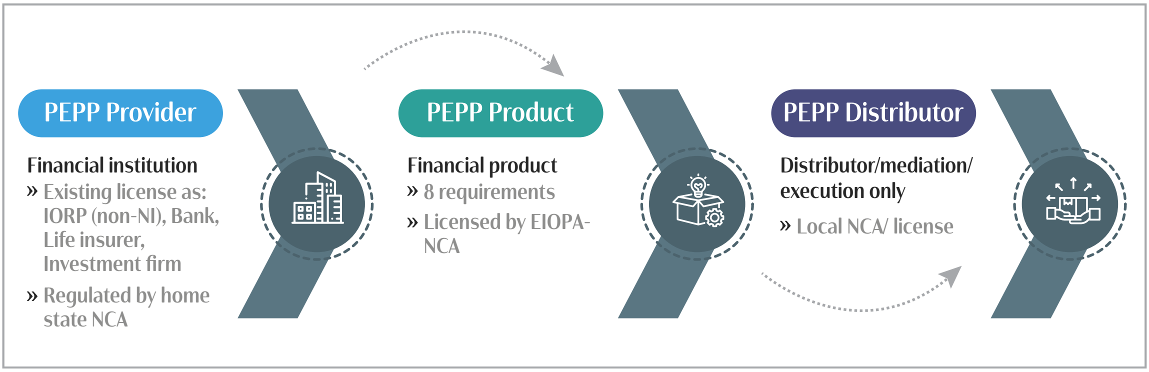
d. Investment firms or asset management companies; and

e. Alternative investment management companies.

[23] Source: Hans van Meerten

[24] Article 6 PEPP Regulation.

[25] Source: Hans van Meerten en Tjitsger Hulshoff, see footnote 2.



3.4 Basic PEPP

There are two types of PEPPs: the basic PEPP, and the non-basic PEPP. The original Commission proposal of 2017 did not make this distinction. A PEPP can take many forms, from a 'Solvency II PEPP' with hard guarantees, to a UCITS/Tontine PEPP, with a risk-sharing mechanism. In other words, the PEPP-provider has the choice of whether the PEPP offers a guarantee of capital with a security mechanism of 99.5% or takes the form of a risk-mitigation technique.

3.5 Investment Policy

The PEPP regulations contain various investment policy provisions. PEPP-providers may offer PEPP-savers up to six investment choices. These investment options must include at least the basic PEPP and can also include alternative investment choices. All investment options are designed by PEPP-providers on the basis of a guarantee or a risk limitation technique that provides adequate protection for PEPP-savers. The basic PEPP is subject to strict requirements. For example, it must be based on a lifecycle investment strategy, or on a guarantee. The provision of guarantees is subject to the relevant sectoral law applicable to the PEPP-provider.

An individual PEPP product needs to have an explicit pension purpose. For the most part, the subscriber and the provider can put the PEPP together themselves. There are various options to choose from, which are designed using investment protection techniques that can ensure a high level of consumer protection.[26] The duty of care lies in all cases with the PEPP-provider.

The basic PEPP offers a standard investment option with a capital guarantee. For the design of the capital guarantee, various techniques exist. This, however, is not a Solvency II guarantee (with a 99.5% security measure, that is described in section 4).

To ensure optimal product transparency, PEPP-providers must prepare a 'PEPP key information document' (PEPP-KID) for the PEPPs they develop, before these can be distributed to PEPP-savers. PEPP-providers are responsible for the accuracy of this document. Where a PEPP-provider offers an alternative investment option, relevant key information documents should be provided, which may also contain references to other documents, such as for the basic PEPP.

3.6 PEPP Regulation

As mentioned above, PEPP regulations provide for a 'basic' PEPP and a 'non-basic' PEPP.[27]

The basic PEPP should, according to the PEPP regulation, be a 'safe' product and should function as a default investment option. It could take the form of either (i) a risk-limitation technique allowing a PEPP saver to retrieve the invested capital or (ii) a guarantee on the invested capital. These techniques also apply to the non-basic PEPP.

A risk-mitigation technique may be (a) a conservative investment strategy, or (b) a life cycle option, where the overall risk is gradually reduced. Guarantees provided under the standard investment option should at least cover the contribution made during the accumulation phase, after deducting all fees and charges.

[26] *H. van Meerten, A. Minto, J. van Zanden, 'Picking Up the Gauntlet – Europe's Answer to the 'Pension Problem': The PEPP', Open Review of Management, Banking and Finance, 2020, 11.*

[27] *H. van Meerten, Het nieuwe Europese pensioenakkoord: het PEPP, op. cit.*

Guarantees may provide full or partial protection against inflation. A guarantee on the invested capital must be due at the beginning of the decumulation phase and, if applicable, during the decumulation phase. The much-discussed '1% fee cap' applies only to the basic PEPP and amounts to 1% of the accrued capital. Furthermore, it includes all costs except the 'guarantees', as shown below.

Article 46 of the PEPP regulation stipulates that the applicable risk-limitation techniques may include provisions for:

- the gradual adjustment of the investment allocation to limit the financial risks of investments for cohorts in accordance with the remaining maturity (life-cycle strategy);
- the establishment of reserves of contributions or investment results, which are allocated to PEPP-savers in a fair and transparent manner, in order to limit investment losses; or
- providing appropriate financial guarantees to protect against investment losses.

PEPP-savers are permitted to switch to a different savings option every five years.

3.7 PEPP Level 2[28]

At the end of 2020, the European Commission issued the aforementioned draft PEPP Level 2 texts. These draft delegated regulations give further substance to a number of technical details of the Level 1 PEPP regulation:

- Chapter I sets out the requirement for information documents in electronic format, with specific online features such as layering;
- Chapter II introduces general requirements for both presentation (in a standard format), and the content of the PEPP-KID, including sections on 'What kind of product is this?', 'What are the risks and what can I get in return?', 'What are the costs?';

[28] These can be found here: https://finance.ec.europa.eu/regulation-and-supervision/implementing-and-delegated-acts/pan-european-personal-pension-product-regulation_en

- Chapter III lays down the requirements for the evaluation, review and provision of the PEPP-KID;
- Chapter IV sets out the requirements and standard format for the presentation of the PEPP statement;
- Chapter V lays down the requirements for fees and charges for basic PEPPs; and
- Chapter VI contains the requirements for risk mitigation techniques, such as objective, lifecycle investing and the need to build reserves, minimum return guarantees and a holistic assessment of risk and return.

I now focus on chapters V and VI, as this is where the biggest changes with regard to investments can be expected.

3.8 Risk mitigation techniques

While using risk-mitigation techniques, providers are required to set an investment strategy that matches the specific pension objectives of the PEPP-saver(s). A PEPP-provider is required to design the risk-mitigation technique in a manner that achieves the objective of providing a stable and adequate future retirement income from the PEPP, taking into account the expected remaining duration of the individual accumulation phase of the PEPP-saver, or group of PEPP-savers, and their choice of decumulation. To achieve this objective, the risk-mitigation technique is designed as follows:

a. it is ensured that the expected loss, defined as the 'shortfall' between the projected sum of contributions and the projected accrued capital at the end of the accumulation phase, does not exceed 20 percent in the stress scenario corresponding to the fifth percentile of the distribution;
b. it is aimed at outperforming the annual inflation rate by at least 80 percent over an accumulation period of 40 years; and
c. the results of stochastic modelling shall be taken into account.

For the basic PEPP, if the PEPP provider does not offer a capital guarantee, the provider shall apply an investment strategy that guarantees that, taking into account the results of stochastic modelling, capital is recovered with a probability of at least 92.5%, both at the beginning of, and during the decumulation phase. If the remaining accumulation phase is 10 years or less at the time of drawing down the basic PEPP, a probability of at least 80 percent may be used when applying the investment strategy. When designing a risk-mitigation technique for a group of PEPP-savers, the PEPP-provider shall design the risk-mitigation technique in such a way as to ensure fair and equal protection for each individual PEPP-saver within the group and shall build in disincentives against opportunistic actions by individual PEPP-savers within that group. PEPP-providers shall ensure that any performance-based remuneration of persons acting on behalf of the PEPP-provider and applying the risk-mitigation techniques, encourages the achievement of the objective of the risk-mitigation techniques.

3.9 Basic PEPP and Costs

As per regulations, the basic PEPP is a safe product that constitutes a standard investment option. Every provider must offer a basic PEPP. This is designed by PEPP-providers on the basis of a guarantee of the capital due at the beginning of the decumulation phase, as well as during the decumulation phase, if applicable, or on the basis of a risk-mitigation technique that is consistent with the objective of allowing a PEPP-saver to recover the capital.[29]

Article 45 of the regulation states that the costs and fees to be charged, shall not exceed 1 percent of the accrued capital. Article 12 of the Delegated regulation states that the charges and fees, to which in article 45 (2) of the regulation is referred, in respect to the saver's capital accumulated in the basic PEPP at the end of the relevant year, shall include all costs and fees actually incurred,

[29] *Article 4 PEPP Regulation*

whether directly at the level of the provider, or at the level of an outsourced activity, including appropriate general costs and fees relating to the saving in the basic PEPP and the distribution of the basic PEPP. Such costs and fees all relate in particular to[30]

a) administrative costs;

b) investment costs; and

c) distribution costs.

Costs and fees associated with additional elements or features of the basic PEPP that are not required by Article 45, and any costs and fees associated with switching services described in the PEPP regulation shall, in principle, not be included in this calculation. With regard to the transfer service, which is a crucial component of the PEPP, savers can access their personal information, held by the transferring or receiving PEPP-provider, free of charge. The transferring PEPP-provider will provide the information requested by the receiving PEPP-provider without charging the PEPP-saver or the receiving PEPP-provider any fees. The total fees and charges that the transferring PEPP-provider charges the PEPP-saver for closing the PEPP account held with it, are limited to the actual administrative costs incurred, and cannot exceed 0.5 percent of the corresponding amounts or monetary value of the assets in kind to be transferred to the receiving PEPP-provider. Member States may set a lower percentage for these fees and charges. The transferring PEPP-provider shall charge the receiving PEPP-provider no additional fees or charges. The receiving PEPP-provider may only use the actual administrative costs and transaction costs of the switching service.

3.10 Cost and Fees for Guarantees of the Basic PEPP

If the basic PEPP provides for a guarantee of capital that may be expected at the beginning of the decumulation phase, and during the decumulation phase (as referred to in article 45(1) of the PEPP regulation), the costs directly associated with that capital

[30] *See for more detail: H. van Meerten, A. Wouters, 'The PEPP Regulation (PEPPR): Pepper for the Capital Markets Union?', Zeitschrift für Versicherungsrecht, 2019, 14; H. van Meerten, A. Minto, J.J. van Zanden, op. cit.*

guarantee will not be included in the cost referred to in article 45(2) of the PEPP regulation. The PEPP Provider shall explicitly and separately disclose the costs for the capital guarantee in the section 'What are the costs?' in the PEPP-KID and in the section 'How has my PEPP changed over the last year?' in the PEPP statement. When appropriate, the PEPP-provider shall be able to provide, at the request of the competent national authority or EIOPA, evidence that the costs in question are directly related to the capital guarantee.

3.11 Lifecycle Investing

If a risk-mitigation technique is used that adjusts the allocation of investments in order to limit the financial risks of investments in accordance with the residual maturity, the PEPP-provider shall give average exposures to equity and debt instruments, but shall ensure that all potential sub-portfolios corresponding to the phases of the life cycle investment are invested in. The PEPP-provider shall design the life cycle investments in such a way that the PEPP-savers that are the furthest from the expected end of the accumulation phase shall contractually invest in long-term investments that provide higher investment returns due to their specific higher risk and return characteristics, such as low liquidity and equity characteristics. For those PEPP-savers who are the closest to the expected end of the accumulation phase, the PEPP-provider shall ensure that the investments are predominantly liquid, high quality and have fixed investments returns.

3.12 Method for Calculating Costs

In the PEPP-KID, the PEPP-provider is required to present the total annual costs, which include all costs incurred and calculated within 12 months, as an amount and as a percentage of projected capital accrued after 12 months. If necessary, these amounts may be calculated as the average total annual costs over the lifetime of the PEPP agreement. The calculation of the compounding effect of the costs is made on the basis of an accumulation period of forty years, assuming a monthly contribution of EUR100, and on the projected accumulated capital in the best estimate scenario.

In the PEPP summary, the PEPP-provider presents the estimated effect of costs on the final PEPP benefit using the 'welfare loss' method. The 'welfare loss' is calculated as the difference between the projected accumulated savings at the end of the accumulation period with costs, and the projected accumulated savings at the end of the accumulation period in a no-cost scenario.

3.13 Taxation

A final word about the Tax regime. The tax regime for PEPP is not harmonised in the regulations. Taxation of pension schemes is a competence of individual Member States. Therefore, the national tax regime applicable to the PEPP, the PEPP provider and PEPP distributor continues to apply to the pension schemes. In principle, as the PEPP regulates only the accrual phase, taxation should not be an issue as the accrual phase is usually tax exempt across most EU Member States and only pension pay-outs are subject to tax. However, no distinction can be made in the tax treatment between PEPP and national third pillar pension products, during the the accrual and benefit pay-out phases. This tax equality can be enforced under EU case law. The Skandia[31] ruling of the EU Court considered:

"Article 49 EC precludes an insurance policy taken out with an insurer established in another Member State which meets all the conditions laid down by national law for supplementary pension insurance, except the condition that it be taken out with an insurer established in the national territory, from being treated differently for tax purposes, with income tax consequences which may be more unfavourable, depending on the circumstances of the case.'

With this ruling in hand, the same benefits that apply to a comparable national pension product can be enforced for a PEPP.

[31] *C-422/01, Skandia.*

4. CONCLUSION AND CLOSING REMARKS

This chapter outlined what the PEPP is and how a PEPP can be offered. Also, it deals with some EU Pension Law 'basics'. I believe that the PEPP has interesting characteristics. It introduces simple pension transfers, clear property rights, standardised investment options and advice, and an internationally portable personal pension account within EU Member States.

An exclusively digital PEPP offer, which consumers could set up and access online from anywhere in the world, is imminent. Some providers are already developing this. '*PEPP on WhatsApp*' (similar to the digital micro-pension platform built by pinBox Solutions and WhatsApp for India and Kenya) is something that could be explored further.

If the PEPP follows the trends on costs and charges observed for the US '401(k)' or the Dutch PPI (the second pillar D.C. vehicle), where costs of DC pension products reduced by as much as 50 percent[32], the PEPP should eventually lead to considerable improvements in retirement benefits for savers.

As the PEPP gathers momentum and is offered by more asset managers, it can help achieve the EU's capital markets development objectives while more effectively addressing the fiscal challenges that Member States are facing due to their huge ageing population. This is a top priority of the EU.

The rationale, design principles, features, and administration of PEPP, as also its early implementation experience, has several important lessons for other regional blocs in Africa, as also for other continents. Based on the experience with PEPP thus far, there is also scope for an improved PEPP 2.0 which can address some gaps that are evident with the benefit of hindsight. For example, the definition of 'guarantees' should be clearly articulated in the legislation.

[32] *https://www.eiopa.europa.eu/sites/default/files/sg/opsg-20-13-irsg-20-14-joint-advice-on-pepp-consultation.pdf*

A product such as PEPP should have a common tax treatment. For many EU Member States, this may appear to be a 'bridge too far'. However, as per EU case law[33], once a Member State provides a certain tax treatment to its national third pillar pension products, such tax treatment should also apply to similar EU third pillar pension products and thus, mutatis mutandis, to the PEPP.

It may be feasible also to aim at some form of auto-enrolment[34] into PEPP – with quasi-mandatory participation, where an employer is permitted to choose the provider, while providing an opt-out.[35]

To conclude, cross-border portability of pensions in an increasingly globalised economy, with easy and therefore more frequent cross-border movement of labour is both desirable, and a key feature of the PEPP. However, national requirements sometimes render impossible the transfer of pension capital across borders. This is contrary to the core objectives and principles of the PEPP and the European Union.

PEPP 2.0 should therefore seek to specifically ensure that the concept of free movement of persons and capital precludes any national measure that may impede the exercise of the guaranteed fundamental freedoms.[36]

It is safe to conclude that the PEPP is a 'Catalyst for Pension Innovation'.[37]

[33] In the case of Skandia, the court held that:' Article 49 EC precludes an insurance policy issued by an insurance company established in another Member State which meets the conditions laid down in national law for occupational pension insurance, apart from the condition that the policy must be issued by an insurance company operating in the national territory, from being treated differently in terms of taxation, with income tax effects which, depending on the circumstances in the individual case, may be less favourable.'

[34] See for more detail: H. van Meerten, J.J. van Zanden,' Shaping the Future of Retirement: Aspects of Sustainability', European Journal of Social Security, 2021, 8.

[35] H. van Meerten, E. Schmidt, 'Compulsory Membership of Pension Schemes and the Free Movement of Services in the EU', European Journal for Social Security, 2017, 19(2).

[36] K. Borg, A. Minto, H. van Meerten, 'The EU's regulatory commitment to a European harmonised pension product: The portability of pension rights vis-à-vis the free movement of capital', Journal of Financial Regulation, 2019, 5(2).

[37] H. van Meerten, T.J.B. Hulshoff, 'PEPP: Catalyst for pension innovation?', SSRN 2022: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4278689