INSURANCE MATTERS

PENSIONS

Shifting demographics, resulting notably in a growing imbalance in the ratio of active workers to retirees, and evolving labour market dynamics are exerting significant pressure on the financial sustainability of pension systems. This raises concerns about the extent to which pension systems can continue to ensure adequate retirement income for all citizens. This also means that, without sufficient savings, retirees could be led into financial hardship, impacting their ability to afford essential healthcare, but also straining public finances further. It is therefore imperative for individuals to save and invest more for their retirement, but many are not doing so, for different reasons.

Life insurers, as providers of both occupational and personal pensions, play a key role in addressing the pension savings gap. As such, insurers help diversify retirement income sources, thereby enhancing financial security for individuals and alleviating pressure on public resources.

39 percent of Europeans are not saving for their retirement.

Source: Insurance Europe's Pan-European Pension Survey, 2023

"Closing the global pension protection gap of $51trn would require an additional annuity payment of approximately $1trn per year."

Source: Global protection gaps and recommendations for bridging them, GFIA, 2023

With insurance…

Diversification of income sources
Insurance products, whether they provide annuities or a lump sum, can provide income streams on top of state-funded pensions and personal savings. This diversification helps spread risk and ensures a more stable income during retirement.

Guaranteed income and risk management
Annuities offer the option of a guaranteed income for life, regardless of market fluctuations or longevity risk (the risk of outliving one's savings). This provides retirees with peace of mind, knowing they will have a steady income throughout their retirement years. Insurance solutions also help retirees manage longevity risk or healthcare expenses. Products like long-term care insurance can protect against the financial burden of medical or nursing home costs in later years.

Flexibility and customisation
Insurance solutions often offer flexibility in terms of payment options, withdrawal strategies, and beneficiaries. This allows retirees to tailor their insurance plans to their specific needs and preferences, ensuring a personalised approach to retirement planning.

Tax advantages
Some life insurance products, such as certain types of annuities or pension insurance policies, may offer tax advantages that can help retirees maximise their retirement income.

Without insurance…

Reduced number of pension options
Without insurance-based pension options, individuals would primarily rely on government-funded pensions or personal savings. This limited income stream might not be sufficient to maintain a comfortable standard of living in retirement, especially considering longer life expectancies and potential healthcare expenses.

Increased financial vulnerability
The absence of insurance solutions leaves retirees more vulnerable to financial shocks, such as unexpected medical expenses. This vulnerability results in higher rates of poverty and financial insecurity among the elderly population. Insurance solutions typically offer various risk management tools, such as annuities or biometric coverage, which can protect retirees and their families from unforeseen circumstances. Without these options, retirees may lack adequate protection against risks like longevity risk or the financial impact of a premature death.

Increased pressure on social welfare systems
In the absence of private insurance solutions, the burden on state pension systems would escalate. This could strain public finances and potentially lead to benefit cuts or increased taxes, negatively impacting all citizens.

Without insurance solutions, people's retirement prospects could be significantly compromised.

WHY THE PEPP IS FAILING…

The pan-European Personal Pension Product (PEPP) was put forward to complement national pension solutions. This ambitious project was aimed at increasing pension adequacy, allowing for portability between EU member states, and increasing the range of products available to EU citizens, among other goals. Unfortunately, it has yet to meet policymakers' high expectations, as, so far, just one provider is offering PEPPs, in a limited number of countries.

The primary reason for the PEPP's "failure" is the overly complex PEPP regulation, the administrative burden it puts on providers, legal uncertainties, as well as unrealistic requirements, such as the requirement to outperform future inflation, in most cases through risk mitigation techniques and the 1% annual fee cap on the accumulated capital for the basic version. And it is a fact that the taxation of pension products is not harmonised in the EU. These regulatory challenges have deterred providers from offering PEPP products. Indeed, to make the PEPP a viable option, substantial changes to the PEPP regulation are necessary.

Nonetheless, it is key for policymakers across Europe to prioritise national solutions that promote increased personal savings. Europe's policymakers have a key role to play.

INSURERS CAN DO EVEN MORE…

How can policymakers help?

- **Ensure regulation enables insurers to continue providing their role as protectors.** There is a strong demand for the financial guarantees, annuities, and biometric coverage that insurers have traditionally offered. It is vital that regulations, especially the Solvency II Directive and the new Retail Investment Strategy, do not hinder or discourage insurers from fulfilling their critical protective role.
- **Raise awareness and ensure that citizens can access accurate and easily understandable information about their future pension entitlements.** Being informed empowers citizens to make decisions that align with their personal circumstances. The European Commission has a pivotal role in promoting best practices and encouraging all member states to advance in this regard, for instance by promoting pension dashboards or tracking systems, and incorporating European Retirement Week as an official EU calendar event.
- **At national level, consider implementing automatic enrollment schemes for employees where appropriate and on a voluntary basis.** Research indicates that people are more inclined to join pension savings programmes through auto-enrollment, as long as they have the option to opt out if they prefer. Here, too, "one size fits all" will not work because the national pension systems differ greatly.
- **Introduce fiscal incentives to encourage all citizens, whatever their personal circumstances, to save for their old age.** Tax incentives can encourage people to save by providing financial rewards or benefits for saving money in certain accounts or investments. These incentives typically come in the form of tax deductions, credits, or deferrals.
- **Reduce complexity: make disclosures more user-friendly and simplify the sales process.** Policymakers should ensure that consumers have easy access to simple and clear information, which makes it easy to understand the benefits that insurance products can offer. It is important to reduce and not add to the current information overload. It is equally fundamental to simplify complicated, lengthy sales processes that discourage EU citizens from investing. Legislation should not hinder the use of digital solutions to assist, simplify, and streamline the process. In addition, having a wide choice of product types/structures/features and distribution channels allows consumers to have access to pension and life insurance products through their preferred channel.
- **Take stock of why PEPP failed before introducing any alternative pan-European product.** For the PEPP to be realised, significant reforms will be needed, impacting various aspects of the regulation.