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REPORT FROM THE COMMISSION TO THE COUNCIL

on the Pension Scheme of European Officials and Other Servants of the European Union

EXECUTIVE SUMMARY

The Pension Scheme of Officials and Other Servants of the European Union (hereinafter 'the PSEO') functions as a notional fund with defined benefits. Although there is no actual investment fund, it is considered that the amount which would have been collected by such a fund is reflected in the pension liability guaranteed by Article 83 of the Staff Regulations and Article 4(3) TEU.

The PSEO follows an actuarial balance principle and the pension contribution rate is the mechanism that maintains the scheme in balance. If the actuarial assessment, based on various parameters defined by the Staff Regulations, shows that a pension contribution rate different from the rate in force should be applied in order to fully cover the pension rights acquired during a given year, that rate is adjusted by the Council on the basis of a Commission proposal and a Eurostat report. When staff members pay the pension contribution adjusted by this rate, they acquire pension rights for a given year, which are protected by the principle of acquired rights.

The PSEO is a mandatory occupational pension scheme for EU civil servants and as such shall be compared to pension schemes for civil servants in Member States and other international organisations, rather than to general national pension schemes for the private sector.

1. The main parameters to be assessed

All aspects of the pension scheme have to be considered as a whole, while also taking into account the specific aspects of the EU civil service, to ensure adequate, sustainable and safe pensions for the staff of EU Institutions.

As regards the pension age (normal, mandatory and minimum retirement age), the EU Institutions appear within the range of the schemes of Member States for national civil servants. If the Commission Proposal of 2011 on the review of the Staff Regulations (hereinafter 'the Commission Proposal') is adopted by the Council and the Parliament, the EU Institutions will be in line with those Member States that are the most advanced in reforming their pension systems and fully in line with the orientations of the Green Paper towards adequate, sustainable and safe European pension systems (hereinafter 'the Green Paper').Many of the Member States still need to carry out structural reforms to this end.

The PSEO is either in line or even compares less favourably (by granting lower entitlements) with the schemes of the Member States as regards the accrual rate, the basis for pension, the maximum possible pension rate and the staff contribution rate. The pensions in the PSEO are adjusted at the same level as the remuneration in the EU Institutions. As a result, the pensions paid from the PSEO have lost 5.4%[1] of the purchasing power since 2004.

As regards the individual progression in the salary scheme, even though it has an impact on pension costs, the career system should not be changed if its only aim is to

[1] The figure takes into account the Council Decision (2011/866/EU) of 19 December 2011 not to adopt the Commission proposal to adjust the remuneration and pensions.

achieve savings on pensions. The first consideration should be the need to attract, retain and motivate the active staff of the EU Institutions. These were the considerations behind the complete overhaul of the career structure in 2004, which established a merit based career structure providing performance incentives throughout the entire career.

The Commission has also considered a number of other policy aspects related to pensions listed in the Council request, notably the role of pensions in the overall reward package for EU staff and ensuring fair future pension provision across the EU workforce. The Commission reached the conclusion that the PSEO provisions are up to date and comply with the policy goals of the EU Institutions, as well as the orientations of the Green Paper.

2. A reflection on possible changes to the PSEO

The possible creation of a pension fund may entail additional costs, as the value of the notional fund would have to be transferred to an investment fund. In the long run, however, annual budgetary pension expenditure would decrease, as pensions would be paid from the fund. Incentives for private pension provision could be considered, although certain issues such as additional costs for management and security of investment should be addressed.

The creation of the category of contract staff in 2004 has brought and will continue to bring considerable savings. However, it is also important to keep the same pension scheme for officials and contract agents in order to maintain contract agents' positions attractive for qualified staff.

Therefore, the Commission concludes that all parameters of the PSEO are in line with the pension schemes for national civil servants of the Member States. However, in order to comply with the orientations of the Green Paper, the early retirement scheme should be restricted, and both the normal retirement age and the mandatory retirement age should be postponed until 65 and 67 respectively, as provided for in the Commission Proposal.

Lastly, the Commission has assessed the additional savings that would result from the Commission Proposal based on three approaches: annual pension expenditure, the service cost which reflects the annual cost of pension rights and corresponds to the amount to be invested in the pension fund if it existed, and pension liability.

The measures set out in the Commission Proposal, if adopted, would have a considerable impact in terms of reducing the long-term pension costs. As a result of those measures, the annual pension expenditure would decrease by around 500 million Euros in the long run, and the service cost, which corresponds to the annual cost of acquired pension rights, would be reduced by 9.5%. This would have an immediate impact on the pension liability for active staff, which would fall by 14.5%.

1. INTRODUCTION

1.1. Request for the report

As part of the discussion in the Council concerning the Commission report on Annex XI (mid-term review)[2], the Council invited the Commission to undertake a study on the long-term budgetary implications of the pension costs of staff of all EU Institutions and agencies. On 18 August 2010 the Commission presented a Eurostat study on the long-term budgetary implications of pension costs[3].

Eurostat recalled the main principles of the PSEO and emphasised that "it is important to appreciate that the new pension expenditure due to a staff member retiring today has already been paid for, in the form of the pension contributions paid during that staff member's period of service."[4] When staff members pay the pension contribution adjusted by this rate, they acquire pension rights for a given year, that a protected by the principle of acquired rights.

That abovementioned study addressed the major trends in pension expenditure of the PSEO over a period of 50 years (2010-2059) and showed that the PSEO is not yet mature. This is because, even though the scheme has been in existence since 1962, the number of staff has grown over time as a result of successive EU enlargements, new tasks for the EU institutions and the steady trend in establishing new EU bodies. Consequently, between 2010 and 2059, the number of beneficiaries will increase by 109%.

Another consequence of the fact that the scheme is not yet mature is that annual pension expenditure will grow during the projection period. Total pension expenditure (at constant prices) will rise from 1 235 million Euros in 2010 to peak at 2 490 million Euros in 2045, before falling to 2 259 million Euros in 2059. Pension expenditure is therefore projected to grow more slowly than the number of pensioners and will then start to decrease, largely due to the effects of the 2004 reform of the Staff Regulations[5].

Eurostat calculated that the annual savings for EU budget between 2010 and 2059 resulting from the 2004 reform will increase over time to reach 1 047 million Euros in 2059. This means that the total pension expenditure in 2059, which is now projected to increase by 83% as compared to 2010, would otherwise have increased by 168% without the 2004 reform. The total cost savings over 50 years are projected to be 24 785 million Euros. This may even be an underestimate of the total savings from the 2004 reform, as it does not take into account savings from the changes to invalidity and survivors' pensions.

The Council took note of the study and asked the Commission to make an assessment of all elements that have a significant impact on pension costs, and it called upon the Commission to have regard in its assessment to a number of policy aspects. In addition, the Council requested the Commission to present, by the end of

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2 COM (2008/443).
3 SEC (2010) 989.
4 SEC (2010) 989, p.3.
5 Hereinafter '2004 reform'.

2011, appropriate proposals for amending the Staff Regulations based on this assessment.

The structure of the present report is in line with that of the abovementioned request of the Council.

1.2. Green Paper towards adequate, sustainable and safe European pension systems

In parallel with the abovementioned process initiated by the Council, the Green Paper towards adequate, sustainable and safe European pension systems[6] launched a European debate on the key challenges facing pension systems i.e. demographic ageing and the financial and economic crisis. It defined the priorities for modernising pension policies in the EU in order to achieve two overarching objectives i.e. addressing pension adequacy and securing sustainability. These objectives can be achieved, inter alia, by:

– achieving a sustainable balance between time spent in work and in retirement;

– removing obstacles to mobility in the EU by strengthening the internal market for pensions and enhancing the mobility of pensions;

– promoting safer, more transparent pensions with better awareness and information.

2. METHODOLOGY

2.1. Comparative approach

In order to assess whether the PSEO is in line with national pension schemes, the Commission used a comparative approach. This approach meant defining the methodology, i.e. defining the comparable sample, time frame and comparable elements of different pension schemes for civil servants. It goes without saying that, while assessing separate elements across pension schemes, we should remember that they are interrelated and interdependent. Therefore, only by combining all of these elements we can provide the full picture of a given pension scheme for civil servants. At the same time we need to be mindful of the complexity and particular features of the pension schemes that are being compared.

When defining the time frame we need to bear in mind the dynamism and diversity of pension schemes for civil servants. Often different conditions apply to civil servants depending on their age, the department in which they work or the day on which they started their service (or the date of their entry into the employment market). This diversity is inherent in the way the reforms in pension schemes are introduced, sometimes, as a result of the need to preserve certain acquired rights. In order to have comparable results, this report takes into account the present situation for civil servants that enter into service in 2011 and transitory measures that are put in place.

[6] SEC (2010/830).

2.2. *Making proper comparisons*

The PSEO is a mandatory occupational pension scheme for EU civil servants and as such should be compared with pension schemes for civil servants in Member States and other international organisations rather than with general national pension schemes for the private sector. General pension schemes are defined by the State and normally do not apply to civil servants.

Although the Commission did not compare the PSEO with the pension schemes of other international organisations in this report, it considers such a comparison fully appropriate due to the similar staff features and the comparable nature of the work. The Commission does not rule out the possibility of conducting such an analysis in the future.

In order to assess whether the PSEO is in line with the pension schemes for national civil servants, the Commission asked the Member States to reply to a questionnaire on their pension schemes for national civil servants in central government. Twenty-six Member States sent the replies, while France failed to do so despite several reminders. This report is based on the replies sent in by the Member States.

When assessing the PSEO, the specific situation of EU staff should be borne in mind: the EU Institutions recruit mainly expatriate staff coming from 27 Member States which have significantly different national pension systems. This is not the case for the civil services of the Member States. In terms of other international organisations, only the United Nations is of a comparable size and this makes it difficult to compare like with like. Although the Commission considers that the pension schemes of other international organisations and national pension schemes are the most appropriate for purposes of comparison, such comparisons have inherent limitations, which are underlined in the report. For example, many schemes in the Member States are pay-as-you go schemes, whereas the PSEO operates as a notional fund.

All components of the pension scheme have to be considered altogether, while taking into account the specific aspects of the EU civil service, in order to ensure adequate, sustainable and safe pensions for the staff of EU Institutions.

EU Institutions recruit mainly expatriate staff from all 27 Member States, and compete in the international labour market with other international organisations, diplomatic services, central government services, multinational companies, law firms, financial consultancies, etc. They need to continue to be an attractive employer so as to maintain the geographical balance among staff and be able to deliver on policies in order to meet the expectations of EU citizens and the Member States.

2.3. *Separate pension schemes for civil servants*

There are separate occupational pension schemes for civil servants in all international organisations, in about half of the countries of the world and in the majority of EU Member States. Integrated schemes are universal in the new Member States, albeit often with different rules for different groups of workers. In Ireland and Spain, civil servants are covered by the national pension scheme, but have their own top-up retirement income arrangements (additional defined-benefit pensions for civil servants). In the United Kingdom, civil servants are covered by part of the mandatory pension arrangements that apply to private-sector workers.

The rationale for providing pensions for civil servants is somewhat different from that behind the creation of general national pension schemes, the purpose of which is to ensure an adequate retirement income. The objectives are the following: securing the independence of public servants, making a career in public service attractive, postponing the cost of remunerating public servants into the future and ensuring that retirement provision for older civil servants is politically and socially acceptable.

While civil service pension schemes share some of the social-policy goals of national pension programmes, they must also accommodate the human-resources policy of the employer. Therefore civil service pension policy also involves general issues of civil-service remuneration and compensation[7].

3. THE PENSION SCHEME OF EUROPEAN OFFICIALS (PSEO)

3.1. Main concepts

3.1.1. *Legal references*

Pursuant to Article 83 of the Staff Regulations:

– the benefits paid under this pension scheme are to be charged to the budget of the Union,

– Member States are to jointly guarantee the payment of such benefits,

– officials are to contribute one third of the cost of financing the pension scheme.

Article 83a and Annex XII of the Staff Regulations set out the *actuarial rules* for computing the contribution rate in order to guarantee the balance of the pension scheme.

The benefits paid under the scheme are laid down in Chapter 3 of Title V of the Staff Regulations, as well as in Annex VIII thereto.

3.1.2. *Notional fund principle*

The European Coal and Steel Community (ECSC) had a pension fund, but it was dismantled and replaced by the notional fund upon the merger of the institutions of the Communities in 1967. The notional fund has been put in place for the European Economic Community with the adoption of the Staff Regulations in 1962.

It must be borne in mind that the PSEO does not operate as a pay-as-you-go scheme. In a pay-as-you-go scheme, the pension contribution rate or pension benefits are adjusted in order to have yearly balance between the collected contribution and the

[7] Robert Palacios, Edward Whitehouse. Civil-service Pension Schemes Around the World. May 2006. SP discussion paper NO. 0602. World Bank.

pension expenditure. In case the balance cannot be achieved, the budget finances the difference through taxes.

This is not the case in the PSEO, in which the pension contribution actually covers the cost of the pension rights acquired in a given year and is not in any way linked to the pension expenditure of that year. When the PSEO reaches the maturity, there will necessarily be a gap between pension contribution and the pension expenditure, which is due to the interest that is applied to the collected contribution until it has to be paid back in the form of pension benefits.

Although there is no actual investment fund, it is considered that the amount which would have been collected by such a fund, is invested in the Member States (on the basis of the observed average annual interest rates on the long-term public debt of Member States) and is reflected in the pension liability, which is guaranteed by Article 83 of the Staff Regulations and Article 4(3) TEU.

As far as the budget is concerned, the pension scheme produced net revenue in the past, because active staff paid contributions for pension rights they acquired, whereas very few retired or invalided staff actually drew benefits. This revenue consisted of the pension contribution paid by the staff plus the employer's contribution, which was however not paid into a fund, but was only reflected in the pension liability.

In the longer term, as active staff go into retirement, there will be an inevitable increase in the pension expenditure. The increase will continue until around the time when the pension scheme reaches maturity – that is, until the number of deceased retirees in a given year balances out the number of new beneficiaries. The amounts which would have been covered by the pension fund are now covered (and will continue to be covered) by the budget and have an impact on the pension liability.

Under the notional fund approach, staff contributions have not been set aside in an actual pension fund, but have been credited instead to the EU budget at the time when they were collected and spent in accordance with the decisions of the budgetary authority, i.e. they were not assigned to any particular policy field. As for the remainder, which would normally correspond to the employer's part of the contribution, it was decided that it would not be collected[8]; instead, the EU Institutions have undertaken to pay future pension benefits (to be charged to the Union budget) when staff retire. Pursuant to Article 83 of the Staff Regulations, Member States shall jointly guarantee payment of the benefits. As a result the budget was, in effect, borrowing this money from the members of the scheme, in return for a guarantee to pay future benefits. The balance of the amounts borrowed and the amounts repaid is reflected in the pension liability.

As members of the PSEO reach retirement age, the money has to be repaid to them in the form of retirement benefits. Therefore, pension expenditure has gradually increased in the past, and this trend will continue until around the time when the scheme matures.

8 With the exception of self-financing agencies, which pay the employer's part of the contribution to the EU budget.

In relation to this growth in pension expenditure, it is important to understand that the new pension expenditure due to a staff member retiring today has already been paid for[9] in the form of the pension contributions paid during that staff member's period of service, and their pension entitlements that will have to be paid from the moment of retirement are covered by the pension liability.

3.1.3. Actuarial balance principle

The PSEO follows the actuarial balance principle. The annual contribution paid by the staff has to cover one third of the rights that the staff have acquired during a given year. The acquired rights of EU civil servants during that given year correspond to the future pensions that the staff will receive after retirement, as well as to the entitlement (under certain conditions) to an invalidity allowance, a survivor's pension, and an orphan's pension. In other words, the annual contribution is designed to finance one third of the service cost under the pension scheme, i.e. a series of payments that will arise in the future. In order to make this computation possible, the series of payments for European civil servants has to be evaluated at its present value (using an interest rate "discount rate"). The computation is thus an actuarial valuation.

In technical terms, the method used in the computation of the pension contribution rate is that prescribed by international accounting standard IPSAS25[10] and referred to as “projected unit credit”. The sum of the actuarial values of rights acquired by active members of staff, referred to in actuarial practice as “service cost”, is compared to the annual total of their basic salaries in order to calculate the contribution rate.

The pension contribution rate maintains the PSEO in balance. If the actuarial assessment, based on the various parameters defined by the Staff Regulations, shows that a pension contribution rate which is different from the rate in force should be applied in order to cover the pension rights acquired during that year, that rate is adjusted by the Council on the basis of a Commission proposal.

The contributions paid during the current year are not calculated so as to cover the pension payments for the current year: they might be higher or lower. The actuarial balance principle guarantees a balance in the long term, not a yearly balance: this is a different concept from a yearly cash-flow balance.

4. COMPARATIVE ANALYSIS OF THE MAIN FEATURES OF THE PENSION SCHEMES OF NATIONAL CIVIL SERVANTS AND EUROPEAN CIVIL SERVANTS

4.1. Pensionable age

The Green Paper defines the "normal pension age" as the "age at which a member of the pension scheme is eligible to receive full pension benefits". The "mandatory retirement age" is the age at which the employment contract automatically expires as an effect of chronological age. The "effective retirement age" is the age at which an

[9] Active staff paid the pension contributions for the pension rights they acquired.

[10] The International Public Sector Accounting Standard (IPSAS) 25 is the equivalent of the International Accounting Standard (IAS) 19 applied in the private sector.

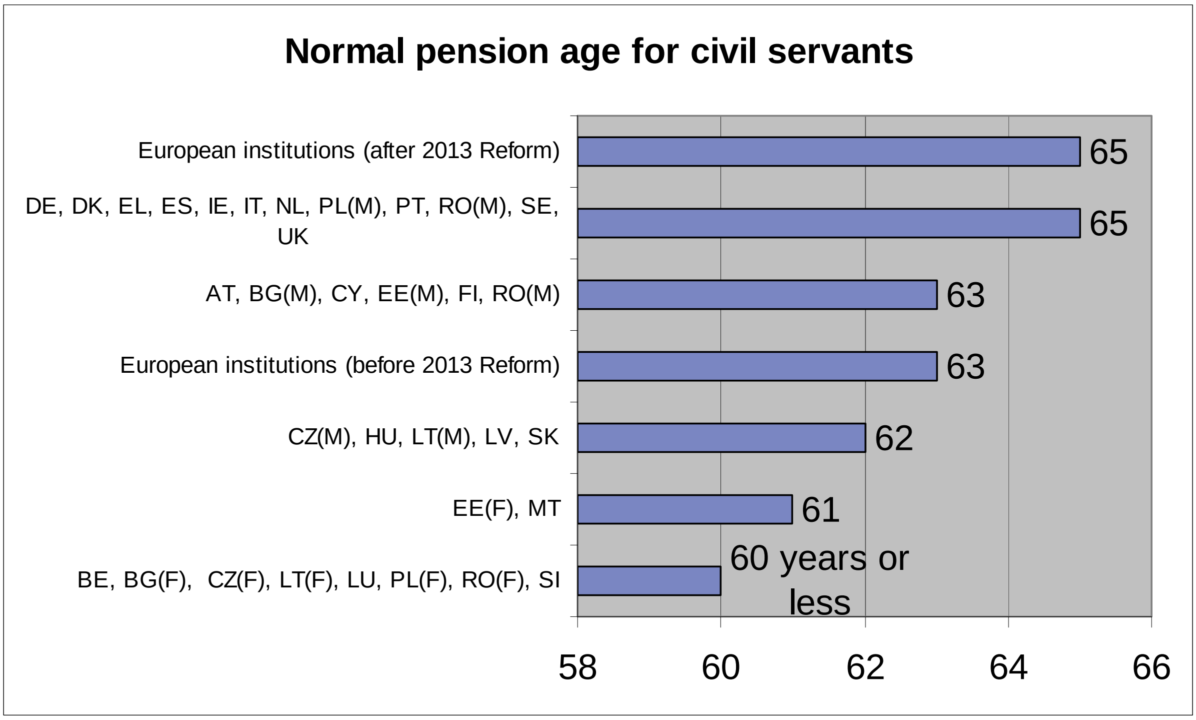
individual actually retires. As a general rule, the effective retirement age tends to be below the normal pension age. However, for reasons of data availability, the labour market exit age is often used as a proxy for the effective retirement age.

For example, in 2008 the average age of exit from the labour force in the Member States[11] ranged from 55.5 in Romania, 59.3 in France and Poland to 63.2 in the Netherlands and 63.8 in Sweden. The average exit age of all Member States was 61.4. The effective retirement age in the EU Institutions varies between 61 and 62.

4.1.1. *Normal pension age*

In a number of Member States the normal pension age for civil servants is lower than in general schemes.

The following chart shows the normal pension age for central civil services of the Member States: [12]



NB: France is not included in the chart as no reply was provided to the questionnaire.

If only the pension age for men is taken into account, it should be pointed out that the majority of the Member States have set the normal pension age between 61 and 63 years. In three Member States it is still 60 and in ten of them it is as high as 65. In six Member States the normal pension age is lower for women than for men and is set at the age of 61 or below.

The normal pension age for EU civil servants was raised from 60 to 63 (for both men and women) in 2004, with transitional provisions applying for staff already in place

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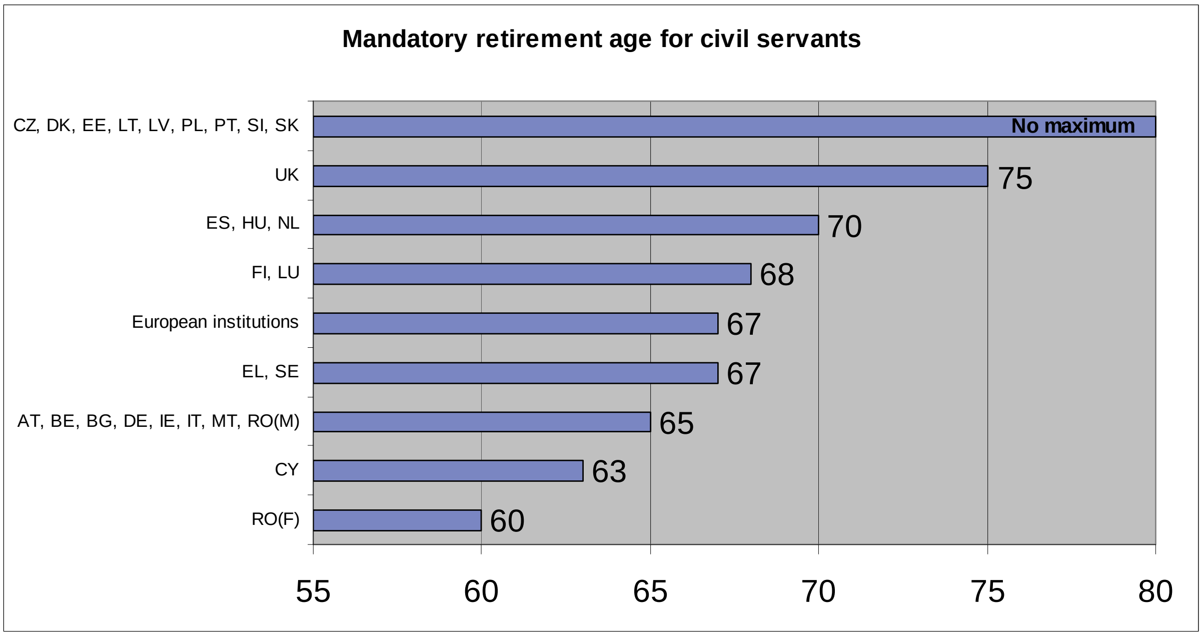
11 Source: Green Paper.

12 In the following tables, "F" stands for "Female" and "M" stands for "Male".

(ranging from 60 to 63 depending on the age of the civil servants on 1 May 2004). The current normal pension age of 63 is broadly in line with the standard pension eligibility ages for civil servants in the Member States. If the EU Institutions raise the normal pension age to 65, it will be higher than the normal pension age for civil servants in most Member States.

4.1.2. *Mandatory retirement age*

The mandatory retirement age is also a relevant indicator that should be observed when describing pension schemes. A third of the Member States have established 63 or 65 as the age at which the tenure or employment contract for a civil servant expires, and in nine Member States there is no upper age limit for staff in public employment. It should be pointed out that the suggestion in the Commission Proposal is that civil servants should be allowed to work until the maximum age of 67 if it is in the interests of the service, which previously was possible only in exceptional circumstances.

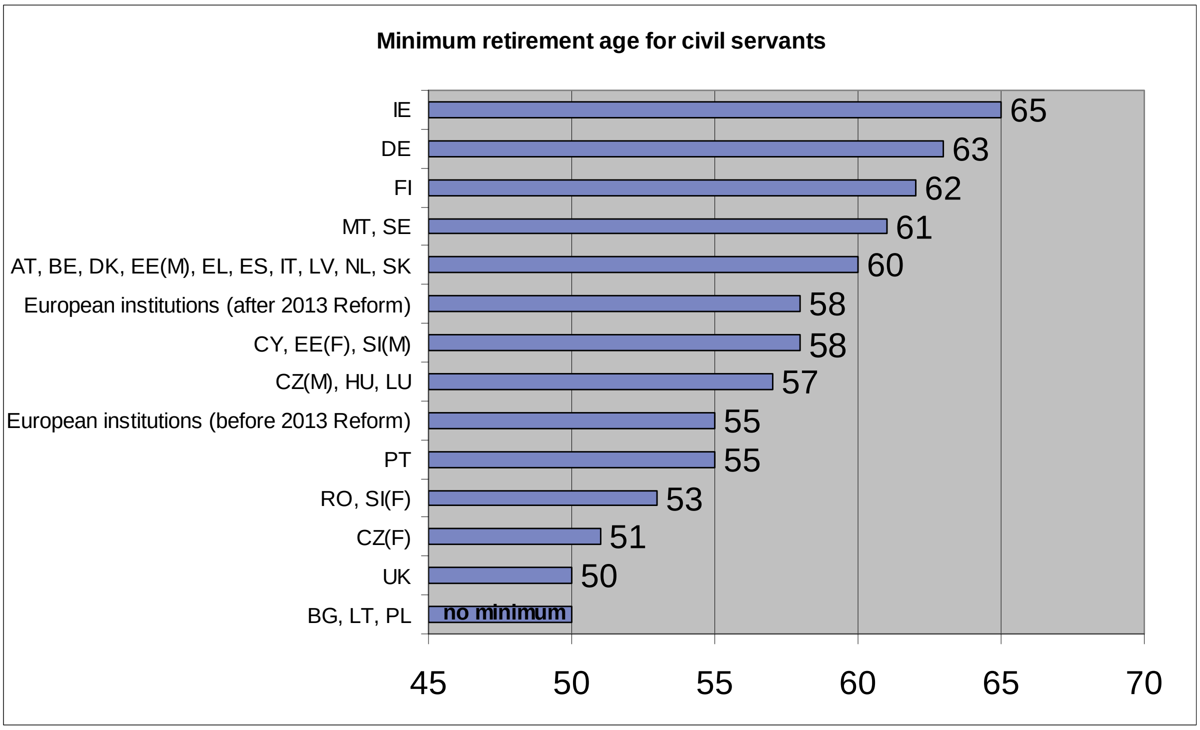


NB: France is not included in the chart as no reply was provided to the questionnaire.

This increase in the mandatory retirement age will put the EU Institutions in the category as those Member States in which civil servants have the possibility to work the longest, whereas most of the Member States need to implement structural reforms in order to encourage longer working lives.

4.1.3. *Minimum retirement age*

As far as early retirement is concerned, a majority of Member States maintain a minimum pensionable age close to 58 years. However, at least ten Member States still offer the possibility for civil servants who have a certain minimum number of years of service to leave the service before reaching the age of 58. This is the case in the United Kingdom, where civil servants can retire at the age of 50.



NB: France is not included in the chart as no reply was provided to the questionnaire.

In its Proposal, the Commission suggested measures restricting access to early retirement schemes and other early exit pathways in order to enable civil servants to stay longer in activity. In particular, the number of staff members that can take up early retirement without a reduction of pension rights would be diminished and the early retirement age increased to 58. Some Member States have started similar reforms, while the others have yet to implement such measures.

4.2. Accrual rate

The Green Paper defines the accrual rate as "the rate at which future pension benefits are built up. It is used in defined benefit schemes and based on the formula linked to the scheme".

When comparing the accrual rates existing in the Member States, it is relevant to consider at the same time the basis, which makes the exercise very complex.

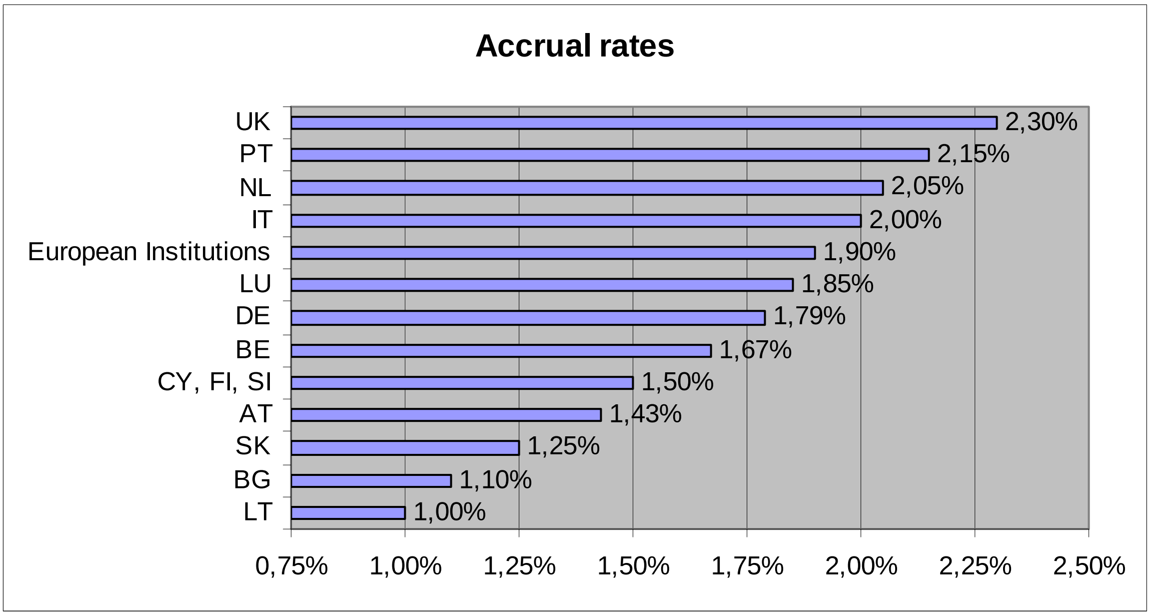
First of all, in nearly a dozen Member States, part of the pension could be paid under different rules than the accrual rate.

There is a wide range of situations in the various Member States that apply accrual rates. To give some examples, in the United Kingdom the accrual rate is up to 2.30 % of the last salary, in Portugal it is between 2.00% and 2.30% of each relevant calendar year, in the Netherlands it is 2.05 % of the pensionable income and in Germany, it accrues 1.80% of the final salary and family allowances for each year of service.

The current accrual rate for the officials and servants of the European Union is 1.90% of their final basic salary for each year of service; this rate was reduced from 2 % to 1.9 % in the 2004 reform[13]. This level is fully justified by the particular situation of EU staff. It has to be taken into consideration that the average age of entry into the European civil service is 35 years. Therefore, staff have a shorter period of time to acquire pension rights than do national civil servants. Moreover, when European civil servants transfer pension rights from Member States, it is not the number of years worked but the monetary value transferred that is taken into account.

There is another aspect that makes the situation even more complex when comparing Member States and EU Institutions: the accrual rate may also vary depending on the age. Finland offers a progressive accrual rate, which is 1.5 % of earnings between the ages of 18 to 52, 1.9 % of earnings between the ages of 53 to 62 and 4.5 % of earnings between the ages of 63 and 68. This provides a clear incentive for the civil servants to work longer. The EU Institutions adopted a similar approach by creating an incentive of additional pension rights for work after reaching the normal retirement age (known as the "Barcelona incentive").

The chart below shows accrual rates in the Member States that use accrual rates to calculate pensions.



NB: France is not included in the chart as no reply was provided to the questionnaire.

4.3. Basis for pensions

Member States apply very different systems when it comes to the basis for calculating the pension once an official retires. Some Member States such as Cyprus, Ireland or the United Kingdom, base the pension on the last salary or on the last year's salaries. In other Member States (for example in Finland, Hungary and Slovakia) the average of pay over the whole career is taken into account for the

13 For staff recruited before 1 May 2004 the accrual rate is 2 %.

pension calculation. This means that the career progression is very important for the definition of the basis for pension. For example, in the systems that take into account the last years of service as a basis and where the end of career progression is very slow, this has only a very limited impact on the pensions. The effect is similar in the systems using the average career salary, when the difference between starting salary and final salary is small.

In the EU Institutions the basis for the pension is the basic salary of the last grade that the official has held for at least one year. There are important reasons to maintain this system. In the 2004 reform of the Staff Regulations, the career structure in the EU Institutions was revamped and made longer by introducing additional grades, in order to create performance incentives throughout the entire career. The salaries at entry level were consequently lowered. In addition, given the high average age of recruited staff, it would be impossible for many of them to progress to the higher grades if they followed the average career pace. Therefore, changing the basis for the pension would much more affect the level of pensions in the EU Institutions than it would in national services with a lower number of grades, and would make the entry grades even less attractive for experienced staff. As a consequence, the EU Institutions would need to find alternative solutions, which might be more costly, in order to attract qualified staff from all Member States (for example, by organising competitions in higher grades for experienced staff, the result of which would be not only higher salaries, but also higher pensions).

4.4. Maximum possible pension rate

The maximum pension rate puts a cap on the pension rights that a person can accumulate during his working life. As this notion does not exist in some Member States, such as Czech Republic, Finland, Romania, Latvia, Estonia, the pension rights of civil servants in those Member States correspond to their years of service, while the EU Institutions and other Member States have established a cap. The effect of having such a cap is that a person may be obliged to work until he reaches the normal retirement age without acquiring any additional pension rights, but would still be under an obligation to contribute to the scheme, if he has reached the maximum pension rate.

The maximum pension rates can vary considerably from one Member State to another. For example, although in France[14] the maximum pension rate is 75%, it could be raised to 80% as a result of various premiums. Germany has a maximum pension rate of 71.75% of the final basic salary plus family allowances. Some Member States have set the rate on the basis of the highest salary throughout the career. This is the case in the United Kingdom, where employees could receive a maximum pension equivalent to 66 or 75% of the highest salaries depending on the pension scheme. In Slovenia and Austria, the maximum is 80% of the highest salary received during a number of years.

[14] As far as France is concerned, as data was not made available to Eurostat, the data included in this report rely on the following French public authority portal: http://www.info-retraite.fr/index.php?id=144

The maximum retirement pension for officials and other servants of the European Union is 70% of the final basic salary corresponding to the last grade which the official or servant occupied for at least one year. In order to achieve the maximum pension rate, EU civil servants have to work at least 37 years, and with the increase in the retirement age to 65 they have to start at the age of 28, in order to acquire maximum pension rights in the EU civil service. As the average recruitment age in the European Commission is 35, the majority of staff will be unable to achieve the maximum pension rate. This is already the case: the accumulated pension rights of the staff members who retired in 2010 are equivalent to 63% on average and will be around 57% for staff recruited after 1 May 2004.

The only possibility of receiving a pension exceeding 70 % of the pension rights is if the minimum subsistence figure is applied. An official or other servant becomes entitled to a pension equal to the basic salary of an official in grade 1 step 1 after 25 years of service. However, this applies only to the lowest categories of staff (for more details, see the chapter of this Report on use of contract agents and conditions of contract agents). In a few Member States the maximum pension rate is set below 70%, but it is applied to a different basis. In Denmark, for example, the maximum possible pension rate is fixed at 57%, but it applies only to the statutory pension and not to the state pension, which is dependent on the length of residence in Denmark. A person must have lived in Denmark for 40 years after their 15th birthday in order to be entitled to a full state pension from Denmark. The State pension consists of a basic amount and a pension supplement. The gross basic amount is 58 032 Danish krona (7 780 Euros[15]) annually. The pension supplement for single persons is 58 416 Danish krona (7 831 Euros) annually, whereas it is 27 276 Danish krona (3 657 Euros) for married and cohabitating persons[16].

For purposes of comparison, the theoretical replacement rates[17] in the Member States could be used as a comparator. These have been developed by the Indicators Subgroup of the Social Protection Committee. In the majority of Member States the replacement rates can be found in the range between 60% and 80% of last earnings. The median rate would be around 75%, i.e. the rate applied in the United Kingdom.

4.5. Staff contribution rate

The staff contribution rate is the part of the EU official's salary to be paid to finance one third of the actuarial cost of the pension scheme. The remaining two thirds are to be financed by the employer’s contribution. In practice, EU Institutions do not pay their corresponding part to finance the scheme, but – by way of compensation - pension payments are jointly guaranteed by the Member States (Article 83 of the SR) (see 5.8).

Here again, comparisons between Member States are complex because of the diverse nature of the bases on which the contribution relies (which includes the basic salary, gross earnings, real salary, gross wages, etc).

15 Figures in Euros are calculated with exchange rate of 1 July 2011, 1€=7.4592 DKK.

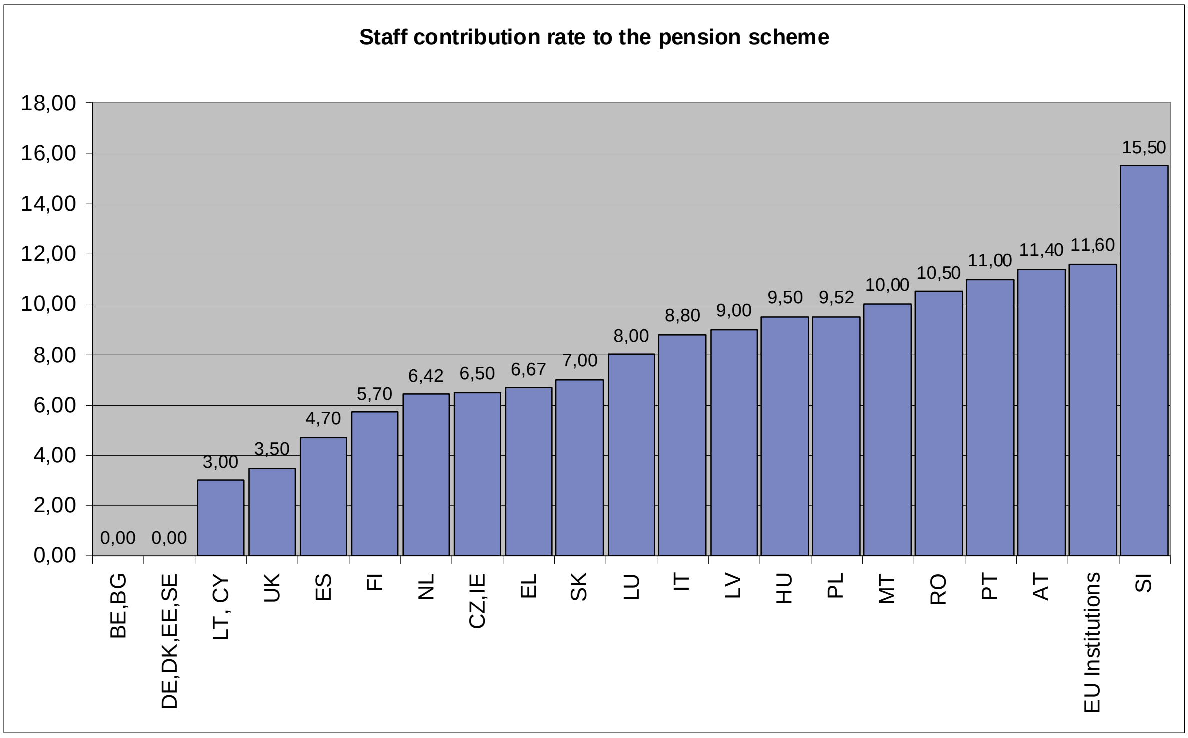
16 https://www.workindenmark.dk/Find%20information/Til%20arbejdstagere/Naar%20du%20arbejder%20i%20Danmark/Pension/Folkepension.aspx

17 Replacement rates show the level of pensions as a percentage of previous individual earnings at the moment of take-up of pensions.

It should be noted that, in some Member States, officials do not have to contribute to the pension scheme at all, as all contributions are covered by the State and their pensions are paid from the budget. This is the case in Bulgaria, Estonia, Germany, Sweden, as well as some pension schemes in Belgium and Denmark.

At the level of the European civil service, it should be remembered that the total pension contribution rate is needed in order to maintain the PSEO in balance and it is calculated every year. The share to be paid by EU officials (1/3 of this total contribution) is adjusted accordingly (according to Article 83 of the Staff Regulations). For example, for the year 2009, the pension contribution rate for EU officials was set at 10.9%, at 11.3% for 2010 and at 11.6% of the basic salary for 2011[18].

In by far the majority of Member States, the staff pension contribution rate is lower than the rate of the PSEO. The rate in some of the Member States is around 5% or below (the United Kingdom, Cyprus, Lithuania and Spain), while others have set the rate at between 5% and 10% (Finland, the Netherlands, the Czech Republic, Ireland, Greece, Slovakia, Luxembourg, Italy, Latvia, Hungary and Poland). The pension contribution rate is higher than that of the PSEO only in two Member States: in Austria, where it ranges from 10.25 % to 12.55 % and, in Slovenia, where its upper limit is 15.5 %.



BE:7% contribution paid by staf for survivor's pensions
DK: in the case of Labour Market PS, CR varies between 8% and 17%
PL: 7,3% for OPF part and 2,22% for PAYG part.
CY: in the case of CY Widows PS, CR is 2%
ES: 3,86% as regards Régimen de Clases Pasivas del Estado
FI: In 2010 contribution is 4,5% for persons aged under 53 and 5,7 % for persons having reached the age of 53.
UK: 1,5% for some categories

[18] The Commission has proposed an 11.0% pension contribution rate for 2012.

NB: France is not included in the chart as no reply was provided to the questionnaire.

4.6. Annual adjustment of pensions

A key determinant of the dynamics in pension expenditure is the indexation rule. As underlined in the Joint Report on pensions for 2010, many reform packages have featured changes in the indexation of pensions during retirement. The indexation issue can be seen as a choice between a lower initial pension plus earnings indexation and a higher starting benefit plus price indexation. [19]

By far the majority of Member States (all except Hungary, Lithuania and some of the Danish and Polish pension schemes)[20] are adjusting pensions in central governments in line with a number of relevant indicators, such as: the Consumer Price Index (CPI), pay increases, GDP growth, or the growth in social tax revenues. Some Member States use a single indicator (CPI or pay increases) to adjust pensions, whereas others use a weighted index based on two indicators. Some Member States (Slovenia, Denmark for the official pension scheme, Ireland and the Netherlands) are adjusting their pensions on the basis of changes in wages, whereas several others are adjusting their pensions in line with both prices in wages (Belgium, Cyprus, Czech Republic, Finland, Luxembourg, Slovakia and some pension schemes in Poland).

As far as the EU Institutions are concerned, pensions are adjusted according to the same method as the salaries of EU officials. These salaries are adjusted yearly to take account of changes in the purchasing power of officials in the central government of Member States and in the prices in Brussels (Brussels International Index).

This method is in line with the practice of all but a few Member States that are indexing the trend in pensions according to the trend in a number of relevant indicators, as explained above. A number of Member States are adjusting their pensions either based on the changes in wages or on the basis of a combined index which includes the changes in wages. However, most systems are indexed to inflation or on the basis of a combined index including inflation. At the same time the method used by the EU Institutions has led to adjustments of salaries and pensions that are below the rate of inflation. During the period 2004-2010, the pension adjustments have been below the rate of inflation (by 1.8%).

If the method for adjusting pensions were to be changed and linked to the adjustment of the pensions of officials in the Member States, it is likely that the result would have been more favourable to the pensioners of the EU Institutions than the current method, as most of the Member States index their pensions on inflation.

It is worth underlining that the annual adjustment of pensions has already been taken into account when the staff pay pension contributions. Therefore, failure to adjust current pensions paid may be open to legal challenge, since it is clearly a violation of acquired rights.

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[19] Joint Report on Pensions 2010 by the Economic Policy Committee, the Social Protection Committee and the Commission services, p. 25 and 26.

[20] Denmark: Labour market pension scheme; Poland: New pension scheme: OPF.

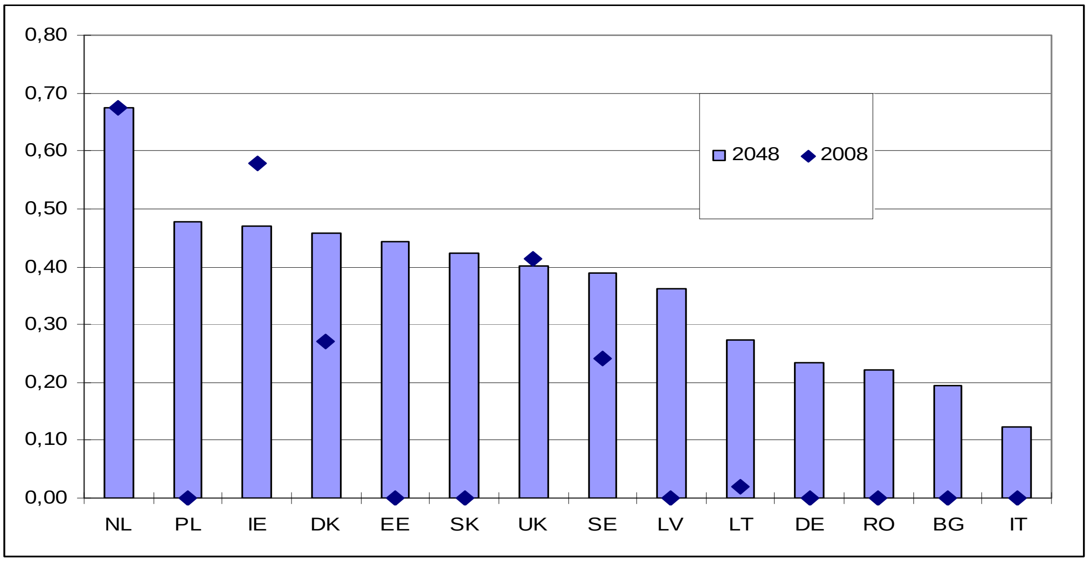
4.7. Possible creation of an actual pension fund

As already explained, the PSEO operates as a notional fund and this means that there is no investment fund as such. Greater pre-funding, in one form or another, has been a popular policy response on the part of Member States to the demographic challenge.[21] However, it is important to note that, for most European citizens, pay-as-you-go (PAYG) is and will always be the most important issue in overall pension provision.

Until recently, pre-funded pension schemes played a significant role in Denmark, Ireland, the Netherlands, Sweden and the United Kingdom, where the initial limitation on the pay-as-you-go public provision to basic, flat rate pensions for all has prompted the growth of private provision, whether in the form of collective occupational pensions or individual pension insurance contracts.

However, in the past decade of pension reforms, a number of countries have expanded the role of existing private schemes (e.g. Denmark, Germany) or introduced new elements of pre-funded, privately managed pensions into their statutory pension systems (Bulgaria, Estonia, Latvia, Lithuania, Hungary, Poland, Romania, Slovakia, Sweden). Some of the reforms have been partially reversed (e.g. in Latvia, Poland) or reversed entirely (e.g. Hungary) in the wake of the crisis, but the contribution by pre-funded schemes to pensioners' incomes will grow as the schemes mature.

Proportion of pension income coming from prefunded pension schemes projected for a hypothetical pensioner retiring in 2008 and 2048[22]



21 Funded schemes are pension schemes whose benefit promises are backed by a fund of assets set aside and invested for the purpose of meeting the scheme's liability for benefit payments as they arise.

22 Source: Social Protection Committee's Indicator Sub-Group's calculations. Calculations are based on the theoretical replacement rates for individuals working in the private sector, having a 40-year careers without interruptions (from the age of 25 to 65), and average earnings in the economy. Proportion of income coming from mandatory funded pension schemes will be probably lower than presented in the Figure for a number of Member States, where the contribution rates to the funded schemes have been reduced (temporarily or permanently) in the wake of the recent economic crisis.

By far the majority of the pension schemes in the Member States are also unfunded, which means that pension contributions are not transferred to a fund. Some Member States (Austria, Latvia, Portugal, Slovakia, Netherlands, Sweden, Poland and Denmark) have partially funded schemes.

The situation is different in other international organisations, which either have a complete pension fund or are going through a period of transition after introducing a pension fund.

Four possibilities for creating an actual pension fund for the EU Institutions could be envisaged. Each of the tables below presents in column I the service cost (meaning the yearly employer's contribution to the newly created fund), in column II the yearly pension expenditure as regards the notional fund in the framework of the current pension scheme in force and in column III the yearly total of both costs ("total cost in Heading V"). An analysis of the total annual costs in long term, as well as of the different options for the period 2013-2020, is helpful in terms of assessing the pros and the cons of each scenario.

– **Scenario n°1: Transfer of the value of the notional fund to the actual fund**. This scenario is somewhat hypothetical, as the first year would involve enormous cost since the equivalent of the pension liability would need to be transferred to the actual fund. In the years that followed the employer's contribution would remain low and stable (at around 800 million Euros) and would have to be paid into the fund together with the staff contribution (about 400 million Euros). In the short term and during the period 2013-2020, this option is by far the most costly for the EU budget. However, it does have a considerable impact on pension liability, because the amount in the pension fund would cover the pension liability.

	Projected number of active staff covered by the new pension fund from 2013	I Service cost (employer's contribution)	II Pension expenditure under the current pension scheme	III Total cost in Heading V [1] (I + II)
2013	55 000	800	37 700	38 500
2014	55 000	800	0	800
2015	55 000	800	0	800
2016	55 000	800	0	800
2017	55 000	800	0	800
2018	55 000	800	0	800
2019	55 000	800	0	800
2020	55 000	800	0	800
Total cost 2013-2020		**6400**	**37 700**	**44 100**
2060	*55 000*	*800*	*0*	*800*
In the long term when the new pension scheme becomes mature	*55 000*	*800*	*0*	*800*

[1] With 2011 legal provisions and methodology

– **Scenario n°2: Newly recruited staff would be covered by the pension fund, while current staff would continue to be covered by the current pension scheme.** Under this hypothesis, the yearly pension expenditure as well as the pension expenditure in the period 2013-2020 related to the notional fund would remain the same as if no actual pension fund had been created. The current staff would indeed continue to be covered by the current pension scheme and it is assumed that almost no newcomers would retire before 2020. The employer's annual contribution to the fund would increase according to the number of new staff covered by the actual pension fund. This number appears high in the first years due to the large turnover of contract and temporary staff.

This scenario would therefore involve a higher cost than the current pension scheme in the short to medium term (13 520 million Euros over the 2013-2020 period instead of 12 600 million Euros). However, the cost would decrease significantly in the long run, when the pension fund reaches maturity.

	Projected number of active staff covered by the new pension fund from 2013	I Service cost (employer's contribution)	II Pension expenditure under the current pension scheme	III Total cost in Heading V [1] (I + II)
2013	4 200	40	1 400	1 440
2014	7 700	70	1 450	1 520
2015	10 700	90	1 500	1 590
2016	13 200	100	1 550	1 650
2017	15 500	130	1 600	1 730
2018	17 600	140	1 650	1 790
2019	20 000	160	1 700	1 860
2020	21 400	190	1 750	1 940
Total cost 2013-2020		**920**	**12 600**	**13 520**
2060	*55 000*	*800*	*1 100*	*1 900*
In the long term when the new pension scheme becomes mature	*55 000*	*800*	*0*	*800*

[1] With 2011 legal provisions and methodology

– **Scenario n°3: New pension rights would be covered by the real pension fund, while past pension rights would be covered by the notional fund**.

Under this assumption, the yearly pension expenditure of the current pension scheme would be lower than the forecast pension expenditure until 2020 if no actual fund is created. The employer's contribution to the actual fund would remain stable (at around 800 million Euros per year), but would be much greater during the period 2013-2020 than in Scenario n°2 (6.4 billion Euros compared to 920 million Euros).

Therefore, this scenario would entail an even higher cost in the medium term than scenario n°2 above, although the transition would be faster.

	Projected number of active staff covered by the new pension fund from 2013	I Service cost (employer's contribution)	II Pension expenditure under the current pension scheme	III Total cost in Heading V [1] (I + II)
2013	55 000	800	1 280	2 080
2014	55 000	800	1 320	2 120
2015	55 000	800	1 360	2 160
2016	55 000	800	1 400	2 200
2017	55 000	800	1 420	2 220
2018	55 000	800	1 450	2 250
2019	55 000	800	1 470	2 270
2020	55 000	800	1 490	2 290
Total cost 2013-2020		**6400**	**11 190**	**17 590**
2060	*55 000*	*800*	*300*	*1 100*
In the long term when the new pension scheme becomes mature	*55 000*	*800*	*0*	*800*

[1] With 2011 legal provisions and methodology

– **Scenario n°4: Actual fund covering one third of all newly acquired rights, covered by the pension contributions of the staff.** The remaining two thirds of pension rights, plus all pension rights acquired in the past, would continue to be covered by the notional fund. This scenario would entail transferring staff pension contributions to the investment fund and, given that one third of the pension costs would be partially covered by this fund in the future, pension expenditure would decrease by one third in the long run.

Under this assumption, until 2020 the pension expenditure under the notional pension scheme, covering two thirds of newly acquired pension rights, would be slightly less than the forecasted pension expenditure if no change is made (12 100 million Euros compared to 12 600 million Euros). There would be no employer's contribution to the actual fund, as one third of the newly acquired rights would be fully covered by the pension contributions of the staff.

Therefore, in the short and medium term, Scenario n°4 would be the least costly of all the scenarios for the EU budget. However, in the long term, the total cost in heading V would be twice that of the other scenarios (1650 million Euros as compared to 800 million Euros).

	Projected number of active staff covered by the new pension fund from 2013	I Service cost (employer's contribution)	II Pension expenditure under the current pension scheme	III Total cost in Heading V[1] (I + II)
2013	55 000	0	1 350	1 350
2014	55 000	0	1 400	1 400
2015	55 000	0	1 450	1 450
2016	55 000	0	1 500	1 500
2017	55 000	0	1 540	1 540
2018	55 000	0	1 580	1 580
2019	55 000	0	1 620	1 620
2020	55 000	0	1 660	1 660
Total cost 2013-2020		**0**	**12 100**	**12 100**
2060	*55 000*	*0*	*1 750*	*1 750*
In the long term when the new pension scheme becomes mature	*55 000*	*0*	*1 650*	*1 650*

[1] With 2011 legal provisions and methodology

4.8. Incentives for private pension provision

Nowadays, private pension schemes are being used increasingly in a number of Member States to achieve the objectives of adequacy and sustainability. In its Green Paper, the Commission pointed out the importance of providing sufficient opportunities for complementary entitlements: such as making it possible for people to have longer working lives and increasing access to supplementary pension schemes. In addition, the Commission underlined the need to put in place a proper framework for complementary retirement savings, the success of which depends above all on measures that increase the cost-effectiveness and safety of supplementary pension schemes.

Some Member States have introduced measures to complement their public pay-as-you-go pension schemes with private pre-funded schemes. However, the crisis has highlighted how vulnerable pre-funded pension schemes are to the financial crisis and economic downturns, and the need to review the regulatory framework so as to guarantee the safety of private pensions. It is also worth noting that the NATO pension scheme is entirely managed through private funds. Staff can choose to invest their holdings in private equity, bond and cash funds and may elect to make additional voluntary contributions to the scheme of up to 2% of basic salary.

As regards the EU Institutions, if the path of introducing mandatory or voluntary private supplementary pension schemes were to be followed, it would be essential to ensure that there was an appropriate framework for such a scheme. According to constant case-law, the EU Institutions, which act not only as an employer but also as a public authority, have a duty of care towards their staff. Therefore, it is important to make a careful assessment of the potential impact on the EU budget of the inadequacy or even bankruptcy of the private pension scheme.

If a decision was taken to introduce such incentives, the authorisation of tax deduction for those investing in private pension schemes could be considered a possibility, because it would involve a fairly low burden on the EU budget compared to other options, such as subsidising investment by staff in private pension schemes. The EU Institutions could propose opt-out or opt-in private pension schemes, in conjunction with private actors.

If the private pension schemes were to invest partly in equities, as is the case for example in the United Nations Joint Staff Pension Fund[23] or NATO, where staff can choose to invest their holdings in equity, bonds and cash funds, the eventual return rate on investment could be expected to be higher than the rate of return in the PSEO, but it would also be associated with higher risk.

Such a scheme has a number drawbacks which would need to be considered, principally the additional cost for managing the investment and the safety of investments and, therefore, future pensions.

5. OTHER ASPECTS THAT HAVE AN IMPORTANT IMPACT ON THE PENSION SCHEMES OF CIVIL SERVANTS

5.1. Use of contract agents and conditions of contract agents

By far the majority of Member States differentiate between civil servants and other public employees. In most Member States there are different rules for civil servants with regard to their legal status, recruitment procedures, job security, career and salary systems. However, in most Member States, civil servants and other public employees have the same or similar rules when it comes to social dialogue, ethical rules, disciplinary rules and in particular pension systems. According to the publication *Civil Services in the EU of 27, Reform Outcomes and the Future of the Civil Service*, Member States that have a separate pension scheme for civil servants and other public employees are Germany, Lithuania, Estonia, Cyprus, Belgium, France, Greece, Luxembourg, Spain, Austria, the Netherlands and Denmark. The

23 http://www.unjspf.org/UNJSPF_Web/page.jsp?role=info&page=Invest&lang=eng

remaining 15 have the same pension scheme for both civil servants and other public employees.[24]

The 2004 reform of the Staff Regulations established the category of contract agents in the EU Institutions. Since then, contract agents have contributed to the work of the institutions by performing administrative support tasks and by providing additional skills. At the end of 2009, there were around 9000 contract agents in total for all institutions and agencies, and around two thirds of the total were employed by the Commission. Under the Staff Regulations, the same pension scheme applies to officials and contract agents. This is in line with the situation in the majority of the Member States that have the same scheme for officials and for other public service employees.

As regards the provisions on the minimum subsistence figure[25], these refer to the basic salary of an official in grade 1 step 1. An official or other servant acquires 4% of the minimum subsistence figure per year of service, i.e. after 25 years of service the retirement pension of an official or other servant cannot be lower than the minimum subsistence figure. Although the same provisions apply to officials and temporary staff, contract agents in particularly in the lower grades benefit more from this provision, as their entitlements are generally lower. For example, a contract agent in function group I may be entitled to a pension equal to the minimum subsistence figure, which would exceed 70% of their final salary. However, this is the only exception to the rule that the maximum pension entitlement is set at 70% of the final salary in any event.

The replacement of officials by contract agents, although not directly related to pension cost, has a major impact on the overall cost of pensions as it limits the final salaries on which pension benefits are calculated. This is due to contract agents having a lower salary grid and a shorter average duration of contracts by comparison with officials.

The 2010 Eurostat study shows that the introduction of the category of contract staff in 2004 will generate considerable annual savings (300 million Euros in 2059).

Keeping the same pension scheme for officials and contract agents is important in order to preserve the attractiveness of contract agents' positions, so as to attract qualified staff. It is already difficult to achieve geographical balance among different nationalities, and proposing a less attractive pension scheme for contract agents would further reduce the ability of the institutions to achieve geographical balance for this category of staff.

5.2. Individual progression in the salary scheme

The 2004 reform of the Staff Regulations introduced changes in the career structure. Although it is not related directly to pension cost, it does have an impact on the overall cost of pensions because it limits the final salaries on which pension benefits

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[24] See *Civil Services in the EU of 27, Reform Outcomes and the Future of the Civil Service*, by C. Demmke, and T. Moilanen, Edition Peter Lang, 2010, p.98. See also Table 13 p. 99.

[25] Article 77, alinea 4 of the Staff Regulations states that the amount of the retirement pension must not be less than 4% of the minimum subsistence figure per year of service.

are calculated. These include lower entry level salaries combined with a longer career path involving more grades, but faster promotions. According to the 2010 Eurostat study, this aspect of the 2004 reform will generate annual savings of 94 million Euros in 2059.

The restructuring of the career stream in the AST function group provided for in the Commission Proposal will generate additional savings in the long term. In future, AST officials in charge of administrative, technical or training activities requiring a certain degree of autonomy (this excludes secretarial tasks), who wish to progress to the two highest grades (Senior Assistants), will have to demonstrate, in a selection procedure, that they possess an appropriate level of expertise and qualifications in terms of staff management, budget implementation and/or coordination. There is likely to be a new career structure for newly recruited secretarial staff with a linear career, as well as lower promotion rates than in the AST career and only six grades.

However, even though the progression of an individual in the salary scheme has an impact on pension costs, this aspect is only secondary when it comes to thinking about how to revamp the career system within the EU Institutions. It would be conceptually wrong to change the career system if its only aim were to achieve savings on pensions, while ignoring the fact that it has a major impact on active staff of the EU Institutions.

5.3. Gap between the benefits to employees of public service and private sector pensions

In almost all Member States, civil servants are subjected to separate regimes, and a separate pension scheme is often part thereof. There might be a number of reasons for having such special schemes, as well as pension benefits that are possibly higher than the general pension schemes. Firstly, pension benefits should be seen as a deferred portion of the civil servant’s salary that would be paid when they retire, and as an important component of a comprehensive package offered to civil service employees. Secondly, higher pension benefits in the civil service make it possible to attract highly qualified staff, even in cases where they are being paid a higher salary in the private sector for a comparable job with a similar level of responsibilities.

By offering higher pension benefits, the Member States can take into account the fact that, for certain job profiles, the level of salaries is lower than in the private sector and therefore has to be compensated by a higher level of social security. However, as the Green Paper points out, Member States are generally responsible for the design and organisation of their pension system and for pension provision. The gap between the benefits to public service employees and the level of private sector pensions is the overriding issue to be considered by the Member States. They are in charge of restructuring pension schemes in a manner which ensures that these pension schemes are adequate, sustainable and safe.

As regards the issue of whether there is a gap between the pension benefits of EU staff and those paid on the private market, it is important to realise that, as explained above, the main comparators for the pension benefits of EU civil servants, who are mainly expatriates, are the ones who recruit comparable staff and have a similar career and salary structure, i.e. other international organisations, national diplomatic services, and central government services in the Member States. As regards the private sector, the comparison should be based not only on pensions, but should be much wider and include other aspects, such as general salary levels and career progression, because of the huge gap between the private and the public sector in this respect.

Lastly, it should not be forgotten that many private multinational companies have supplementary pension funds and offer additional pension benefits as a way to attract and keep qualified employees.

5.4. Costs for the EU Institutions to provide pensions

The 2010 Eurostat study showed that the PSEO is not yet mature, and that the number of pensioners and pension expenditure are bound to increase until such time as the pension scheme reaches maturity. Given that the PSEO operates as a notional fund, the staff pay for the pension rights that they acquire in a given year from their pension contribution, which covers one third of the actuarial cost of those pension rights. This contribution, together with the employer's contribution which is not paid, is considered to be invested in long term bonds issued by the Member States. For the purposes of comparison, this would be the most conservative approach to adopt for a private pension fund, which gives low returns compared to a mixed fund.

In the assessment of the actuarial balance of the PSEO carried out in 2010, Eurostat calculated that the total service cost, which should be paid to the fund in order to cover the pension rights acquired in 2011 should be 1 206 million Euros. EU civil servants will pay one third of this amount, i.e. 402 million Euros, corresponding to 11% of their basic salaries. Therefore, the portion to be covered by the employer in 2011 is 804 million Euros. Absent any significant change in the other parameters, the total cost of pension rights, and therefore the employer's contribution, is likely to remain of the same order.

5.5. Role of pensions in the overall reward package for EU staff

When being offered a job, older people seeking employment are likely to give more consideration to the role of pensions in the reward package than are younger candidates. Also, candidates who have previously worked in the private or public sector have acquired some experience and sensitivity in dealing with retirement issues. Candidates who leave the system with which they are familiar to enter a new, unfamiliar system are likely to pay particular attention to this new system. Lastly, candidates who put a premium on (job) security and a predictable career over top salaries in less stable employment will pay greater attention to the pension scheme. The typical official newly recruited by the EU Institutions is likely to fall into one of these categories.

As the institutions typically employ persons who started their career elsewhere and who are therefore 35 years old on average, the importance of the pension system in the overall reward package is believed to be higher than, for example, for public employees in Member States who start their careers in public administration immediately after they graduate. The fact that almost all new recruits have previously worked elsewhere is also attested to by the number of transfers to the PSEO of pension rights acquired outside the institutions. On average, the officials who were in active employment on 31 December 2009 have transferred 1.6 years of acquired rights in the PSEO, which resulted from a much longer period of work in the Member States.

Another feature of new recruits to the institutions, which is also linked to the fact that they are relatively older, is that many of them have started a family or were about to do so around the time when they were recruited. Their individual situation is likely to prompt applicants to give careful consideration to the social benefits, including pensions, and to compare them with their other options.

Although the Commission has not carried out any specific research on this topic, which also appears difficult to assess methodologically, it is reasonable to conclude that pensions play a significant role in the decision by would-be employees to choose the EU Institutions as a career.

5.6. Future recruitment and retention needs of the EU Institutions

Although recruitment needs for officials for 2011-2013 at the Commission are estimated at 1,393 AD officials and 1,251 AST officials[26], as part of the envisaged Financial Framework 2014 - 2020 the Commission is proposing to cut staff in each EU Institution by 5 % during the period 2013 – 2017; this will be done in part by not replacing staff who retire or those whose contracts expire.

It should be mentioned that there is a growing geographical imbalance between nationals of different Member States and this is particularly visible in the case of certain nationalities. This is mainly due to the fact that the EU Institutions are confronting the challenge of offering sufficiently attractive working conditions to potential employees from those Member States.

Pension benefits should definitely be considered as part of the package that enables the most qualified candidates from all Member States to be recruiting and retained, including those countries with the highest salaries and the most competitive labour market.

5.7. Ensuring that future pension provision is fair across the EU workforce

Ensuring that future pension provision is fair across the workforce is a conceptual issue faced by Member States when reforming their own pension scheme. They need to protect acquired rights and, at the same time, ensure that the pension benefits and the burden of providing these benefits is distributed fairly across the different generations.

To a certain extent, the EU Institutions are confronted by the same issues. Following the reform of the Staff Regulations in 2004, there is now a slightly different set of rules that apply to the staff recruited before the effective date of the 2004 reform and after that date, because the staff members that were already in place are covered by transitional provisions. This was in line with the principle of acquired rights and non-discrimination.

[26] Human Resources Report 2011, p. 43.

Under the terms of the Commission proposal, the staff recruited before the entry into force of this proposal would be covered by a similar transition as in 2004 as regards the increase in the normal pension age. This transition will result in greater consistency between the situation of colleagues recruited before 2004 and those recruited after 2004.

5.8. Sharing risk between the EU Institutions (the employer) and employees

The PSEO is not directly exposed to investment risks because contributions are not paid to a real fund; thus the capital is not invested. Article 10 of Annex XII to the Staff Regulations indicates *"interest rates to be taken into consideration for the actuarial calculations shall be based on the observed average annual interest rates on the long term public debt of Member States…"*. Thus it is as if contributions were paid to a notional fund and the corresponding capital is invested in the bonds of Member States. This is probably the most conservative investment available, which means that the rate of return is rather low.

If the pension system were to be restructured in such a way that an element of risk is indeed included, it should be borne in mind that the staff of the EU Institutions might be ready to accept higher risk in return for a higher rate of return that would result in a lower contribution rate being necessary to maintain the pension scheme in balance. Nevertheless, since the institutions have the duty of care towards their staff, the issue of providing additional resources in case of the fund's failure to pay pensions remains.

The financial burden of the contribution to the pension system is not a risk in this sense. One third of this burden is borne by the staff of the institutions; the remaining two thirds are covered by the EU budget to which EU taxpayers contribute in their turn.

Member States operate different systems in this respect. It is not uncommon for public officials not to contribute to their pensions at all. The Member States submitted the following information on how the burden is shared between employer and employees:

Proportion of pension contribution paid by the employee and by the employer in the pension schemes applicable to civil servants in central government of Member States

Member State	Contribution paid by the employee (%)	Contribution paid by the employer (%)
AT	33,3%	66,7%
BE	0%[27]	100%
BG	Not specified	Not specified
CY	Not specified	Not specified

27 Please note that in Belgium a 7.5% contribution rate is paid by the employee to finance survivor's pensions only.

CZ	23.2%	76.8%
DE	0%	100%
DK	0%	100%
EE	0%	100%
EL	33,3%	66,7%
ES	16,6%	83,4%
FI	18,2% to 22% depending on the age	81,8% to 78%
HU	28.4%	71.6%
IE	Not specified	Not specified
IT	26,7%	73,3%
LT	11,4%	88,6%
LU	50%	50%
LV	27,2%	72.8%
MT	33,3%	66,7%
NL	30%	70%
PL	50% or 20% or 100%, depending on the scheme	50% or 80% or 0%, depending on the scheme
PT	40% or 33,3%, depending on the scheme	60% or 66,7%, depending on the scheme
RO	25.4% to 33.5%	74.6% to 66.5%
SE	0%	100%
SI	63,6%	36,4%
SK	29,2%	70,8%
UK	7.4% or 15.6%,	92.6% or 84.4%,

NB: France is not included in the table as no reply was provided to the questionnaire.

5.9. Wider EU staffing and HR policy to encourage longer working lives and adequate saving for retirement

In its proposal the Commission suggested increasing the normal pension age and enhancing the possibility of working beyond the pension age. The Commission will consider the human resources measures that would help elderly people to work, in addition to those measures that are already laid down in the Staff Regulations, for example the possibility of working part-time to prepare for retirement, subject to payment of a small supplement. Some of these measures do not require any change to the Staff Regulations and they would be implemented by the EU Institutions.

6. SAVINGS RESULTING FROM THE COMMISSION PROPOSAL

While savings in the pension cost from the 2004 reform of the Staff Regulations will continue to grow over time, the Commission proposal, if adopted, would yield further savings. A number of the changes to the Staff Regulations suggested by the Commission would directly limit the cost of pensions. These include: raising the normal pension age from 63 to 65, the effective postponement of the mandatory retirement age until 67, and limiting access to early retirement by raising the minimum age of retirement from 55 to 58.

Changes have also been suggested to the Staff Regulations which, while not directly related to pension cost, do have an impact on the overall cost of pensions by limiting the final salaries on which pension benefits are calculated. Careers of AST officials carrying out secretarial tasks would be reviewed and capped with the creation of a new function group (AST/SC). For other AST officials, access to the top AST grades (AST 10 and 11) would be limited by linking them to a higher level of responsibilities. The suggested 5% staff cut would result in a lower number of future beneficiaries and will also reduce future pension costs.

An analysis of the impact of these changes shows that the Commission proposal will significantly reduce pension costs in the long run. The Commission presents the pension related savings from three angles: the impact on pension expenditure in the long term, the impact on the service cost to be financed each year and the impact on pension liability.

The three approaches are complementary. The assessment of pension savings in the long term focuses on the time at which pensions are paid (Cash Flow Approach). Service cost focuses on the time when the pension rights are acquired and financed (Projected Unit Credit Method). Lastly, pension liability focuses on pension rights cumulated at a reference date (normally 31 December of each year).

6.1. Long-term Impact of the Commission Proposal on pension expenditure

If the methodology and the assumptions of the 2010 Eurostat study were used to measure the effect of the Commission proposal (including the 5% staff cut), the annual pension expenditure would grow more slowly over the projection period (2013 - 2059)[28]. This simulation shows that, if the Commission proposal entered into force on 1 January 2013, the annual pension expenditure after 2060 would decrease by an additional 500 million Euros. This would add to savings of 1 047 million Euros yielded by the 2004 reform of the Staff Regulations, giving total annual pension savings in 2059 of 1 550 million Euros. This means that the Commission proposal, if it were in force from 2013, would result in further savings of around 50% in annual pension expenditure.

[28] It must be noted that the 2010 Eurostat study on the long-term budgetary implications of pension costs has not been updated. Pension savings presented in this part were calculated with a simplified methodology.

The table below shows the total estimated savings in annual pension expenditure in 2059 (in constant prices) generated by the 2004 reform and the Commission proposal, if it entered into force on 1 January 2013.

Table: Impact analysis of the Commission proposal and the 2004 reform (million EUR) on annual pension expenditure in the long term (2059)

Item	2008 prices
Total impact of the 2004 reform:	**1047**
- Correction coefficients	120
- Establishment in 2004 of the contract agents' statute	300
- Salary progression due to seniority and promotions	-227
- Entry salary level	321
- Pension accrual rate	106
- Retirement table	426
Total impact of the Commission proposal	**500**
Total impact of the Commission proposal and the 2004 reform	**1547**

6.2. *Impact of the Commission proposal on the service cost*

The pension contribution rate is calculated annually in order to finance the pension rights that will be acquired in the coming year (service cost), regardless of the date from which the corresponding pension will be paid. The service cost represents the amount which would be paid into the pension fund, if it existed.

However, the service cost can only measure those aspects of the Commission proposal that directly reduce the cost of pensions, i.e. raising the normal pension age from 63 to 65, postponing the mandatory retirement age until 67 and limiting access to early retirement by raising the minimum retirement age from 55 to 58[29]. Other factors that indirectly limit the overall cost of pensions (see above) are left aside.

If the Commission proposal were in force[30], the service cost would be 9.5% lower than the cost currently calculated at 31 December 2010[31], i.e. it would be 1 092 million Euros instead of 1 206 million Euros. However, this saving would be seen only in the long term, once the new parameters are applied to all active members.

29 Their impact on the yearly service cost, expressed in percentages, is representative of the whole career service cost (i.e. total pensions to be paid till the person dies), if other assumptions remain unchanged (ceteris paribus).

30 Simulation based on active population at 31.12.2010, which exclude any impact due to change on the structure of the population.

31 Pension assessment at 31.12.2010 based on parameters and assumptions of the Staff Regulations in force from 2004.

The saving is likely to be negligible in the very short term and will increase gradually each year to reach about 9.5% as a result of the implementation of transitional measures.

The calculation of the current service cost is based on the assumption that the staff recruited prior to the 2004 reform of the Staff Regulations and after that reform will retire at the ages of 63 and 64 respectively. This has been compared with the service cost calculated on the assumptions deriving from the Commission proposal (assumed minimum retirement age of 65 and assumed maximum retirement age of 67). Changes to the minimum retirement age, a penalty for early retirement and incentives for late retirement have also been considered.

6.3. Impact of the Commission proposal on the PSEO liability

The Commission proposal would have an impact on the PSEO liability because calculation parameters would have to be updated accordingly[32]. The gross PSEO liability at 31 December 2010 has been valued at 37 702 million Euros, including family allowances and the effect of correction coefficients.

The increase in the normal pension age from 63 to 65 provides a greater incentive for late retirement (work until age 67) and limited access to early retirement (by raising the minimum retirement age from 55 to 58) is bound to reduce the PSEO liability.

The above measures only have an impact on the liability of contributing members, which was evaluated at 21 246 million Euros at 31 December 2010 (56% of the total PSEO liability).

The savings of the pension cost generated by the Commission proposal at an individual level depends on the age of the person. Higher savings will be made for young staff aged under 30 years on 1 May 2013, whereas, the transitional measures mean that there will be no savings in relation to staff aged 59 and over.

The simulations show that the Commission proposal would reduce the liability of all contributing members by 14.5%; this means that the liability at 31 December 2010 would be 18 166 million Euros instead of the current figure of 21 246 million Euros.

7. CONCLUSIONS

After having considered the above, the Commission has reached the following conclusions:

– As regards the accrual rate, the basis for the pension, the maximum possible pension rate and the staff contribution rate, the PSEO is fully in line with the schemes of the Member States. As far as some aspects are concerned, such as the level of the employee's pension contribution, the PSEO is among the

[32] The PSEO liability also called "Defined Benefit Obligation" (DBO) is determined by discounting the estimated future cash outflows attributed to past services using a discount rate based on interest rates of government bonds denominated in the currency in which the benefits will be paid, and with maturity terms approximating those of the PSEO. This liability corresponds to pension rights acquired by active staff (pension contributions) and to transfers from other pension schemes.

schemes of the Member States where the rate is the highest. As far as the above issues are concerned, the PSEO is also in line with the Green Paper.

– The EU Institutions fall within the range of the schemes of Member States for national officials as regards normal pension age. However, in order to comply fully with the orientations of the Green Paper, the measures that are set out in the Commission proposal need to be implemented. In particular this involves restricting early retirement by raising the minimum retirement age to 58 and lowering the number of early retirements without reduction of pension rights to 5%, ensuring longer working lives by raising the normal pension age to 65 and postponing the mandatory retirement age to 67. These measures would bring the Commission into line with the most advanced Member States, whereas many of them still have to carry out similar reforms.

– If a decision were taken to consider establishing an actual pension fund, such a measure would result in a higher expenditure on the pension scheme in short and medium term. However, it would reduce the pension costs in long term, since pension expenditure would be partly or fully financed from the pension fund, depending on the solution adopted.

– The measures contained in the Commission proposal, if adopted, would have a considerable impact in terms of reducing long-term pension costs. In the long run, the annual pension expenditure would fall by around 500 million Euros, and the service cost – which reflects the amount to be invested in the real pension fund if it existed – would be reduced by 9.5%. They would have an immediate impact on the share of the pension liability for active staff, which would fall by 14.5%.