Newsletter

February 2016

New rules for supplementary pensions in 2016

The law passed on 18 December 2015 to ensure the sustainability and social character of the supplementary pensions and to strengthen the supplementary character with regard to the retirement pensions was published in the Belgian Official Gazette of 24 December 2015.

Now that these texts have been approved, we will take a closer look at the changes that have been enacted. We will focus on the measures that apply to employees and their supplementary pension schemes. The impact on self-employed persons (executives) is roughly the same.

1. Summary

1.1. The minimum return guarantee is to decrease

If payments into the plan are made by the employee or by the employer within the framework of a Defined Contribution plan (DC plan) or a cash balance plan, the employer is legally required to guarantee a minimum return.

Until 1 January 2016, this guaranteed return was equal to a fixed percentage, namely 3.25% of the payments by the employer and 3.75% of the payments by the employee.

Since 1 January 2016, the guaranteed return varies per year. This is determined on the basis of the average of the 10-year Belgian OLOs multiplied by 65%; this percentage can be adjusted in future. The result of this calculation may not be less than 1.75% and may not exceed 3.75%.

In concrete terms, as of 1 January 2016, the guaranteed return for contributions by employers as well as employees has been reduced to 1.75%.

In case of adjustments to the guaranteed return, the legislator has come up with two methods to protect the established reserves in the long term. In addition to the existing vertical method (savings account method), which can be used for pension plans that are structured in practice within a pension fund or Tak/Branch 23 group insurance, there is also the horizontal method for pension plans that rely on a Tak/Branch 21 group insurance.

1.2. As a minimum, the pension institution must offer death benefit insurance if the employee’s employment contract is terminated

As of 1 January 2016, persons who took part in a supplementary pension scheme will be given an additional choice of options for the acquired reserves if the employment contract is terminated. At that point, they can choose to have the acquired reserves remain with the pension institution of the former employer with the addition of death benefit coverage that is in line with the amount of the acquired reserves.

1.3. Payment date for supplementary pension = legally mandated pension

The basic rule is that the supplementary pension scheme pays the benefit on the date that the insured person reaches the legal (early) retirement age.

Simultaneously with the adjustments made to the legal retirement age, transitional arrangements apply to those who have at least reached the age of 55 in 2016. A transitional measure also applies to persons who benefit from an SWT framework (framework for unemployment with company supplement, previously referred to as the bridging pension) registered before 1 October 2015. They can still receive benefits from the age of 60 if the pension regulations provided for such benefits.

Some pension plans grant participants favourable facilities if their employment contract is terminated before the legal retirement age. These favourable provisions (anticipation rules) will become completely null and void except for plan members who are 55 years or older in 2016.

The logical result of this is that the retirement age specified in new pension regulations can no longer be less than the legal retirement age. This principle also applies to changes in the retirement age for existing pension plans and for new employment contracts as of 1 January 2019.

Employees who earn extra income on the side after their legal retirement age can no longer be covered by a pension entitlement.

1.4. Additional IFRS accounting requirements for DC plans

If your company is subject to the IFRS (IAS19/FAS87), you may need to take a different approach to your Defined Contribution plans as a result of the new legislation with regard to the minimum guaranteed return for the employer.

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2. Changes to the minimum guaranteed return for supplementary pensions: what does this mean for participants?

2.1. What type of plan is impacted?

Which plans are impacted by the changes to the minimum guaranteed return as implemented in the Supplementary Pensions Act (in the following referred to as the WAP guarantee)?

2.1.1. Defined Benefits plan (DB plan)

This new legislation does not have any impact on the supplementary pension schemes that are structured as a Defined Benefit plan (so-called DB plans) and that are funded solely by the employer. After all, under these pension plans, the amount of capital available on the end date is fixed and compulsory. Employees who are participants in such plans will therefore not be affected by the new legislation.

However, the new WAP guarantee will have an impact on DB plans that are also partially funded by the employee, in particular on the employee contributions. However, in practice, the amount of capital available on the end date will almost always exceed these employee contributions and the WAP guarantee. Accordingly, the new legislation will also not have any impact for employees on the end date if they participate in this type of plan (DB plan also funded by employee contributions).

2.1.2. Defined Contribution plans (DC plan) and Cash Balance plans

The new legislation does have consequences for supplementary pension schemes that are structured as Defined Contribution plans (so-called DC plans) or Cash Balance plans. Under these pension plans, the amount of the contributions paid into the plan is fixed, but the amount of capital available on the end date depends upon the return realised during the accrual phase in the case of DC plans; in Cash Balance plans, the return is also defined beforehand.

2.2. What exactly are the details of the new legislation?

2.2.1. Legal obligations incumbent upon the organiser/ employer before the new legislation

The legislation with regard to supplementary pensions specifies that the employer must provide a WAP guarantee for a contribution paid into the plan that is equal to 3.25% for employer contributions and 3.75% for employee contributions and must do so until the date on which the participant leaves the company or reaches retirement age or the date on which the plan is terminated.

2.2.2. Legal obligations incumbent upon the organiser/ employer after the new legislation

The substantive details of the new legislation are as follows:

As of 2016, the exact amount of this WAP guarantee to be provided by the organiser will be variable and will depend upon the return realised on Belgian linear bonds (10-year OLOs) as calculated with the following formula:

65% of the average return realised over the last 24 months on 10-year OLOs, rounded off to 0.25%.

However, the WAP guarantee must always be equal to a minimum of 1.75% and may never exceed a maximum of 3.75%.

If the supervising authority (National Bank of Belgium: NBB) is of the opinion that such an increase is insurable, the figure of 65% used in the formula could potentially be increased to 75% in 2018 and possibly to 85% in 2020. If this increase is not implemented, then the NBB must provide a recommendation in this regard each year.

The WAP guarantee is determined a new each year. The result of this annual calculation must differ by at least 0.25% from the percentage applied in the previous year in order for the WAP guarantee percentage to be revised in future. The Financial Services and Markets Authority (FSMA) will publish the applicable WAP percentage each year no later than 1 December.

In contrast to the situation that existed before 2016, the WAP guarantee will in future also not make any distinction between the employer contributions and the employee contributions. Both contributions will be covered by the same WAP guarantee.

The WAP guarantee for 2016 was set to the minimum percentage of 1.75%.

In case of adjustments to the WAP guarantee, the legislator has come up with two methods to protect the established reserves in the long term for all pension plans established prior to 1 January 2016. In addition to the existing vertical method (savings account method), which can be used for pension plans that are structured in practice within a pension fund or Tak/Branch 23 group insurance, there is also the horizontal method for pension plans that rely on a Tak/Branch 21 group insurance.

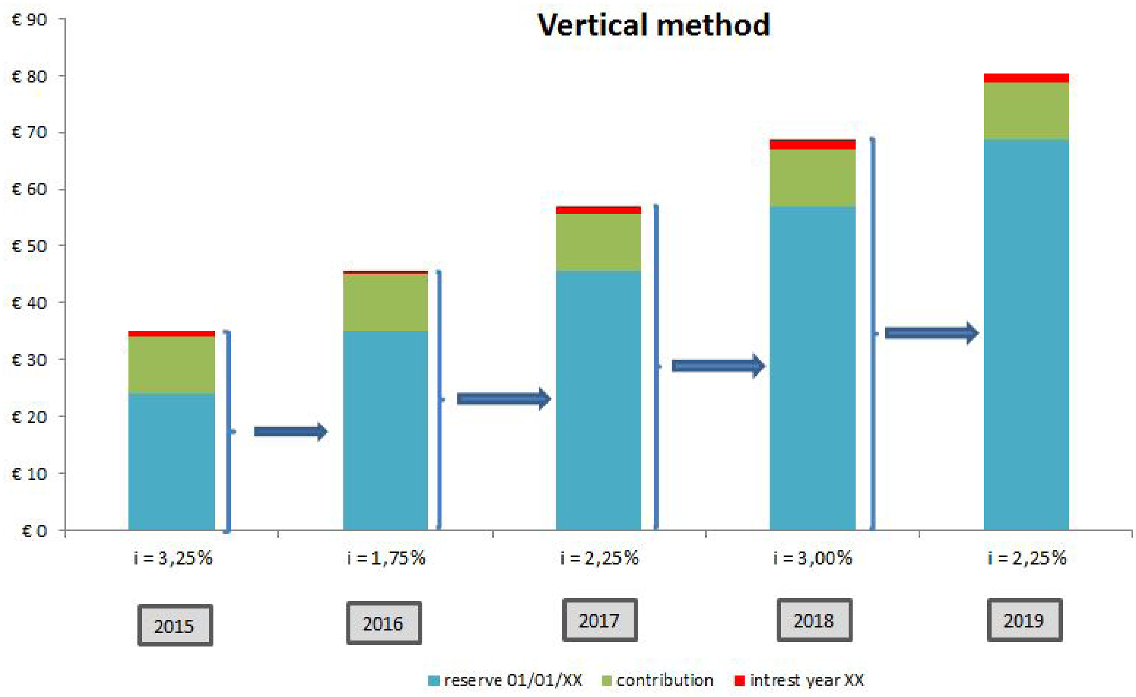
2.2.2.1. Pension fund / Tak/Branch 23 insurer ("vertical" method)

The so-called vertical method can best be compared to the method used for the traditional savings account. The following simplified example illustrates the vertical method.

Example:

- The participant participates in a DC plan funded by the employer.
- As of 31 December 2015, the participant has accrued a reserve of €35.
- In future years, a contribution of €10 will be repeatedly paid into the plan.
- The change in the WAP guarantee over time is as follows:
    - until 31 December 2015: 3.25%
    - from 1 January 2016: 1.75%
    - from 1 January 2017: e.g. 2.25%
    - from 1 January 2018: e.g. 3.00%
    - from 1 January 2019: e.g. 2.25%

The illustration below makes it clear that, for each calendar year (2016, 2017 etc.), the WAP guarantee determined for that calendar year will apply to all the accrued reserves, including the new contributions paid into the plan during that calendar year.



2.2.2.2. Tak/Branch 21 insurer ("horizontal" method)

The legislator has introduced a second method for those pension plans in which the pension institution (often an insurer) guarantees a specific return on the contributions paid into the plan up until the pensionable age for that pension plan (often referred to as Tak/Branch 21 products).

The principle underlying the horizontal method is to permanently link the contributions during a calendar year to the WAP guarantee for that calendar year. In other words, the WAP guarantee that applies when the contribution is paid continues to apply throughout the entire term, i.e. until the participant leaves the company, retires or until the plan is terminated.

We will illustrate the horizontal method using the same example as we did for the vertical method.

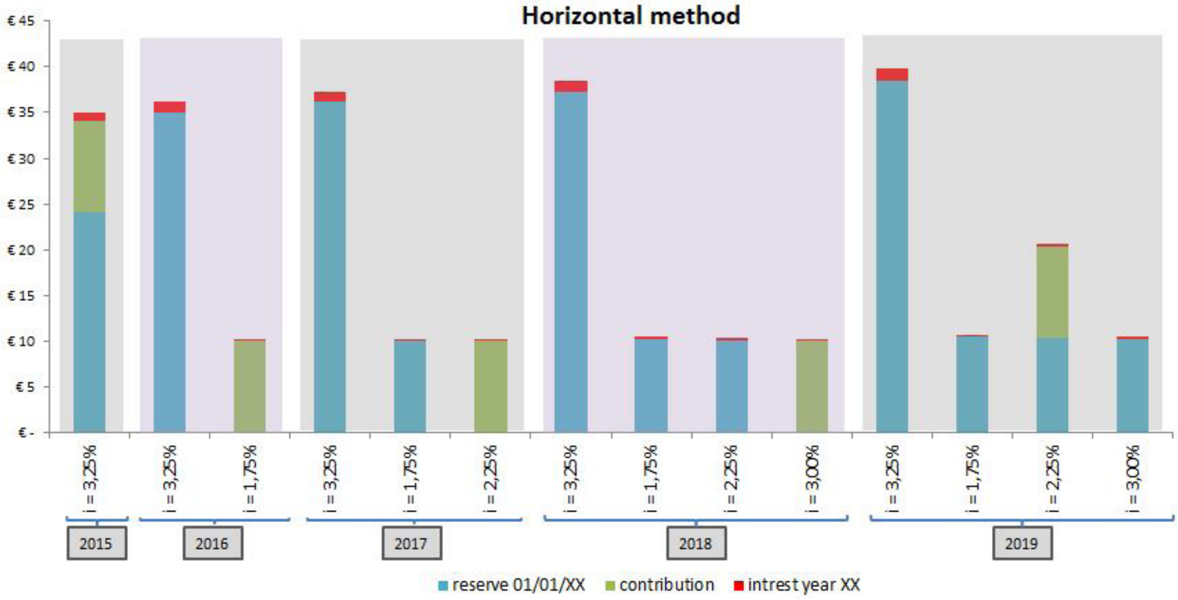
Example:

- The participant participates in a DC plan funded by the employer.
- As of 31 December 2015, the participant has accrued a reserve of €35.
- In future years, a contribution of €10 will be repeatedly paid into the plan.
- The change in the WAP guarantee over time is as follows:
  - until 31 December 2015: 3.25%
  - from 1 January 2016: 1.75%
  - from 1 January 2017: e.g. 2.25%
  - from 1 January 2018: e.g. 3.00%
  - from 1 January 2019: e.g. 2.25%

Under the horizontal method, the contributions paid into the plan up to and including 31 December 2015 are in future also permanently linked to the 3.25% WAP guarantee for employer contributions (3.75% for employee contributions) that applied until 31 December 2015.

As of 1 January 2016, the WAP guarantee is set at 1.75%, and this percentage will be applied to the contributions paid in 2016 throughout the entire term until the participant leaves the company or reaches retirement age. In our example, as of 2016, the participant will therefore have two "savings accounts" with a fixed rate of return until retirement. If the WAP guarantee is again adjusted in the future (see illustration), a new additional "savings account" will again be opened for each adjustment. In this way, a maximum of nine "savings accounts" with a fixed WAP guaranteed return (1.75% - 2.0% - 2.25% - ... - 3.5% - 3.75%) may be opened in the future.

If we apply this to illustrate our example:



2.2.2.3. What about changing the method used?

With regard to existing pension plans established prior to 1 January 2016, the law does not allow one to choose freely between the vertical or horizontal method. The method of guarantee can be changed only by modifying the pension commitment. To be more specific, there are two possible options in this regard: a change of pension institution (insurer or pension fund) or a change of product (Tak/Branch 21/Tak/Branch 23).

What if the change is not accompanied by a transfer of reserves? If this is case, the "new" method applies only to the contributions paid after the date of the change. However, if the reserves are transferred, then the "new" method also applies to the reserves transferred as of the date of the transfer.

For new supplementary pension schemes, the organiser can choose which guarantee method will apply regardless of what type of product is chosen. If no choice is made, then the guarantee that applies will be in line with the principles described above.

2.2.3. What doesn't change?

Several aspects in relation to the application of the WAP guarantee have not been changed under the new legislation and will therefore remain in force in future as well:

- If the participant's employment contract is terminated during the first five years of participation, the WAP guarantee will be replaced by the level of inflation but this will never exceed the WAP guarantee.
- After the participant's employment contract is terminated, the WAP guarantee that applies to passive participants (so-called "sleepers") is 0%, i.e. preservation of capital.
- The WAP guarantee applies to that part of the contribution intended for the accrual of capital and not to the part intended for risk insurances (risk of death, invalidity, etc.).
- A reduction of the costs (up to a maximum of 5%) may be taken into account for the employer contribution.

2.3. Distinction between organiser/employer and pension institution/insurer

It is important to always distinguish between the WAP guarantee provided by the employer (as described above) and the returns applied by the insurer/pension fund.

The guaranteed return that the employer must provide is based on the WAP and is used, when necessary, to supplement the return applied by the insurer/pension fund.

Initially, in case of a pension plan administered by an insurer/pension fund, the latter will apply a specific rate of return on the individual contracts of the participants. Only if the cumulated return applied by the insurer/pension fund is less than the WAP guarantee provided by the employer to the participants (employees), will the WAP guarantee actually come into effect.

The guaranteed return in Tak/Branch 21 presently being offered by insurers to employers/organisers is roughly around 1.00%. This means that, even after the decrease in the WAP guarantee provided by the employer, the guaranteed return provided by the insurer is (still) inadequate to completely cover this obligation. A deficit is therefore still possible unless the insurer grants sufficient profit-sharing on the contract.

3. Additional option of choosing death insurance in case of termination of employment

There was often no minimum death coverage for passive participants (the “sleepers”) who took leave of their employer and chose to keep the accrued reserves with their existing insurer/pension fund.

In such situations, the participant had the following four options based on the WAP:

- Transferring the accrued reserves to the pension institution of the new employer or the relevant sector plan
- Transferring the accrued reserves to a pension institution that distributes the total profit among the participants and limits the costs (so-called “KB 69 institutions”)
- Allowing the accrued reserves to remain in the pension plan administered by the pension institution of the former employer (the default option if no choice is made)
- Transferring the accrued reserves to the receiving system of the former employer’s pension institution.

As of 1 January 2016, every participant whose employment contract is terminated must be offered a fifth option, which makes it possible for the “sleeper” to at least use the accrued reserves for death insurance coverage:

- Choosing to have the acquired reserves remain with the pension institution of the former employer with the addition of death benefit coverage that is in line with the amount of the acquired reserves.

This death insurance coverage is funded by the participant in question. If the participant opts for death insurance, the total amount of capital accrued on the end date will be less than if the participant does not opt for this coverage.

The “sleeper” has a period of 12 months to make this choice.

4. Payment date for supplementary pension

4.1. General rule

The basic rule is that the supplementary pension scheme starts paying benefits on the date that the participant reaches the legal (early) retirement age and actually starts receiving retirement benefits.

There is one exception to this basic rule: benefits can still be paid out starting on the date that the participant becomes legally eligible for (early) retirement benefits even if such benefits are not yet paid. However, in order to start paying out benefits on this alternative date, this option must be included in the pension plan regulations.

Starting no later than 1 January 2017, Sigedis will inform the pension institution with regard to the retirement of the participant (instead of the organiser or the participant themselves if no longer employed).

As of 1 January 2016, there will also be no end date prior to the legal retirement age for advance payments and pledges.

4.2. Transitional measures

Simultaneously with the adjustments made to the legal retirement age, transitional arrangements in exception to the general rule apply to those who have at least reached the age of 55 in 2016. To be more specific, the transitional measures for these participants are as follows:

Date of birth	Receiving benefits from the supplementary pension scheme
Prior to 1 January 1959	60
During 1959	61
During 1960	62
During 1961	63

Attention: this transitional measure applies only if the pension plan regulations in place before 2016 allow for the participant to receive benefits from the supplementary pension scheme at this age.

An additional transitional measure applies to former employees who became a participant of an SWT (framework for unemployment with company supplement, previously referred to as the bridging pension) at the age of 55 or more; if the Minister of Employment was informed of the SWT before 1 October 2015, benefits may still be paid out from the age of 60. Again, this applies only if this option was also included in the pension plan regulations.

4.3. Elimination of favourable anticipation rules, retirement age regulations and activities after retirement

4.3.1. Elimination of favourable anticipation rules

Many pension plans contain financial incentives for participants who take early retirement, which mitigate or eliminate the financial impact of such early retirement on the supplementary pension.

As of 1 January 2016, such regulations are absolutely null and void with the exception of the existing regulations that may still be applied for participants who reach the age of 55 no later than 31 December 2016. The elimination of these rules may also not result in any decrease in the accrued reserves.

4.3.2. Retirement age regulations

The retirement age specified in new supplementary pension contracts may not be less than the legal retirement age. Any adjustments made to the retirement age in existing supplementary pension contracts must involve only an adjustment in line with the legal retirement age.

In addition, the existing contracts are automatically assumed to work with a retirement age that does not precede the date on which the participant reaches the legal retirement age if the participant in question has been employed since 1 January 2019.

4.3.3. Activities after retirement

Employees who earn extra income after their legal retirement age may no longer become participants in pension or solidarity commitments. This does not apply to pensioners who were already participants before the new legislation came into force.

5. Henceforth IFRS accounting requirements for DC plans

If your company is subject to the IFRS requirements, then you will also have to comply with these IFRS regulations (IAS 19/FAS 87) with regard to the valuation of your supplementary pension schemes in your accounts.

The general principle within IFRS is that the only requirement for Defined Contribution plans (DC plans) is the payment of the contribution itself. Within the Belgian context, the risk framework is expanded in view of the minimal guaranteed return (WAP guarantee) for the employer.

Until the introduction of the new legislation referred to above within the framework of the WAP guarantee, it was generally accepted practice to simply enter any applicable WAP shortfall into the books on the valuation date.

As a result of the new legislation and, in particular, the introduction of the horizontal method (applicable to Tak/Branch 21 insurance policies) whereby a specific WAP guarantee remains permanently linked to a payment, it would be reasonable to increase the risk profile estimate under IFRS regulations.

If you have any questions in this regard or receive any questions from your auditor, we would be happy to assist you further in determining the appropriate IFRS valuation.

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