elipsLife your insurance | echo 06

Our three-pillar principle is a highly intelligent system

Jürg Brechbühl | Director of the Federal Social Insurance Office, in an interview with elipsLife

elipsLife echo: Mr Brechbühl, Switzerland's three-pillar retirement provision system serves as an example to the rest of the world, but in our own country it repeatedly comes under pressure. Why these different perceptions?
You know the proverb that a prophet is without honour in his own country. It can be said with certainty that our three-pillar principle is a highly intelligent system. Why? The risks faced by the AHV (Federal Old Age and Survivors' Insurance) are very different from those involved in the employee benefits insurance: while at the AHV we are confronted by demographic developments, the employee benefits insurance is exposed to a capital market risk. Our system allows us to handle these different risks in different ways. Of course, the three-pillar system also has some problems. We have to do our homework, and comparing ourselves to other countries will not help much. As our society becomes ever more complex, the solutions in our system will also become more complex.

What is your personal assessment of the standard of the employee benefits insurance in Switzerland?
When we compare ourself to other countries, we certainly do not have to hide in the shadows. We have a good system of retirement provision. With our three-pillar principle, which also includes the supplementary benefits, we have mostly solved the problem of poverty among the aged. The extra-mandatory component of the employee benefits insurance makes provision for different professional categories, providing a very comfortable cushion in old age. On the other hand we also have areas where the statutory benefits, i.e. 60% of the previous income covered by the AHV and employee benefits insurance, barely cover the mandate. In these areas we must be sure not to reduce the level of benefits during future reforms of the pension system.

Left-wing politicians demand the expansion of the first pillar, mainly to the disadvantage of the second pillar. Experience gained abroad, however, has shown that concentrating on the first pillar results in massive government debt. How sensible then would it be to expand the AHV?
In the coming months we will be confronted by the "AHV Plus" popular initiative launched by the Swiss Trade Union Federation which demands an expansion of the AHV by 10%, but not at the cost of the employee benefits insurance. At the AHV we have to contend with a demographic challenge. To solve this challenge we proposed increasing the value added tax by up to 2% until 2030. If we should now also further expand the AHV benefits, we will face an additional need for funding.

In Switzerland there is a clear trend towards the individualisation of retirement provision. What do you think of this development?
With our reform and the introduction of a flexible retirement age – which is new – we are also trying to individualise the first pillar to some extent. Currently there are no choices in the first pillar. It is therefore certainly the right thing to further individualise the retirement age. In the employee benefits insurance, however, we must be careful not to go to the other extreme. The employee benefits insurance already offers many options for individualisation, which could lead to a rebuttal of the solidarity principle in this area. Examples of this are the different options for the lump sum payable at death or the promotion of lump-sum payments on retirement, which means that practically all funds are withdrawn from the collective of insured. Individualisation is clearly reaching its limits in the employee benefits insurance, maybe because too much was allowed in the past.

Difficult times are predicted for pension funds, particularly as a result of demographic developments, high discount rates and low interest rates. Will the pension funds – and therefore all of us – become victims of unfundable benefit promises?
The pension funds have already been in stormy waters for the past ten years. We have known for ten years that a pension fund cannot earn the yield it needs to finance the conversion rate without an offensive investment portfolio. The current BVG conversion rate is clearly too high, and this must be corrected. The Federal Council has tabled its proposals. However, as it wants to retain the benefits, the capitalisation of pension funds must be strengthened by higher contributions. Many pension funds have already made this correction to the extra-mandatory benefits. One thing is certain: the employee benefits insurance can only ever pay out the benefits that have also been earned.

A reduction in benefits seems unavoidable, whether in the form of lower conversion rates or an increase in the retirement age. Until now it has seemed as if it is always the payers of contributions who have to carry the burden. For how long can we continue to protect the pensioners in the restructuring of the pension system?
This is the wrong question. We must rather ask ourselves what parameters are needed to ensure that pensions are solidly financed. If these parameters are secured, this question will not arise. That pension funds these days can suffer an actuarial deficiency is related to the fact that some parameters are wrong. If a conversion rate must be guaranteed that cannot be financed with existing investments, the problem must be solved. If we should start to correct or reduce pensioners' benefits now, this would lead to a second, in my view much bigger, problem: confidence in the employee benefits insurance will be eroded. How can I trust an insurance scheme that takes away a considerable portion of my gross salary every month but does not give me any certainty about my pension? Everybody is entitled to certainty when it comes to planning his or her future. We must therefore set the parameters to make sure that the benefits are financed.

The Occupational Pension Supervisory Committee (OAK BV) assumed supervision of the cantonal pension fund supervisory authorities on 1 January 2012. Previously this was the remit of the Federal Social Insurance Office. What changed for pension funds under the OAK BV?
Nothing much should have changed for most pension funds as they were already subject to the direct supervision of the cantonal authorities. The situation did, however, change for national pension funds such as the pension fund of the Swiss Federal Railways or the collective foundations managed by the insurance companies. These institutions were previously supervised by the FSIO but now also report to the competent cantonal supervisory authorities. But this is just a change in supervisory competence, as nothing has changed with regard to the supervisory provisions.

Autonomous collective foundations and full-value insurers are two options in the employee benefits insurance. Collective foundations are subject to cantonal supervision, while full-value insurers are supervised by FINMA. Does this not mean that we apply unequal regulatory provisions to these institutions with regard to solvency capital, investments or partial liquidation?
The structural reform tried to redress the previous unequal treatment. For pension funds insured at full value, the comparison is even more difficult, as these pension funds actually do not have any assets because the assets were transferred to the insurance company backing the pension fund. The insurance company is subject to regulation by FINMA, while autonomous or semi-autonomous collective foundations are independent asset holders and manage their investments themselves. In contrast to insurance at full value, the foundations can suffer an actuarial deficiency, which also explains the different effects of a partial liquidation. Basically the same rules apply, but as a full-value insurance scheme can never suffer an actuarial deficiency, partial liquidation is also never a problem. If a collective foundation on the other hand suffers an actuarial deficiency, a partial liquidation can become a problem and might lead to reduced vested benefits.

It is generally accepted that small pension funds do not have sufficient risk capacity. Do you agree?
Such pension funds are usually affiliated with a collective foundation. Here too there are two options: either the collective foundation has taken out insurance at full value to cover its investment risk, or the pension funds affiliated with the collective foundation bear the investment risk themselves. Generally it is true that the smaller the pension fund, the more interested it is in belonging to a collective foundation with insurance at full value. If a pension fund's risk capacity is higher, a solution that allows it to partly or entirely determine its own investment strategy is more interesting.

So you would say that a bundling of pension funds does not make any sense?
No, it cannot be said in general that small pension funds should be amalgamated. Even small pension funds can belong to companies that wish to have their own pension fund. However, the concentration of pension funds shows that there is a need to join larger pension funds. This is also a consequence of the concentration seen in the business world. It is one of the strengths of our system that every company can choose what kind of pension fund it wants. The pension fund's risk profile must suit the company, but it is unimportant whether it is a big or small pension fund.

Full-value insurance solutions are accused of not being transparent enough. Do you think it is true that financial security under full-value insurance solutions is "bought" with excessively high risk premiums, which are effectively advance restructuring contributions?

We are investigating whether risk premiums are too high as part of the reform of the retirement provision system. FINMA's disclosure report shows that the risk premiums that are collected are around twice as high as the risk benefits that are paid out. This should be questioned, as it seems reasonable to assume that the risk premiums finance the conversion rate. Another question is whether this problem only affects full-value insurers, or whether autonomous pension funds also have to use similar methods to cope. Nowadays it is impossible to finance a conversion rate that is too high via premiums, as this would only work if nobody ever leaves the pension fund and no vested benefits therefore have to be paid out. Risk premiums on the other hand remain with the pension fund. This leads me to believe that some autonomous pension funds also use risk premiums to finance the conversion rate.

These days we often hear about overregulation, also in the pension sector. Too much regulatory interference leads to higher costs. Should the FSIO not endeavour to minimise the regulatory hurdles as much as possible in the interests of the insured?

You are absolutely right. However, less regulation presumes that all pension fund players act exclusively in the interests of the insured. When we propose a new regulation or Parliament adopts such a regulation the intention is not to hogtie the pension funds. Practically all provisions adopted as part of the structural reform of the BVG were intended to remedy grievances at some pension funds or to protect the insured. Regulation can only be reduced if all pension fund players act in the best interests of the insured.

The requirements to be met by the trustees of pension funds are continually on the increase. Does this spell the end of the militia system in the employee benefits insurance?

As the militia system is one of the strengths of the pension funds, we must make sure that it continues. In the end a pension fund is kept afloat by the contributions of the employer and the employees, and it is important that both providers of capital can decide together what should happen with the money. I therefore attach great importance to the militia system. On the other hand, the pension funds manage around 620 billion francs in assets, and these billions must be managed with a certain amount of expertise. Trustees must therefore be required to continuously learn and educate themselves further.

At the beginning of our interview you assessed the current state of the employee benefits insurance in Switzerland. What will the next BVG revisions contribute in this regard?

The Federal Council has proposed a comprehensive reform of the retirement provision system that is designed to secure the AHV and BVG benefits. It has determined key values that we are now using as the basis for preparing the draft law. As we are revising the BVG instead of generous extra-mandatory solutions, the reforms focus only on the minimum retirement provision – and in this area there is no downward leeway. With the corrective measures proposed by us it will be possible for us to maintain the level of benefits provided by the BVG.

Personal information

Jürg Brechbühl was born in 1956 and has been the Director of the Federal Social Insurance Office since 1 July 2012. After studying law at the University of Basel he joined the Pensions Section of the FSIO as a legal advisor. In 1987 he became an assistant to the FSIO directorate before taking up the post as Head of the Pensions Section and Deputy Head of the AHV/EO/EL Section in 1988. He was promoted to Chief of Staff in 1997, and in 2000 he was appointed Deputy Director of the FSIO and Head of the Old Age and Survivors' Insurance domain, with responsibility for the AHV and the second pillar. In 2005, Mr Brechbühl left the FSIO to become a private insurance consultant, and served on the management boards and boards of trustees of several pension funds until June 2012.