INSOL INTERNATIONAL

Pensions and Insolvency – An International Survey

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International Association of Restructuring, Insolvency & Bankruptcy Professionals

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Price £100.00 plus post & package

ISBN: 978-1-907764-19-6

Published November 2015

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INSOL INTERNATIONAL

International Association of Restructuring, Insolvency & Bankruptcy Professionals

This latest publication from INSOL International gives a detailed overview of the restructuring and insolvency law governing pensions in twenty one key jurisdictions around the world. Thanks to the contributions of more than twenty leading restructuring and insolvency professionals, this guide offers a detailed and thorough overview of many aspects of pensions and insolvency.

In almost all jurisdictions, any restructuring or insolvency brings with it an examination of the debtor's liability for pension plan entitlements. In many countries pension entitlements have a special priority, are subject to a dedicated legal framework and governed by an independent or government authority.

Accordingly, the assessment and recovery of pensions is a very important element of our worldwide restructuring and insolvency practice. In the right circumstances, pension plan entitlements can be preserved or restored - at the same time, though, the legal and statutory framework governing pensions can be very complex and if not successfully navigated, can adversely impact the restructuring or insolvency.

For all of these reasons, the information set forth in this publication should offer a very helpful practical guide for any restructuring and insolvency practitioner. Specifically, it discusses the legal framework for pension plans, regulating authorities, governance of pension plans, compensation funds, defined benefit pension plans, remedies and cross-border features of pension regimes.

On behalf of INSOL International and all of its associated restructuring and insolvency practitioners, I thank the project leader Gale Rubenstein of Goodmans LLP Canada and everyone else whose hard work has gone into producing this excellent resource.

Mark Robinson
President
INSOL International

Foreword

Providing basic financial security for retirement has become a major societal challenge globally during the last number of years of economic turmoil. Stretched government coffers render government funded support for the retired more difficult. At the same time, private pension plans that provide defined benefits, long a cherished feature of labour contracts and a cornerstone of many people's retirement planning, are being phased out all over the world. Low interest rates and improvements in longevity combine to make pension liabilities more expensive to fund than ever before. Further, pension deficits in defined benefit pension plans have become a significant feature of insolvent companies and, sometimes, the driver to insolvency.

This book provides a survey of the current state of private pension plan regulation and of how private pensions factor in insolvencies in the contributors' twenty one different jurisdictions. Each chapter is structured on a template of questions. Because of the significant differences in the social safety nets among the various jurisdictions, and many other differences, the authors at times found the questions had, in effect, to be reformulated to be relevant. They also provided general comments on the state of private pensions in their jurisdictions to provide meaningful context and commentary. While clearly there are significant differences, the results bear out the serious challenges for retirement security all jurisdictions face.

I wish to thank all the authors for their valuable contributions to this important and intractable subject, one that urgently warrants study and the sharing of insights among thoughtful professionals internationally. My special thanks to my colleague, Jesse Mighton, who worked closely and diligently with me throughout, and to Sonali Abeyratne and Waheeda Lafir for their astute management of this project and for their guidance and patience.

Gale Rubenstein
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ARGENTINA

QUESTION 1

What is the legal framework for private pension plans in your country?

Argentine Law No. 26,425 passed by the National Congress in 2008 ("New Pensions System Law") eliminated the private pensions regime governed by Argentine Law 24,241 (the "Private Pensions System") that co-existed with a public pension regime until such date. Until then, those individuals who opted for the private pension regime were entitled to make voluntary payments in to their individual accounts in order to either increase their retirement benefits or to be entitled to earlier payments of such retirement benefits.

Prior to passing the New Pensions System Law, the Private Pensions System also allowed individuals to make "agreed deposits". These "agreed deposits" constituted single payments or regular contributions made into individual capitalization accounts by the respective individual or by the employer if previously agreed with the contributor.

The Private Pensions System expressly provided that these "agreed deposits" neither constituted part of the individual's salary (i.e., no social security contributions were due in connection therewith) nor were they considered income for tax purposes. In turn, the employer making the "agreed deposits" in favour of employees was entitled to consider such contributions as deductible expenses for income tax purposes.

As anticipated above, the Private Pensions System was replaced in 2008 by a State-controlled pension system under the New Pensions System Law and pursuant to which all employees and self-employed employees are compulsorily included in the Argentine Integrated System of Retirements ("SIPA"). Under the New Pensions System Law, employees and employers must make certain mandatory social security contributions to the SIPA.

Currently, only the employer contribution aimed at paying a retirement insurance policy is subject to legal regulation[1].

In accordance with the applicable local regulations:

> "under any collective retirement insurance where the policy holder is the employer of the insured individuals and such employer assumes full or partial payment of the insurance premium, partial withdrawals by the beneficiary may be made only after the first anniversary of the insurance coverage. From that moment on, no more than three (3) withdrawals per calendar year or less than ninety (90) days term between each other are permitted; none of the withdrawals can exceed thirty percent (30%) of the accumulated fund".

The amounts paid or contributed by the insured employee (and not the employer) are not subject to the above described restriction.

The contributions made by the employer to the retirement insurance hired with respect to its employees do not qualify as "salary" for local law purposes (i.e. no social security contributions are due in connection thereof)[2].

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1 Pursuant to Resolutions 19.106/87 and 23.079/94 of the Argentine Superintendency of Insurance.

2 Pursuant to resolutions 933/88 and 25/89 of the Ministry of Labor.

In some cases, however, the local tax administration (Agencia Federal de Ingresos Públicos or “AFIP”) has claimed the payment of social security contributions, based on the understanding that the employer payments towards the retirement insurance policy were motivated in the employment contract and not in an insurance contract. Further, AFIP also argued that such payments were made on a regular basis and that they are therefore part of the salary.

However, court decisions were against the AFIP. Local courts have concluded that, social security contributions do not apply with respect to the amount contributed by the employer to a retirement insurance policy[3].

With respect to the tax aspects of the retirement insurance policy:

(a) deductions of contributions made by employers to private retirement plans is limited to $630.053[4] per year and per employee. The amounts that exceed that limit will not be deductible in the tax balance of the employer, who, accordingly, should pay the income tax on the excess; and

(b) regarding the beneficiaries, the tax base to be determined by the employees in the event of recovery, would consist of the difference between perceived benefit and the contribution amount not deducted by the company.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

As discussed above, only the employer contributions to a retirement insurance policy are regulated.

However, some companies (generally, the local subsidiary of a multinational company) have established private pension plans for their employees, and subject to their own terms and conditions (agreed by the parties).

Those plans are aimed at complementing and enhancing the benefits provided by the SIPA.

These private plans have the disadvantage that they neither constitute an “improvement of the individual capitalization account” (as such possibility existed until 2008) nor an employer contribution to a retirement insurance policy. Therefore, these plans are not expressly covered in the current regulation. Furthermore, these plans do not enjoy the tax benefits afforded to the payments under the individual capitalization account (Private Pensions System until 2008).

[3] Pursuant to the Social Security Court, Court I, court decision dated 10/13/2000, in re “Tía S.A. v/D.G.I.”, “Derecho del Trabajo”, 2001-B, page. 2021.

[4] General resolution of the General Direction of Tax Matters N° 3503/92.

QUESTION 3

How are the plans governed?

Since these plans are not subject to any governmental regulation (except when they are implemented through a retirement insurance policy), each plan may have its own scheme and terms and conditions.

QUESTION 4

Is there a compensation fund for pension benefits?

There is no compensation fund.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

Due to the above mentioned considerations, there are very few private pension plans in Argentina. As a result, issues such as the enforceability of pension rights in the insolvency or bankruptcy of the employer / sponsor have not been yet raised at local courts.

Local insolvency and bankruptcy laws, however, grant preference to labour and social security creditors. Accordingly, we believe that pension rights may eventually enjoy such preference in a bankruptcy (the employee or beneficiary of the pension plan will be required to submit proof of their claim in court).

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

Please refer to the response stated in number 5.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

In principle, the remedies to collect in respect of pension deficits are only available against the employer company. In certain cases, a course of action against the employer's controlling company (if any) may be available.

Further, while the employer can unilaterally and voluntarily establish a private pension plan, that does not mean that the employer can unilaterally and voluntarily terminate or modify it to the detriment of the employees / beneficiaries. The obligations assumed by the employer under the private pension plan become part of the employment contract with the employee.

Thus, the Courts have held that:

> "…If the employer, unilaterally and voluntarily, undertook to pay the plaintiff a monthly pension when he/she retires from the company without reserving the right to modify or suspend it, this obligation is part of the employment contract and it cannot be modified unilaterally…".

Further, local courts have not upheld provisions of a private pension plan that would entitle the employer to modify unilaterally the terms and conditions of the plan.

In fact, it has been held that:

> "…the unilateral amendment of the pension plan by the employer is null and void because such amendment affected seriously and notoriously the rights of the employee thereunder, without any compensation in exchange, thus depriving the employee of legitimately vested rights"[5].

QUESTION 8

Are there any cross-border features of your pension regime?

Yes. Argentina has entered into some international treaties on social security issues (including treaties with Mercosur countries – Uruguay, Paraguay and Brazil, Italy, Spain, Portugal, Greece, France, Chile, Colombia), whereby it is allowed:

(a) to acknowledge services rendered in one or another State. This means that if Argentina requires 30 years of service with contributions, for that calculation, services rendered in any of the other countries that are parties to the respective treaty shall be acknowledged.

[5] National Labour Court of Appeals, Chamber VI, 29/5/2002, "Murman, Gabriel L. vs. IBM Argentina S.A. y otro".

(b) the services of the social security benefits are paid pro rata to the time worked in the respective country.

(c) the foregoing only applies with respect to the official social security system.

QUESTION 9

Discuss the state of defined benefit plans in your country

As discussed above, there are very few private pension plans in Argentina. Generally speaking, local companies that implement private pension plans are subsidiaries of multinational companies. Within such context, in a few cases where local courts were asked to resolve controversies regarding private pension plans, local courts have imposed limits on the ability of employer companies to amend unilaterally the terms and conditions of such plans.

Another factor that explains why these private pension plans are not frequent in Argentina are the claims that have been raised by employees alleging the remunerative nature of the benefits under private pension plans in cases of “flexibilities” that allow the employee to have access to the respective benefits prior to retirement.

Finally, and given that in many cases the private pension plans are administered by foreign entities, the current foreign exchange regulations in Argentina (that restrict the transfer of funds outside the country) also constitute an important barrier to funding private pension plans.

AUSTRALIA

QUESTION 1

What is the legal framework for private pension plans in your country?

The superannuation industry in Australia is regulated at the federal level of government. The source of this power is the Australian Constitution which gives the Commonwealth the power to govern corporations[1] and pensions[2].

Australia's superannuation system is based on 3 pillars:

- A compulsory superannuation guarantee regime that requires all employers to make mandated minimum levels of superannuation contributions to a superannuation fund on behalf of their employees. These superannuation funds are separate from employers and governed independently by trustee boards.

- Tax incentives to encourage people to contribute voluntarily to their superannuation fund to help fund a better standard of living in retirement. There are also tax concessions in respect of benefits received and on investment earnings while in the superannuation fund.

- A means-tested old age pension that provides a basic minimum safety net for retirement.

Within this framework, a combination of government policy, statute and common law, impact on and regulate the operation of the superannuation industry in Australia.

The main legislation governing superannuation entities are:

- Superannuation Industry (Supervision) Act 1993 (Cth) (SIS Act);

- Corporations Act 2001 (Cth) (Corporations Act);

- Income Tax Assessment Act 1936 (Cth) (ITAA).

Also of importance is the legislation that established the superannuation guarantee scheme in 1992: the Superannuation Guarantee (Administration) Act 1992 (Cth) (SGAA), discussed below.

The Superannuation Industry (Supervision) Act 1993 (Cth)

The SIS Act regulates superannuation entities and provides for their supervision by three regulatory bodies being the Australian Prudential and Regulation Authority (APRA), the Australian Securities and Investments Commission (ASIC), and the Commissioner of Taxation[3]. There are also extensive Superannuation Industry (Supervision) Regulations 1994 (SISR) that provide subordinate regulation of the superannuation industry under the SIS Act.

1 Australian Constitution s 51(xx), SIS Act s 3(2).
2 Australian Constitution s 51(xxiii), SIS Act 3(2).
3 SIS Act s 3(1).

'Superannuation entity' is a generic term used widely under the SIS Act[4] and is defined to mean:

(a) a regulated superannuation fund[5];

(b) an approved deposit fund[6]; or

(c) a pooled superannuation trust[7].

Regulated superannuation entities are also referred to as "complying superannuation funds" as this term is used under the ITAA to refer to superannuation funds that are entitled to concessional tax treatment.

Regulated superannuation entities can be further classified into the following categories:

(a) public offer superannuation funds that offer superannuation interests to the public;

(b) non-public or other APRA-regulated funds;

(c) eligible rollover funds (ERFs) - eligible to receive benefits automatically rolled over from other funds;

(d) pooled superannuation trusts (PST) - a trust in which assets of superannuation funds, approved deposit funds and other PSTs can only be invested;

(e) approved deposit funds (ADFs) - permitted to receive, hold and invest certain types of rollovers until funds are withdrawn;

(f) self-managed superannuation funds (SMSFs) - These funds are in fact regulated by the Australian Taxation Office (ATO). These are funds that have:

    (i) fewer than five members;

    (ii) each individual member of the fund is a trustee of the fund; and

    (iii) no trustee of the fund is remunerated for acting as trustee[8].

The focus of this chapter is on superannuation entities other than SMSFs unless specifically included. SMSFs are generally family based or private funds and are not regulated by APRA or ASIC.

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4 SIS Act s 10(1).
5 SIS Act s 19.
6 SIS Act s 10(1).
7 SIS Act s 10(1).
8 SIS Act s 17A(1).

The Corporations Act

The market integrity and consumer protection aspects of the Corporations Act are applicable to investment in financial products, including superannuation. Accordingly, superannuation entities are required to comply with the disclosure, licensing and conduct requirements in the Corporations Act and accompanying Corporations Regulations 2001 (Cth) (Corporations Regulations) and ASIC Regulatory Guides that are applicable to superannuation interests, superannuation trustees and administrators.

Tax Regime

Broadly, the tax regime as it relates to superannuation in Australia is made up of the following features:

- concessional tax treatment for 'complying' superannuation entities;
- rules relating to contributions made by members and employers of members; and
- rules on the payment of benefits.

Superannuation entities that comply with the relevant provisions of the SIS Act, and are thus deemed 'complying' entities are entitled to concessional tax treatment[9].

Contributions made to superannuation entities by members and employers are also subject to a specific tax regime under Division 290 of the ITAA. Contributions made by employers to complying superannuation entities for their employees are also deductible (to the benefit of the employer) if the conditions within Division 290 of the ITAA are met. Tax penalties arise where contributions over a determined amount are made in the prescribed period in respect of an individual, regardless of whether the employer or the individual themselves has made the contribution[10].

Superannuation Guarantee Scheme

The Superannuation Guarantee Scheme was established in 1992 by the SGAA. It is the primary legislation affecting employers and details the administrative arrangements for the operation of the Superannuation Guarantee Scheme, including the assessment of employers' liability, calculation of the SG charge, payment of the charge and distribution of payment received.

This Act ensures that employers pay and employees receive the benefit of compulsory superannuation payments into a superannuation fund. Currently employers are required to make payments equivalent to 9.5% of an employee's salary (subject to a cap) to a super fund. This percentage will increase between 1 July 2021 and 30 June 2026 to 12%.

The SGAA imposes a penalty on employers for failing to make the required contribution on behalf of employees into a complying superannuation fund, a retirement savings account or the Superannuation Holdings Account Special Account (SHASA). The penalty is comprised of an amount being the shortfall in contribution plus interest and administration charges, which is paid to the ATO and then distributed to the individual whose superannuation entitlement was not initially paid in full[11].

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9 SIS Act ss 3(2), 45.

10 See Income Tax Assessment Act 1997 (Cth) s 280.15 for a guide to limits on superannuation tax concessions.

11 SGAA Part 8.

Trust law

Trust law also plays an important role in regulating the conduct of those who manage superannuation entities, as the SIS Act requires a trust (or trust like) framework to form the basis of the fund, with the requisite fiduciary obligations attaching to the trustees.

Future reforms

The superannuation legal and regulatory system has been the subject of regular reviews and reforms by successive governments since the introduction of a compulsory superannuation system.

The latest of these reviews is the Financial Systems Inquiry[12] that has made 44 recommendations to government on changes to the Australian financial system. Of these, a number of recommendations are directed at improving the superannuation system in Australia to increase its competitiveness and efficiency and better develop the retirement phase of the superannuation system to meet the needs of Australia's ageing population. This review has highlighted that the retirement phase of the superannuation system in Australia is relatively underdeveloped in comparison to other jurisdictions. We expect that there will be focused reform and changes directed to enhancing the retirement outcomes of the superannuation system in the forthcoming years.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

Superannuation entities in Australia are regulated by three government bodies:

- The Australian Prudential Regulation Authority (APRA);
- The Commissioner of Taxation or ATO; and
- The Australian Securities and Investments Commission (ASIC).

Each of these entities has the responsibility of administering a part of the SIS Act[13].

In general, APRA is responsible for the prudential supervision of regulated superannuation entities under the SIS Act. Superannuation entities are also required, under the Financial Sector (Collection of Data) Act 2001 (Cth) and its reporting standards, to provide data to APRA. The data is defined in the set of reporting forms and instructions that are available from APRA's website[14]. These extensive reporting standards require reporting on investment performance, inflows, payment of benefits, defined benefits, fees and costs and a statement of the fund's financial position. Some forms are also subject to audit requirements.

[12] The Government appointed Mr. David Murray to head an inquiry into Australia's financial system in 2014. The Financial Systems Inquiry (FSI) was charged to examine how the financial system could be positioned to best meet Australia's evolving needs and support Australian's economic growth. Recommendations were to foster an efficient, competitive and flexible financial system, consistent with financial stability, prudence, public confidence and capacity to meet the needs of users.

[13] SIS Act s 6.

[14] http://www.apra.gov.au/Super/ReportingFramework/Pages/Final-reporting-standards-for-Superannuation-June-2013.aspx. See also APRA's Reporting Practice Guide SRPG700 - Superannuation Disclosure Reporting.

Formulae for contributions to superannuation funds

Employers are required to make superannuation contributions to a complying superannuation fund on behalf of their employees on at least a quarterly basis. Employees have a choice of fund unless they are subject to an industrial award or agreement that has mandated a superannuation fund for members of the award for SG purposes. If an employee does not elect a fund of choice, the contributions will be paid into a default superannuation fund.

The minimum contribution amount of an employee's ordinary earnings is mandated under the SGAA[15].

The following table illustrates the current and proposed changes to the minimum contribution levels imposed on employers.

Figure 1		
Charge percentage (unless reduced under section 22 or 23)		
Item	Column 1 Year	Column 2 Charge percentage
1	Year starting on 1 July 2013	9.25
2	Year starting on 1 July 2014	9.5
3	Year starting on 1 July 2015	9.5
4	Year starting on 1 July 2016	9.5
5	Year starting on 1 July 2017	9.5
6	Year starting on 1 July 2018	9.5
7	Year starting on 1 July 2019	9.5
8	Year starting on 1 July 2020	9.5
9	Year starting on 1 July 2021	10
10	Year starting on 1 July 2022	10.5
11	Year starting on 1 July 2023	11
12	Year starting on 1 July 2024	11.5
13	Year starting on or after 1 July 2025	12

If sufficient contributions are not received by the trustee of a superannuation fund by the end of each quarter, a superannuation guarantee shortfall arises which must be made up by applying a formula as prescribed in the legislation (see Figure 2)[16]. Contributions already made in that quarter are applied to reduce the 'charge percentage' (see Figure 1)[17]. For example, if the employer has made contributions of 8%, during 2015, the charge percentage to be applied to the calculation of the SG shortfall is 1.5%[18].

[15] SGAA s 19(2).

[16] Superannuation Guarantee (Administration) Act 1992 (Cth), s 19(1).

[17] Superannuation Guarantee (Administration) Act 1992 (Cth), ss 19(1), 19(2).

[18] Superannuation Guarantee (Administration) Act 1992 (Cth), s 19(2).

Figure 2

$$\text{Total salary or wages paid by the employer to the employee for the quarter} \times \frac{\text{Charge percentage for the employer for the quarter}}{100}$$

Individuals may make contributions to their superannuation fund in addition to the employer compulsory contributions, however there are concessional contribution caps that apply[19]. There is a tax consequence for concessional contributions made over and above these specified caps.

A trustee is obliged to allocate all contributions to members as soon as practicable and in any case no later than 3 business days after receiving the contribution and certain relevant information.

All benefits that accrue and accumulate in a superannuation fund on behalf of an individual member must be treated as minimum benefits in accordance with the minimum benefit standards set out in the SISR. The minimum benefits must be maintained in the fund until such time as they are cashed out or rolled over or transferred as benefits of the member to say another fund.

Release of benefits

An individual member of a superannuation fund does not have a beneficial interest in the underlying assets of the fund but rather rights against the trustee to have the superannuation fund administered according to law. The right to receive a benefit under the superannuation fund is a contingent right to receive a benefit upon the happening of a specified event e.g. retirement or death.

Trustees of regulated superannuation entities must comply with the rules regarding the preservation of benefits in the SISR. A trustee of a regulated superannuation entity must not release, or cash a member's benefit unless a condition of release is fulfilled, as specified under Schedule 1 of the SISR. The main conditions of release include:

- reaching pensionable age, which is between 55 to 60 years, depending on the members' year of birth;
- retirement;
- death;
- terminal medical condition;
- permanent or temporary incapacity; and
- severe financial hardship[20].

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[19] See s 291-20 of the ITAA 1997. Concessional contributions below the caps receive favourable tax treatment – 15% in the hands of the fund. For the 2015 / 2016 FY, the cap for individuals under the age of 50 is $30,000 per annum, and for members 50 years and over, is $35,000 per annum. Any contributions received by or on behalf of an individual in excess of the contribution cap, will be included in the individual's assessable income and taxed at their income tax marginal rate. An excess concessionable contribution charge will also be payable.

[20] SISR Sch 1.

Forfeiture of benefits

There are limited circumstances in which a member of a superannuation fund may potentially forfeit their right to their benefits in the fund. These include bankruptcy, incapacity, assignment or mortgage of benefits to another or in relation to an employer-sponsored superannuation fund, where the member leaves employment prior to retirement age and some or all of a member's benefits have not been vested.

The Bankruptcy Act 1966 (Cth)[21] enables bankruptcy trustees to recover superannuation contributions that have been made by or on behalf of a member of a superannuation fund prior to a member's bankruptcy where it is clear that the contributions have been made with the intention to defeat creditors.

The SISR also allow for the confiscation of superannuation assets funded directly with the proceeds of crime in accordance with court orders under Commonwealth, State and Territory legislation[22].

QUESTION 3

How are the plans governed?

All registrable superannuation entities (or RSEs)[23] must be registered with APRA and trustees of APRA regulated superannuation entities are required to obtain a RSE licence with APRA. The SIS Act regulates who may be appointed as a trustee of a superannuation fund and their powers, duties, rights and responsibilities. While there may be employer and employee representation on a trustee board, this is not mandated.

In addition, APRA determines prudential standards that regulated superannuation entities and other connected entities, such as auditors, must comply with[24]. These standards cover issues such as the outsourcing of material business activities,[25] insurance offered by superannuation entities to members,[26] auditing of the fund,[27] risk management,[28] and matters specific to defined benefit funds[29].

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21 Bankruptcy Act 1966 (Cth), s 128B, s 128c.

22 SISR r 5.08(1A), 6.17(2C) and 6.22(6).

23 SIS Act s 10 (i) defines a registrable superannuation entity to mean: (a) a regulated superannuation fund; or (b) an approved deposit fund; or (c) a pooled superannuation trust, but does not include a self managed superannuation fund.

24 SIS Act s 34C.

25 APRA Prudential Standard SPS 231: Outsourcing.

65 APRA Prudential Standard SPS 250: Insurance in Superannuation.

27 APRA Prudential Standard SPS 310: Audit and Related Matters.

28 APRA Prudential Standard SPS 220: Risk Management .

29 APRA Prudential Standard SPS 160: Defined Benefit Matters. For a full list of relevant APRA Prudential Standards applicable to registrable superannuation entities, see http://www.apra.gov.au/Super/PrudentialFramework/Pages/superannuation-prudential-standards.aspx. These Prudential Standards are supported by Prudential Practice Guides which set out APRA's expectations on how compliance with the prudential standards may be achieved and best practice. See http://www.apra.gov.au/Super/PrudentialFramework/Pages/superannuation-ppgs.aspx for list of superannuation prudential practice guides.

The governance of superannuation entities is undertaken by the trustee of the fund, for the benefit of members as beneficiaries. Trustees of superannuation funds are subject to strict obligations in relation to governance[30], management, investment and reporting on the performance of the fund, as stipulated by the SIS Act and APRA prudential standards.

Unlike other APRA regulated entities, there is no current requirement that there be a majority of independent directors on the board of a RSE licensed trustee. Nonetheless, APRA Prudential standards do require that the directors and senior management of the RSE licensee collectively have the full range of skills needed for the effective and prudent operation of the RSE licensee's business operations and that each director has the skills that allow them to make an effective contribution to Board deliberations and processes. In addition, the directors and senior management of a RSE licensee must satisfy APRA's fit and proper requirements[31].

In July 2013, new trustee covenants in the SIS Act[32] require trustees to:

- act fairly in dealing with classes of beneficiaries within the entity and with beneficiaries within a single class; and
- to give priority to the interests of beneficiaries where there is a conflict of interest and duties and comply with the prudential standards in relation to conflicts.

The final report of the Financial Systems Inquiry has made recommendations that there be amendments to superannuation laws requiring that there be a majority of independent directors on RSE licensee boards and that directors be subject to the same personal liability and penalty regime applicable to directors of managed investment schemes under the Corporations Act 2001. This would mean superannuation trustee directors would be subject to criminal and civil penalties.

Governing rules

Superannuation entities must operate in accordance with the 'governing rules'. The governing rules of a superannuation entity are defined as:

> "any rules contained in a trust instrument, other document or legislation, or combinations of them, or any unwritten rules governing the establishment or operation of the fund, scheme or trust[33]".

Certain provisions of the SIS Act do however prevail over any other governing rule to the extent that they are contrary to that specific provision of the Act[34].

Part 6 of the SIS Act sets out covenants that are deemed to form part of the governing rules of the superannuation entity, even where the trust deed or other instrument does not contain express provisions to the same effect.

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30 APRA Prudential Standard SPS 520: Fit and Proper and Prudential Standard 510: Governance.

31 See APRA's Prudential Standard SPS 520 which sets out minimum requirements for RSE licensees in determining the fitness and proprietary of individuals holding positions of responsibility.

32 SIS Act ss 52, 52A.

33 SIS Act s 10(1) definition 'governing rules'.

34 See SIS Act, ss 29VQ, 55A, 55B and 242N.

Accounting and auditing obligations

In terms of reporting and record keeping obligations, trustees of registrable superannuation entities are required to comply with accounting and auditing standards set out under Division 2 of Part 4 of the SIS Act. Similar obligations are imposed on SMSFs under Division 3 of Part 4 of the SIS Act.

Trust law obligations

As superannuation entities most commonly take the form of a trust in Australia, trustees of these funds must also comply with the strict obligations imposed by trust law. Trust law is comprised of both case law, and state based statutes in Australia[35].

Generally, a trustee owes fiduciary obligations to the beneficiaries of the trust, and must act in the best interests of the beneficiaries. The basis of the trust relationship is most often contained within a trust deed, setting out the obligations of the trustee in dealing with trust assets.

QUESTION 4

Is there a compensation fund for pension benefits?

There is no general compensation or fund of last resort available for pension / superannuation funds in Australia. There is some limited financial support available through Part 23 of the SIS Act. The reason for this may be explained in part by the fact that the majority of superannuation funds in Australia are defined contribution funds and not defined benefit funds.

Part 23 of the SIS Act

Part 23 of the SIS Act makes provision for the grant of financial assistance for certain superannuation entities that suffer loss as a result of fraudulent conduct or theft. The financial assistance is limited to loss to a fund as a result of such conduct but does not include any amounts a fund does not receive because of the failure of a person to pay contributions to the fund.

The provision only applies to a fund that is a regulated superannuation fund (other than a self-managed superannuation fund) or an approved deposit fund and the loss results in the fund having difficulties in paying benefits to its members.

The fund is required to make an application to the relevant governmental minister seeking financial assistance for the fund. The minister is required to seek advice from APRA should such a situation arise. If the minister is satisfied that the fund has suffered an eligible loss after having consulted with APRA, then the minister is required to make a written determination as to whether it is in the public interest to grant financial assistance. Any such assistance is paid out of the Consolidated Revenue Fund. The SIS Act provides that any such financial assistance granted to a fund must be subject to certain conditions[36].

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[35] For example, Trustee Act 1925 (NSW), Trustee Act 1925 (ACT), Trusts Act 1973 (QLD), Trustee Act 1936 (SA), Trustee Act 1958 (VIC), Trustees Act 1962 (WA), Trustee Act 1898 (TAS), Trustee Act (NT).

[36] See SIS Act s 233.

These include that the amount of any financial assistance will be deposited in the corpus of the fund and the amounts must be applied to payments to beneficiaries of the fund (who were beneficiaries at the time the fund suffered loss).

The government has the right to clawback any such payments if it is subsequently found that a condition of the financial assistance has been contravened or a condition of payment does not occur. Any such amount payable has priority over all other debts (whether preferential, secured or unsecured)[37].

The source of funding of any financial assistance under Part 23 of the SIS Act is via the imposition of a levy on superannuation funds and approved deposit funds as provided under the Superannuation (Financial Assistance Funding) Levy Act 1993 (Cth). In summary, this legislation permits the making of regulations to impose levies on superannuation funds and the amount of levy imposed as determined by the formula:

$$\text{applicable rate} \times \text{value of assets}$$

Where applicable rate is that rate as determined by the regulations. Value of the assets means that value of the assets of the fund at the end of the previous financial year of the fund before the effective date of the regulations. The applicable rate must not exceed 0.0005. The levy may be different for different classes of funds[38].

Therefore any financial assistance given to a superannuation fund in those circumstances is effectively financed by the superannuation industry broadly through the imposition of the levy.

General Employee Entitlement and Redundancy Scheme and Fair Entitlements Guarantee

Prior to 5 December 2012, the General Employee Entitlement and Redundancy Scheme (GEERS) provided for up to three months of an employee's personal superannuation contributions for an employee where the employer had entered insolvency (but not for an employer's superannuation contributors). The Fair Entitlements Guarantee (FEG) Scheme[39] that has now replaced GEERS does not make an equivalent provision for the payment of personal superannuation contributions for employees of an insolvent employer[40].

Future Fund

The Future Fund is Australia's Sovereign Wealth Fund, established in 2006 to make provision generally for Commonwealth unfunded superannuation liabilities owed to current and former employees of the public service. The Future Fund received $18 billion in seed capital in 2006, with further contributions being made out of government budget surpluses and the sale of government assets[41].

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[37] SIS Act s 240.

[38] Superannuation (Financial Assistance Funding) Levy Act 1993 s 10.

[39] FEG came into effect on 5 December 2012 and applies to employer insolvency events that occurred on or after that date.

[40] Fair Entitlements Guarantee Act 2012 (Cth).

[41] Australian Government Department of Finance, *Transfers to the Future Fund* http://www.finance.gov.au/investment-funds/future-fund/transfers.html.

The Future Fund is administered by the Future Fund Board of Guardians (Future Fund Board) which is made up of seven members who are appointed by government ministers. The Future Fund Board is responsible for investing the fund assets in accordance with the statute establishing the fund as well as the legislated Investment Mandate[42].

The Future Fund does not however extend to the compensation of individuals whose non-government superannuation funds are unable to meet liabilities owed to members.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

If an employer has failed to make superannuation contributions in respect of an employee, a complaint can be lodged by the employee with the ATO who will conduct an investigation. This process may be of limited success however where an employer has entered insolvency. Superannuation entitlements required to be paid by employers for the benefit for employees rank as a priority entitlement together with other employee entitlements during an insolvency[43]. In some circumstances, company directors may be personally liable for a company's unpaid SG contributions. The SGAA does not however provide an avenue for employees to directly sue for unpaid SG contributions. Nevertheless, there may be private rights of action available at common law to enforce contractual superannuation entitlements or where an individual award or agreement exists, a right to sue for breach of the industrial award arrangement.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

Employee and employer superannuation contributions

Superannuation contributions and entitlements are held within separate trust funds from an employer / sponsor and are independent of theassets of a company. Outstanding superannuation contributions required under the Superannuation Guarantee Scheme rank as a priority entitlement together with other employee entitlements (such as unpaid wages and annual leave) in the case of an employer company insolvency[44]. Similarly, the SG charge has the same priority as other employee entitlements.

The SG charge is deemed to be a debt payable to the employee in respect of services rendered to the company notwithstanding that the SG charge is payable to the Commonwealth[45].

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[42] Future Fund Act 2006 s 18.

[43] CA s 556(1)(e)(i).

[44] CA s 556(1)(e)(i).

[45] CA s 556(IAB), (IAC).

This means that outstanding superannuation contributions and SG charges are to be paid to employees after priority creditors and liquidators' fees are paid and before payments to ordinary unsecured creditors.

If a company enters into voluntary administration and proposes a deed of company arrangement with its creditors, the same priority must be given to superannuation entitlements[46]. A company is only permitted to vary the priority regime with the consent of a majority of employee creditors or by proving in court that the employee creditors are treated at least as favourably under the arrangement as they would have been under the Corporations Act.

In the case of personal bankruptcy, there is no legislative requirement that the SG charge be given priority in arrangements made pursuant to Part IX and X of the Bankruptcy Act 1966. However it is not unusual to find the trust deed includes a clause that gives the SG charge similar priority to what it would have received in bankruptcy as it is possible the Commissioner for Taxation may vote against a deed that does not give priority for SG charge if bankruptcy would yield a greater return.

In the case of personal bankruptcy, the SG charge receives priority in bankruptcy and is included in the category of employee entitlements such as salary, usages and commission[47].

As noted in 4 above, while there was federal government assistance for employees under the GEERS safety net scheme for liquidations occurring before 5 December 2012 in the form of 3 months of an employee's personal contributions, this support is no longer available under the current FEG scheme.

Superannuation fund financial management obligations

Superannuation entities are subject to financial management obligations under Part 9 of the SISR. In the case of a technically insolvent fund, the fund must either implement a program to restore solvency of the fund within five years, or initiate a winding up process[48].

Accumulation style funds

In the case of the winding up of an accumulation style superannuation fund, benefits are to be paid back to or on behalf of members to another fund, once the administration costs of the winding up are satisfied[49] and if the fund is solvent at the winding up date, a trustee must allocate an amount that is not less than the minimum guaranteed benefit of each member[50].

If the fund is technically insolvent at the winding up date, an amount equal to the net realisable value of the assets at the winding up date must be apportioned among all the members of the fund at that date so that the proportion of that amount that is apportioned to an individual member bears the same relation to the whole amount as the 'minimum guaranteed benefit' of that member to the total of the minimum guaranteed benefits in respect of all of the members of the fund at the winding up date[51].

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[46] CA s 4440A.

[47] Bankruptcy Act 1966, s 109 (IC).

[48] Superannuation Industry (Supervision) Regulations 1994 (Cth), r 9.17, 9.38.

[49] Superannuation Industry (Supervision) Regulations 1994 (Cth), r 9.45.

[50] SISR, r 9.45(4).

[51] SISR, r 9.45(5).

The SISR[52] define the concept of 'minimum guaranteed benefit' in relation to a member of an accumulation fund to mean an amount that is the sum of:

(a) the *member-financed benefits* of the member, and

(b) the *mandated employer-financed benefits* of the member; and

(c) any minimum benefits of the member under Reg 5.06B, that are included in paragraph (a) or (b).

The concepts of 'member-financed benefits' and 'mandated employer-financed benefits' are also defined in the SISR[53]. In summary, member-financed benefits are the sum of contributions made by or on behalf of the member (other than employer contributions) and any investment earnings on those contributions to those amounts.

Mandated employer-financed benefits are those benefits paid by an employer as a requirement of the Superannuation Guarantee Scheme and any amounts payable under an industrial scheme or award together with any investment earnings less the cost applicable to those amounts.

Defined benefit style funds

In relation to the winding up of a defined benefit superannuation fund, the priority given to the repayment of member benefits ranks after the payment of the administration costs of winding up, as with accumulation style funds[54]. The SISR determine the priority to be given to the liabilities of a defined benefit fund on winding up[55]. The first charge on the assets of the fund must be any liability in respect of administration and other costs associated with the winding up proceedings.

If the funds minimum benefit index as at the winding up date is equal to or greater than 1, the benefit entitlement allocated to each individual member of the fund at the winding up must be an amount that is not less than the sum of the funded minimum benefit and the benefit entitlements of former members, as is attributed to an individual member.

If the fund's minimum benefit index as at the winding up date is less than 1, the benefit entitlement allocated to each individual member of the fund at the winding up date must not be greater than either:

(a) the amount determined for each individual member if the minimum benefit index was equal to or greater than 1; or

(b) less than an amount calculated by multiplying the amount determined in respect of each individual member in (a) by the funds minimum benefit index as at the winding up date.

[52] SISR, r 9.35 (1).
[53] SISR, Pt 5, Div 5.1, R5.01 (1).
[54] SISR r 9.25.
[55] SISR r 9.25.

While a defined benefit fund is technically insolvent, a trustee is not permitted to make any payment from the fund unless the responsible actuary has given written approval for the particular payment or the amount of the payment has been determined in accordance with a scheme for payment approved by the responsible actuary[56].

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

The Superannuation Complaints Tribunal

The Superannuation Complaints Tribunal is established under the Superannuation (Resolution of Complaints) Act 1993. The Tribunal exists to resolve complaints relating to decisions and conduct of trustees of superannuation funds, approved deposit funds and RSA providers and insurers[57].

While the Superannuation Complaints Tribunal provides a mechanism for members of superannuation funds to make a complaint relating to the conduct of the trustee of the fund, the Tribunal does not have the power to compensate the member for loss. The Tribunal is not empowered to provide compensation to a successful applicant or require one party to compensate another beyond the repayment of funds that may have been wrongly received or withheld.

QUESTION 8

Are there any cross-border features of your pension regime?

While it is possible to have a superannuation fund in Australia that is a foreign superannuation fund, foreign superannuation funds cannot be complying superannuation funds and therefore cannot enjoy tax concessions.

There is specific treatment for transfers from foreign superannuation funds to Australian superannuation funds and assessable contributions to a non-complying fund that is a foreign fund.

Trans-Tasman Retirement Savings Portability

The Arrangement between the Government of Australia and the Government of New Zealand on Trans-Tasman Retirement Savings Portability (Arrangement) established a scheme for Australians and New Zealanders to transfer their retirement savings when they move between Australia and New Zealand, while preserving the integrity of the retirement savings systems of both countries[58].

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56 SISR r 9.19.

57 Superannuation (Resolution of Complaints) Act 1993 Pts 1, 2.

58 ITAA 1997 Div 312 and SISR Pt 12A govern the tax treatment of payments under this arrangement.

An amount transferred from a KiwiSaver scheme to an Australian complying superannuation fund is treated as a personal contribution of the person for whom the transfer is made[59]. Consequently, the contribution is not included in the assessable income of the receiving Australian superannuation fund and the contribution is not subject to the tax arrangements that may apply to transfers from foreign superannuation funds.

The contribution is also treated as a non-concessional contribution of the member and is included in the contributions segment of the member's superannuation interest in the fund.

QUESTION 9

Discuss the state of defined benefit plans in your country

Defined benefit funds are either corporate or public sector funds and have certainly declined in popularity in Australia.

The federal government has traditionally provided defined benefit plans to its employees. However, defined benefit funds, as well as a hybrid scheme, operated by the federal government are now closed to new members[60].

Defined benefit funds that continue to operate are regulated by the SIS Act and SISR in the same way that accumulation style funds are governed.

At present, there is no regulatory push to phase out defined benefits funds but the reality is that there are unlikely to be any new defined benefit funds in view of the present Australian superannuation system and the Superannuation Guarantee Charge scheme that favours accumulation style funds.

[59] ITAA 1997 s 312-10.

[60] The Public Sector Superannuation Scheme (PSS) and the Military Superannuation and Benefits Scheme, both defined benefit funds, are closed to new members from 2005 and 2016 respectively. Hybrid fund, the Commonwealth Superannuation Scheme (CSS), closed to new

BERMUDA

QUESTION 1

What is the legal framework for private pension plans in your country?

Discovered in 1609, Bermuda is the oldest remaining self-governing overseas territory of the United Kingdom. Bermuda's legal system is comprised of its own statutes – both public and private Acts of Parliament and subsidiary legislation – and, where there is no applicable statutory provision, common law which is derived from Bermuda precedent, as well as English and Commonwealth case law, which is of persuasive authority and generally followed. Appeals from the Bermuda Supreme Court are to the Court of Appeal in Bermuda and then to the Privy Council in London.

Until 1998 there was no mandatory private pensions law in Bermuda. In 1998 the National Pension Scheme (Occupational Pensions) Act 1998 (the "Act") was passed and came into force on 1 January 2000. Since then there have been three amendments to the Act[1], together with six sets of regulations[2], which together with the Act are hereafter referred to as the "NPS Act". The NPS Act continues to provide the comprehensive legislative framework for mandatory private pensions in Bermuda. Among other things, the NPS Act requires that pension plans be registered with the Bermuda Pension Commission, sets out eligibility requirements, minimum contribution requirements, provides a general prohibition on refunds and requires the pension funds to be held separate from the employer's funds. Further features of the NPS Act are set out at section 3 below.

The NPS Act requires employers in Bermuda to establish and maintain pension plans under that Act only in respect of employees who are either citizens of Bermuda (under local law referred to as having Bermuda "status") or spouses of Bermuda citizens. There is no requirement for employers not employing Bermudians or their spouses to have any pension arrangements in place, and if they do, there is no need for such arrangements to be registered, therefore plans for employees who are not Bermudian or the spouse of a Bermudian are entirely voluntary.

In practice most employers employ both Bermudians and non-Bermudians, and will therefore have two, sometimes more, plans in place. Typically they will have a "registered" plan, that is one that complies with the NPS Act requirements, and an "unregistered" plan. Sometimes, for the sake of employee harmony, the "unregistered" plan will mirror the statutory provisions in the "registered" plan. Employers will sometimes also have further unregistered "supplemental benefits" plans which, being superfluous to the requirements of the NPS Act, are not required and therefore almost invariably are not registered under the NPS Act.

1 The National Pension Scheme (Occupational Pensions) Temporary Amendment Act 2012, the National Pension Scheme (Occupational Pensions) Amendment Act 2010 and the National Pension Scheme (Occupational Pensions) Amendment Act 2006.

2 The National Pension Scheme (Financial Hardship) Amendment Regulations 2011, the National Pension Scheme (Financial Hardship) Regulations 2010, the National Pension Scheme (General) Amendment Regulations 2004, the National Pension Scheme (General) Amendment Regulations (No. 2) 2000, the National Pension Scheme (General) Amendment Regulations 2000 and the National Pension Scheme (General) Regulations 1999.

Before 1998, any local employer (as opposed to foreign owned employers, known as "exempted companies") establishing a pension trust fund was required to register that fund under the Pension Trust Funds Act 1966 (the "PTFA 66"). The PTFA 66 contained, among other things, provision for registration, annual filing and approval of plan amendments with the local Registrar General. There is provision for exempted companies to register their pension trust funds on a voluntary basis. This has been, and continues to be of use to international employers with pension funds for international employees (i.e. employees who are not Bermudian or the spouse of a Bermudian) who seek to have those plans qualify for recognition and favourable status in other jurisdictions.

These are the only pieces of specific Bermuda legislation regulating private pension plans. The remainder of the legal framework will be legislation that is of tangential application and not specific to pensions, for example the Companies Act 1981 and the Employment Act 2000. Finally, the common law may be relevant where legal questions are not specifically addressed in statutes, for example trustee or director duties.

There are no taxes in Bermuda on income, capital gains or profits, so taxation is generally not an issue for pensions in Bermuda. Local employers are subject a tax on their total remuneration known as Payroll Tax, however application can be made for contributions to a registered plan to be excluded from remuneration for the purposes of that tax.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

Plans registered under the NPS Act are regulated by the Bermuda Pension Commission, a government appointed and funded regulator. The Pension Commission is charged with overseeing employers' compliance with the NPS Act and has broad regulatory powers, including powers of audit. The Pension Commission ultimately reports to the Ministry of Finance.

Pension trust funds registered under the PTFA 66 are regulated by the Registrar General.

QUESTION 3

How are the plans governed?

Plans are governed by their governing documentation (trust deed and rules) and the overriding regulatory requirements described below.

The NPS Act

Each plan registered under the NPS Act must have an "administrator" which has legal responsibility for compliance with the requirements of the NPS Act. Administrators can be employers, trustees or approved third party service providers.

Rather than specifying approved investments, regulations limit or prohibit certain investments, for example local real estate is not permitted, and shares of the employer cannot comprise more than 50% of a plan's investments.

The NPS Act requires each plan to file an annual return which will set out, among other things, the number of employees joining and leaving, contributions during the period and any changes to the plan.

The NPS Act is generally geared towards defined contribution plans, currently mandating contributions from both employee and employer at a minimum of 5% of "pensionable earnings". The NPS Act does however permit defined benefit plans and there are still a number registered under the legislation.

The NPS Act imposes various other requirements, for example it generally prohibits refunds of contributions except in very limited circumstances.

The PTFA 66

The Registrar General exercises oversight of plans registered under the PTFA 66. There is a requirement to submit audited accounts and a balance sheet to the Registrar General each year, and an actuarial report every five years.

The PTFA 66 does not apply to plans which are registered under the NPS Act, so effectively the remaining application of the PTFA 66 is for international plans which it is desirable to register in order to achieve favourable status in other jurisdictions.

International Benefit Trusts

It is now clear, there is no other mandatory pensions legislation in Bermuda so employers have wide (but not free) rein to create efficient and innovative pension plans, especially ones for international, globally mobile employees. Examples will include plans established through offshore trusts. The trust structure will be used to keep the plan assets separate from those of the employer in order to protect them in the event of employer insolvency; they also offer a clean canvas to create governance structures which can include private trust companies and committees. Trusts can be drafted to hold a number of separate plans and the assets and liabilities of each can be segregated. As mentioned previously, unregistered international benefit trusts in Bermuda are not subject to pension specific legislation but the trustees will be subject to duties and liabilities imposed by Bermuda's trusts legislation and common law, which are beyond the scope of this chapter.

QUESTION 4

Is there a compensation fund for pension benefits?

There is no compensation fund for employees whose pension benefits have been lost (because their defined benefit plan is under-funded on employer insolvency for example).

There is a social insurance plan in place in Bermuda under the Contributory Pensions Act 1970 (the "Social Insurance Plan"). Every employer is required to pay social insurance contributions on behalf of each employee, half of which may be deducted from the employee's salary. Payment is required in respect of all employees over the age of 16 who are gainfully employed in Bermuda for a period of more than four hours per week. Eligibility for pension arises after 65 years of age. In the case of non-Bermudian employees, if they are resident for more than six months or intend to work in Bermuda for more than six months their employer must contribute. If they intend to reside in Bermuda for less than six months, but in fact remain longer, they will be required to contribute retrospectively. Non-Bermudians who leave the country before the age of 65 are not eligible for a contributory pension, but on reaching the age of 65 they may apply to receive their contributory old age gratuity which is a refund of the total contributions paid into the scheme on their behalf. All employers must provide the Social Insurance Department (the "Department") at the Government Administration Building with a list of their employees and their social insurance numbers. The Department will bill employers directly (monthly in arrears) for the amounts due in respect of their employees.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

Assets in the pension fund

For any trust-based scheme, the assets will not be available to the liquidator of the employer on insolvency because they will not form part of the property of the employer (but rather will be the property of the trustees, held on trust for the employees).

Under section 26 of the NPS Act all monies payable under a plan registered under that Act will be exempt from execution, seizure or attachment or any other process taken by a creditor. "Creditor" is not defined and so can be taken to extend to creditors of either the employee or employer. This protection does not however extend to transfers required by a court pursuant to a property settlement agreement on divorce or for the maintenance of a spouse.

Money owing but not yet paid to the pension fund

Section 44(3) of the NPS Act provides that, in any case where -

"(a) any warrant of distress is executed against the property of an employer and the property is seized or sold in pursuance of the execution; or

(b) on the application of a secured creditor the property of an employer is seized or sold,

the property or the proceeds of sale of the property shall not be distributed to any person entitled thereto until the court ordering the seizure or sale has made provision for the payment into a pension fund of any amount payable by the employer".

This provision is fairly limited, for example (b) seems to imply that there must be an application by a secured creditor – this arguably would carve out situations where the secured creditor simply exercises its security. There is a dearth of case law on this issue.

Contributions which are due to the Social Insurance Plan have limited preferential treatment on insolvency under s.236 of the Companies Act 1981.

Under Section 19A(2) of the NPS Act, the directors and officers of a company or other body corporate that, as an employer, owes contributions to a NPS Act registered scheme are liable jointly and severally for contributions that became due while they were directors or officers.

QUESTION 6

Are there special priorities for pension deficits in the insolvency?

The Pension Commission can order the winding up of pension schemes registered under the NPS Act in some circumstances, including where all or a significant part of the business of the employer is discontinued or where the employer becomes insolvent.

When a pension scheme winds up, the employer is obliged to pay into the pension fund all payments that, under the NPS Act and the pension plan rules, are due or that have accrued and that have not been paid into the pension fund.

In the very limited circumstances outlined above, section 44(3) of the NPS Act may be used to secure preferential payment of such amounts.

Otherwise, there are no special priorities for pension deficits on insolvency.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

Generally under Bermuda law only the sponsoring employers themselves are responsible for funding the deficits in defined benefit pension schemes; there is no equivalent in Bermuda to the United Kingdom ‘moral hazard’ provisions pursuant to which third parties can be held liable for deficits in defined benefit pension schemes.

Under the NPS Act, administrators are required to be appointed to ensure that pension plans and the pension fund are at all times administered in accordance with the documents establishing the plan, the NPS Act and the best standards of management designed to protect and promote the interests of the members. The administrator is required to exercise the care, skill and diligence of the administration and investment of the pension plan and the pension fund that a person of ordinary prudence would exercise in dealing with the property of another person. Therefore, for example, an action in negligence could be commenced against the administrator if such misconduct caused loss to the fund.

A trustee of a pension trust must act in the best interests of the beneficiaries and in accordance with the terms of the trust which would include the plan documents. Failure to do so could render the trustee liable for breach of trust.

QUESTION 8

Are there any cross-border features of your pension regime?

There are no cross-border features of the NPS Act or the PTFA 66. However the Pension Commission is willing to work with employers to solve cross border issues, for example employers with US citizen employees subject to worldwide income tax. Registration under the PTFA 66 has been used by international employers to show regulation to other regulators. It should be noted that plans registered under the NPS Act and possibly the PTFA 66 are exempt from requirements under the US Foreign Account Tax Compliance Act (FATCA) as well as the UK Bermuda Agreement to Implement International Tax Compliance (“UK FATCA”).

QUESTION 9

Discuss the state of defined benefit plans in your country

Defined benefit plans were reasonably popular in the 1960s, 1970s and even 1980s and some employers still have such plans in place. It is of interest that neither the NPS Act, nor the PTFA 66 which preceded it, mandated the establishment of defined contribution pension plans so it is permissible to establish new defined benefit plans. For the same reasons as elsewhere (principally escalating deficits owing to mortality improvements and other factors), most defined benefit plans still in existence have been closed to future accrual. There are almost no defined benefit plans seen in the international plans space.

BRAZIL

QUESTION 1

What is the legal framework for private pension plans in your country?

General overview

Brazilian Social Security is divided into two systems: the Social Security General System (social security) and the Private Pension System (private pension).

The Social Security General System is a part of the Brazilian Social Security System, and in comparison to the health care system, it requires contributions or participation in the funding. This system includes employees from the private sector. The legal basis of the General Social Security System is the Brazilian Federal Constitution (article 201), Law 8,212/91 (funding), Law No. 8,213/91 (benefits) and Decree 3,048/99 (which governs both laws).

The Private Pension System, in turn, has a supplementary, facultative nature, and is organized in an autonomous manner in relation to the Social Security General System. It is provided by article 202 of the 1988 Federal Constitution and subject to Supplementary Law No. 109, of May 29, 2001.

Private pensions operate in addition to (and are organized separately from) Social Security. They are optional and based on the creation of reserves that will support the benefits promised.

Generally, there are three types of private pensions: defined benefit, defined contribution and variable contribution. Resolution No. 16 of 22 November 2005, issued by the Superintendent of National Private Pension (“PREVIC”), regulates these types of private pensions and retirement plans.

In general, a defined benefit plan consists of a planned benefit value or level previously established, the cost is actuarially determined, to guarantee the granting and maintenance thereof. In turn, a defined contribution plan refers to a planned benefit value that is permanently adjusted to the account balance in favor of the participant, including receipt of contributions, considering the net result of their application, the amounts allocated and benefits paid. Finally, a variable contribution plan characterizes a planned benefit that blends the features of the defined benefit and the defined contribution.

Any of these plans are formalized through a private contract between the interested parties, which means that it is not provided by the government.

The supplementary pension contributions are made to a fund administered by a private pension plan entity, either an open-ended or closed-ended fund. Closed-ended private pension funds are available to certain workers only, usually employees of a company or group of companies. Open-ended private pension funds, in turn, are available to any interested individual.

It is also important to observe that the retirement benefits related to private pension plans provided to employees in a trade union are called “Associative Pension Plans”. The law has established specific rules for Associative Pension Plans, such as the mandatory use of definite contributions, in which case the final benefit can vary according to the contributions made throughout the years. Also, there is the possibility that the respective trade union will provide specific and occasional contributions to benefit the employees they represent. The assets belonging to the Associative Pension Plans must be run separately from the ones pertaining to the trade union. Also, the trade unions must hire professional and specialized companies to manage the Associative Pension Plan and its assets.

The levels of benefits are widely variable according to the type of plan previously described. The customary benefits are: (i) normal retirement; (ii) early retirement; (iii) deferred retirement; (iv) postponed benefit due to termination of employment relationship; (v) disability retirement; (vi) survivor’s pension; (vii) quittance; (viii) minimum benefit; and (ix) annual bonus.

In Brazil, all employees, whether in a trade union or not, are represented by a trade union and a collective bargaining agreement. Consequently, except where the trade union has an optional private pension plan that can be offered to its members, there are no differences in relation to the retirement benefits.

Finally, it is relevant to say that is possible to transfer supplementary pension plans, for example sponsorship, groups of participants, plans and reserves, between closed-ended entities. Therefore, for example, an employee’s existing plan can be transferred to the supplementary pension scheme of a new employer.

Regarding the tax regime, payments made directly to private pension plans are not subject to the Withholding Income Tax (“IRF”), according to the progressive table. The taxation of such amounts is deferred until their redemption by the beneficiary. It is worth noting that investors in private pension plans may opt either for a progressive or regressive taxation system.

According to Law 9.532/97, investors in private pension plans have the possibility to discount, to a limit of 12% of their taxable yearly gross revenue, the contributions made to the plan.

The regressive system may reduce the income tax rate to up to 10% and the payment of the income tax is made only at the time of redemption or receipt of the income. In other words, under the regressive system, the income tax is charged exclusively at source and cannot be offset or refunded in the relevant yearly income tax return, and the longer the contributions remain invested, the lower the income tax rate will be. The taxation of payments made to private pension plans is deferred until their redemption by the beneficiary, who can choose either for a progressive or regressive taxation system.

The income tax rate starts at 35 per cent and is reduced according to the length of the investment, until reaching a 10 per cent rate for investments longer than 10 years. The payment of income tax is made only at the time of redemption or receipt of the income. This system is recommended for beneficiaries who are aiming at long-term investments, since the longer the contributions remain invested, the lower the income tax rate will be, as follows:

Term of accrual of each contribution	Income tax rate
Up to two years	35%
From two to four years	30%
From four to six years	25%
From six to eight years	20%
From eight to 10 years	15%
Over 10 years	10%

The income tax due under the progressive system, on the other hand, is assessed in two different ways. In the first one, a fixed percentage of 15 per cent at source is paid on the total redeemed amount or income, regardless of the value. In the second one, any differences must be offset in the yearly income tax return by the beneficiary, according to the progressive table above. One advantage of this system is that beneficiaries have the possibility to discount the contributions made to the plan each year, up to a limit of 12 per cent of his or her taxable yearly gross revenue.

It is important to mention that companies are exempted from paying official social security contributions on the amounts contributed to open-ended or closed-ended private pension plans if that benefit is offered to all employees and officers. Decree No. 3048 of 5 March 1999 expressly provides that companies do not pay social security contributions on amounts paid to employees resulting from an open or closed-end private pension fund, provided that such plan is available for all employees and senior managers of the company. All that means is that pension plans in Brazil must operate under non-discriminatory manners towards the employees and associates.

Also, Supplementary Law No. 109 of 29 May 2001 establishes that the private pension system is operated by private pension entities whose primary purpose is to institute and administer pension plans in addition to the General Social Security System. Within this context, private pension plans must, effectively, be intended as a savings mechanism targeted at the accumulation of resources for payment of future benefits, especially in furtherance of the participants' retirement pay.

Although, under the same mentioned supplementary law, and according to Summary No. 40 of 2009, issued by the National Social Security Institute, and to Resolution CGPC No. 8 of 19 February 2004, private pension plan companies are allowed to impose conditions, provided they are non-discriminatory ones, for admission and dismissal of employees from the private plan. Note that the employees and associates are not obliged to join the private plan, as it is an optional benefit, organized autonomously in relation to the public social security general scheme.

Additionally, companies can deduct as operational expenses the contributions to supplementary pension schemes, in order to calculate corporate profit, up to a 20% limit of the payroll of the employees and officers that participate in the plan.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

In the Social Security General System (which is the state pension system), the Social Security National Institute (INSS), a federal independent agency, has jurisdiction to implement governmental actions in the Social Security General System and the duty of granting and maintaining the benefits as well as social and health care. In relation to its funding plan, it is incumbent upon the Brazilian Federal Revenue Office, the agency of the direct administration subordinated to the Ministry of Treasury, to collect and survey the social security contributions levied on the remunerations paid to the insured employees and to individual taxpayers.

Under the Private Pension System, the functions of regulation and surveillance are exercised by the Ministry of Social Security, with the intermediation, respectively, of the Supplementary Pension Management Council and of the Supplementary Pension National Superintendence (PREVIC). All of this is in relation to non-listed entities. The regulation and surveillance of listed entities is by the Ministry of Treasury, with the intermediation of the Private Insurance National Council and of the Private Insurance Superintendence (SUSEP).

Further, the following agencies within PREVIC are responsible for supplementary pension schemes (Supplementary Law No. 109/2001 and its regulations): (i) *Conselho Nacional de Previdência Complementar* (CNPC), which is responsible for regulation; (ii) *Câmara de Recursos da Previdência Complementar* (CRPC), which acts as a court of appeal against the decisions of the CNPC; and (iii) *Secretaria de Políticas de Previdência Complementar* (SPPC/MPS), which is responsible for policy.

QUESTION 3

How are the plans governed?

As mentioned above, supplementary pension contributions are made to a fund administered by a private pension plan entity, either an open-ended or closed-ended fund. Closed-ended private pension funds are available to certain workers only, usually employees of a company or group of companies. Open-ended private pension funds, in turn, are available to any interested individual.

The open-ended private pension entity is managed by joint-stock companies operating for profit, usually insurance companies or banks, which offer individual or collective plans. This regime can be accessed by any person. They can also be an insurance company authorized to provide pension plans and the like. The Private Insurance Authority (SUSEP – *Superintendência de Seguros Privados*) is responsible for supervising open-ended pension entities.

The closed-ended private pension entity makes use of the identity of organized groups, through an employment bond or association, to make available plans of benefits of a social security nature to the employees of the sponsor company or members associated with entities representing workers' categories or sectors. Closed private pension entities are in charge of managing and implementing benefit plans.

According to article 35 of the supplementary law no. 109/2001 the closed-ended private pension plans must sustain a structure composed of a minimum of a decision-making council, a board of auditors and an executive committee. It can be observed that the above-mentioned law determines the minimum structure that needs to be followed by the closed-ended private pension plans. However, there is no restriction for the creation of any other administrative bodies that may be considered essential by the council member.

The 1st paragraph of article 35 of the supplementary law no. 109/2001 states that the decision-making councils and the board of auditors should be composed by a minimum of one third of the assisted participants' representatives.

The closed-ended private pension plans shall adopt principles, rules and governance practices, management and internal controls, which are deemed adequate to the carriage, complexity and risks involved to the benefit plans operated by them, seeking to ensure the full compliance of their goals. The agency (Decision-making Council, board of auditors and executive committee) has to observe the safety patterns of financial and auctorial safety, with specific purposes of maintaining the plan's benefit liquidity, balance and solvency, singularly, and also of the closed-ended private pension plans on its own, and all its activities.

QUESTION 4

Is there a compensation fund for pension benefits?

Private pension plans are generally managed by a bank in open-ended pension plans (the ones available for any person) and by a specialized manager hired by the company in closed-ended pension plans, who normally submits relevant decisions to a group of selected employees of the company.

The pension plan administrators are obliged to, once a year, contract independent auditors to analyze their accounting statements and certify their accuracy. Also, Brazilian law establishes that plan administrators must stipulate corporate governance rules in all levels of administration in order to preserve the liquidity and solvency of the fund.

The plan administrators are also obliged to request authorization from PREVIC in order to proceed with the constitution of private plans, corporate restructuring, sponsor withdrawal or the transference of sponsorship, plan participants and plans between pensions.

Therefore, the funds remain under the administration of the private pension entity, but subject to the regulation and oversight of the public authorities and kept apart from the assets of the pension entity. The pension entity may also take out a reinsurance policy, or be required to do so by the public authorities, in order to guarantee the obligations of the pension plan.

In summary, pension plans are subject to periodic actuarial valuations for the analysis of the sufficiency of reserves for payment of benefits, in which the benefits that are being paid and those to be paid are taken into account.

Independent accounting firms audit the pension plans once a year to confirm the accuracy of their records and statements and observe corporate governance rules to preserve their solvency. Besides all this, a continuous risk assessment analysis of any potential liabilities that could affect the pension plan is made during the year.

Moreover, PREVIC has powers to inspect pension plans in Brazil and request any documents and information regarding the plan that they may deem necessary to check compliance with applicable law. In addition, managers submit annual reports to PREVIC with relevant information about the plan and request previous approval before making relevant changes to their rules or structure.

In the administrative field, failure to comply with rules on supplementary pension laws may result in: (i) warnings; (ii) suspensions of rights to work with a supplementary pension for 180 days; (iii) prohibitions on working with a supplementary pension, insurance, banking and public services for 2 to 10 years; and (iv) fines that may vary between two thousand to one million Brazilian reais.

Such penalties may be applied jointly or individually, and are doubled if repeated.

QUESTION 5

How are pension rights enforced in an insolvency of the employers / sponsor?

The enforcement of any rights or rules by the participants can be made before the Brazilian judicial courts or, in certain cases, under the arbitration system. PREVIC has the authority to mediate disputes in specific cases through its Committee for Mediation, Conciliation and Arbitration (in closed-ended pension plans).

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

The PREVIC (the regulatory body - in closed-ended pension plans) can designate a special administrator with powers to intervene or conduct the extra-judicial liquidation of a plan if its liquidity and solvency cannot be assured any more.

It is important to highlight that, according to article 47 of the Supplementary Law No. 109/2001, closed-ended private pension entities are not subject to the bankruptcy proceedings set forth under Law 11,101/05, but only to extra-judicial liquidation to be conducted by the liquidator appointed by PREVIC. This legal regime also applies to the open-ended private pension entities.

Thus, in the event of an extra-judicial liquidation, the liquidator will prepare the general list of creditors, sell all of the relevant assets and will pay the creditors. Participants, including the beneficiaries, of the benefit plans, are not required to file proofs of claims in order for their respective claims to be recognized under the extra-judicial liquidation proceeding.

Both the participants and the beneficiaries will hold claims with special privileges over the assets guaranteeing the technical reserves. If such assets are not sufficient to pay the claims of the participants and beneficiaries, they will then hold claims with general privileges, which still rank higher than the general unsecured claims. Participants who are already receiving benefits, or who acquired this right before declaration of the extra-judicial liquidation, have preference over other participants.

The claims held by the participants and the beneficiaries however, will rank below labor claims, secured claims and tax claims.

In the event of extra-judicial liquidation, as soon as the relevant liabilities are paid, the remaining assets are distributed proportionately between all participants. In such a scenario, the beneficiaries may receive values that represent not only contributions of their own, but also amounts related to the sponsor's contribution and investment of the entity itself.

In general, in the event of the liquidation or bankruptcy of sponsors, credits held by pension funds will have special privilege over all other unsecured creditors, except over labor and tax creditors.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than employer?

As mentioned above, it is important to note that pension plans should be audited by independent accounting firms once a year to check the accuracy of their records and statements and also observe corporate governance rules to preserve their solvency. Also, a continuous risk assessment analysis of any potential liabilities that could affect the pension plan should made during the year, so that it is possible to determine the amount of contribution necessary for its solvency.

In this sense, the supervision by PREVIC (the regulatory body) is a form of protection itself. In addition, the private pension entity can get insurance cover for risks due to (i) the disablement of participants; (ii) the death of participants and pensioners; (iii) the survival of pensioners; and (iv) variances of biometric assumptions.

Nonetheless, the administrators and the management of the entity have to comply with their duties accordingly. It is important to establish corporate governance rules, since they have to seek the long-term sustainability of the pension plan and work for the best execution of the objectives of the pension entity.

To better achieve this goal, administrators and management must have a certain technical level of knowledge in order to be qualified for their job. In this sense, laws and regulations provide that members of councils of pension entities must have proven experience in financial, administrative, accounting, legal, supervision or auditing activities and must have a good reputation and not have been penalized criminally or administratively for any breach of the pension legislation, or as a public servant.

The pension entity must adopt procedures for the certification, eligibility and qualification of those who occupy any position in the entity, and must prove to PREVIC that these procedures have been adopted.

QUESTION 8

Are there any cross-border features of your pension regime?

Not applicable.

QUESTION 9

Discuss the state of defined benefit plans in your country

Defined benefit private pension plans are only administrated by a closed-ended private pension entity. Past pension plans usually assured participants and pensioners a fixed pension benefit or profitability corresponding to monetary correction and high interest indexes such as of 6 per cent (that could reach, in certain years, a 12 per cent rate of profitability, for example).

These criteria are considered too high or difficult to follow nowadays, due to present economic conditions and also considering that, because of demographic ageing, benefits have to be paid for longer periods. Therefore, current pension plans tend not to assure a 'defined benefit' to participants any more but rather determine that sponsors and participants have to pay a 'defined contribution' and that the future pension benefit will be calculated according to the individual mathematical provision of the participants.

CANADA

QUESTION 1

What is the legal framework for private pension plans in your country?

Legislation, common law, and other sources of governance

Over 6.2 million Canadian private sector workers participate in employer-sponsored pension plans[1].

In Canada, private pension plans are regulated by both the federal and provincial laws and, to a certain extent, by the common law. Each province has enacted its own minimum standards pension legislation[2]. In addition, federally regulated companies are governed by the federal Pensions Benefit Standards Act[3]. Although registering a pension plan is optional, doing so affords the plan certain benefits, which are summarized below.

The following is a summary of the relevant pension legislation and regulators in each Canadian jurisdiction:

Chart A

Jurisdiction	Legislation	Regulator
Federal and Territories	Pension Benefits Standards Act	Office of the Superintendent of Financial Institutions
British Columbia	Pension Benefits Standards Act	Financial Institutions Commission
Alberta	Employment Pension Plans Act	Alberta Superintendent of Pensions
Saskatchewan	The Pension Benefits Act, 1992	Pensions Division
Manitoba	Pension Benefits Act	Manitoba Pension Commission
Ontario	Pension Benefits Act	Financial Services Commission of Ontario – Pensions Plans Branch
Québec	Supplemental Pension Plans Act	Régie des rentes du Québec – Direction des régimes de retraite
PEI	Pension Benefits Act (Not yet in force)	–
New Brunswick	Pension Benefits Act	Office of the Superintendent of Pensions
Nova Scotia	Pension Benefits Act	The Pension Regulation Division
Newfoundland & Labrador	Pension Benefits Act, 1997	Financial Services Regulation Division

1 Statistics Canada, as of March 10, 2015.

2 Pension legislation in Prince Edward Island ("PEI") has received royal assent but has not yet been proclaimed into force.

3 *The Pension Benefit Standards Act* also applies in Canada's three territories in the place of any similar provincial laws.

While pension legislation differs somewhat between provinces, there are common issues addressed in each instance, including:

- membership eligibility requirements;
- minimum funding requirements;
- plan asset investment considerations;
- the division of plan benefits on marriage breakdown; and
- entitlements upon death.

This list is certainly not exhaustive, and the breadth of protection is far-reaching.

Plan sponsor employers with employees in multiple provinces are required to comply with pension legislation in each relevant jurisdiction.

The common law also governs pension law in Canada in a number of ways. Jurisprudence aids in the interpretation and application of pension legislation, particularly regarding the rights and obligations of stakeholders (see Questions 5 and 6, below). Jurisprudence in the areas of trusts and employment law also frequently intersect with pension law, as does administrative law, which ensures employers and pension beneficiaries are accorded procedural fairness in their dealings with regulators. Constitutional considerations also apply, particularly to resolve issues surrounding the conflict between provincial and federal laws (e.g. paramountcy discussed in Question 6, below), and where the terms of pension plans are alleged to contradict citizens' rights under the *Canadian Charter of Rights and Freedoms*[4].

Tax considerations

While registration is not compulsory under the Canadian Income Tax Act, registered pension plans generally receive the beneficial treatment described below. However, registered plans are subject to enhanced reporting requirements.

Employers may deduct its employee plan contributions. Member contributions are similarly deductible in the year in which they are made, and members are taxed for amounts paid only when they begin to draw their pension. Investment income earned on pension funds are typically tax exempt. There are, however, maximum caps on contributions and deductions for both employers and employees.

[4] For example, section 15 of the *Charter* enshrines the right to equality, and has been applied to require the definition of "spouse" under a pension plan to extend to same-sex spouses.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

Regulatory agencies

Pension plans in Canada are regulated on a provincial level by specific regulatory agencies, as outlined in the chart above. The extent of regulation depends on whether the plan is registered or non-registered. Registered plans are heavily regulated but also receive the tax benefits discussed above. Non-registered plans do not receive these benefits but are not subject to such comprehensive regulatory requirements.

The Canadian Association of Pension Supervisory Authorities ("CAPSA") is an inter-provincial body comprised of representatives of the provincial regulators that seeks to harmonize pension standards across the country. This association also established the National Pension Compliance Officers Association, tasked with ensuring consistency in administrative policies and processes.

Mandatory reporting on plan values

Defined benefit plans must comply with various financial reporting requirements, including the filing of an actuarial valuation report on a triennial basis. These reports address service costs, gains and deficiencies, unfunded liabilities, solvency deficiencies, and amortization payments, among others. In certain circumstances, reports must be filed annually; for example, in Ontario, where a plan falls below a specified solvency funding threshold, a valuation report must be filed annually.

Formulae for contributions and funding requirements

Various formulae for pension contributions are found across the Canadian legislative landscape. These formulae vary based on the type of plan. A variety of plan types are available, provided the plan complies with the minimum legislative standards in each relevant provincial jurisdiction[5].

Funding requirements also vary between jurisdictions and plan types. For example, defined benefit plans require both ongoing and solvency valuations every three years to ensure the plan is able to meet its funding obligations. Plan sponsors may be required to make special payments to amortize an actuarial deficit in the plan if a deficit is revealed in the plan valuation.

Plan sponsor employers are typically permitted to take contribution holidays under certain circumstances, generally where actuarial analysis reveals a plan surplus (i.e., where the plan's assets exceed its liabilities). However, minimum standard legislation only permits such holidays to the extent the plan remains fully funded without requiring additional contributions. Further, some provinces have legislated caps on contribution holidays, where contribution holidays may only be taken where plan solvency exceeds a specified percentage of solvency liabilities – typically between 5-10%.

[5] The most common plan types in Canada are defined benefit, defined contribution, and combination or hybrid plans. Each plan type has its own contribution formula.

Since the global financial crisis in 2008, many Canadian jurisdictions have enacted funding relief measures for specified periods of time. These measures allow, for example, the extension of solvency funding periods and the consolidation of debt.

Ability to take away benefits and withdraw funds subject to regulatory approval

Minimum legislative standards that govern vesting, locking-in, and portability vary between jurisdictions. Typically, vesting and locking-in occur at the same time. Age requirements for vesting and locking-in have been abolished. Instead, the criteria for both is typically the completion of a prescribed length of employment. In Manitoba and Québec, pension benefits vest and lock-in immediately.

There are several exceptions to the locking-in rules, most notably the contribution refund exception. When an employment relationship ends prior to a pension's vesting date, employees are entitled to a refund of their own contributions, with interest. Minimum standard legislation in every jurisdiction also provides for a "benefit unlocking rule". Typically, a plan provides for unlocking where the annual pension at the normal retirement date is less than 4% of the year's maximum pensionable earnings – typically from the termination year. Additional exceptions to the locking-in rules include those for shortened life expectancy and financial hardship.

Employees also have the right to transfer the commuted value of a vested pension to another retirement savings vehicle. For defined benefit plans, portability rights are not mandatory for employees who have attained early or normal retirement age. Such rights may be mandatory in defined contribution plans. Permissible locked-in retirement savings arrangements are prescribed by legislation. Some jurisdictions offer creditor-protected arrangements. For example, Saskatchewan allows transfers to creditor-protected Registered Retirement Income Funds.

QUESTION 3

How are the plans governed?

Employer responsibilities

Many constituencies are involved in the administration of pension plans in Canada. Employers are often "plan sponsors". Plan sponsors cannot delegate their fiduciary responsibilities. They may, however, delegate administrative or investment functions to outside professionals. An employer may also elect to be the plan administrator. Other relevant governing bodies may include pension committees (with employer and employee representatives and/or plan members), insurance companies, and boards of directors. These options are prescribed by minimum standards legislation across all jurisdictions.

The standard of care applicable to plan administrators is generally that of an ordinary person dealing with the property of another. Effectively, this duty requires administrators to consider the best interests of plan members, beneficiaries, and the plan itself. This is a legislated standard in many jurisdictions.

An employer may serve as a plan administrator; however, this dual role may result in an apprehension of conflict in certain circumstances, such as where there is a conflict between the best interests of the company and the best interests of the plan.

Employee responsibilities

Employees may participate in the administration of a plan by virtue of a plan committee. Depending on the size and type of plan, pension committees often include employees or employee representatives. Plan members may also appoint other members to such committees. In some jurisdictions, an employer is required to establish a pension advisory committee at the request of a majority of members.

Pension committees have a range of duties that are outlined in the minimum standards legislation, including, for example, making improvement recommendations and monitoring plan administration.

Plan members may also have administrative responsibilities, including ongoing reporting obligations. Such reporting is required where the employee makes a beneficiary designation change, has a change of address or contact information, and on marriage breakdown. This list is not exhaustive.

Board of directors

The board of directors of a private company often oversees plan matters. Depending on the size of an organization, the board may establish a sub-committee specifically for pension issues, including employee representatives from key departments. The board may also delegate certain administrative functions to external professionals. However, as discussed below, administrators are fiduciaries and they cannot delegate the responsibility to act in the best interest of plan members.

Fiduciary obligations

Plan administrators serve in a fiduciary capacity and as such must act in the best interest of plan members. Minimum standards legislation explicitly refers to such a role to varying degrees. While the legislation in some jurisdictions does not describe the administrator as a fiduciary, the legislated standard of care implies it. Significant fines may be imposed for breaches of statutory duties, in addition to traditional remedies available at common law through civil actions.

Other administrative requirements

Plan sponsors who elect to register a plan must do so within 60 days of its establishment. The registration process is subject to several procedural and substantive requirements to ensure coverage by minimum standards legislation and to receive applicable tax benefits under the Income Tax Act.

In addition to the financial reporting obligations discussed above, plan administrators have a number of additional regulatory reporting requirements. For example, investment reporting, reconciliation and audited financial statements must typically be filed every year. In particular, administrators of pension plans must file an Annual Information Return in the jurisdiction in which the plan is registered. Specific requirements under these returns vary between jurisdictions. The Canada Revenue Agency (Canada's federal tax authority) also has a number of filing requirements, for example with respect to notification of a plan amendment.

QUESTION 4

Is there a compensation fund for pension benefits?

There is one pension benefit guarantee fund in Canada, in the Province of Ontario.

The Pension Benefits Guarantee Fund (“PBGF”) was established in 1980 and is governed by the Ontario Pension Benefits Act. It provides protection to Ontario members and beneficiaries of privately-sponsored, single-employer defined benefit plans in the event of plan sponsor insolvency. The PBGF guarantees specified pension benefits of up to $1,000 per month for service performed by eligible employees while employed in Ontario, subject to certain age and service criteria. As of March 2010, the PBGF covered more than 1.1 million plan members in over 1,500 defined benefit plans. The PBGF is administered by the Superintendent of Financial Services of Ontario, and PBGF investments are managed by the Ontario Financing Authority.

The PBGF is funded by plan sponsor employers through annual premium payments, capped at a maximum of $4 million per year. The annual premium is comprised of two main components – a per-member fee (a nominal amount of $5 per beneficiary), and a risk-based fee. The risk-based fee applies to underfunded plans.

To date, Québec is the only other province to attempt to establish a pension benefits guarantee fund. A bill currently working through the National Assembly of Québec would amend the Québec Supplemental Pension Plans Act to establish a fund that would provide up to $700 per month to eligible employees for a period of five years in the event of plan sponsor insolvency. In its current draft form, the fund would apply to over one million Quebec employees registered in more than 950 privately sponsored plans.

Québec has passed legislation that provides ad hoc support to employees whose employers are insolvent due to exceptional circumstances. Passed in the aftermath of the insolvency of Nortel Networks Corporation and in the wake of the 2008 global financial crisis, Bill 34, “An Act to amend the Supplemental Pension Plans Act”, permits affected employees to apply to have their benefits paid through the provincial pension authority, the Régie des rents du Québec.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

Canada has two primary insolvency statutes, the *Bankruptcy and Insolvency Act* ("*BIA*"), and the *Companies' Creditors Arrangement Act* ("*CCAA*"). The *BIA* is used primarily to effect bankruptcies, receiverships and liquidations, although creditor proposals are also possible. The *CCAA* is fundamentally a corporate restructuring statute, although it is also used in some cases to effect sales of assets, particularly in large and complex corporate entities. A common feature of both the *BIA* and *CCAA* is the "stay of proceedings" that freezes creditor rights (including the right to initiate or continue claims or enforcement of any kind against the debtor company outside the proceedings). The effect of the stay of proceedings is to force all of the debtor's creditors, including pension plan participants, where relevant, to deal with the debtor company within the insolvency proceedings.

Both the *BIA* and the *CCAA* contain provisions that offer various forms of protection to pension creditors in insolvency scenarios, as discussed in Question 6 below.

Regulatory intervention

Provincial legislation in some cases permits the provincial regulator to take certain steps to protect a pension fund's assets upon the sponsor employer's insolvency, including the acceleration of claims for contributions to underfunded plans.

The regulator may also, in certain circumstances, take steps to initiate the wind-up of a pension plan, particularly where the plan sponsor will no longer carry on business as a result of its insolvency.

Finally, where the employer serves as plan administrator, the provincial regulator may appoint an alternate plan administrator where there is a perceived conflict between the interests of the pension plan and the employers' duties to other stakeholders.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

The *BIA* and the *CCAA* both provide protections for certain pension-related claims. In addition, provincial pension legislation provides statutory priorities for certain unpaid pension amounts.

In some cases, these provincial statutory priorities directly conflict with the priorities set out in the federal insolvency statutes. This conflict between provincial pension legislation and federal insolvency law has been at least partly resolved by a recent decision of the Supreme Court of Canada (Canada's highest appellate court) in *Sun Indalex Finance, LLC v United Steelworkers*, 2013 SCC 6 ("Indalex").

CCAA

The *CCAA* is fundamentally a corporate restructuring statute rather than a bankruptcy statute, so it does not expressly provide a scheme of creditor priorities. However, a court may sanction a restructuring plan pursuant to the *CCAA* only if it provides for the payment of the following unpaid pension amounts:

1. amounts deducted as pension contributions from employee wages that have not been contributed to the pension plan; and

2. amounts that are required to be contributed to the pension plan in respect of "normal cost" contributions that have not been paid[6].

There is a significant exception to this restriction, which is that a court may sanction a restructuring plan that does not provide for the payment of the above noted amounts if it is satisfied that the relevant parties have entered into an agreement, approved by the relevant pension regulator, that provides for alternative arrangements in respect of the foregoing amounts.

The *CCAA* provides similar protections in circumstances where the court is asked to sanction a sale of assets. Specifically, a debtor company subject to the *CCAA* may only sell or dispose of assets outside the ordinary course of business if it is authorised to do so by the court. The *CCAA* provides that the court may grant that authorization only if it is satisfied that the company will make the pension payments that would have been required if it had been asked to sanction a restructuring plan[7].

The *CCAA* does not provide any special status for unpaid "special payments", which are the payments that the employer is required to make to amortize the actuarial deficiency in the pension plan.

The protection of employee deductions and normal cost contributions is also reflected in practice in the court orders that are typically granted to stay proceedings in respect of debtor companies pursuant to the *CCAA*. In particular, *CCAA* debtors are typically authorized to continue paying normal cost payments into their pension plans during a *CCAA* stay of proceedings. However, the debtor company's obligation to pay special payments has been stayed in several recent cases[8].

BIA

The *BIA*, which is primarily a bankruptcy, receivership and liquidation statute, provides a statutory scheme of priorities that includes priorities for pension amounts similar to those that must be paid in the context of a *CCAA* restructuring plan. Specifically, the *BIA* provides a statutory security in both bankruptcy and receivership for:

1. amounts deducted as pension contributions from employee wages that have not been contributed to the pension plan; and

2. amounts that are required to be contributed to the pension plan in respect of "normal cost" contributions that have not been paid[9].

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[6] *CCAA*, section 6(6).

[7] *CCAA*, section 36(7).

[8] See for example *Re Fraser Papers Inc.* [2009] 55 C.B.R. (5th) 217 (SCJ Commercial List).

[9] BIA, sections 81.5(1) and 81.6 (2).

This statutory security interest ranks in priority to every other claim against the debtor company other than certain rights of suppliers to repossess goods or produce, certain priorities for unpaid wages and certain tax amounts that are deemed to be held in trust[10].

Once again, there is no special protection for special payments owing to a pension plan.

Provincial priorities

In addition to the protections in the federal insolvency legislation, provincial pension benefits legislation provides for statutory deemed trusts for certain unpaid pension amounts. Deemed trusts operate in a manner akin to a floating charge by deeming the general assets of the debtor to be subject to a trust, as if the assets had been kept separate and apart for the benefit of the pension plan. Provincial pension legislation also typically provides a statutory lien and charge for these unremitted contributions.

For example, the Provincial pension legislation in Ontario provides for a statutory deemed trust that applies to:

1. money withheld or collected from an employee as a pension contribution that has not been deposited into the pension plan;

2. employer contributions due and not paid into the pension plan; and

3. employer contributions accrued to the date of the wind-up of a pension plan but not yet due[11].

The Ontario legislation also provides that the administrator of the pension plan has a lien and charge on the assets equal to the amounts deemed to be held in trust. In the recent Indalex decision, referred to above, the Supreme Court of Canada held that the Ontario provincial deemed trust applies to the full wind-up deficiency that arises on the wind-up of a pension plan.

Conflicts between federal insolvency law and provincial pension law

The more difficult question with provincial deemed trusts is how they apply in the context of insolvency proceedings, especially where they conflict with competing priorities established by the applicable federal insolvency statute. This question is resolved based on the constitutional law doctrine of federal paramountcy, in which direct conflicts between federal and provincial laws are resolved in favour of the federal law. Consequently, a provincial legislature cannot affect priorities established under a federal insolvency statute through legislation imposing deemed trusts or liens.

A party relying on paramountcy is required to demonstrate the direct incompatibility of the federal and provincial law, so the central question in a duel of provincial pension legislation and federal insolvency legislation becomes whether the provincial legislation is, in fact, incompatible with the federal legislation.

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[10] BIA, sections 81.5(2) and 81.6(2).

[11] *Pension Benefits Act* (Ontario), section 57.

In the case of the *BIA*, the answer appears to be relatively straightforward. Since the *BIA* establishes an express scheme of creditor priorities, any provincial law that purports to subvert that scheme of priorities is in direct conflict, so the scheme of priorities in the federal law governs. As a result, it is frequently said that pension deemed trusts are not effective in proceedings under the *BIA* because they would have the effect of reordering the statutory priorities set out in the federal legislation.

The *CCAA* is different because it does not set forth an express scheme of creditor priorities. Accordingly, it is said that a provincial deemed trust continues to operate in the context of a *CCAA* proceeding, subject to specific conflicts necessitating the application of federal paramountcy. Under the *CCAA*, the conflict necessitating federal paramountcy may arise from the orders granted by the court under its *CCAA* jurisdiction rather than specific priorities set out in the statute. For example, the *CCAA* authorises the court to grant certain super-priority charges, including charges to secure interim debtor-in-possession financing, administrative costs, director and officer indemnities and critical supplier payments[12]. To the extent that the priorities granted to these charges by a court acting under the *CCAA* conflict with the priorities established by the provincial pension legislation, the priority charge granted pursuant to the *CCAA* will govern. The decision of the Supreme Court of Canada in Indalex unanimously confirmed the ability of a court exercising authority under the *CCAA* to grant a super-priority debtor-in-possession financing charge in priority to a provincial deemed trust.

In light of these differences between the application of provincial pension priorities under the *BIA* versus the *CCAA*, there is frequently a tension between creditors who would benefit from an adjudication of priorities under the *CCAA* (typically employees, pensioners, pension administrators) and creditors who would prefer to see provincial pension priorities eliminated under the *BIA* (typically secured creditors who would otherwise rank behind pension deemed trusts or liens). In Indalex, the Supreme Court of Canada held that courts will favour an interpretation of the *CCAA* that avoids a race to liquidation under the *BIA*; however, courts will not read a *BIA* priority scheme into the *CCAA*.

Consequently, perhaps the most accurate way to characterize the situation in *CCAA* is that pension administrators, regulators and beneficiaries continue to benefit from the application of provincial pension priorities absent a direct conflict with the *CCAA*, but they do so under the specter that other creditors could seek a conversion of the proceedings into a receivership or bankruptcy under the *BIA* to eliminate the pension priorities. In fact, the recent decision of the Ontario Court of Appeal in Grant Forest Products Inc. v. The Toronto-Dominion Bank confirms that a supervising *CCAA* judge has the discretion to permit a creditor to bankrupt the debtor company to alter provincial pension priorities[13].

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[12] *CCAA*, sections 11.2, 11.4, 11.51 and 11.52.
[13] 2015 ONCA 570.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

Generally speaking, unpaid pension contributions and plan deficits are owed by the plan sponsor without recourse to third parties.

However, recourse to the plan administrator and directors and officers of the employer may be available where they have acted negligently in exercising their duties or where they have failed to comply with the governing pension legislation. The administrator is a fiduciary and owes a stringent duty of care (this duty is both codified under provincial legislation and exists independently at common law). Where this duty is alleged to have been breached, plan beneficiaries may claim against the administrator. These kinds of claims may include, among other things:

- imprudent investment decisions;
- inequality of treatment between different plan members; and
- improvident funding decisions.

Consequently, where the board of directors of a corporation is responsible for the administration of a pension plan, the directors continue to be responsible for the prudent management of the pension assets. Claims against the directors and officers of the plan sponsor are also possible where the plan sponsor is also the administrator of the plan (this occurred, for example in Indalex). Additional claims and fines may also apply where an offence has been committed under the applicable pension legislation[14].

There is also limited relief available against a Trustee under the *BIA* where the Trustee disposes of assets that are properly subject to the special priorities created for unremitted pension contributions. The *BIA* secures certain unpaid employer pension contributions. Such security ranks above all other claims against a bankrupt's assets, with limited exceptions. Where the trustee improperly disposes of such assets covered by the security, the trustee can be liable up to the amount realised on the improvident disposition.

QUESTION 8

Are there any cross-border features of your pension regime?

The *CCAA* Part IV and *BIA* Part XIII govern cross-border insolvencies in Canada. These insolvency statutes were substantially amended in 2009 to adopt the United Nations Commission on International Trade Law (UNCITRAL) Model Law on Cross-Border Insolvencies. The most notable amendment is that both the *CCAA* and *BIA* now addresses the recognition of foreign proceedings and obligations where a foreign proceeding is recognised.

[14] See section 110, *Pension Benefits Act* (Ontario).

There are three main requirements for a foreign proceeding to be recognised in Canada: the proceeding is a foreign proceeding, the applicant is a foreign representative, and the foreign proceeding is either a "foreign main proceeding" or a "foreign non-main proceeding". Where an application for recognition meets these requirements as defined under the relevant legislation, court recognition will be granted. These foreign recognition mechanisms have simplified cross-border proceedings in Canada and are useful in maximising worldwide creditor recovery and avoiding the multiplicity of claims.

As a result of these provisions, Canadian pension beneficiaries in the context of a foreign corporate group may find their claims adjudicated in proceedings outside Canada where a cross-border insolvency is being administered in a foreign jurisdiction. Similarly, foreign pension beneficiaries may find their claims adjudicated in Canada where Canada is the main jurisdiction for the administration of a cross-border insolvency.

In the summer of 2014, the Ontario Superior Court of Justice (Re Nortel Networks Corp., 2014 ONSC 6973) heard a trial of various claims asserted by a United Kingdom ("UK") pension trust and the UK Pension Protection Fund against Canadian domiciled companies under creditor protection. The trial included numerous cross-border pension issues, including the application of UK pension law (such as the UK financial support direction scheme) extraterritorially. The discovery process for the pension claims trial was conducted in co-ordination with the discovery process for other litigation in the Nortel bankruptcy proceedings that featured negotiated cross-border protocols governing discovery matters that incorporated a hybrid of Canadian provincial and United States federal civil procedures. The pension trial decision is currently under appeal, but the protocols implemented in the Nortel trial are an example of Canada's leadership in facilitating cross-border comity to complex cross-border insolvency scenarios, including those relating to the adjudication of pension claims.

QUESTION 9

Discuss the state of defined benefit plans in your country

The same forces of low interest rates, improved longevity and global market volatility that are creating issues for defined benefit plans internationally are causing their decline in Canada. In 2010, there were 11,744 registered defined benefit plans. This number dropped to 10,856 in 2013 and 10,414 in 2014. These plans are becoming less common in non-unionized, private sector workforces and new ones are not being introduced.

Other plan types have also emerged that are beginning to gain traction in the Canadian pension landscape. These so-called "hybrid plans", which have features of both defined benefit and defined contribution plans, have been implemented in some provinces in certain instances to help maintain existing defined benefit plans.

For example, “target” benefit plans allow fixed employer contributions with the same benefit promise to plan members. Target benefit plans provide greater flexibility since benefits and/or contributions can be adjusted when a plan encounters funding or solvency issues. Where implemented, these plans are increasingly popular among large employers which currently maintain defined benefit plans and do not want to make a full switch to defined contribution plans because they allow for greater risk sharing between employers and employees.

On September 1, 2014, the Alberta Employment Pension Plans Act came into effect. This new piece of legislation introduced a target benefit pension plan regime to the province. Alberta is the second province (after New Brunswick) to implement regulations to allow alternative plan types. The new Alberta rules provide that when a plan encounters funding concerns, it may reduce or eliminate ancillary benefits, reduce the targeted defined benefit (this reduction may apply to accrued benefits), or increase contributions. Unlike the New Brunswick reforms, the Alberta rules do not permit the conversion from a defined benefit plan to a target benefit plan on a retroactive basis.

Certain provinces have implemented legislative amendments to allow plans the option of converting to a “shared risk” plan. Generally, shared risk plans offer a modest initial benefit promise and future surpluses adjust for inflation before and after retirement rather than having indexation after retirement. The initial benefit is based on career average earnings. Under specific circumstances, these plans allow benefits to be reduced or redesigned to ensure pensions have sufficient surpluses in event of market shocks.

New Brunswick was the first province to adopt shared risk plans in its provincial pension framework under the Pension Benefits Act. Several pension plans within New Brunswick have since converted to shared risk plans.

As Canadian plan sponsors continue to move away from defined benefit plans, hybrid alternatives such as target benefit plans and shared risk plans may become increasingly popular.

FRANCE

This chapter only relates to defined benefit private pension plans.

QUESTION 1

What is the legal framework for private pension plans in your country?

There are two types of defined benefit pension plans in France depending on how the retirement benefits are to be paid: the differential schemes and the additive schemes.

Under the differential schemes, a certain level of retirement benefits is guaranteed for all retirement schemes combined. The differential schemes therefore fill the difference between that guaranteed level of pension and the total amount of benefits paid under other retirement schemes (and notably the French State base scheme and the French State additional scheme (known as "ARRCO" and "AGIRC") as well as, as the case may be, any benefits paid under a private defined contribution retirement scheme).

Under the additive schemes, a set amount of benefits is guaranteed in addition to the mandatory pension schemes as well as, as the case may be, any benefits paid under a private defined contribution retirement scheme.

Subject to the following conditions:

- the benefits are defined;

- the benefits are paid only if the beneficiary ends the career in the company in which the scheme is in place; and

- the scheme is entirely financed by the company and the funds are not individualized by the employee.

Defined benefit pension schemes are subject to the following specific contributions (and not on the social security contributions applicable to salary) to be paid by the employer either on the benefits paid (with a rate between 16% and 32% depending on the date on which the benefits started to be paid) or the premium paid to finance the scheme (with a rate of 24% in case of external management and 48% in case of internal management).

Moreover, as of 1 January 2015, an additional contribution equal to 45% is due in addition to the above contribution on the total amount of the pension benefits exceeding €304,320 in 2015.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

The plans are not regulated. However, in the case of external management (cf. below response 3), the insurance company managing the funds is subject to very strict rules governing this type of company notably to avoid their insolvency.

QUESTION 3

How are the plans governed?

A company implementing a defined benefit pension scheme is able to choose among the following two options for its management:

- Internal management: the company itself guarantees its pension obligations.

- External management: a specific contract is entered into with an insurance company guaranteeing the sponsor company's obligations.

All defined benefit pension schemes created as of 1 January 2010, must have external management.

Internal management

The Company is subject to accounting obligations.

Publicly listed companies which have consolidated accounts must book reserves equal to their commitments and record these reserves in their balance sheet liabilities.

Other companies can choose between the above option and the mere statement of the amount of their obligations, for information purpose, in the annex of their accounts.

A draft Bill has been introduced pursuant to which the companies managing a pension scheme internally would be granted a 5-year period to transition to external management. To date, the Bill has not been passed but it may come into effect in the near future.

External management

The company subscribes to an insurance contract with an insurance company, a mutual fund or a contingency fund. The company pays a premium to the insurer which establishes a fund for the management of the pension assets. For each retirement, capital corresponding to the pension benefits is withheld from the fund. The amount of the capital withheld depends primarily on the amount of the pension benefits to be paid and the age of the beneficiary. The insurer is liable only to the limit of the fund. Therefore, in order for the company to guarantee all of its obligations, it must contribute regularly to the fund and compare its obligations and those of the insurer to ensure that they are aligned (and if not, make additional contributions).

The external management protects the retirees whose benefits are guaranteed as well as the current employees to the extent that the fund is sufficient to cover their employer's obligations.

QUESTION 4

Is there a compensation fund for pension benefits?

There is no compensation fund. Please refer to response 3 above for the protection offered to pensioners.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

In the case of external management, the employer's insolvency will not impact the retirees (whose benefits are guaranteed by the insurer). For the current employees for whom the employer contributed to the fund, the insurer will only guarantee the obligations within the limit of the fund and therefore may only cover part or none of these obligations.

In the case of internal management, the beneficiaries (already retired or currently working) have no guarantee that their employer's obligations will actually be implemented if the company is under an insolvency procedure. Given this high level of uncertainty, as mentioned above, internal management is not available for pension schemes implemented as of 1 January 2010. Moreover, as discussed, a draft Bill (not yet passed) provides for the conversion of the internal management into external management within a 5 year-period.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

There is no special priority. However, in the case of external management of the scheme, and subject to certain conditions, the amount of the premium unpaid to the insurer by a company in insolvency can be guaranteed by the French State Salary Insurance.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

There are no such remedies.

QUESTION 8

Are there any cross-border features of your pension regime?

There are none.

QUESTION 9

Discuss the state of defined benefit plans in your country

The contributions required for these types of scheme have significantly increased over the past 10 years and are now much less attractive than in the past. However, they remain a tool used to attract and retain top executives.

As mentioned above, there may be a change in the law in the coming months to ensure that, in case of internal management, the employees and beneficiaries would be protected against the insolvency of their employer company.

GERMANY

The template of questions mentions ‘private pension plans’ but in this chapter it has been assumed that occupational pension plans are also required to be covered. This chapter therefore focuses on corporate pension arrangements in Germany.

QUESTION 1

What is the legal framework for private pension plans in your country?

In Germany, any type of pension benefit stemming from a private employer finds its legal basis in the German Corporate Pension Act, the so-called ‘Betriebsrentengesetz (BetrAVG)’ (the “Corporate Pension Act”). This Bill was passed in 1974. Given that prior to that date there had not been any legislative foundation regarding the labour law and civil law aspects for occupational pensions (there were numerous tax regulations), the new law encompasses a variety of different types of plans and funding vehicles that had developed across an almost 150 year history since the early years of industrialization in the 19th century.

Hence, the new Corporate Pension Act laid a legal foundation for these benefit arrangements in the area of labour law, establishing four funding vehicles for corporate pensions, general vesting rules and a revolutionary new insolvency protection regime. In 2002 a fifth funding vehicle was added to this impressive array.

The funding vehicles in the German corporate pension landscape are discussed below.

Direct Pension Promise

This is the initial, simplest and most broadly used type of benefit arrangement. It is nothing more than an employer’s oral or written promise to one, several or all employees to grant benefits in case of old age, disability or to his/her dependents in case of death. It is usually called a ‘Pensionszusage’ or a ‘Direktzusage’.

There is no requirement for any funding or reservation of dedicated pension assets nor are any assets legally separted from the employer’s assets in any way. The employer does accrue the pension liability on its balance sheet and later simply pays out the pension as it reduces this liability over time. It is obvious that this type of pension regime bears the large risk of an employer’s insolvency and thus the loss of all entitlements for the beneficiary. This is the main reason why the Insolvency Protection Fund (‘Pensions-Sicherungs-Verein a.G. - PSVaG’) was established (see below no. 4.).

Direct Life Insurance

A rather easy to understand and very straight-forward funding vehicle is the so-called ‘Direct Life Insurance’ (‘Direktversicherung’). It is simply a life insurance (annuity) contract stemming from any commercial life insurance carrier where the employee is the beneficiary. The employer is the policyholder and also pays the premium. Internally, the employee often is the true sponsor of the contract due to a deferred compensation arrangement with the employer. Within such a deferred compensation arrangement (often referred to as ‘salary sacrifice’) the employee reduces his cash salary in return for receiving such a direct life insurance. Still, formally it is always the employer who pays the premium. As with all corporate pension plans, the employee has no means to dispose of his benefit entitlements (i.e. the life insurance contract) prior to his retirement age. This applies also if it is a self-funded (deferred compensation) life insurance contract. In turn, the employee receives substantial tax and social security contribution advantages.

Insurance Pension Fund

This funding vehicle is very similar to the previously described 'Direct Life Insurance'. The difference lies with the carrier. Although it is also structured as a life insurance company (mostly as a mutual) it must foresee that any benefits may only be paid out if the beneficiary no longer receives any work income. Mostly, insurance pension funds only cover employees of one (usually very large) employer or one industry.

Support Fund

Perhaps the oldest form of externally funded benefit vehicles is the unique support fund. Very often the support fund foresees benefits in unexpected situations, uncommon for corporate pensions. It usually has a provision that allows the fund to react and grant benefits in case an eligible employee falls into severe calamity. A very special feature of the support fund is the fact that, formally, it does not grant the beneficiary a claim against the fund. This is a historic relict which differentiates the support fund from an insurance company and thus spares the support fund from falling under the supervision of the financial supervisory authority.

The support fund however, is very limited with its financial leeway. Ahead of retirement and due to fiscal limitations, the employer can only accrue up to two annual pensions ('Reservepolster-finanzierung'). This is, of course, far too little given that on average and depending on retirement age and interest rates applied some 12-15 annual pensions would have to be accrued for a life-long pension. Only once the employee reaches retirement age can the employer fund the obligation completely. Yet, within its limits the support fund is rather flexible as it allows the employer to fund very freely as its earnings situation permits.

An important version of the support fund is the so called 're-insured support fund'. While this is in essence a support fund like any other, the tax treatment is completely different. In this case, the fund takes out annuity insurance to fully fund the pension obligation. If that happens the employer can contribute to the fund in the full amount of the applicable insurance premium.

Pensions Fund

Only first established in 2002, these funds have some similarities with pension funds in many other countries. These funds resemble the above-mentioned insurance pension fund. The main difference from the insurance pension fund is that they must not give a full guarantee to all components of the benefit obligations. Hence there is a variable component in their benefit structure which allows them to adapt to varying economic situations. However, legally, the German pension fund is structured like a life insurance company, i.e. either as a corporation or as a mutual. Pension funds also fall under the supervision of the insurance industry's supervisory authority. And should note that German pension funds do not entertain an independent board of trustees that govern the fund.

Tax rules and social security contributions around the five funding vehicles

The tax and social security contribution regime that applies to each of these five funding vehicles is quite different in each case.

The direct pension promise is the most convenient for the beneficiary because irrespective of the amount granted there is no tax effect during active working life. Only the later pension is fully taxed and also requires contributions to statutory health insurance (unless the individual is privately insured). The employer can accrue a pension provision on its (tax) balance sheet, but is obliged to apply a 6% discount rate which in the current capital market environment is not sufficient for an appropriate funding of its pension liability. As a rule of thumb one might say that the tax provision is only some two thirds of the according IAS 19 provision for the same pension liability.

The support fund is similarly convenient for the beneficiary, as he or she only has to pay taxes for the later benefit and as a pensioner also pay the according social security contributions, i.e. health insurance. To the beneficiary it is entirely irrelevant which funding regime the employer applies (reserve accrual method or full funding via life insurance contracts).

For direct life insurance contracts, insurance pension funds and pension funds the tax and social security contribution rules are mostly identical. During the accrual period the employer can make contributions of up to 4% of the social security ceiling (i.e. in 2015 the maximum amount is 4% of € 72,600 or € 2,904 per annum). This amount remains tax-free and also free of social security contributions. A further € 1,800 of contributions can be made and remain tax but not social security contribution free. All later benefits are fully taxed and also require health insurance contributions.

Set of general rules for all funding vehicles

There is a general vesting period of 5 years regardless of funding method. Also, there are very strict general rules for pension settlements that apply to all funding vehicles. Furthermore there is a general rule that foresees the indexation of ongoing pension.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

As mentioned above, only the insurance-related funding vehicles (direct life insurance, insurance support fund and support fund) fall under the supervision of the German Financial Supervisory authority (‘Bundesanstalt für Finanzdienstleistungsaufsicht - BaFin’). In particular, the direct pension promise does not require any funding or external oversight whatsoever. Still, they are tied to multiple legal restrictions that are subject to comprehensive legal control by the labour courts. For example this includes multiple general rules such as the Anti Discrimination Act.

The absence of an independent board of trustees as is common in the Anglo-Saxon world of corporate pensions can best be understood when knowing that, in Germany, the employer up until now is always fully liable for the pension commitments, totally irrespective of the funding vehicle used. Therefore, the legal and economic relevance and hence the governance hot spot of any corporate pension plan in Germany ultimately lies within the employment relationship and not the fund structure and its respective governance.

QUESTION 3

How are the plans governed?

In German corporate pensions, the focus is not primarily on the funding vehicle but more on the entitlements that, in turn, are tied to the employment relationship. Therefore, governance and control focuses on the applicable labour rules. And here one finds a dense net of rules that must be adhered to. In a nutshell, the employer basically can make the decision on whether or not to launch any benefit arrangement and can determine the type of funding vehicle. Also, upon launch of the plan the employer can determine the financial volume of the benefit package unilaterally. But beyond that all further decisions fall under the employee participation through unions and/or work councils, respectively. That encompasses the distribution of the funds available amongst the various groups of employees and all further plan details, too.

QUESTION 4

Is there a compensation fund for pension benefits?

Germany was one of the first countries to implement an insolvency protection fund for corporate pensions in 1975 ('Pensions-Sicherungsverein a.G. - PSVaG). It secures all ongoing pensions as well as entitlements that have reached the statutory vesting maturity of 5 years. Pensions and future entitlements are secured on a nominal basis without inflation indexation. The funding of this insolvency protection fund is simple: Each year the cash value of all secured pensions that would drop out due to employers' insolvencies is dispersed across the community of employers that entertain corporate pension plans.

The only exception of corporate pensions in Germany that are not included in the statutory insolvency protection fund are the insurance pension funds mentioned above that, being fully fledged insurance companies (with few exceptions), receive coverage through the separate insolvency protection fund established for life insurance companies.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

Ultimately, each individual with either an ongoing pension or with vested entitlements can claim insolvency protection from the insolvency protection fund. Naturally, in reality the PSVaG steps in immediately in the case of insolvency of an employer and spares courts and individuals having to sue for the insolvency protection of their pensions or future entitlements. Yet, any beneficiary has the right to sue the insolvency protection fund for his pension.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

The insolvency protection fund covers the nominal value of ongoing pensions and of vested entitlements regardless of their funding status. A 'pension funding deficit' is therefore entirely irrelevant from the individual beneficiary's point of view.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

Again, given that ultimately the employer is always liable for the corporate pension and that in case of his insolvency the insolvency protection fund steps in, there are no binding and enforceable funding requirements for corporate pensions in Germany. In other words, regardless of the existence of any external funding vehicle the employer is always liable for the pension obligations. And in case the employer discontinued its contribution obligations to the insolvency protection fund due to insolvency, the community of employers that entertain corporate pension plans would come up for the ongoing pensions and the vested entitlements through their contributions to the insolvency protection fund. Hence, in the German corporate pension environment up until now there is no legal need to ensure appropriate funding of the external funding vehicle.

QUESTION 8

Are there any cross-border features of your pension regime?

There are no general cross-border features that apply to German corporate pensions. Although, the federal government intends to implement the so-called EU mobility directive into local legislation, in the course of the year 2015 further reducing the corporate pension vesting period to three years.

QUESTION 9

Discuss the state of defined benefit plans in your country

Broadly speaking, defined benefit plans are diminishing throughout the country. The reason for this is of course the difficulty to predict - and to budget for - the financial burden of this type of pension plan. Nowadays, the unpredictability of the financial impact of any entrepreneurial measure is viewed as one of the biggest threats to a company whose primary objective usually is to persist. Any unforeseen cost impact is a threat to this prime target. Further, pension cost impacts can be substantial and thus can potentially be a threat to the company. In Germany, this trend is somewhat fuelled by labour court rulings that tend to observe very closely the needs of the individual who is seeking protection from them. In turn, the cost effects of such court rulings on the respective companies can be quite substantial.

As a consequence, employer sponsored corporate pension plans and particularly defined benefit plans are on the retreat. Most defined benefit plans are closed and have been replaced by plans that have a much stronger contribution-oriented component. And the government's proposal for a further corporate pension reform that was presented in late 2014 foresees a 100% defined contribution option that would relieve employers of any further obligation once they have made the contribution they had committed to. The year 2015 will show if this is to become a reality.

HONG KONG

Introduction

Historically, occupational retirement schemes in Hong Kong were voluntarily established by employers for the benefit of their employees. Prior to 15 October 1993, legislative involvement was limited to specifying a process by which the Commissioner of Inland Revenue (the CIR) approved retirement schemes in order for employees to receive tax-free benefits[1]. There was no legislation governing the operation of those retirement schemes and there was no statutory body in Hong Kong to regulate them.

In addition to these unregulated Hong Kong schemes, some large multinational corporations with operations in Hong Kong rolled out their overseas retirement schemes for employees working in Hong Kong. Such overseas retirement schemes could either be defined benefit schemes (DB schemes) or defined contribution schemes (DC schemes). Again, these schemes were not subject to registration or legislative oversight.

The commencement of the Occupational Retirement Schemes Ordinance (the ORSO)[2] on 15 October 1993 made dramatic changes to this retirement benefit landscape. The ORSO regulates both Hong Kong-domiciled schemes and offshore schemes[3] that provide retirement benefits to members employed in Hong Kong. It introduced a registration system and aims to ensure that all voluntary schemes are properly administered and funded.

An even more significant legislative change occurred in December 2000 when the Mandatory Provident Fund Schemes Ordinance (the MPFSO)[4] came into effect and introduced a mandatory retirement benefit regime in Hong Kong. Save for a number of limited exceptions described below, all employees aged between 18 and 64 must be enrolled in a mandatory provident fund scheme (an MPF scheme) under the MPFSO or be enrolled in a scheme that has been granted an exemption certificate.

All MPF schemes are DC schemes. MPF schemes are a less costly option for employers to offer their employees than a scheme under the ORSO. As a result of this and other factors such as transparency, DB schemes are not common in Hong Kong and, as of March 2015, there were only 519 DB schemes registered in Hong Kong under the ORSO.

A shortfall in a DB scheme's funding is therefore relatively rarely an issue in an insolvency of a Hong Kong company.

1 The criteria for approval were laid out in section 87A of the Inland Revenue Ordinance but the relevant provisions are now repealed.

2 Chapter 426, Laws of Hong Kong.

3 Offshore schemes are schemes whose domicile is outside Hong Kong and where the scheme or trust is governed by a foreign system of law.

4 Chapter 485, Laws of Hong Kong.

QUESTION 1

What is the legal framework for private pension plans in your country?

It is no longer permissible for a private employer to offer an occupational retirement scheme unless it is registered under the ORSO, the MPFSO or other applicable legislation[5] or granted an exemption from registration under the ORSO.

Exemptions from registration under the ORSO may be granted where the relevant scheme is an offshore scheme and supervised by an overseas authority performing a similar role to the Hong Kong regulator or where 10% or less of the members of the scheme (and in any event no more than 50) hold Hong Kong permanent identity cards.

In this chapter a reference to an ORSO scheme means a scheme required to be registered under the ORSO or in respect of which an exemption from registration has been granted. There are certain forms of scheme such as those set up by the government of a country or territory outside Hong Kong or its agency not operating for the purpose of gain that fall outside the scope of the ORSO registration requirements. In Hong Kong these are not considered private pension plans and therefore fall outside the scope of this chapter.

ORSO schemes

On 15 October 1993, the ORSO came into operation and is the governing legislation for the regulation of ORSO schemes. The ORSO did not compel employers to set up occupational retirement schemes nor did it specify any minimum level of benefits. The primary objective of the ORSO was (and remains) to regulate the retirement schemes industry through a registration system to ensure that all voluntarily established schemes are properly administered and funded, and to provide greater certainty that retirement scheme benefits promised to employees will be paid when they fall due.

Under the ORSO, all ORSO schemes, whether DB or DC schemes, must either be registered or granted an exemption certificate by the Registrar of Occupational Retirement Schemes. This role is currently performed by the Mandatory Provident Fund Schemes Authority (MPFA).

Following the implementation of a mandatory retirement benefit system in Hong Kong in December 2000, ORSO schemes are further regulated by the Mandatory Provident Fund Schemes (Exemption) Regulation (the Regulation) which sets out in detail the arrangements for the interface between ORSO schemes and MPF schemes. The key requirement is that an ORSO scheme must be registered as exempt under the MPFSO or the employer will still be obliged to provide employees with an MPF scheme in addition to the ORSO scheme.

MPF schemes

For completeness, we also consider below the legal framework applicable to MPF schemes notwithstanding that all MPF schemes are DC schemes. Unlike DC schemes in some jurisdictions, there are specific rights with respect to MPF schemes in an insolvency.

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[5] The other applicable legislation is relevant only to specific schemes such as the scheme available to civil servants.

The ORSO did not address the fundamental issue relating to the mandatory provision of basic retirement protection to all employees and self-employed persons. Therefore, following extensive political debate and consultation, the MPFSO was introduced. The MPF system fully started operation from 1 December 2000[6].

The MPFSO and its subsidiary legislation govern the overall administration of the MPF system and determine certain aspects of the MPF schemes[7]. Under the MPFSO, every MPF scheme is required to be registered with the MPFA[8]. Employers must enrol their employees aged between 18 and 64 into MPF schemes, save for a number of limited exemptions[9].

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

ORSO schemes

The MPFA is currently responsible for the registering and overseeing the operation of ORSO schemes[10].

Under the ORSO, the functions of the MPFA for the administration of ORSO schemes include:

(i) monitoring ORSO schemes through processing the annual returns, financial statements, compliance certificates and membership statements[11];

(ii) processing applications for ORSO registration and exemptions, applications in relation to MPF exemptions, applications regarding changes in ORSO schemes and periodic certification of registered DB schemes[12];

(iii) maintaining registers for ORSO schemes[13];

6 Details relating to the operations of the MPF system can be found on the website of the MPFA at www.mpfa.org.hk.

7 MPF schemes are further subject to the codes, guidelines and standards published by the MPFA and the Securities and Futures Commission (SFC) from time to time.

8 Section 21 and 21A of the MPFSO. The MPFSO regulates the following main types of MPF schemes, namely (i) employer-sponsored schemes; (ii) industry schemes; and (iii) master trust schemes.

9 The following categories of individuals are exempt from MPF requirements: (a) employees and self-employed persons who had attained the age of 64 when the MPFSO was implemented; (b) domestic employees; (c) self-employed hawkers; (d) people covered by statutory pension and provident fund schemes, such as civil servants and subsidized or grant school teachers; (e) members of occupational retirement schemes which are granted exemption certificates; (f) people from overseas who enter Hong Kong for employment for less than 13 months, or who are covered by overseas retirement schemes; and (g) employees of the European Union Office of the European Commission in Hong Kong.

10 Section 5 of the ORSO.

11 Section 30 of the ORSO.

12 Sections 3, 7, 31 and 33 of the ORSO.

13 Section 6(1) of the ORSO.

(iv) intervening when ORSO scheme members' interests are jeopardised or statutory requirements have been breached[14]; and

(v) providing for the constitution of an appeal board to consider appeals against the MPFA's decisions regarding applications for registration and exemption[15].

MPF schemes

The MPFA also has primary responsibility for overseeing the administration of MPF schemes. Under the mandatory retirement benefit regime, all MPF schemes must be registered with the MPFA[16]. MPF schemes must be constituted under a Hong Kong trust with "approved trustees[17]" and provide defined contribution benefits.

The MPFA is entrusted to carry out a supervising and monitoring role. For instance, the MPFA is empowered to carry out proactive routine on-site inspections to monitor the performance and compliance of the requirements under the MPFSO[18].

Further, the MPFA is empowered to initiate prosecution proceedings in case of serious offences for failure to comply with the statutory requirements and may impose financial penalties on less serious offences in order to deter non-compliance and expedite rectification[19].

QUESTION 3

How are the plans governed?

ORSO schemes

ORSO schemes are privately managed and run by the employers. The operation of an ORSO scheme is primarily governed by the ORSO scheme documentation (e.g. trust deeds and plan rules) which generally includes matters such as coverage of eligible employees, vesting of the scheme's benefits, retirement age, amount of contributions, responsibility for administration charges and withdrawal rules, subject to the provisions as set out in the ORSO and related subsidiary legislation.

An ORSO scheme must be established as a trust or insurance arrangement unless it is an offshore scheme.

14 Section 42 of the ORSO.
15 Sections 61 and 62 of the ORSO.
16 Section 21 and 21A of the MPFSO.
17 The trustee of an MPF scheme may be (i) a local corporate trustee; (ii) an offshore corporate trustee; or (iii) an individual trustee (i.e. a natural person).
18 Section 30A of the MPFSO.
19 Section 45B of the MPFSO.

Hong Kong permits two options to allow an individual company to mitigate the burden of providing a retirement benefit scheme for its employees. The first is to allow companies within a "grouping of companies[20]" to have a group scheme in respect of which one member of group will be the representative employer and, broadly speaking, will be responsible for fulfilling the applicable regulatory requirements[21].

The second is through the use of pooling agreements. In short, pooling agreements are retirement products provided by professional third-party providers, who are subject to regulatory oversight of the Securities and Futures Commission[22]. A simpler registration and reporting process, with less documentation, applies in the case of schemes that are participating in a pooling agreement.

The ORSO imposes certain regulatory requirements upon employers in the operation of registered ORSO schemes. Below are some key regulatory requirements under the ORSO:

(i) Keeping proper accounts and records

The administrator of an ORSO scheme must keep proper accounts and records of schemes with regard to all assets, liabilities and financial transactions of the scheme and cause financial statements to be prepared after each of the scheme's financial years[23]. The financial statements must be submitted to an auditor for audit purpose except where[24]:

- the ORSO scheme participates in a pooling arrangement;
- the assets of the ORSO scheme are sufficient to meet its aggregate vested liabilities; and
- a majority of over 50% of the members of the ORSO scheme passes a resolution that no audit be conducted.

The employer must allow the auditor to have access to books and records and give to the auditor such information and explanation as required by the auditor as soon as reasonably practicable after a written request is made of it by the auditor[25].

(ii) Asset requirement

Except in cases where an ORSO scheme is an insurance arrangement, the assets of an ORSO scheme are to be kept separate and distinct from the assets of the employer or the scheme administrator and must not form part of the assets of the employer[26]. A scheme's assets may only be used for the purposes of the

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20 Defined as "companies that are associated companies or are within a group of companies and includes associated companies of a member of a group of companies".

21 Section 67 of the ORSO.

22 For further detail on the requirements for a scheme to be a "pooling agreement" refer to section 2(4) of the ORSO.

23 Section 20(1) of the ORSO.

24 Section 20(5) of the ORSO.

25 Section 20(7) of the ORSO.

26 Section 21(1) of the ORSO.

scheme[27]. The scheme's assets may only be encumbered by the trust governing the scheme, a charge or pledge created for the purpose of securing loans necessary to meet the liabilities of the scheme, and an option to acquire any interest in the assets of the scheme granted in the normal course of business[28].

A similar position is reached where a registered ORSO scheme is the subject of or regulated by an insurance arrangement because legislation provides that the assets or estate of the employer available for distribution in the event of the bankruptcy or winding up of that employer does not include so much of the assets of that scheme as equals the aggregate past service liability of the members of that scheme[29].

Where a registered scheme is a participating scheme of a pooling arrangement, assets of the scheme can be held together with the assets of other schemes vested in the administrator in his capacity as administrator of the pooling agreement[30].

(iii) Funding requirement

Employers must contribute in accordance with the terms of any scheme, and must ensure the scheme's assets are sufficient to meet the aggregate vested liabilities payable to scheme members[31]. In the case of DB schemes, the employer must implement actuaries' recommendations regarding funding and actuarial reviews[32].

(iv) Trusteeship requirement

Schemes governed by trusts must employ at least one independent trustee who is not the employer or an employee or associate of the employer, as defined in the ORSO, unless that associate is a registered trust company[33].

(v) Investment restrictions

No loans may be made to the employer or his associates out of the scheme's assets. Not more than 10% of the scheme's assets may consist of restricted investments[34]. For the purpose of the ORSO, "restricted investment" means (i) any security of, or issued by, the employer of a registered ORSO scheme or an associate of such employer except security issued by an associate of such employer in the form of an option which if exercised will constitute investment in the share capital of a body corporate other than the employer or an associate of such employer; or (ii) any security in the form of an option which if exercised will constitute investment in the share capital of the relevant employer of a registered ORSO scheme or an associate of such employer[35].

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27 Section 21(1)(c) of the ORSO.
28 Section 21(1)(b) of the ORSO.
29 Section 21(4) of the ORSO.
30 Section 21(4A) of the ORSO.
31 Sections 24(2) of the ORSO.
32 Section 24(1) of the ORSO.
33 Section 25 of the ORSO.
34 Section 27(2) of the ORSO.
35 Section 27(1) of the ORSO.

(vi) Actuarial reviews and reporting requirements

On an annual basis, the employer of the ORSO scheme must submit the following to the MPFA: an annual return in the prescribed form, the auditor's reports, the audited financial statements and prescribed fees[36].

DC schemes and DB schemes each have specific compliance requirements which have to be stated in the report to the MPFA. For example, if the ORSO scheme is a DB scheme, actuarial reviews must be undertaken by an actuary once every three years to ascertain the financial position of the scheme. These actuarial reports must be submitted to the MPFA. If the scheme is found to be insolvent the actuarial reports must be prepared on an annual basis.

In the case of an ORSO-exempt scheme, the employer does not have to provide the MPFA with the same documents as those required to be submitted by employers of ORSO registered schemes. However, the employer of an ORSO-exempted scheme must pay prescribed fees and provide annual documentation to the MPFA to prove that they continue to satisfy the requirements to be exempted from registration[37].

The employer must also submit forms to the MPFA when it terminates the ORSO scheme to notify the MPFA of the effective date of termination and showing that all benefits under the ORSO registered scheme have been paid to members or transferred to another scheme[38].

(vii) Information disclosure

The ORSO requires the disclosure of retirement scheme information to scheme members or to their consultative committee if one has been established[39]. Scheme members may obtain such information upon request, must be informed of any scheme amendments, and receive an annual statement listing benefit entitlements. Within two months of scheme registration or within two months of any new employee joining the scheme, an employer must fully disclose the criteria and conditions of membership, and explain how contributions and benefits are calculated[40].

Upon written request of a member who leaves the company, employers must provide particulars of that member's benefit entitlement within three months[41].

MPF schemes

Under MPFSO, all MPF schemes shall be properly constituted under trust which is governed by Hong Kong law. The governing rules contained in the trust instrument of the scheme must comply with all the provisions of the MPFSO.

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36 Section 30 of the ORSO.
37 Section 10 of the ORSO.
38 Section 29 of the ORSO.
39 Section 35 of the ORSO.
40 Section 35(10) of the ORSO.
41 Section 35(6) of the ORSO.

QUESTION 4

Is there a compensation fund for pension benefits?

There is no compensation fund for DB schemes.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

ORSO schemes

A registered ORSO scheme must be established through use of a trust or an insurance arrangement unless it is an offshore scheme.

It is a requirement that the assets of a registered ORSO scheme other than an offshore scheme[42] must be kept separate and distinct from and must not form part of the assets of the relevant employer or administrator of the scheme. So, the assets of the scheme ought to be unaffected by an insolvency of the employer / sponsor and the employees will claim against the scheme in accordance with the applicable scheme documentation.

If there are deficits in contributions, the deficits will be paid in a special priority (see below for further details). A claim of this nature against the employer should be brought by the administrator of the scheme or, if the scheme is being wound up, its liquidator.

If an employee is not able to recover a deficit to which he or she is properly entitled, the employee may lodge a complaint with the MPFA to seek further assistance.

MPF schemes

If the employer has become insolvent, the MPFA may collect relevant information from the employees and file claims with the insolvency officers of the Official Receiver's Office or liquidator in accordance with the insolvency proceedings, in the hope of recovering the deficits on the employees' behalf. Upon receiving the sum from the liquidator, the MPFA will pay the amount to the MPF trustee for allocation to the relevant employees' MPF accounts. The deficits will be paid in priority to general unsecured claims (see below for further details).

If the company is wound up, the mandatory contributions paid to MPF schemes will be fully and immediately vested as accrued benefits in the scheme members and kept by the custodian, and will not be affected by the company's winding-up.

[42] Where the relevant ORSO scheme is an offshore scheme then registration is possible even without segregation of assets if the MPFA is satisfied that such segregation would not be possible or reasonably practicable.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

When an employer is being wound up or is bankrupt, the following are preferential payments:

(a) any amount of unpaid contribution to the ORSO scheme[43]; or

(b) any amount deemed to be unpaid contribution calculated in accordance with the rules made by the MPFA[44]; or

(c) any amount of salary deducted by an employer from its employees' salaries for the purpose of making employees' contributions to ORSO schemes or MPF schemes which have not been paid into the scheme[45]; or

(d) any amount of unpaid contribution under the MPF schemes[46]; or

(e) any amount of unpaid contribution calculated in accordance with the MPF schemes[47].

If the claim amount under paragraphs (a) and (b) or (as the case may be) (d) and (e) above exceeds HK$50,000 in respect of an employee, 50% of such part of the amount that exceeds HK$50,000 will not be paid as a preferential debt, but will be a general unsecured debt[48].

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

There is no legislation in which other parties or entities or directors who have complied with their duties would be liable for the pension deficits when the employer is insolvent. If there is a guarantee as regards the ORSO or MPF contributions, remedies may be available against the guarantors.

43 Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) section 265(cf) and Bankruptcy Ordinance (Cap. 6) section 38(cf).

44 Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) section 265(cf) and Bankruptcy Ordinance (Cap. 6) section 38(cf). These provisions are of limited protection to creditors as it appears that no relevant rules have yet been made by the MPFA pursuant to section 73(1)(n) of the ORSO.

45 Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) sections 265(cg) and 265(ci) and Bankruptcy Ordinance (Cap. 6) sections 38(cg) and (ci).

46 Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) section 265(ch) and Bankruptcy Ordinance (Cap. 6) section 38(ch).

47 Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) section 265(ch) and Bankruptcy Ordinance (Cap. 6) section 38(ch).

48 Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) section 265(cf) to (ci).

QUESTION 8

Are there any cross-border features of your pension regime?

Both the ORSO and the MPFSO do not have extra-territorial jurisdiction.

An offshore scheme may either register under the ORSO or seek exemption. In either case the ORSO scheme operating in Hong Kong will need to comply with the obligations described above.

QUESTION 9

Discuss the state of defined benefit plans in your country

In Hong Kong, there is a gradual decline in the number of DB schemes operated in Hong Kong, and DB schemes are increasingly being replaced by DC schemes[49].

In the past, ORSO schemes were implemented by employers as a tool to help retain talents through offering some form of benefit in retirement for long-serving employees. Voluntary schemes were once attractive because both the employer and the employee would receive preferential tax treatments through making contributions. However, since the implementation of the ORSO, the regulatory requirements under ORSO have made it more cumbersome and expensive for employers to offer such schemes.

Further, and more importantly, given the nature of a DB scheme, an employer's contribution rates are not defined but are recommended by an actuary from time to time after performing actuarial valuations. This creates uncertainty for the employer and makes it difficult for employers to budget for future contribution obligations. During economic downturn, when obligations under a DB scheme surpass its current value, an employer is required to make up the shortfall of contributions.

Following the onset of the Asian financial crisis, many employers became more cost conscious and opted for retirement plans which result in greater certainty in terms of investment risks. This coincided with the time when the MPF regime was about to be implemented. It is observed that, since 1999, there is a trend for employers to switch to setting up DC schemes, or to opt for the simpler MPF schemes which could further reduce the administrative and financial burden on the employer.

49 According to statistics published by the MPFA, as at March 2015, the percentage of the population that are enrolled in retirement schemes are as follows:

- 73% of the employed population joined MPF schemes (which are by nature defined contribution schemes);
- 13% joined other retirement schemes, which includes statutory pension schemes and ORSO schemes;
- 12% of the employed population are not required to join any local retirement schemes; and
- 3% of the employed population should have joined but have not yet joined any MPF schemes.

The statistics also reveal that 89% of ORSO schemes are defined contribution schemes and only 11% are defined benefit schemes.

The preference to switch from DB schemes to DC schemes is not limited to employers. To employees, DB schemes lack transparency as employers are not required to disclose the fund's holdings or allocations. Hence, when employees are being offered an option to choose between an ORSO scheme and a MPF scheme, employees tend to choose MPF schemes as they have autonomy over the choice of funds.

INDONESIA

QUESTION 1

What is the legal framework for private pension plans in your country?

There is no mandatory requirement under Indonesian law for private sector employers to put pension plans in place for their employees. The only mandatory pension or quasi-pension plans under Indonesian law relate to public sector employees or severance benefits applicable to both private and public sector employees, the scope of which fall outside this chapter.

The legal framework for private pension plans in Indonesia is regulated under, inter alia, Indonesia's Pension Fund Law No. 11 of 1992 ("Pension Fund Law") which, broadly speaking, pertains to two main types of private pension funds, namely:

a. Employer's Pension Fund ("EPF"): A pension plan, being either a defined benefit or defined contribution plan, that is set up by an employer for the benefit of its employees; and

b. Financial Institution Pension Fund ("FIPF"): A defined contribution pension plan formed by a bank or life insurance company for the benefit of its employees, separate and distinct from any EPF.

The Pension Fund Law broadly regulates the following key areas:

a. The legal status of a pension fund as a body corporate;

b. The management of the pension fund;

c. Contributions to the pension fund;

d. Employees' rights under the pension fund;

e. Management of the assets of the pension fund;

f. Settlement of the pension fund;

g. Establishment and supervision of the pension fund; and

h. Criminal sanctions for breaches of the Pension Fund Law.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

The Pension Fund Law provides that regulation and overall supervision of any pension fund vests in the Indonesian Minister of Finance ("Minister"), with further requirements for auditing and reporting by certified public accountants and actuaries.

However, pursuant to the Article 55 paragraph (1) of Indonesian Law No. 21 of 2011, all functions, duties and responsibilities of the Minister under the Pension Fund Law have been transferred from the Minister to the Otoritas Jasa Keuangan (OJK) (Indonesian Financial Services Authority).

Consequently, the functions, duties and responsibilities of the Minister as provided for under the following Articles of the Pension Fund Law are under the purview of OJK:

a. Any pension fund's commencement of its activities as such and its recognition as a body corporate is only effective upon legalization by OJK. (Article 7)

b. OJK will determine the conditions for any candidate to be appointed to a pension fund's management board. (Article 10)

c. Any pension fund which is unable to meet its payment obligations to its beneficiaries for 3 successive months is obliged to notify OJK. (Article 16)

d. The management of the pension fund's assets must be executed in accordance with, inter alia, stipulations on investments issued by OJK. (Article 30)

e. A pension fund may only be liquidated and a liquidator appointed subject to a decision of OJK. (Part 6)

f. The founding and supervision of any pension fund, covering all financial and technical aspects of the pension fund's management of its assets, are under the purview of OJK. (Article 50)

g. Various financial and technical reports of every pension fund must be submitted to OJK. (Article 52)

QUESTION 3

How are the plans governed?

The Pension Fund Law provides for a two-tiered governance system, with the first tier being a management board responsible for the implementation of the pension fund regulations, the overall management of the pension fund and legal measures taken for and on behalf of the pension fund, and the second tier being a supervisory board (the "Supervisory Board") responsible for, inter alia, the supervision of the activities of the management board. Article 12 of the Pension Fund Law provides that the members of the supervisory board shall be appointed by the employer / sponsor, with membership thereof being equal numbers from representatives of the employer / sponsor and those of the beneficiaries / employees, with the qualification that supervisory board members may not also double as management board members.

As mentioned in the response to query 2 above, OJK will determine the conditions for any candidate to be appointed to a pension fund's management board but the actual task of appointing the management board is that of the employer / sponsor. In addition, Article 10 of the Pension Fund Law provides, inter alia, that the task, duty and responsibility of the management board are to be determined by Indonesian government regulations.

Insofar as the actual framework for the governance of private pension plans is concerned, Article 30 of the Pension Fund Law provides that management of the pension fund must be executed by the management board in accordance with investment directives set by the employer and stipulations concerning investments established by OJK. Various other Articles govern certain rights, obligations and restrictions on the manner in which the pension fund is to be managed, for example prohibitions on borrowing or securitization of assets by the pension fund.

In addition to the various provisions of the Pension Fund Law summarized above, Government Regulation No. 76 of 1992 (GR 76) further elaborates on various requirements concerning the governance of private pension funds.

Article 15 of GR 76 provides that the management board's term in office is for a renewable period of five (5) years, whilst Articles 17 and 18 provide that the responsibilities of the management board include having to:

a. manage the pension fund in the interests of the beneficiaries / employees;

b. maintain books, records and documents required in order to manage the pension fund;

c. act diligently in executing its responsibilities in managing the pension fund;

d. keep personal information on every beneficiary / employee under the pension fund; and

e. submit financial statements audited by a public accountant, and technical reports prepared by the management board or by the management board together with an actuary to the OJK.

Article 21 of GR 76 provides that members of the management board are jointly and severally personally liable for any losses due to any actions of the management board which violate or are in dereliction of duties and / or obligations as set out in the Pension Fund Law or any other applicable regulations.

Insofar as the responsibilities of the Supervisory Board are concerned, Article 25 of GR 76 provides that the Supervisory Board's responsibilities include having to:

a. supervise the management board's management of the pension fund;

b. submit a written annual report to the sponsor / employer, with copies made available to the beneficiaries / employees;

c. appoint a public accountant to audit the financial statements of the pension fund;

d. appoint an actuary to prepare reports in respect of defined benefit plans;

e. together with sponsor / employer, establish investment criteria in respect of defined contribution plans.

QUESTION 4

Is there a compensation fund for pension benefits?

There is no express provision in the Pension Fund Law pertaining to a compensation fund for pension benefits

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QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

Part Six of the Pension Fund Law sets out the guidelines which are applicable in the event of the insolvency of the pension fund by reason of the insolvency of the employer / sponsor.

Specifically, the Pension Fund Law provides for the Minister (and currently, OJK) to have the authority to appoint a liquidator in instances where the Minister is of the view that the pension fund is unable to meet its obligations to the beneficiaries / employees or where contributions to the pension fund have stopped[1].

[1] Articles 33 and 34 Pension Fund Law.

Once appointed by OJK, the liquidator is responsible for taking over management of the pension fund, settling a list of assets and liabilities as well as determining the beneficiaries / employees and their entitlement under the pension plan as of the time of appointment.[2]

In addition to the Pension Fund Law, OJK Regulation No. 9/2014 also contains various regulations pertaining to the insolvency of the employer / sponsor, such as a requirement for the rights of beneficiaries / employees under a Defined Benefit Plan to be determined based on actuarial reports[3], and in the case of Defined Contribution Plans, to be determined based on financial reports audited by public accountants[4].

Article 36 of the Pension Fund Law expressly provides that the employer / sponsor remains liable for all outstanding contributions until such time as the pension fund is liquidated.

The entire liquidation process will be supervised by the Supervisory Board, which is obliged to report to OJK[5].

In the event of the liquidation of the pension fund, the affected beneficiaries / employees are required to file / register their claim with the appointed liquidation team for adjudication.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

Article 37 of the Pension Fund Law provides that in the distribution of the pension fund's assets by the liquidator, the right of the beneficiaries / employees take priority over the claims by all other creditors, secured or unsecured, except for national tax liabilities, if any.

Furthermore, pursuant to the Article 95 paragraph (4) of Indonesian Law No. 13 of 2003 concerning Manpower, in the event of the bankruptcy / insolvency of a company, payment of that company's employees' wages shall take priority over the payment of other debts.

It should be noted that the Pension Fund Law is silent as to whether the costs of the liquidation, including liquidators' fees and expenses, would take priority over the claims of the beneficiaries / employees.

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2 Article 35(1) Pension Fund Law.
3 Article 17 Paragraph 2 – OJK Regulation.
4 Article 17 Paragraph 3 and Article 11 Paragraph 1 (a).
5 Articles 21 and 22 OJK Regulation.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

The availability of any such remedies against third parties would very much depend on whether there is a valid cause of action under Indonesian law (e.g. in fraud or negligence) against such third party.

The Pension Fund Law itself is silent on this particular issue.

QUESTION 8

Are there any cross-border features of pension regime in Indonesia?

No. The private pension regime in Indonesia is still very much nascent, with existing regulations not addressing any specific cross-border issues.

QUESTION 9

Discuss the state of defined benefit plans in Indonesia

There is, at present, poor adoption of private pension plans, be they defined benefit or defined contribution plans, by private sector employers in Indonesia.

It may be surmised that a number of factors contribute to this. Firstly, as previously mentioned, private pension plans are non-mandatory under Indonesian law at present. Secondly, Indonesian Labour Law No. 13 of 2003 (“Labour Law”) mandates that all employers are required to provide retirement / severance / termination benefits to employees based on a specific method of calculation set out therein. Employers therefore take the position that no further pension plan benefits are required in addition to what the Labour Law already prescribes. Thirdly, the existing laws and regulations governing private pension plans are convoluted, presenting what many private sector employers deem as being an unnecessary burden for them to undertake.

That being said, it should be noted that the Pension Fund Law was enacted in 1992 and has not been amended to take into consideration significant changes in Indonesian demographics and economy since that time. However, the Indonesian government is in the process of promulgating various new Government Regulations regarding pension benefits, the enactment of which is scheduled for July 2015. Whilst details on these new Government Regulations have not been made clear, the indication from the relevant Indonesian authorities is that these new Government Regulations are intended to apply to both public as well as private sector employees. In light of the foregoing, it is anticipated that there will be significant changes in the law which would impact upon private pension plans, be they defined benefit or defined contribution plans, and it is hoped that the revised regime will incentivize private sector employers to institute pension plans for their employees.

ITALY

QUESTION 1

What is the legal framework for private pension plans in your country?

Italian public social security system provides for old age pension benefits. The system is managed by the Italian Social Security Contribution Authority ("Istituto Nazionale della Previdenza Sociale", hereinafter referred to as "INPS").

In Italy, the social security system is based on two different pillars: the compulsory one and the integrative voluntary one.

i. The compulsory social security contribution system, which concerns the social security contribution due to INPS is divided between the amount to be paid by the employer and that to be paid by the employee (which is withheld from the employees' gross monthly salary directly from the employer)[1], and it is aimed to grant employees with a pension revenue proportional to the social security contribution amounts paid during the employees' working life[2];

ii. The voluntary and integrative social security contribution, concerns the social security contribution to be paid to non-state pension funds (Fondi Pensione).

Under certain conditions and up to a limit (of €5,164.57), contributions made by either the employer or the employee into a non-state pension fund do not constitute taxable income for the employee since they are tax-deductible. Trattamento di fine Rapporto (TFR - the statutory severance indemnity) is excluded from this limit.

Starting from 2007, employees are also able to transfer their TFR[3], to non-state pension funds or to a special state pension fund managed by INPS. Moreover, should the employer be staffed with less than 50 employees, employees may decide to allow the TFR to remain in the company and it be managed by the employer as an internal financial resource, according to the Italian Civil Code.

Should the employees not make an active choice on the TFR allocation for pension purposes after a six-month period from hiring, the TFR will be automatically paid into a non-state pension fund according to the mechanism provided by national or local collective agreements applied to the employment relationship (in the absence of an applicable rule in such agreements, the TFR is automatically invested in the state pension fund managed by INPS)[4].

An employer that invests the accrued TFR in the INPS fund or a non-state pension fund enjoys a tax reduction ranging from 4% to 6%.

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1 The standard total social security contribution quota charged on employees is equal to approx. 10% of their gross salary, while the employer's social security contribution quota is equal to approx. 35% of employee's salary.

2 Following Law no. 214/11, Italian pension system is a purely "contributive" one, as defined benefit provisions have been suppressed also for employees approaching pension.

3 Employers have to pay the TFR to employees upon termination of employment for any reason. The amount of TFR to be paid varies depending on the employee's salary and length of service. Typically, it is equal to approximately one month's salary multiplied by the years of service with the same company.

4 Since 2015 – but for a limited period from March 2015 to June 2018 – employee may also opt to receive on a monthly basis their accrued quota of TFR.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

There are two main types of non-state pension funds[5], both based on the defined contribution method.

- Closed or contractual pension funds ("*Fondi Pensione Chiusi*") which are implemented either as company pension funds by a single company or as industry-wide pension funds set up in the national collective local agreements by the employers' association and the trade unions for a specific group of participants. Participation in this type of pension fund is restricted to those who are party to the agreement setting up the fund and for that reason they are referred to as 'closed' pension funds;

- Open pension funds ("*Fondi Pensione Aperti*") that are offered by authorised intermediaries, such as banks, insurance companies or investment management companies for a generic group of participants, i.e. the self-employed.

Non-state pension schemes may only be formed in addition to the state scheme and not in substitution for it, thus employees may not 'contract out' of the state scheme. All pension funds have to sign an agreement with an external investment manager that can only be an insurance company, a bank or a registered asset management company ("Società Gestione Risparmio" or "SGR").

Pension funds, whether open or closed, require the prior authorisation of the Ministry of Labour ("Ministero del Lavoro") before being set up and are then subject to supervision by a special monitoring authority ("Commissione di Vigilanza sui Fondi Pensione – COVIP").

When the employee achieves the requirements to obtain the payment of the state retirement pension, and provided they have been enrolled with the integrative pension fund for at least 5 years, they may opt for annuity or a lump-sum payment up to 50% of the overall accrued contributions[6].

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[5] In addition to closed and open pension funds, there are also the so-called "*Fondi Pensione Preesistenti*" or pre-existing pension funds operating before Decree 124/1993 applicable to "old" members only and the individual pension plans so-called "PIPs" based on traditional life insurance contracts offered to individuals by insurance companies.

[6] A lump-sum payment may be also obtained by the employee during his/her employment while contributing to the pension fund (i.e., before his/her retirement) under certain conditions and for specific reasons (e.g., health) established by law and/or by the pension fund's regulation.

QUESTION 3

How are the plans governed?

- *Fondi Pensione Chiusi* (closed plans) are independent legal entities. In fact there is a legal separation between the fund and the sponsoring employer(s). Such funds are not allowed to directly manage plan assets, since such activity shall be delegated by the governing board to professional managers (banks, insurance companies, investment firms and asset management companies).

  The governing board and board of auditors of such funds are composed of equal numbers of employer and employee representatives. The governing board is required to appoint a so-called "*Responsabile del Fondo*" in charge of verifying that the fund is managed according to the interests of members and beneficiaries and in compliance with legal and statutory provisions (conflicts of interest rules, investment rules, etc.).

- *Fondi Pensione Aperti* (open plans) do not have independent legal status; however, their assets are required to be separated with respect to those of the financial company managing them. Also in such funds a "*Responsabile del Fondo*" – meeting independent requirements set by law – must be appointed in order to carry out the above-referred verification tasks and a reporting activity to a supervisory board so-called "*Organismo di Vigilanza*" overseeing the activity of the fund and having a whistle-blowing role also with respect to the monitoring authority, *COVIP*.

QUESTION 4

Is there a compensation fund for pension benefits?

Ad hoc compensation funds have been established in order to protect employees in case of insolvency of the employer: (i) a fund aimed at granting the payment of the accrued TFR to employees ("*Fondo di Garanzia TFR*"), and (ii) a fund protecting the employees in case of non-payment or partial payment of contributions to integrative pension funds ("*Fondo di Garanzia per la Previdenza Complementare*"). Both funds are managed by INPS.

By means of the *Fondo di Garanzia TFR*, INPS directly pays the employees the TFR due but not paid by the employer on the basis of a request made by the employee (or his/her heirs and, according to recent case-law, other qualified creditors[7]) who are required to submit an *ad hoc* form.

The concerned fund is financed by the same employers that are required to pay a contribution to INPS (ranging from 0.20% to 0.40%, depending upon if referred to as an employee or executive relationship). Under certain conditions, the INPS fund grants also the payment of the last 3 months' salaries (not paid by the employer) to the employees involved.

[7] The TFR is usually offered as guarantee in case the employee obtained a loan from a bank or other authorized companies which may be interested to obtain the payment of TFR in case of employer's insolvency and/or other cases of non-payment of the same to integrative pension funds.

Provided that the employment relationship is terminated and the employee is enrolled with an integrative pension fund, the same employee or their heirs may claim (within specific terms varying upon the type of insolvency procedures started, if any) the *Fondo di Garanzia per la Previdenza Complementare* to intervene:

- in case of non-payment of contributions to the integrative pension fund from the employer subject to insolvency procedures (i.e., bankruptcy, composition with creditors, compulsory administrative liquidation and extraordinary administration). In this scenario, evidence should be given that a specific credit concerning the non-payment of contributions to the integrative pension fund has been assessed, and;

- in case of non-payment of contributions to the integrative pension fund from the employer to whom the above-mentioned insolvency procedures are not applicable (i.e., in the absence of the requirements set forth by article 1 of Royal Decree 267/1942, so-called "*Legge Fallimentare*"). In this scenario, the *Fondo di Garanzia per la Previdenza Complementare* provides for the payment of labour-related credits where there are insufficient assets to repay the debt to the integrative pension fund. In this scenario, the intervention of the *Fondo di Garanzia per la Previdenza Complementare* is conditioned to the assessment before the Court of the non-payment of contributions to the integrative pension fund.

The fund directly pays to the integrative pension fund the contributions due but not paid by the employer (including the quota withheld from employee's salary, if any, and TFR, if allocated to the pension fund) for the purposes of retirement age pension (i.e., "*pensione di vecchiaia*"), while disability pension or other additional treatments (e.g., "*pensione di anzianità, invalidità, inabilità"*, etc.) are not covered.

It is understood that in case of payment, INPS (in its capacity as manager and regulator of both compensation funds) is subrogated to the employee's claim in the insolvency procedures.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

The non-payment of contributions is usually governed by the integrative pension fund's internal regulation which typically provide for the payment of the amount due plus specified interest.

On the contrary, in case of insolvency of the employer, the employee is entitled – as a sole person holding the relevant right to contributions – to request the intervention of the *Fondo di Garanzia per la Previdenza Complementare*, should the above mentioned requirements be met.

According to an opinion of the *Commissione di Vigilanza*, in specific circumstances, in case of bankruptcy, the pension fund may act in order to ensure that the employee carries out the required actions in order to obtain the payment of the contributions due but not paid (i.e., file a proof of claim). Should the pension fund carry out certain activities to preserve the employee's right to contributions and so the debt towards the employer, it is advisable that an *ad hoc* proxy to be executed indicating *inter alia* the amount of the employee's debt.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

Employees' entitlements are strongly protected in case of insolvency of the employer.

In particular, the Italian Civil Code provides for special priority of labour-related entitlements on movable (article 2751-bis and article 2753) and immovable (article 2776) assets, including *inter alia* damages arising from the non-payment of contributions from the employer, contributions not paid to state and non-state pension fund covering disability, age and survivor's pension and TFR.

The preferred ranking for labour-related entitlements is as a general rule, applicable in any insolvency procedure.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

The employee's pension credits are protected in case of an employer's insolvency since Italian law established the rules of priority and the compensation fund, the so-called *Fondo di Garanzia per la Previdenza Complementare* described above.

In certain specific situations however, the Italian legislator provides for a joint-liability for salary and social security contributions between the companies involved in a transfer of a going concern or part thereof pursuant to article 2112 of the Italian Civil Code and / or in case of contract (contratto di appalto) pursuant to article 29 of Legislative Decree 276/2003. Due to such joint-liability (i) in case of transfer, the transferee (cessionario) may be interested in filing a proof of claim in case of insolvency of the transferor (cedente); as well as (ii) since the contractor (appaltatore) and client (committente) are jointly liable[8] for salary and social security contributions of the employees dedicated to the services rendered under the contract, the client may be interested in filing a proof of claim in case of insolvency of the contractor[9].

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8 For a period of two years following the termination of the contract.

9 A further hypothesis of joint-liability is envisaged in case of sub-contract.

However, it is disputable among Courts as to whether the transferee and / or the client may be entitled to have recourse to the Fondo di Garanzia TFR in the event they paid the TFR on behalf of the transferor and the contractor respectively.

Furthermore, under supply contracts (contratti di appalto) the principal is jointly liable with the contractor for any employee's pension entitlements. In other words, the employees of the contractor are protected by an additional remedy against the principal in the event of non-payment by the contractor of salary and social security contributions.

QUESTION 8

Are there any cross-border features of your pension regime?

Fondo di Garanzia per la Previdenza Complementare applies also in the case of an employer carrying out its activity at least in two Member States provided that the employees carried out their activities in the Italian territory. Therefore, the intervention of the fund may also be requested if the insolvency procedure has been commenced in a Member State other than Italy (in line with EU Directive 2002/74/Ce implemented by Legislative Decree 186/2005).

With reference to cross-border features, it is important to recall that Article 10 of the Council Regulation no. 1346/2000 on cross-border insolvency proceedings provides that *"The effects of insolvency proceedings on employment contracts and relationships shall be governed solely by the law of the Member State applicable to the contract of employment".* Such rule would apply only to the effects of the insolvency proceedings on contracts of employment, while other matters which may arise out of contracts of employment in the context of insolvency proceedings (such as the admission of claims and the priority of any claims) will be governed by the law of the State of the opening of proceedings.

QUESTION 9

Discuss the state of defined benefit plans in your country

In recent years the Italian legislature has tried to increase the use of integrative pension funds, but has not succeeded so far. In fact, due to the heavy mandatory contributions and limited tax deductions offered by the law in the current scenario, the recourse to integrative pension funds appears to be very limited. Considering the above, it is possible the Italian Government will try in the future to launch such new reforms but they are not yet under discussion as of today.

JAPAN

QUESTION 1

What is the legal framework for private pension plans in your country?

Overview of the Japanese pension system

The Japanese pension system consists of both public and private pension systems.

The public pension system in Japan is mainly composed of (i) the National Pension, which applies to every Japanese citizen aged between 20 and 60, regardless of occupation, income or other factors, (ii) the Employees' Pension Insurance, which applies to employees under 70 years of age in the private sector, and (iii) the Mutual Aid Pension, which applies to government employees. On the other hand, Japanese private pension systems have a variety of choices. People can select from a variety of plans to "top-up" the benefits of public pensions.

It is said that the Japanese pension system consists of three layers. The National Pension is the so-called "first layer" of the Japanese pension system, which ensures that every citizen of working-age has a basic pension in their old age. Both the Employees' Pension Insurance and the Mutual Aid Pension are regarded as "second layers" which enable participants to receive an earnings-related pension in addition to the basic pension based on the National Pension. Additionally, the private pension is seen as a "third layer" which enables participants to receive benefits that top-up public pensions.

Japanese private pension plans include both corporate-types and individual-types. Japanese private pension plans are also categorized as either defined benefit type or defined contribution type. Defined benefit type pension (the "DB" pension) means a pension plan where the amount of benefit is defined in advance according to the participation period, etc. A defined contribution type pension (the "DC" pension) means a pension plan where the amount of contribution is defined in advance and the amount of benefit is determined due to the total amount of contributions and its investment return.

As to corporate-type private pensions in Japan, there are Employees' Pension Funds, DB corporate pensions, DC corporate pensions, and other voluntary pension plans uniquely designed by an individual company without limitation of specific laws. As to individual-type private pensions in Japan, there are National Pension Funds, DB individual pensions, DC individual pensions, savings-type individual pensions and insurance-type individual pensions, etc.

In this chapter, we would like to cover corporate-type and defined benefit type pensions that are registered or otherwise recognized by the government. To be more precise, the content below will discuss the DB corporate pensions and Employees' Pension Funds as two main pension plans both of which have features of corporate-type and defined benefit type.

Overview of DB corporate pensions

DB corporate pensions are corporate-type pension plans governed under the Defined Benefit Corporate Pension Law. DB corporate pensions were recently introduced in 2002 but since then their uptake has been increasing rapidly.

There are two forms of DB corporate pension plans, "fund-type" and "rule-type". With regard to a fund-type DB pension, the pension assets are managed and invested by a fund, which is an entity independent from an employer that is established by the employer with the approval of the Minister of Health, Labor and Welfare (the "Minister"). The independent fund is managed in accordance with a pension rule mutually agreed between the employees and the management. The fund pays topping-up benefits over the old-age employees' pension as a public pension to employees of the employer.

On the other hand, under a rule-type pension plan, an employer executes an agreement with a trust company, a life insurance company and / or an investment advisor (collectively, the "Plan Administrator") in order to manage the pension plan and invest the pension assets segregated from the other assets of the employer in accordance with pension rules mutually agreed between the employees and the management. The Plan Administrator pays topping-up benefits over the old-age employees' pension as a public pension to employees of the employer on behalf of the employer and according to instructions by the employer.

Overview of Employees' Pension Funds

Employees' Pension Funds are corporate-type and defined benefit type pension plans governed under the former Employees' Pension Insurance Law. An Employees' Pension Fund is managed by a fund, which is a special corporation independent from an employer and established with the approval of the Minister. The fund may be established by an employer which employs more than 1,000 employees on an ongoing basis, or by more than two employers which hire more than a certain number of employees in total. The independent fund manages the pension plan in accordance with pension rules mutually agreed between the employees and the management. The fund pays benefits partly substituting the old-age employees' pension as a public pension and independent top-up benefits to the participants. Because the fund substitutes a portion of the public pension, it is said that Employees' Pension Funds are a hybrid of a public pension and a private pension.

Employees' Pension Funds started in 1966 and used to be a core corporate pension plan in Japan. However, because of the bubble economy collapse and the ensuing long recession in Japan, many funds classified as Employees' Pension Funds have struggled with substantial amounts of pension deficits including pension deficits for the portion substituting the public pension. On top of this, the global financial crisis since 2007 delivered a serious additional blow to these funds. Furthermore, a big scandal whereby an investment advisor (AIJ Investment Advisor Co., Ltd) defrauded its clients, including many funds which ran Employees' Pension Funds and lost a huge amount of pension assets entrusted by these clients, heavily deteriorated the financial conditions of Employees' Pension Funds. These circumstances pushed the government to conduct fundamental reforms of Employees' Pension Funds. Consequently, the Employees' Pension Insurance Law was amended to remove all articles providing for Employees' Pension Funds and the amendment came into force in April 2014. According to the amended law, it is forbidden to establish a new fund as an Employees' Pension Fund from the date of commencement. The amended law also encourages existing funds classified as Employees' Pension Funds to dissolve voluntarily or transfer to other corporate pension plans including DB corporate pensions or DC corporate pensions within 5 years from the date of the commencement. If an Employees' Pension Fund in a state of financial difficulties remains in distress after

5 years have passed from the date of commencement, the amended law allows the Minister to order the fund to dissolve through consultation between the Minister and an independent committee. As a result, the numbers of Employees' Pension Funds and their participants have been rapidly decreasing due to voluntary dissolutions or transfers to other corporate pension plans.

The tax regime for DB corporate pensions and Employees' Pension Funds

The tax regime for Japanese private pension plans differs with respect to the timing of contributions, accumulated funds, and the payment of benefits. It also differs with regard to who is defined as a taxable person.

(i) DB corporate pensions

First of all, in the case where an employer pays contributions for a DB corporate pension, the entire amount of contributions is classified as a deductible expense.

Secondly, the accumulated fund is subject to special corporate tax, however the calculation of the special corporate tax is suspended until the end of March, 2017. This special corporate tax has been introduced as a kind of overdue tax because taxation on accumulated funds has been postponed until the time of each employee's retirement.

Thirdly, when the benefit is paid, it is subject to income tax for each participant with the exception of the disability benefit and the survivor benefit (the survivor benefit is subject to inheritance tax). With regard to the annual pension, there is a certain range of income deduction for the participant. On the other hand, benefits of a lump-sum pension are subject to income tax as retirement benefits (participants can utilize income deduction for retirement benefits).

(ii) Employees' Pension Funds

The tax regime of Employees' Pension Funds is quite similar to that for DB corporate pensions.

That is to say, the contributions paid by an employer to a fund are allowed as deductible expenses in full. The accumulated fund is subject to special corporate tax, provided that the calculation of the special corporate tax is pending until the end of March 2017. The benefit is subject to income tax with the exception of the disability benefit and the survivor benefit (these are non-taxable). Regarding the annual pension, an income deduction applied to the public pension is also available for participants who receive an annual pension under an Employees' Pension Fund. The benefits of a lump-sum pension are subject to income tax as retirement benefits (participants can utilize income deduction for retirement benefits).

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

DB corporate pensions and Employees' Pension Funds are regulated by the Japanese government, in particular and the Ministry of Health, Labor and Welfare (the "Ministry"). The regulations applied to both DB corporate pensions and Employees' Pension Funds are similar.

First of all, when an employer establishes a fund-type DB corporate pension plan or an Employees' Pension Fund (a fund-type DB corporate pension plan and an Employees' Pension Fund are defined collectively as "Fund-type Pensions"), the fund must be approved by the Minister. When an employer establishes a rule-type DB corporate pension plan, the rules mutually agreed between the employees and the management must be approved by the Minister. It is also necessary that the employer (for a rule-type DB corporate pension) or the fund (for Fund-type Pensions) obtain the approval of the Minister in order to close the DB pension or dissolve the fund.

Secondly, when the employer (for a rule-type DB corporate pension) or the fund (for Fund-type Pensions) modifies its rules, it must obtain the approval of the Minister except for minor modifications. In particular, if the employer or the fund tries to modify the rules for the purpose of reducing the pension rights of employees or retirees which have accrued (or will accrue with certainty), it must fulfill special requirements to obtain the approval of the Minister. This modification for reducing the accrued pension rights often becomes a major issue in restructuring of an employer in financial distress or insolvency. The special requirements consist of substantive and procedural requirements. The substantive requirement means that there must be reasons for it being inevitable that the employer or the fund reduce the accrued pension rights because it is expected that the employer will not be able to pay the contributions if the employer or the fund does not succeed in cutting the pension rights due to either its financial deterioration or significant increase of the amount of contributions. As a procedural requirement, the employer or the fund must obtain consent from no less than two-thirds of all employees and retirees who hold accrued pension rights. In addition, the employer or the fund must seek appropriate alternatives including making a certain amount of lump-sum payments to these employees and retirees. These requirements must be satisfied even if the employer enters into court procedures for insolvency in Japan. For example, in the case of Japan Airline Co., Ltd. ("JAL"), which entered into corporate reorganization proceedings in Japan in 2010, JAL Pension Fund, which is the fund-type DB corporate pension established by JAL, succeeded in modifying the rule for the purpose of reducing the accrued pension rights of the employees and retirees by satisfying the above mentioned substantive and procedural requirements.

Thirdly, regarding mandatory reporting for DB corporate pensions, the employer or the fund must submit its annual report about business conditions and financial statements to the Minister within four months from its fiscal year end. On the other hand, an Employees' Pension Fund must submit its annual budget in advance of the beginning of every fiscal year and its annual report about business conditions and financial statements within six months from its fiscal year end to the Minister.

Moreover, the Minister has legal authority to monitor and investigate these pension plans, to take charge of their administrative actions including ordering modification of the rules, dismissal of the management of a fund, revocation of approval for the establishment of the rules of a fund, and dissolution of a fund, etc.

QUESTION 3

How are the plans governed?

Fund-type DB corporation pensions and Employees' Pension Funds are administered as independent funds, which are each a separate entity from the employer. Therefore, each fund is responsible for running the plan, rather than the employer. The fund entrusts management of the pension plan and investment of the pension assets to the Plan Administrator such as a trust company, a life insurance company and / or an investment advisor in accordance with an agreement between them.

With regard to Fund-type Pensions, the fund must establish delegates which decide substantive matters relating to the fund, such as modification of the rules and approval of the budget, business plan and financial statements every fiscal year. There must be an even number of delegates, and half of them are selected by the employer, and the other half are chosen by plan participants (employees / retirees). Furthermore, the fund must establish directors and inspectors of the fund. One half of the directors are selected by delegates appointed by the employer, and the other half of directors are selected by delegates appointed by plan participants. Directors select the managing director who represents the fund. Regarding the inspectors, delegates appointed by the employer and delegates appointed by plan participants each choose one inspector respectively. The inspector owes a duty to audit the business of the fund, and must not be a director and an officer of the fund concurrently. In conclusion, in these pension plans, participants including employees and retirees engage in the governance of the fund to some extent directly or indirectly through the appointment of delegates, directors and inspectors. However, there is no engagement of an independent body other than inspectors in the governance structures of these plans.

On the other hand, rule-type DB corporate pension funds are governed by an employer so that the employer is still responsible for running the plan. However, the actual management of the pension plan and investment of the pension assets are entrusted to the Plan Administrator such as a trust company, a life insurance company and / or an investment advisor in accordance with the agreement between them. There is no specialized governance system for rule-type DB corporate pensions like the one for fund-type DB corporate pensions and Employees' Pension Funds in the law.

QUESTION 4

Is there a compensation fund for pension benefits?

In Japan, there is no compensation fund for pension benefits. Therefore, in order to protect vested benefits of participants, there are regulations to avoid pension deficits in each pension plan. Briefly, regarding DB corporate pensions and Employees' Pension Funds, there are three types of regulations, (i) obligation of the employer to compensate pension deficits, (ii) duty of loyalty of the employer, directors of the fund, and the Plan Administrator, and (iii) a disclosure system for plan participants. The regulations to avoid pension deficits for Employees' Pension Funds are similar to those for fund-type DB corporate pensions.

Firstly, the employer must pay contributions calculated in accordance with the rule to the Plan Administrator (for a rule-type DB corporate pension) or the fund (for Fund-type Pensions) one or more times at regular intervals each year. The amount of contributions is recalculated every five years for the purpose of adjustment due to the financial condition of the employer to address expanding pension deficits. In addition, the amount of accumulated funds must exceed the minimum amount stipulated in the respective governing statute. Every fiscal year end, the employer or the fund examines whether the accumulated amount in the fund exceeds the minimum amount. If the accumulated funds fall below the minimum amount, the employer is obliged to compensate the deficits within a given period.

In addition, the employer or directors of the fund must perform their duties to plan participants in a loyal manner in compliance with law, regulation and the pension rules. The Plan Administrator also owes a duty of loyalty to the employer or the fund in compliance with law, regulations and the agreement between them.

The employer or the fund must also disclose and explain the business conditions of the pension plan to the participants once or more times in a year, including the information about the amount of contributions that the employer pays to the Plan Administrator / the fund, the accumulated amount in the fund, and its investment results, etc.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

Fund-type Pensions

In terms of fund-type DB corporate pensions and Employees' Pension Funds (Fund-type Pensions), each pension plan and assets are managed by an independent fund of the employer. Therefore, theoretically, the insolvency of the employer does not affect pension rights of the participants and participants can receive benefits from the fund even after the employer becomes insolvent. Also, from a legal perspective, each participant holds its pension rights not against the employer but against the fund. Therefore, in principle, no participant is able to enforce a pension right directly against the employer whether or not the employer is insolvent. On the other hand, the employer owes an obligation to pay contributions to the fund. In other words, the fund has direct claims against the employer including claims related to unpaid contributions and contributions which will accrue in the future. Therefore, in this case, the fund has a right to enforce the claim against the employer in insolvency.

However, in reality, it is likely that the financial condition of the fund will also deteriorate in circumstances of insolvency of the employer, because it is highly possible that the employer will run up bills for unpaid contributions or will not be able to afford to pay contributions in the future. As a result, it is not uncommon that the fund itself is forced to reduce the accrued pension rights of participants or dissolve itself because of insolvency of the employer.

For example, as described above, in connection with the corporate reorganization proceedings of JAL, the JAL Pension Fund modified the pension rules in order to reduce the accrued pension rights of employees and retirees by obtaining the approval of the Minister, which satisfied the special requirements. Furthermore, it was planned that the JAL Pension Fund would have been dissolved if the fund had failed to modify its rules. In this situation, participants may lose all or part of their pension rights to the fund, therefore an issue arises as to whether participants are still able to claim against an employer to pay their benefits instead of the fund. For example, in the TWR Holdings Case litigation, participants of an Employees' Pension Fund claimed against the trustee of an employer, which entered into corporate reorganization proceedings in Japan in 2002, to allow their direct claims of retirement allowances against the employer. In this case, participants could not receive their benefits from the fund because the fund entered into dissolution. The participants argued that the work rules of the employer could be construed so that the employer assured the direct claims against it for participants if the fund could not pay the entire amount of benefits to them. However, the court rejected the argument raised by the participants on the basis that the work rules of the employer could not be interpreted in a way so as to allow direct claims of the participants against the employer. Considering this precedent, if there is a special clause in work rules or regulations of retirement allowances, etc. which clearly guarantee direct payment by the employer to participants in circumstances where the fund cannot pay benefits in full, it is possible that the court will accept such direct claims of participants in the said case. However, it is practically uncommon that an employer which establishes a Fund-type Pension will guarantee such rights to participants in the work rules because generally speaking the purpose of establishing a Fund-type Pension is to separate duties of pension rights to participants from the employer. Therefore, it would be quite difficult for participants of Fund-type Pensions to enforce their pension rights against an employer in substitution of a fund.

Rule-type DB corporate pensions

With regard to the rule-type DB corporate pensions, the employer has a responsibility for running the plan and owes an obligation to pay benefits directly to the participants. In other words, participants have pension claims directly against the employer so that they can enforce the claims against the employer. There is no specialized legal system only for the enforcement of pension claims in Japan so that the participants' claims against an employer are protected in the same manner as labor claims under the civil procedures, the civil preservation procedures and the civil execution procedures. When an employer enters into court proceedings for insolvency, an issue arises as to whether pension claims against the employer under the rule-type DB corporate pension are treated with the same priority as labor claims such as retirement allowances. This is further discussed in section 6 of this chapter.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

Overview of in-court insolvency procedures in Japan

Court procedures for insolvency in Japan are mainly categorized into civil rehabilitation proceedings under the Civil Rehabilitation Act (Minji-Saisei) and corporate reorganization proceedings under the Corporate Reorganization Act (Kaisha-Kosei) as in-court restructuring procedures, and bankruptcy proceedings under the Bankruptcy Act (Hasan) as in-court liquidation procedures.

Both civil rehabilitation proceedings and corporate reorganization proceedings are similar to the proceedings prescribed in Chapter 11 of the US Bankruptcy Code. In civil rehabilitation proceedings, as a general rule, a debtor continues to have the power to manage its business and dispose of its assets after the commencement of the proceedings (debtor-in-possession). On the other hand, in corporate reorganization proceedings, as a general rule, the debtor's business is managed by a court-appointed trustee instead of the debtor. Corporate reorganization proceedings impair not only the claims of unsecured creditors, but also the claims of secured creditors and priority claims under the reorganization plan, which is one of the biggest differences from bankruptcy proceedings and civil rehabilitation proceedings. In both civil rehabilitation proceedings and corporate reorganization proceedings, distributions to creditors will be made after the rehabilitation plan or the reorganization plan is approved by a statutory majority at the creditors' meeting, and the plan is confirmed by the court.

Bankruptcy proceedings are similar to the proceedings prescribed in Chapter 7 of the US Bankruptcy Code. In bankruptcy proceedings, the debtor company basically stops running its business, and a court-appointed trustee disposes of the assets for the benefit of the debtor company's estate. The trustee makes distributions to creditors according to the priority order prescribed by law during the final stage of the proceedings, and approval by creditors is not needed for the distribution.

Overview of priorities of claims in Japanese in-court insolvency procedures

The in-court procedures described above assign no special priority to pension deficits alone. However, each in-court procedure classifies labor claims with some special priorities different from unsecured claims in different ways. Therefore, if pension deficits are construed as labor claims, they can be treated with such special priority.

The classifications of claims vary between bankruptcy proceedings, civil rehabilitation proceedings, and corporate reorganization proceedings. In general, claims are classified according to the following priorities: (i) administrative expenses, (ii) priority claims, (iii) secured claims, (iv) unsecured claims, and (v) post-filing claims.

The fund's claims in Fund-type Pensions

In a Fund-type Pension, the pension plan is managed by an independent fund and the fund has direct claims against the employer including claims of unpaid contributions and claims of contributions which will accrue in the future. As we mentioned, participants do not have direct pension rights against the employer in principle. Therefore, in each case, we need to consider what kind of priority the fund's claims against the employer will be afforded when the employer enters into in-court insolvency procedures in Japan.

In corporate reorganization proceedings, claims related to contributions which will accrue after the commencement of the proceedings are generally regarded as administrative expenses, which are claims for expenses for the management of the business of the company subject to reorganization. Therefore, the fund can continue to receive payment of the contributions in the future on a timely basis outside of the corporate reorganization proceedings even after the proceedings are commenced. However, as described in the case involving JAL, it is possible that the fund will be compelled to modify the rule to reduce pension rights or to dissolve itself because the employer in insolvency cannot recover without cutting the amount of contributions in the future. On the other hand, unpaid contributions of a fund-type DB corporate pension accrued at the time of the commencement of corporate reorganization proceedings are categorized as unsecured claims arising from a cause that has occurred before the commencement of the proceedings. It is difficult to deem the unpaid contributions accrued before the commencement of the proceedings as priority claims. This is firstly because the holder of the claims for the unpaid contributions against the employer is not the employees but the fund, therefore it is difficult to regard the claims as labor claims arising on the basis of the employment relationship between an employer and its employees, which are given special preference in the proceedings. This is secondly because there is no other basis for ascribing priority under the Defined Benefit Corporate Pension Law. Therefore, a fund-type DB corporate pension fund can only receive payment of these unpaid contributions under the reorganization plan. However, there is an argument among practitioners and academics that it is possible to provide different treatment for the unpaid contributions accrued before the commencement of the proceedings, such as providing a higher payment rate than general unsecured claims. This is because these unpaid contributions practically assume the characteristics of labor claims and therefore different treatment under the plan can be justified where equity will not be undermined. On the other hand, unpaid contributions under an Employees' Pension Fund accrued before the commencement of corporate reorganization proceedings are categorized as priority claims because there is a special provision under the former Employees' Pension Insurance Law that ascribes priority to the claims of the fund. Therefore, these claims of Employees' Pension Funds are paid with preference under a reorganization plan.

In civil rehabilitation proceedings, the claims of the fund against the employer are treated with similar priority to those in corporate reorganization proceedings. More specifically, the fund's claims of contributions which will accrue after the commencement of the proceedings are generally regarded as administrative expenses. The unpaid contributions for fund-type DB corporate pensions which are accrued before commencement of the proceedings are regarded as unsecured claims. In addition, the same argument as described above can be applied as to whether the unpaid contributions accrued before the commencement can be treated differently from other unsecured claims under the rehabilitation plan. The unpaid contributions for an Employees' Pension Fund which are accrued before commencement of the proceedings are regarded as priority claims therefore they are fully paid as long as the debtor's estate has sufficient cash to pay in civil rehabilitation proceedings.

In bankruptcy proceedings, the fund's contribution claims which accrue after the commencement of the proceedings are regarded as administrative expenses in theory. However, in practice, it is likely that the fund will be forced to dissolve because the amount of the debtor's estate is insufficient to meet these administrative expenses. The unpaid contributions for fund-type DB corporate pensions which are accrued before commencement of the proceedings are regarded as unsecured claims. Although the unpaid contributions for Employees' Pension Funds which are accrued before commencement of the proceedings are regarded as priority claims, in practice, it is also unlikely that these claims will be paid in full because the debtor's estate is usually insufficient to satisfy these priority claims.

The participants' claims under rule-type DB corporate pensions

With regard to a rule-type DB corporate pension, the employer has a responsibility for running the plan and owes an obligation to pay benefits directly to the participants. In other words, participants have pension rights to claim both benefits and contributions directly against the employer, therefore they can enforce the claims against the employer.

In the corporate reorganization proceedings, the pension claims of the participants which will accrue after the commencement of the proceedings are generally regarded as administrative expenses, which are claims for expenses for the management of the reorganization company's business. Therefore, the participants can continue to receive benefits from the employer in the future and also request payment of contributions which will accrue after the commencement of the proceedings against the employer on a timely basis even after the proceedings are commenced. If the employer wants to modify its rules for the purpose of reducing accrued pension rights of participants, the employer has to go through the process described above by satisfying the special requirements. On the other hand, there is some debate over how to interpret the priorities for unpaid pension claims accrued before commencement of proceedings. One interpretation is that the pension rights of participants are similar to claims for retirement allowances and therefore the priorities for retirement allowances should be applied to pension rights. That is to say, a claim for the retirement allowance of an employee who has retired before an order confirming the reorganization plan is made, is regarded as an administrative expense up to the amount equivalent to the total amount of the employee's salaries for the six months preceding the retirement or one-third of the amount of the retirement allowance, whichever is larger. Therefore, it can be interpreted that unpaid pension claims accrued before commencement of the proceedings should be accepted as administrative expenses to the extent of the said limitation of the amount (one-third of the amount of the retirement allowance). The rest of the amount of unpaid pension claims accrued before commencement of the proceedings can be deemed as priority labor claims.

In civil rehabilitation proceedings, pension claims which will accrue after the commencement of the proceedings are regarded as administrative expenses, and pension claims accrued before the commencement of the proceedings are regarded as priority labor claims. Neither the administrative expenses nor priority claims may be impaired and shall be fully paid as long as the debtor's estate has sufficient cash to pay in civil rehabilitation proceedings.

In bankruptcy proceedings, although the participants' pension claims which will accrue after the commencement of the proceedings are legally accepted to be administrative expenses, practically it is likely that the employer will be unable to afford to pay the expenses because the amount of the debtor's estate is insufficient. The participants' claims which have accrued before commencement of the proceedings are regarded as priority claims. However, it is also practically unlikely that these will be paid in full because the debtor's estate is usually insufficient.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

Fund-type Pensions are governed by independent funds, which are responsible for running the plans. The directors of each fund owe a duty of loyalty to the fund. Therefore, if a breach of duty of loyalty by a director causes a pension deficit, the fund can claim against the director to collect the amount of the pension deficit. Furthermore, each participant in a fund-type DB corporate pension may charge the director on the basis of the unlawful conduct. However, participants in Employees' Pension Funds are not allowed to bring claims for pension deficits against directors of a fund even when directors commit unlawful acts including breach of their duty of loyalty. This is because, according to court precedents, the funds for Employees' Pension Funds are public bodies therefore rather than the director of a fund as a public officer, the fund itself as a public body must be responsible for exercise of public authority under the State Redress Act. However, there are critics saying that these precedents lead to imbalanced results compared to the case of fund-type DB corporate pensions and that management of a pension plan is not an exercise of public authority but a private action for the benefit of the fund and its participants.

On the other hand, in rule-type DB corporate pensions, the employer has a responsibility to run the plan. Therefore, if the pension deficits are caused by a breach of duty of loyalty by directors of the employer, participants can raise derivative actions and seek monetary damages on the basis of wrongful conduct against the directors.

QUESTION 8

Are there any cross-border features of your pension regime?

While there are pension plans that invest in certain overseas assets, plans themselves are established, formed and funded in Japan, so there are no cross-border pension regimes in the true sense of the word. In addition, while Japanese conglomerate companies that are functioning as multi-national enterprises are looking into formulation of cross-border pensions that universally covers employees in multiple jurisdictions, we have yet to see truly cross-border pension plans, and therefore we are not aware of any active discussion about legal issues in relation to cross-border features for Japanese private pension systems.

QUESTION 9

Discuss the state of defined benefit plans in your country

As mentioned above, Employees' Pension Funds used to be a core system of Japanese corporate pension plans. However, both the numbers of and participants in Employees' Pension Funds have plummeted recently, firstly because a number of these funds were dissolved due to severe financial distress, and secondly because many of these funds shifted to fund-type DB corporate pension plans. For example, according to a survey by the Ministry in 2012, the peak in the number of the funds was 1,883 in 1996. The peak of the numbers of participants was about 12.25 million in 1997. However, in 2011, the numbers of funds decreased to 577, and the numbers of participants decreased to 4.3 million. In addition, as described above, the Employees' Pension Insurance Law was amended in 2013 and came into force in 2014. This amendment forbids establishment of a new fund for Employees' Pension Funds after the date of commencement, and encourages the existing funds to either dissolve or transition to a DB corporate pension or other pension plan within five years from the date of commencement. Therefore, Employees' Pension Funds are in the process of being phased out.

On the other hand, DB corporate pensions have continued to increase in number. For example, the number of DB pension plans increased from 15 (0 fund-type, 15 rule-type) in 2003 to 14,985 (612 fund-type, 14,373 rule-type) in 2012, according to the abovementioned survey. DC corporate pensions have also been widely implemented. The number of participants began at 880 thousand but increased to 4.2 million in 2012 according to the survey by the Minister. Therefore, DB corporate pensions and DC corporate pensions have become the primary systems for Japanese private pension plans.

MALAYSIA

QUESTION 1

What is the legal framework for private pension plans in your country?

The concept of private pension plans, otherwise known as the Private Retirement Scheme ("PRS"), is still relatively new, only coming into force on 3 October 2011, when the PRS was introduced through the Capital Markets and Services (Amendment) Act 2011[1], amending the Capital Markets and Services Act 2007[2] ("the CMSA") to include Part IIIA: Private Retirement Scheme Industry. The CMSA[3] forms the main regulatory framework that governs the implementation of the PRS. It is further supplemented by the Capital Markets and Services (Private Retirement Scheme Industry) Regulations 2012[4] which essentially specifies the scope or extent of the provisions of the CMSA.

Following the amendment to the CMSA[5], there were also amendments made to the Income Tax Act 1967[6] in relation to withdrawals from the PRS. Generally, an 8 per cent tax penalty is imposed on any amount of contribution withdrawn by an individual from the PRS before a member reaches the age of 55.

There are however exemptions in cases of permanent total disablement, serious diseases, mental disabilities, deaths or permanently leaving Malaysia. In addition, the PRS is not without its tax incentives. On the budget tabled on 25 October 2013[7], the Government of Malaysia announced an incentive of RM 500 to contributors who participate in the PRS applying on a one-off basis only to members aged between 20 and 30 years old, being made available for a period of 5 years from 2014 to 2018.

The Government has also made allocations to provide for a RM 3,000 tax relief as announced in Budget 2012[8]. The tax relief of up to RM 3,000 per annum is applicable on gross contributions inclusive of upfront charges and is applied on taxable income, for individual contributions made to the PRS for the first 10 years from assessment year 2012.

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1 Capital Markets and Services (Amendment) Act 2011 (Act A1406).

2 Capital Markets and Services Act 2007 (Act 671).

3 Ibid.

4 Capital Markets and Services (Private Retirement Scheme Industry) Regulations 2012 (PU(A) 77/2012).

5 Supra at 2.

6 Income Tax Act 1967 (Act 53).

7 The 2014 Budget Speech in the Dewan Rakyat, Friday, 25th October 2013.

8 The 2012 Budget Speech in the Dewan Rakyat, Friday, 7th October 2013.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

The main regulator and supervisor is the Security Commissions of Malaysia (SC)[9]. The SC oversees the Private Pension Administrators (PPA). The roles of each of the participants in the PRS are discussed below.

PRS offers a wide range of funds for members. Members can choose to contribute to more than one fund or to more than one PRS fund offered by different PRS providers that is recognized and registered with the SC.

If members do not specify the funds of their choice upon investment, the funds fall under default options. The default options are appropriate for each age group, as provided for under the CMSA.

Individual

Any individual, Malaysian or non-Malaysian, who has attained the age of 18 years on the date of the opening of the private pension account, may make a contribution to any fund under the PRS.

The contributions will be divided and maintained in two sub-accounts namely A and B which consist of 70% and 30% ratio, respectively, of the total contributions. The values of the sub-account A and B may be increased or decreased according to the unit price offered by the PRS fund chosen by the investor.

As the scheme is a voluntary scheme, there are no fixed amounts or fixed intervals for making contributions and the investors can contribute to more than one fund under a PRS or contribute to more than one PRS, offered by different PRS Providers[10].

Investors may switch funds within a PRS managed by the same PRS Providers and may change to another PRS Provider on a once a year basis, provided that an investor has participated in the PRS fund for one year.

Employers

If an employer contributes to a PRS on behalf of its employees it may do so with one or more PRS Providers of its choice. Being voluntary, the amount and the intervals of contribution is determined by the employer while the employees choose the type of fund(s) under the Scheme offered by the PRS Provider. If the employees do not choose any it will fall under default options.

[9] Capital Markets and Services Act 2007 (Act 671).

[10] http://www.ppa.my/prs/about-prs/prs-scheme-features/

QUESTION 3

How are the plans governed?

The Capital Markets and Services Act 2007 empowers the SC to regulate and supervise the PRS industry. Below is the regulatory framework of the PRS.

The private pension plans on the other hand are governed by a Governance Board comprising of public interest directors whose appointment must be made with approval from the SC. The roles and responsibilities of the participants are described below.

Private pension administrator

(i) Provide a life-time central account management, facilitating transactions and promoting efficient administration.

(ii) Act as a one-stop centre.

(iii) Educate the public and promoting awareness on PRS.

(iv) Provide central administration and developing the industry.

(v) Protect members' interests.

PRS providers

i. Exercise its powers for a proper purpose and in good faith, in the best interest of the members as a whole.

ii. Exercise the degree of care and diligence.

iii. Keeps complete and accurate records of all information.

iv. Not make investments in which it could have a financial interest or derive a benefit without approval of the Scheme Trustee.

v. Provide interim reports, annual reports and account statements.

Scheme trustees

i. Ensure compliance of PRS Officers and Delegates.

ii. Provide accurate valuation and pricing.

iii. Ensure accuracy of all transactions to avoid unnecessary costs or risk to the fund.

iv. Adequate accounting for all accounts.

PRS distributors and consultants

i. PRS Distributors are licensed under the Capital Markets and Services Act 2007.

ii. PRS Consultants are representatives of PRS Distributors and must be registered with the Federation of Investment Managers Malaysia (FIMM).

iii. Institutional PRS advisers are bankers licensed to distribute PRS schemes from more than one PRS provider.

iv. Corporate PRS advisers are financial planning firms that represent and distribute products from more than one PRS provider and can act on behalf of the contributors.

v. PRS Consultants must have minimum knowledge of the PRS industry and act with integrity and a high level of professionalism.

A PRS administrator[11] is a person who is approved to perform the function of record keeping, administration and customer service for members and contributors in relation to contributions made in respect of a PRS and such other duties and functions as may be specified by the Commission.

Private pension plans are governed by a Governance Board of public interest directors who represent the public at large. They must exercise their duties: (i) in the interest of the public and based on the need of protecting member's interests; (ii) free from any business or other relationship which could interfere with the exercise of independent judgment; and (iii) independent of the industries of fund management and the management of private pension administrator. Their appointment must be approved by the Commission by virtue of section 139E (1)[12].

If the Commission believes the interests of the members are likely to be adversely affected, it may issue a written direction under section 139L[13] and require a private scheme administrator to take any action to do or not to do any act or thing in relation to its business and affairs, or its directors or officers, which the Commission considers necessary. Further, by virtue of this provision[14], the Commission may also issue a written direction and do the following:

i. Remove any director or chief executive of the private retirement scheme administrator from office;

ii. Appoint any person to be a director or chief executive of the private retirement scheme administrator and provide direction for the person appointed to be paid by the private retirement scheme administrator;

iii. Appoint a person to advise the private retirement scheme administrator in relation to the proper conduct of its business and affairs and provide direction for the person appointed to be paid by the private retirement scheme administrator; or

iv. Require the private retirement scheme administrator to furnish the Commission any information or record as the Commission considers necessary.

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11 Capital Markets and Services Act 2007, s. 139.

12 Ibid.

13 Ibid.

14 Section 139L of the Capital Markets and Services Act 2007.

QUESTION 4

Is there a compensation fund for pension benefits?

Both public and private employees' pension schemes in Malaysia are governed by the Ministry of Human Resources. Public sector employees in Malaysia are covered by the Government Pension scheme. The private sector employees are covered by the Employee Provident Fund (EPF).

The Government pension scheme was created not only for retirement, but also to recognize the importance of providing survivor benefits which are of immediate concern for the welfare of the employees' families. The fund aims to compensate the dependants for the permanent loss of financial support. Eligible dependants include the surviving spouse and minor children. The pension scheme is intended to provide financial security for retired Government employees. Retirees who opt for pension schemes will be paid a fixed monthly income, service gratuity payments and enjoy benefits such as free medical treatment at Government hospital.

Pension scheme objective aims to acknowledge and appreciate the excellent service, with loyalty, dedication and honesty rendered to the Government by personnel, act as incentive for personnel to retain their service with the Government, to provide life subsistence for the dependants of personnel who have passed on during their service with the Government or after their retirement and also to develop a form of Compensation Scheme for personnel who are required to retire or passed away due to an injury or contracted a disease because was exposed to harm in the course of carrying out his/her duties[15]. Public sector employees include those employed directly by the government, statutory bodies and local authorities. They are entitled to a number of benefits which comprises of retirement benefits, survivors' benefits and also disability pension. The amount paid for these benefits are essentially a specified proportion of basic salary. That is why the Government pension scheme is a defined benefit scheme.

Article 147(1) of the Federal Constitution[16] provides for the protection of pension rights. The provision clearly states as follows:

> "The law applicable to any pension, gratuity or other like allowance (in this Article referred to as an "award") granted to a member of any of the public services, or to his widow, children, dependant or personal representatives, shall be that in force on the relevant day or any later law not less favourable to the person to whom the award is made."

Furthermore, pension is the responsibility of the Federal government as provided under Article 74[17] 9th Schedule, List I, Para 6(d) Federal List:

> "Under the Federal Constitution, pensions and compensation for loss of office, gratuities and conditions of service are subject to the State List."

[15] http://www.jpapencen.gov.my/english/pension_scheme_obj.html
[16] Article 147 of Federal Constitution.
[17] Article 74 of Federal Constitution.

Private sector employees and employer are required to contribute to the Employees' Provident Fund (EPF) or the Social Security Organisation (SOCSO). Payments of retirement or disability benefits and pensions in the private sector did not affect the public purse as such payments come from the monthly wage deductions of employees and matching contributions from employers. From January 2012 onwards the rate for employer's share contribution is fixed at 12% to 13% subject to monthly wage / salary of RM5000, to be paid by the employer and not to be deducted from the employees' wages. The employees' share contribution is fixed at 11%, to be deducted from the employees' wage at the time the wage is paid every month[18].

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

Malaysia has its own version of a social safety net in the form of the EPF for private sector employees and the Government Pension Scheme for public sector employees. The EPF dates back to 1991 and is considered very successful.

In the event that the employer / sponsor is likely to become, or has become insolvent, employees may enforce their pension rights through several paths.

Regulatory body in charge

The EPF is regulated by the Employees Provident Fund Board ("the Board"), established under s.3 of the EPF Act 1991[19] for the purposes of managing the Fund and for carrying into effect the purposes of the EPF Act 1991.

[18] http://www.kwsp.gov.my/portal/en/employers/employers-responsibility/contribution/contribution-rate

[19] Section 3 of the Employees Provident Fund Act 1991 – For the purposes of managing the Fund and for carrying into effect the purposes of this Act, a body corporate by the name of "Employees Provident Fund Board" is established with perpetual succession and a common seal, and which may sue and be sued in its corporate name and, subject to and for the purposes of this Act, may enter into contracts and may acquire, purchase, take, hold and enjoy movable and immovable property of every description and may convey, assign, surrender, yield up, charge, mortgage, demise, reassign, transfer or otherwise dispose of, or deal with any movable or immovable property or any interest therein vested in the Board upon such terms as it deems fit.

Companies Act 1965

Under the Companies Act 1965 ("the 1965 Act"), a company may go into liquidation, voluntary or compulsory. In such case, the employees of the company in liquidation may enforce their pension rights under s.191[20] and s.292(1)(e) of the 1965 Act; under s.292(1)(e) of the 1965 Act, the employees will be given priority over the employer / sponsor's creditors, such that the employees will be paid in priority all amounts due in respect of the contributions payable during the twelve (12) months before the winding up of the company, either voluntary or compulsory, in relation to the employees' EPF or pensions provided that it is a government approved pension scheme.

In the case of *Chuah Teong Hooi & Anor v Employees Provident Fund Board*[21], the plaintiffs applied to the court pursuant to s.183(3) of the 1965 Act for directions as regards the priority of the claim by the plaintiffs for costs, charges and expenses incurred by them and the claims by the defendant for payment of the employer's and employees' contributions due under the Employee Provident Fund Board Act 1951. His Lordship held that the EPF contributions rank in priority to the sales tax and the customs duties which between them rank equally. This priority extended to the goods which were seized by the Director General of Customs and Excise in view of the application of s.66 of the Employees Provident Fund Act 1991, although this was limited to claims in the immediate preceding twelve (12) months.

It is thus evident that the pension rights of employees may be enforced under the 1965 Act if the employer / sponsor underwent liquidation, even though the rights provided under the 1965 Act seem to be quite limited.

Bankruptcy Act 1967

In a bankruptcy proceeding, the common law priority rules apply in which employees' claim for their EPF or pension funds are given priority pursuant to s.43(1)(d) Bankruptcy Act 1967[22] if their employer / sponsor is an individual. Pursuant to this provision, all contributions to the EPF payable during the twelve (12) months before commencement of the bankruptcy proceedings are to be given priority over the employer's / sponsor's creditors.

Employees Provident Fund Act 1991

The Employees Provident Fund Act 1991 ("EPF Act") requires employees and their employers to contribute towards their retirement savings, and allows workers to withdraw these savings at retirement or for special purposes before they reach their age of retirement.

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[20] Section 191 of the Companies Act 1965 – (1) Where a receiver is appointed on behalf of the holders of any debentures of a company secured by a floating charge or possession is taken by or on behalf of debenture holders of any property comprised in or subject to a floating charge, then if the company is not at the time in the course of being wound up, debts which in every winding up are preferential debts and are due by way of wages salary vacation leave or superannuation or provident fund payments and any amount which in a winding up is payable in pursuance of section 292(3) or (5) shall be paid out of any assets coming to the hands of the receiver or other person taking possession in priority to any claim of principal or interest in respect of the debentures and shall be paid in the same order of priority as is prescribed by that section in respect of those debts.

[21] [1990] 2 MLJ 218.

[22] Section 43 of the Bankruptcy Act 1967 – (1) In the distribution of the property of a bankrupt there shall be paid in priority to all other debts— (d) all amounts due in respect of contributions payable during the twelve months before the date of the receiving order by the bankrupt as the employer of any person under any law relating to provident funds.

The EPF Act appears to be one of the mechanisms for employees to enforce their pension rights in the event that their employer / sponsor is insolvent. Under s.51 of the EPF Act[23], even if the employer / the sponsor are insolvent, their contributions payable to their employees' provident fund or pension fund will not be attached as any debt or claim by the employer's / sponsor's creditors, not even by the Director General of Insolvency.

Employees may also enforce their pension rights through the commencement of a civil proceeding. Pursuant to s.46 of the EPF Act[24], if any contributions remain unpaid, any person, who was a registered director of the company during the period of default, shall together with the company be jointly and severally liable for all contribution, dividend and interest owing[25].

Under s.65 of the EPF Act[26], the Board has a statutory right to pursue a civil action against the employer and its directors for outstanding contributions of the funds owed to the employees. The court in interpreting s.65 of the EPF Act has given a very liberal approach and this section is broad enough to render the Limitation Act 1953 inapplicable. In the case of Lembaga Kumpulan Wang Simpanan Pekerja v. Carimonde Sdn Bhd & Ors[27] it was held that:

> "...s.65 of the EPF Act 1991 is an enabling provision to provide for a right to civil recovery simultaneously with criminal prosecution and, more importantly, to overcome any contention that the cause of action to recover defaulted contributions was only vested in the employees concerned and not the Plaintiff's Board."

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[23] Section 51 of the Employees Provident Fund Act 1991 – Notwithstanding anything to the contrary contained in any other written law—

(a) no sum deducted from the wages of a member of the Fund under section 48;

(b) no amount payable by the employer as his contribution; and

(c) no amount standing to the credit of a member of the Fund, shall be assignable, transferable, liable to be attached, sequestered, levied upon, for, or in respect of, any debt or claim whatsoever, nor shall the *Director General of Insolvency be entitled to or have any claim on any such sum or amount.

[24] Section 46 of the Employees Provident Fund Act 1991 – (1) Where any contributions remaining unpaid by a company, a firm or an association of persons, then, notwithstanding anything to the contrary in this Act or any other written law, the directors of such company including any persons who were directors of such company during such period in which contributions were liable to be paid, or the partners of such firm, including any persons who were partners of such firm during such period in which contributions were liable to be paid, or the office-bearers of such association of persons, including any persons who were office-bearers of such association during such period in which contributions were liable to be paid, as the case may be, shall together with the company, firm or association of persons liable to pay the said contributions, be jointly and severally liable for the contributions due and payable to the Fund.

[25] Lembaga Kumpulan Simpanan Pekerja v. HOL Chainstore (M) Sdn. Bhd & Ors [2014] 1 LNS 376; [2014] 7 MLJ 622.

[26] Section 65 of the Employees Provident Fund Act 1991 – Civil Proceedings to recover contributions.

(1) Notwithstanding the provisions of any other written law all contributions payable under this Act may, without prejudice to any other remedy, be recoverable by the Board summarily as a civil debt.

(2) Proceedings for the summary recovery as civil debts of contributions may be instituted by any officer authorized in that behalf by special or general directions of the Chairman and any such officer may conduct such proceedings.

[27] [2011] 6 CLJ 451.

In other words, it was contended that the provision was intended to give locus standi to the Board of the Plaintiff to institute civil proceedings to recover dues-notwithstanding the provisions of any other written law. This section is to ensure that errant employers / sponsors who default in remitting EPF contributions to the employees do not find protection under this Act.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

Under Section 292 of the Companies Act 1965, there are special priorities in an insolvency for pension contributions payable in the preceding 12 months, discussed under question 5 above.

Further, all monies received by a private retirement scheme administrator are held in trust under Section 139J of the Capital Markets and Services Act 2007.

There are as well certain additional protections discussed in Section 5, so that members are well protected in the event of an insolvency.

QUESTION 7

Are remedies to collect in respect of pension deficit available against parties or entities other than the employer?

Although the EPF Act, generally provides for the regulation of state regulated provident fund, Section 52(9) of the EPF Act provides for the application of the EPF Act in respect of deductions and contributions be subjected to the same offence and penalties for Approved Funds (which is the term used in the EPF Act to refer to private pension scheme).

Further office-bearers of an association also have liability. Therefore, where the employees are unable to recover the deficient amount from the company, liability may be attached to the directors or office-bearers of the company.

Where an employer fails to pay any contributions due within such a period as may be prescribed, the employer shall in addition to such contributions due, be liable to pay dividends which would have accrued on such contributions if such contributions had been paid by the employer within the prescribed period calculated in accordance with Section 45(3) of the EPF Act 1991. Where the employer fails to comply with the order made, the Court has the power to issue a warrant to levy the employer’s property for the whole amount of the arrears by way of distress and sale of the property or by fine, upon an application of the Board – section 63(4) of the EPF Act.

In addition to the dividends to be paid, the employer is liable to pay interest that is to be credited to the Approved Fund on such amount – Section 49(1) of the EPF Act 1991.

All contributions payable under the Act may, without prejudice to any other remedy, be recoverable summarily as a civil debt in a civil proceeding – Section 65 of the EPF Act.

QUESTION 8

Are there any cross-border features in your pension regime?

No, there are no specific abilities to reach across borders to enforce pension rights in another jurisdiction.

QUESTION 9

Discuss the state of defined benefit plans in your country

The defined benefit plan vs the defined contribution plan

The current Malaysian position is that defined benefit plans ("DB") are less prevalent owing to the existence of the EPF which essentially is a defined contribution plan ("DC") in which employees in the private sector are required to contribute. As such, employer sponsored retirement plans are merely additions to the pre-existing EPF.

However, the implementation of the MASB 29[28] by the Malaysian Accounting Standards Board effective 1.1.2003 sought to change the state of being. Pursuant to the MASB 29, five categories of employee benefits are identified, including post-employment benefits such as pensions, other retirement benefits, post-employment life insurance and post-employment medical care.

Pursuant to the foregoing, "long-term employee benefits" can either be categorized as DB or DC but, the liability of an enterprise to its employees depends ultimately on its ability to make good shortfalls in the benefit fund's assets[29].

What may be the key factor in a DB is that the benefits are attributed based on periods of service. As such, an enterprise would account for the period of an employee's service. Generally, a DB is only provided by the government to civil servants whereas employees working in the private sector are to resort to the EPF which as explained earlier, is essentially a DC. This in fact is guaranteed by the EPF Act[30] particularly pursuant to section 43(1)[31] which states as follows:

[28] Lembaga Piawaian Perakaunan Malaysia MASB Standard 29 (Employee Benefits), Malaysian Accounting Standards Board 2002.

[29] Lembaga Piawaian Perakaunan Malaysia MASB Standard 29 (Employee Benefits), Malaysian Accounting Standards Board 2002 at paragraph 50.

[30] Employees Provident Fund Act 1991 (Act 452).

[31] Section 43(1), Employees Provident Fund Act 1991 (Act 452).

> Subject to the provisions of section 52, every employee and every employer of a person who is an employee within the meaning of this Act shall be liable to pay monthly contributions on the amount of wages at the rate respectively set out in the Third Schedule.

Apart from that, the only leeway given to employees and employers is as stated in section 52[32] which in summary allows for an exemption from section 43[33] in cases where there was an approved fund approved by the EPF Board. In this sense, DBs are less prevalent in the private section owing to the existence of the EPF.

[32] Section 52, Employees Provident Fund Act 1991 (Act 452).

[33] Supra.

NEW ZEALAND

QUESTION 1

What is the legal framework for private pension plans in your country?

The operation and regulation of New Zealand's private pension scheme, KiwiSaver, is governed by the KiwiSaver Act 2006 ("KiwiSaver Act"). In addition, the Financial Markets Conduct Act 2013 ("FMCA") regulates the promotion and sale of financial products and financial product providers including KiwiSaver scheme providers ("KiwiSaver Providers").

Participation in the KiwiSaver scheme is not compulsory for employees in New Zealand. Employees are automatically enrolled into KiwiSaver (with some exceptions), however, they do have the opportunity to opt-out. Those employees that are not automatically enrolled may choose to be part of KiwiSaver.

Once enrolled, both employers and employees make contributions to an employee's KiwiSaver account. Employer contributions are required to be at least 3% of the employee's salary or wage. Employees have some flexibility in relation to their level of contribution, being able to elect to contribute 3%, 4% or 8% of their salary or wage. Employer and employee contributions (deducted from an employee's salary or wages) are paid by the employer to the Inland Revenue Department of New Zealand ("IRD") and the IRD in turn pays contributions (plus any interest earned) to the employee's chosen KiwiSaver Provider.

Self-employed people are also able to participate in KiwiSaver by making contributions at a rate agreed with their KiwiSaver Provider (either by lump sum or regular contributions).

There is no concessional tax treatment for employees in relation to their employee contributions. That is, employees still pay income tax on the whole of their wages or salary (despite the employee contribution being calculated and paid on their pre-tax wages or salary). An employee's income generated from their KiwiSaver account (for example, investment income) is also liable to tax at a flat rate of 28% if the KiwiSaver scheme is a widely held superannuation fund, or at variable rates if the scheme is a portfolio investment entity.

Participants in KiwiSaver schemes (and other complying superannuation schemes) can, however, benefit from a member's tax credit, which is paid by the New Zealand Government and credited to their KiwiSaver account on an annual basis if certain criteria are met[1].

In addition, Employer Superannuation Contribution Tax ("ESCT") is payable on employer contributions, with the net contribution being paid to the KiwiSaver Provider. The ESCT rate varies according to the employee's salary or wage.

Other existing registered superannuation schemes, that are no longer able to be converted to a KiwiSaver scheme, can continue to operate independently if approved by the New Zealand Financial Markets Authority ("FMA"). There are also public sector government funded superannuation schemes that continue to operate, but are closed to new members. As such, these schemes will be phased out over time. Those existing funds that qualify as complying superannuation funds receive the same tax treatment as KiwiSaver schemes.

1 Income Tax Act 2007, section MK1.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

In New Zealand, the FMA is primarily responsible for the regulation and supervision of the superannuation industry, including KiwiSaver. In addition, the IRD is responsible for administering contributions to KiwiSaver schemes.

KiwiSaver Providers and providers of complying superannuation funds that are not KiwiSaver schemes (together "Providers") must comply with regulatory obligations under the KiwiSaver Act and the FMCA. These obligations include, relevantly, licensing of key roles, registration requirements, product disclosure and reporting obligations. The reporting obligations include (but are not limited to) requiring Providers to supply an annual return to the FMA which provides an overview of the financial position of the Provider.

In addition, the trustees of public sector schemes must report to the Government's Minister of Finance.

As noted above, employer contributions must be a minimum of 3% of the employee's gross salary or wage and employees can elect to contribute 3%, 4% or 8% of their gross salary or wage. Self-employed people are required to come to an agreement with their KiwiSaver Provider regarding the level of their contribution. In some cases, KiwiSaver Providers will have a minimum contribution requirement.

QUESTION 3

How are the plans governed?

As noted above, the IRD has an intermediary role in administering aspects of the KiwiSaver schemes, including contributions. Beyond that involvement, the KiwiSaver Providers are responsible for managing and administering their own KiwiSaver schemes.

The FMCA provides governance requirements that apply to all KiwiSaver schemes and to other superannuation schemes that are registered as such on the register of managed investment schemes[2]. Each scheme will have its own governance structure but, under the FMCA is required to have a licensed manager and a licensed supervisor[3] (or a licensed independent trustee in place of the manager and supervisor if the scheme is registered as a "restricted scheme"[4]). These requirements are part of the ongoing registration requirements for KiwiSaver schemes and superannuation schemes under the FMCA[5].

2 FMCA, section 6. This also includes, for example schemes which form part of the National Provident Fund ("NPF") pursuant to the National Provident Fund Restructuring Act 1990, section 59A and to a more limited extent, the schemes under the Government Superannuation Fund ("GSF") pursuant to the Government Superannuation Fund Act 1956, section 19H.

3 FMCA, section 127.

4 FMCA, section 131.

5 FMCA, sections 127 to 131.

In addition to the statutory governance requirements, the trustees of the fund will also be governed by the terms and conditions of its trust deed. The KiwiSaver Act provides a range of rules which are, by virtue of that statute, deemed to be implied terms of every trust deed that establishes a KiwiSaver scheme[6]. These are referred to as the KiwiSaver Scheme Rules[7]. These rules include prohibition on unreasonable fees for members[8] and restrictions and guidelines for withdrawing funds[9].

QUESTION 4

Is there a compensation fund for pension benefits?

The New Zealand Government does not guarantee any KiwiSaver schemes or investment products of any KiwiSaver schemes[10]. KiwiSaver Providers are required to make people aware of this by disclosing it in the product disclosure statements issued in relation to their KiwiSaver schemes[11].

There are a small number of superannuation schemes in New Zealand that are guaranteed by the Crown. These are the schemes that make up the New Zealand Government Fund known as the National Provident Fund ("NPF"), however, they are now closed to new members[12].

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

As KiwiSaver schemes are run by KiwiSaver Providers, rather than employers, an employer's solvency is generally not relevant to the operation of the fund, nor does it impact on the continuation of the employee's participation in the fund.

The employee's risk lies with the KiwiSaver Provider. Given that there are no compensation funds (and, in almost all cases, the funds are not guaranteed by Government) and that KiwiSaver funds are invested in the open market, an employee's superannuation is at risk as with any other investor in the market.

The manager of a scheme is required to notify the FMA if it has formed the opinion that either it or the scheme is, or is likely to become, insolvent[13].

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[6] KiwiSaver Act 2006, Subpart 1of Part 4 and Schedule 1.
[7] KiwiSaver Act 2006, Subpart 1of Part 4 and Schedule 1.
[8] KiwiSaver Act 2006, clause 2 of Schedule 1.
[9] KiwiSaver Act 2006, clauses 5 to 14 of Schedule 1.
[10] KiwiSaver Act 2006, section 161.
[11] KiwiSaver Act 2006, section 161.
[12] National Provident Fund Restructuring Act 1990, section 60.
[13] FMCA, section 151.

Nevertheless, employees are offered some protection in respect of KiwiSaver contributions in the event of their employer's insolvency. Particularly, if an employer has failed to on-pay to the IRD the amounts it has withheld from an employee's salary or wage for the purpose of making the employee's KiwiSaver contributions. In that case, the IRD has priority ranking in the event of an insolvency of the employer for any unpaid employee KiwiSaver contributions[14].

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

Superannuation schemes (including KiwiSaver) are established as trusts, and accordingly, the basic rules applying to the treatment of trust assets in an insolvency of the trustee apply to superannuation schemes. This position is reaffirmed by the FMCA[15]. This would afford some protection in relation to employee and employer contributions in the event of the Provider's insolvency.

As there is no guarantee from the Crown or any other entity, in respect of any KiwiSaver scheme or investment product, members of KiwiSaver schemes cannot expect to obtain priority for a superannuation fund deficit in the event of the Provider's insolvency.

However, there is scope for the scheme supervisor, or the FMA, to apply to Court for orders to remedy problems if it is satisfied, inter alia, that the registered scheme is insolvent[16]. The Court's order can include, for example, appointment of receivers and mangers or directions it considers necessary to protect the interests of product holders, any guarantor of the financial products or the public. In exercising its powers, the Court must have regard to the interests of all creditors of the registered scheme[17].

Under the FMCA, a member's claim on the scheme property is "pooled". While not specified in the legislation (but set out in a number of investment statements), a claim is likely to rank equally, or "*pari passu*", with the claims of other members of the scheme.

The KiwiSaver scheme is a personal pension scheme and can be distinguished from employment-based schemes[18]. It is not tied to any particular employment and the legislation; there is no distinction between actively employed members and retired members. Accordingly, the treatment of employees and retirees is not expected to vary.

Following the insolvency or winding up of the scheme, members will be required to transfer to another KiwiSaver scheme in accordance with the KiwiSaver Act.

[14] Companies Act 1993, Schedule 7, clause 1(2)(g).

[15] FMCA, section 157.

[16] FMCA, section 207.

[17] FMCA, section 208.

[18] The Official Assignee v Trustees Executors Limited [2014] NZHC 345 at [43].

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

As noted above, the New Zealand Government does not guarantee an employee's KiwiSaver funds. Accordingly, deficits in funds are likely to be difficult to recover.

Nevertheless, the FMCA provides that certain key individuals with control or responsibility over the KiwiSaver or other superannuation schemes will be liable to penalties for certain breaches of the legislation[19]. In addition, a person who has suffered loss or damage due to a contravention of the governance provisions under the FMCA may be able to obtain a compensatory order requiring payment of the amount reflecting the loss or damage (or part thereof) to the aggrieved person[20].

Although the FMCA focuses less on criminal liability than civil liability, there are some instances of criminal liability provisions, for example knowing or reckless behaviour and false or misleading statements. Consequences of conviction can include fines, reparation (ie payment made directly to the victim) and imprisonment[21].

In addition to the statutory penalties, Managers of KiwiSaver schemes owe their members fiduciary duties[22], which provides members with enforcement options should the Manager fail to meet those duties. They will also have professional duties (and be subject to sanctions) if they are chartered accountants

QUESTION 8

Are there any cross-border features of your pension regime?

A KiwiSaver interest of a bankrupt is "property" for the purposes of the Insolvency Act 2006[23].

Generally speaking, all property of a bankrupt, whether held upon adjudication or acquired during bankruptcy, vests in the Official Assignee[24]. However, the Kiwisaver interests of a bankrupt (including Kiwisaver funds accumulating for the benefit of a member during bankruptcy) do not vest in the Official Assignee.

As such, it is unlikely that overseas insolvency practitioners would be able to access and realise a bankrupt's KiwiSaver account pursuant to the Insolvency (Cross-border) Act 2006[25].

[19] FMCA, section 228.

[20] FMCA, subpart 3 of Part 8.

[21] FMCA subpart 4 of Part 8.

[22] Financial Markets Authority "Guidance Note: Monitoring Investment Risk in KiwiSaver Schemes", March 2014, page 8.

[23] The Official Assignee v Trustees Executors Limited [2014] NZHC 345 at [32] and which was not disputed on appeal in Trustees Executors Limited v The Official Assignee [2015] NZCA 118 at [5].

[24] Insolvency Act 2006, sections 101 and 102.

[25] See Insolvency (Cross-border) Act 2006, Article 21.

For completeness, there are also cross-border aspects to the KiwiSaver scheme that are not related to insolvency. These are particularly in relation to Trans-Tasman arrangements between Australia and New Zealand relating to portability of superannuation. The arrangements allow KiwiSaver members (but not members of non-KiwiSaver schemes) to transfer their account balances to a complying Australian superannuation fund[26].

QUESTION 9

Discuss the state of defined benefit plans in your country

Historically, superannuation schemes were often set up by employers or a group of employers to provide a vehicle for retirement saving by their employees. The New Zealand Government established a number of schemes for government or local government employees, one example of which is the NPF. The majority of these are now closed to new members and, as a result, will inevitably be phased out.

However, since the KiwiSaver Act was introduced in 2006, KiwiSaver schemes have dominated New Zealand's superannuation industry. The KiwiSaver Act aims to increase individuals' well-being and financial independence, particularly in retirement. It offers employees a number of advantages (including tax incentives) and schemes are often privately run and operated. As a result, employer run superannuation schemes are becoming less and less common.

The automatic enrolment of employees into a KiwiSaver scheme (with some exceptions) is likely to maintain participation in the schemes.

Recent legislative amendments have also impacted on superannuation schemes in New Zealand, which are now more highly regulated. This is expected to increase consumer confidence, particularly on the basis that the industry will be supervised and information will be more readily accessible.

KiwiSaver schemes will only continue to dominate the superannuation regime in New Zealand in the future. We expect that they will become more robust as time goes on given that:

(a) they are a relatively recent addition to the superannuation field and will become more advanced and developed with the passage of time;

(b) the FMA is prioritising supervision and regulation of the KiwiSaver sector; and

(c) they will be relied upon more and more as New Zealand's workforce continues to age and "baby boomers" head towards retirement in this country.

[26] KiwiSaver Rules, rule 14B.

POLAND

QUESTION 1

What is the legal framework for private pension plans in your country?

An outline of the pension system in Poland

Poland's pension system was reformed in 1999 to create a new system with three pillars[1]:

- First pillar – a state pay-as-you-go fund (compulsory enrolment) – the Social Insurance Fund managed by the Polish Social Insurance Institution that maintains records of social insurance contributions and pays out annuitized retirement benefits. In principle, pension benefits currently being paid out are based on a defined benefit and highest earning years formulas (old system). When the reformed pension system becomes fully operational, a defined contribution and life-time earnings formulas would be used to calculate the pension benefits of future pensioners (new system);

- Second pillar – capital funds (compulsory for those who have opted for it) – the Open Pension Funds managed by private institutions, General Pension Societies; these manage and invest parts of the social insurance contribution. The second pillar was reformed in 2013/14 – the amount of social insurance contribution conveyed to the second pillar was reduced; it was also decided that only persons interested in participating in the second pillar would remain in it. As a result, only around 2.56 million from around 14 million people covered by the second pillar chose to remain in it; approx. PLN 153 billion of funds were transferred from the second pillar to the first pillar;

- Third pillar – capital plans and savings (voluntary enrolment), forming additional pension benefits – private Employee Pension Plans (their operation was fundamentally changed in 2004), and two types of private pension savings, Individual Pension Accounts (since 2004; "IKE") and Individual Pension Security Accounts (since 2012; "IKZE"), all managed by private institutions.

In EU Member States, the pension system is conventionally divided into three pillars, where the "first pillar" constitutes state-based social security pensions, the "second pillar" is occupational pension plans, which include an employer contribution, whereas the "third pillar" is made up of non-compulsory private pension savings. In Poland, this typical division does not apply to the second and third pillars. The Polish second pillar is a so-called first pillar BIS. In turn, the Polish third pillar comprises the second pillar (Employee Pension Plans) and third pillar (IKE and IKZE) pursuant to the typical division.

This chapter discusses the occupational private pension plans that are part of the third pillar of the pension system in Poland, i.e.: Employee Pension Plans ("PPE"). PPEs function as defined contribution pension plans ("DC pension plans").

[1] Certain professional groups are subject to a modified pension system and are excluded from the general pension system, in particular, uniformed services, miners, teachers, rail workers, prosecutors, judges and persons insured in the Polish Agricultural Social Insurance Fund.

Defined benefit private pension plans ("DB pension plans") are not a statutory component of the pension system in Poland. They will not be the subject of this chapter, except in a cross-border context, which will be referred to in point 8. Polish law only exceptionally envisages the creation of such statutory forms of PPE where the plan founder is an employer from another EU Member State, a state in the European Economic Area not being a member state of the European Union or Swiss Federation.

Domestic employers may establish DB pension plans only and solely on the basis of the freedom of contract rule in cooperation with e.g. insurance companies. In the same non-statutory manner, employers can create a variety of forms of DC pension plans or mixed DB/DC pension plans in cases where they do not decide on the form of PPE prescribed by law. These non-statutory pension plans and their participants do not benefit from privileges, particularly tax privileges that the law provides for PPEs.

Legal framework for the operation of Employee Pension Plans

The basic legal Acts governing PPEs are the Act on Employee Pension Plans dated 20 April 2004 ("PPE Act")[2], which specifies the rules for their creation, operation and participation as well as terms and conditions to be met by entities organizing and administering them, and the Act on Organisation and Operation of Pension Funds dated 28 August 1997 ("OIFFE Act") that sets the terms and conditions for creation and operation of employee pension funds. These laws implement EU law – Directive 98/49/EU[3] and Directive 2003/41/EU[4].

In 2003, Poland ratified the Social Security (minimum standards) Convention, 1952 (no. 102)[5].

The creation of a PPE by employers is voluntary. This right is generally accorded to each employer in the private sector. As for the public sector, limitations in this regard arise from provisions regulating management of state finances. It is commonly recognized that public finance sector entities cannot establish a PPE (with the exception of public universities that are specifically granted such a right by law)[6].

An employer may establish a PPE, if the right to participate in it extends to at least half of its employees, and if it employs at least 500 employees – to at least one third of them. The law sets a membership threshold in a plan: an employer cannot set the tenure of persons entitled to participate in a plan at less than three months (minimum vesting period for PPE enrolment) and the maximum participation age is 70. Employee membership in a PPE is also voluntary. Entitled persons are not automatically enrolled when an employer creates a plan or upon becoming a new employee after the required vesting period; each employee must submit a written individual declaration of membership in a PPE to an employer. Should the employer

2 This law replaced the Act on employees' pension plans of 22 August 1997.

3 Council Directive 98/49/EC of 29 June 1998 on safeguarding the supplementary pension rights of employed and self-employed persons moving within the Community.

4 Directive 2003/41/EC of the European Parliament and of the Council of 3 June 2003 on the activities and supervision of institutions for occupational retirement provision.

5 C102 - Social Security (Minimum Standards) Convention, 1952: http://www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:12100:0::NO::P12100_INSTRUMENT_ID:312247, accessed on 26 April 2015.

6 It is also possible, however, to come across views admitting the existence of PPEs in public sector institutions, e.g.: Association of Polish Economists [Towarzystwo Ekonomistów Polskich]. 2014. *The Supplementary Pension System in Poland – diagnosis and recommendations for change [Dodatkowy System Emerytalny w Polsce - diagnoza i rekomendacje zmian], pages 19 and 27, http://tep.org.pl/wp-content/uploads/Raport-DSE-Towarzystwo-Ekonomist%C3%B3w-Polskich.pdf.*

refuse to accept an employee into a PPE, he may pursue his rights before the courts if he considers such refusal to be unjustified.

PPEs are funded by monthly contributions financed by employers (up to 7% of remuneration of an employee being a plan member, including e.g. bonus and remuneration for working overtime, if applicable). These contributions constitute additional income for an employee, irrespective of remuneration. The contribution amount may be determined by an employer as: a specific percentage of each employee's salary; a specific percentage of each employee's salary with an upper threshold amount; or as a specific amount, identical for each employee. PPE members can also make their own personal contributions, if the PPE Agreement does not preclude this (of up to 450% of average monthly remuneration in the national economy forecast for a given year, not less, however, than for the previous year; in 2015, this is PLN 17,815.50); they are then deducted by the employer from employee remuneration.

Certain employers operating a PPE for their employees can also be plan members. This applies to individual entrepreneurs, partners that are liable without limitation in civil law partnerships (spółka cywilna), registered partnerships (*spółka jawna*), professional partnerships (*spółka partnerska*), partnerships limited by shares (*spółka komandytowo-akcyjna*) and limited partnerships (*spółka komandytowa*) and who are subject to pension and disability insurance. Persons who have entered into a civil law contract cannot participate in a PPE; they must have an employment contract.

PPEs may be organized in one of four forms

- An employee pension fund, created and managed by an employee pension society (private, non-profit institution; "PTE"); generally, a PTE can create and manage only one employee pension fund. A PTE has the form of a joint-stock company whose shareholders are employers or an employer. They can establish the PTE themselves or join one already existing on the market (there are currently five operating in Poland[7]). An employee pension fund entrusts its assets to a depositary; moreover, a fund may outsource the management of assets to asset management institutions (so far, all existing funds have done so[8]);

- An agreement on payments by an employer of employee's contributions to an open investment fund that is created and managed by a private investment fund society ("TFI"). This agreement may cover more than one investment fund managed by the same TFI. The employee thus has the right to change the fund or divide resources between the funds; transferring resources between funds during participation is permitted and does not cause any tax consequences;

- An agreement on group life insurance for employees with an insurance capital fund, entered into with a life insurance company;

- A foreign management. A foreign manager of PPE is one that is based in another EU Member State, subject to supervision in that State, which accumulates and invests funds for the purpose of their payment to pension plan participants when they reach retirement age (cf. point 8 of this chapter).

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7 EU Register of Institutions for Occupational Retirement Provision: https://eiopa.europa.eu/Pages/Supervision/Register-of-Institutions-for-Occupational-Retirement-Provision.aspx.

8 Association of Polish Economists [Towarzystwo Ekonomistów Polskich]. 2014. *The Supplementary Pension System in Poland – diagnosis and recommendations for change [Dodatkowy System Emerytalny w Polsce - diagnoza i rekomendacje zmian], page 28, http://tep.org.pl/wp-content/uploads/Raport-DSE-Towarzystwo-Ekonomist%C3%B3w-Polskich.pdf.*

Contributions made to employee pension funds and open investment funds are invested in their entirety. However, apart from the ability to invest funds for future pension benefits, the PPE managed by a life insurance company offers insurance benefits on specific events (e.g. on an employee's death or accident). According to the PPE Act, the cost of insurance protection cannot be less than 1% of the contribution paid by the employer, and at least 85% of this contribution and the entire contribution paid by an employee must be invested. However, capital transaction costs, depositary remuneration or asset management fees, amongst others, are covered from the assets of PPEs.

A PPE can be created for one or more places of employment, and if an employee is simultaneously employed at more than one employer he may obtain membership in a PPE at each one.

The obligation to accumulate and manage funds from employer and employee contributions lies with a financial institution or employee pension fund selected by an employer. The purpose of a PPE is to invest and grow funds in participant accounts on capital markets, in order to attain retirement security, paid at once or in instalments; the plan participants incur the investment risk, not the employer or plan manager.

The following must occur for an employer to create a PPE.

- Execution of an agreement with trade unions or, in their absence, persons selected by employees ("PPE Agreement");
- Execution of a preliminary agreement (prior conclusion of the PPE Agreement) and then an agreement with a financial institution managing a plan ("PPE Management Agreement"); and
- Plan registration by the Polish Financial Supervision Authority (the "KNF") as the public administration authority exercising state supervision over the financial market in Poland. Formal plan creation takes place and both agreements are effective on the date of register entry.

A PPE Agreement specifies all significant issues concerning PPE operation and plan participation, including the following:

- the form of plan and identification of the managing entity;
- conditions for a change of plan form or manager;
- the principles for plan participation and opting out from the plan by employees;
- the contribution levels (employer and employees' contributions) and the deadlines for their calculation and payment by the employer to the PPE employee's account;
- proposed terms and conditions for accumulating and managing funds;
- terms and conditions for payments, transfer payments and withdrawal of funds by employees;
- costs and fees of the plan manager and responsibility for payment by employer and / or employees;

- terms and conditions for unilateral suspension of payment of contributions by the employer and the terms and conditions for unilateral, temporary limitation by the employer of the amount of employer's contributions;

- terms and conditions for amending the PPE Agreement and relevant notice period thereof by employer.

The PPE Management Agreement specifies the terms and conditions for accumulating funds in PPE and managing these. Agreements are not concluded if a plan is created in the form of an employee pension fund. Provisions governing the accumulation and management of plan funds are then stipulated in employee pension fund by-laws.
A PPE Management Agreement is also not concluded if an employer is a financial institution and decides to manage a PPE itself. A PPE Agreement is then sufficient.

Tax issues associated with the operation of Employee Pension Plans

Participation in PPEs in Poland entails certain tax privileges, which are intended to promote their popularity.

An employer creating a PPE for employees has the right to include expenditures associated with the creation and operation of a PPE in accounting costs of generating revenue, e.g. employer's contributions to the plan. This allows for a reduction of the employer's taxable revenue.

Moreover, the employer's contribution to the PPE is not subject to obligatory social security contribution, as opposed to remuneration. It does, however, constitute revenue for the employee and for that reason it is subject to personal income tax. Tax is collected and remitted by the employer.

Additional contributions which the employees decide to contribute to the PPE are deducted from their net remuneration (i.e. after personal income tax and obligatory social security contributions have been deducted).

On the transfer of funds from a PPE to a new PPE or IKE, capital gains are exempt from 19% tax. A capital gains tax exemption also applies to an employee upon payment out of funds from a PPE as pension benefits.

Funds withdrawn by a participant are subject to 19% capital gains tax. In such case, the participant is also subject to a remittance of 30% of employer contributions to the participant's account at the Polish Social Insurance Institution[9] (this account is maintained within the first pillar of the Polish pensions system). The PPE manager remits the calculated tax and remittance amount to the tax office and the Polish Social Insurance Institution.

On the employee's death, the person entitled to the funds accumulated in the PPE may have these paid out or transferred to his IKE. These funds are exempt from 19% capital gains tax as well as inheritance and donation tax.

Transfer of funds, payment of pension benefits and withdrawal of funds from a PPE are not subject to personal income tax; this is neither a tax concession nor inducement, as funds paid into a PPE by an employer and employee have already been taxed before their payment into the PPE.

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[9] A 30% deduction only takes place in the case of plan contributions after 31 May 2004.

The specific conditions that must be met for a PPE participant to obtain a pay-out of pension benefits, transfer payment or withdrawal of funds accumulated in a PPE are discussed in point 3 of this chapter.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

Supervision of Employee Pension Plans compliance with the law

The KNF is the supervisory body overseeing compliance of PPE operations with the law. If information is obtained justifying a suspicion of improprieties in a PPE, the KNF is entitled to demand all information, documents and clarifications from an employer or managing institution. If improprieties in plan operations are uncovered, the KNF notifies an employer about these and calls for these to be rectified by a certain deadline. If improprieties persist, the KNF may impose a monetary fine upon the employer (up to PLN 50,000). In the case of foreign management, any identified improprieties must be notified to the foreign supervisory authority.

Irrespective of PPE supervision, the KNF also directly supervises institutions that manage PPEs, i.e. employee pension societies, investment fund societies and life insurance companies. Moreover, the KNF must approve the instruments offered by institutions through which funds accumulated on PPEs accounts are invested. They also have certain reporting duties toward the KNF.

Employee Pension Plans register

The KNF maintains a public PPEs register[10]. Plan registration is one of the conditions for PPE creation. The register includes PPE data such as, e.g.:

- information about the employer maintaining the plan and form of plan;
- conditions of plan membership and level of employer contributions as well as a minimum additional employee contribution, together with deadlines for paying the contributions to the plan participants' accounts;
- the notice period for terminating plan membership;
- costs and fees to plan participants.

Employer reporting duties

An employer must provide information to the KNF about an administered PPE by 1 March of a given year in respect of the preceding year. Such information should include, e.g.:

- the number of plan participants at the end of each quarter of a given year;
- the number of hired employees at the end of a given year;

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[10] Employees' Pension Plans register: http://www.knf.gov.pl/Images/PPE_23042015_tcm75-5913.xls.

- the total amount of contributions transferred to a PPE in a given year;
- the number of pension benefit payments and transfer payments (distinguishing between transfer payments to another PPE and to an IKE) in a given year;
- information on unilateral suspension by an employer of payment of its contributions to PPE or a temporary limitation of the level of employer contributions.

The KNF makes key decisions with regard to a PPE in a form of administrative decision, e.g. on registration, entry of changes in the plans register, deletion of a plan from the register, permission to suspend payment of employer contributions or the imposition of a monetary fine upon an employer. These decisions are subject to appeal through administrative court proceedings.

Consent for disposal of funds accumulated in an Employee Pension Plan

The PPE Act specifies conditions that must be met for a PPE participant to obtain a pay-out of pension benefits, transfer payment or withdrawal of funds accumulated in a PPE (these are discussed in point 3 of this chapter). Consent of the employer, institution managing a PPE, KNF or any other entity is not such a condition.

A plan participant can also file a statement terminating membership in a PPE at any time. The PPE Agreement specifies the termination notice period, which can be between one and three months. Despite opting out from participation in a PPE, funds accumulated on an account remain on a PPE until conditions for pay-out, transfer payment or withdrawal of funds are met.

QUESTION 3

How are the plans governed?

An employer creating a PPE decides on the plan form, specifies the terms and conditions for its operations (e.g. the employer's contribution amount), and chooses the institution to manage the plan. The proposal prepared by the employer should be subject to negotiations with employees' representatives, who should receive a formal offer from the employer. The last word, however, belongs in practice to the employer; it can, for instance, withdraw from its intention to create a PPE should it not be possible to come to an agreement with employees' representatives on the form and the terms and conditions of the PPE being created.

The operation of the PPE is financed primarily by employer contributions. Each and every permanent change in the amount of these contributions during the PPE operation requires the consent of employees' representatives and amendment of the PPE Agreement. If the terms and conditions of PPE operation do not preclude the opportunity for employees to also pay individual contributions, the employee can at any moment declare the payment of these, withdraw from paying them, or increase or decrease the contribution amount.

Irrespective of the form of operation chosen for the PPE[11], the fund assets are recorded, managed and invested by the chosen manager - financial institution or the employee pension fund (also in cooperation with an asset management institution); whereas the employer does not take part in these activities and only participates in administering the plan. The scope of the employer's obligations includes, among other things:

- notifying employees about the terms and conditions for plan operation;
- calculating and paying monthly plan contributions; and
- receiving and delivering to the plan manager declarations of will from employees regarding the plan, including declarations on joining the plan or withdrawing from it, on increasing or decreasing employee contributions, on payment of pension benefits or transferring payment of funds.

Plan participants usually have a choice from among different investment strategies offered by the plan manager. Participants in a PPE operating in the form of an employee pension fund generally do not have such choice. However, participants have special supervisory entitlements, as at least half of the members comprising the supervisory board must be participants. The employer may carry out cyclical analyses of the investment results attained by the plan manager and, if required, negotiate with trade unions or, in their absence, persons selected by employees, a replacement of the managing institution.

Pay-out of pension benefits from a PPE may be one-off or in instalments and is only possible when the participant meets certain statutory conditions:

- acquires pension rights, reaches the age of 55 and files for pay-out of pension benefits;
- reaches the age of 60 and files for pay-out of pension benefits; and
- reaches the age of 70 and has no employment with an employer maintaining a plan, even without filing for pay-out of pension benefits.

In certain situations the PPE participants are entitled to transfer funds from a PPE to a new PPE or IKE or to withdraw them from a PPE. A participant obtains the right to transfer funds when no longer working for an employer operating a PPE or in case of PPE liquidation, e.g. as a result of employer bankruptcy. If a participant who has ceased to be an employee does not decide on transfer payment, the funds of the participant remain accumulated in his PPE account and continue to be managed by the managing institution acting within the framework of the plan. Funds can be withdrawn by a participant in the event of PPE liquidation and non-transfer of funds to a new PPE or an IKE.

On the participant's death, the person entitled to the funds accumulated in the PPE (i.e. an heir of a participant or a person or persons designated as beneficiary) may have these paid out or transferred to his IKE.

[11] Cf. point 1.2 of this chapter.

The employer may unilaterally temporarily restrict the amount of his contribution or unilaterally suspend the remittance of contributions due from him (up to 3 months in a period of 12 consecutive months, which period may be extended to 6 months in the PPE Agreement). After the allowed period of suspension, the employer may, should this be justified by the financial situation, conclude an agreement with the employees' representative on a further suspension of calculating and remitting employer's contributions (for a period not longer than 24 months in the next 48 months, unless the further calculating and remittance of contributions would result in the need to apply for employer's bankruptcy; in such case, it is possible to extend the agreement for a further 24 months, and after their expiry to conclude a new agreement). The agreement shall be submitted to the KNF; it shall be binding at the earliest upon KNF entry of the agreement into the register.

An employer may also unilaterally decide to liquidate the PPE, provided that at least a 12 month termination notice period has been observed when previously remittance of contributions to the PPE was suspended for at least three months or their amount limited. A PPE may also be liquidated with the consent of employee representatives without notice.

PPE should also be liquidated in several other instances provided for in the PPE Act, for example, liquidation or insolvency of the employer or decrease in the value of funds accumulated in PPE below the amount set in the PPE Agreement.

QUESTION 4

Is there a compensation fund for pension benefits?

Pay-out of pension benefits from PPE is not covered by any state or other compensation fund.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

Employer bankruptcy has no impact on PPE participants' entitlement to funds accumulated in the plan. If employer bankruptcy is declared, PPE funds are not part of the employer's bankruptcy estate. Contributions to the PPE are transferred by the employer on a continuing basis to participants' accounts which are not maintained by the employer.

Employer bankruptcy generally leads to liquidation of a PPE. At such time plan participants are entitled to: transfer payment of accumulated funds to an account at another PPE or at IKE; payment of pension benefits if statutory requirements are met, or to obtain withdrawal of accumulated funds. Plan participants may submit all associated declarations of will directly to the institution managing a PPE, thus without participation of the bankrupt employer or official receiver or administrator of bankruptcy estate.

The security of current PPE assets is also legally guaranteed in the event of the bankruptcy or insolvency of the institution managing the plan or depositary. The insolvency of the employees' pension society managing the fund or depositary to whom the employees' pension fund has entrusted its assets does not affect the funds held in the PPE. They do not form part of bankruptcy estates of the employees' pension society and the depositary. Moreover, the employees' pension fund itself, although it has legal personality, cannot become bankrupt. The foregoing applies also to open investment funds and TFIs.

In turn, life insurance companies should have technical provisions sufficient to cover the claims of PPE participants under insurance contracts. If the insurance company is declared bankrupt, a separate bankruptcy estate is created from these reserves, allocated to meet the claims arising from insurance contracts and estate liquidation costs. Moreover, payment out of the insurance sum in that part not covered by technical provisions is guaranteed by the Polish Insurance Guarantee Fund, up to half of its amount but not more than EUR 30,000. The guarantee is activated on the event of bankruptcy of an insurance company, if a petition for bankruptcy has been dismissed, on the discontinuance of bankruptcy proceedings of an insurance company, if its assets are insufficient to cover the costs of the bankruptcy proceedings, or if the compulsory liquidation of an insurance company that does not fulfil insurance benefits is ordered.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

PPEs belong to the group of DC pension plans, so by definition they cannot be underfunded and face pension deficits. Neither the employer nor the institution managing a plan guarantees a specific amount of pension benefits. The amount of pension benefits due from these plans to future retirees depends on the level of contributions to a PPE and capital gains from investment of funds rather than on a formula involving years of service and salary levels, such as most commonly in DB pension plans.

Plan participants incur the investment risk. If the contributions paid into PPEs are not successfully multiplied by the managing institution or if investments made within PPE operations generate losses, the PPE participants will not receive adequate retirement benefits.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

Please see point 6 of this chapter.

QUESTION 8

Are there any cross-border features of your pension regime?

Foreign management form of Employee Pension Plan

Directive 2003/41/EC[12], has been implemented into Polish law, aimed at creating an internal market of employees' pension plans within the European Union and grounds for the operation of cross-border employees' pension plans.

As a result of the implementation of Directive 2003/41/EC to the PPE Act, an employer may establish a PPE that will be managed by a financial institution based in another EU Member State (foreign management form of PPE).

A condition for establishing a foreign management of PPE is obtaining consent from the KNF and relevant supervisory authority from the EU Member State from which the institution chosen by the employer originates. After granting permission for the creation of PPE the KNF also notifies The European Insurance and Occupational Pensions Authority and the foreign supervisory or regulatory authority.

Pursuant to the PPE Act, contributions from employer and participants in a PPE operating under foreign management should be accumulated in accordance with the rules specified in this Act. If co-operation is established with an insurance institution, the rules relating to contract with a national insurance company should apply, and if this institution has legal personality and the employer is its shareholder, the rules on the operation of PPE in the form of an employees' pension fund should apply. The KNF supervises the financial institution's compliance with Polish law to the required extent; where irregularities are found, KNF immediately informs the foreign supervisory authority.

Employee Pension Plan established by a foreign employer

In turn, implementation of Directive 2003/41/EC to the OIFFE Act enabled employers from other EU Member States, a state in the European Economic Area not being a member state of the European Union or Swiss Federation to establish PPEs in Poland in the form of employees' pension funds. To this end the foreign employer must create or become the shareholder of the employees' pension society.

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[12] Directive 2003/41/EC of the European Parliament and of the Council of 3 June 2003 on the activities and supervision of institutions for occupational retirement provision.

The OIFFE Act provides an exception that allows a foreign employer to institute a PPE in Poland also in the form of a DB pension plan or else a mixed DB/DC pension plan. The reason is to let a foreign employer utilize a PPE to provide a pension plan of the type being run in its home country for employees in Poland; the foreign law appropriate for an employee pension scheme of a foreign employer is then applicable for the implementation of a plan in Poland.

However, for this purpose an employees' pension fund managing a PPE on behalf of a foreign employer must enter into an additional agreement with a life insurance company. In the framework of this agreement the life insurance company will take on the coverage of all biometric risks related to death, disability or longevity or guarantees investment results and a given level of benefits associated with running the DB or DB/DC pension plan for the foreign employer. The life insurance company should have technical provisions sufficient to cover the claims of PPE participants under an insurance agreement.

Establishing a PPE in Poland in the form of a DB pension plan or as a mixed DB/DC pension plan the foreign employer is also obliged to take on liability from the life insurance company in the scope following from the agreement entered into between the insurance company and the employees' pension fund, in particular for the event of the foreign employer ceasing to regularly remit contributions to the insurance company. Moreover, the foreign employer incurs liability in respect of obligations associated with aforementioned biometric risks or guarantees in the scope not covered by the insurance company's liability.

The OIFFE Act contains a number of detailed regulations concerning the running of a PPE in the form of DB or DB/DC pension plan, in particular the obligation to maintain appropriate assets, liabilities and reserves at the insurance company for obligations arising out of the agreement with the employees' pension fund. For example, this Act allows KNF to limit or prohibit a life insurance company from freely disposing of assets that secure obligations arising from the agreement concluded with an employee pension fund, where there is a risk that it will not be able to cover pension deficits. This is a basis for mandatory termination of the contract and concluding a new contract with another insurance company.

It should be pointed out that so far not one PPE has been established in Poland in any of the above cross-border forms, and hence there is a lack of practice as regards organising cross-border type PPEs in Poland. In the author's opinion, it seems unlikely that such plans will be created for foreign employers in Poland in the foreseeable future.

QUESTION 9

Discuss the state of defined benefit plans in your country

The reform of the Polish pension system in 1999, and the creation of the three pillar pension system was to have been a response to the demographic and fiscal challenges faced by Poland. In introducing the PPEs as the third pillar form of DC pension plans, the Polish legislature assumed that funds accumulated in these would satisfactorily supplement the amounts of retirement benefits from the first and second pillars and play an important role in balancing the pension system. Despite this PPEs are still not popular in Poland.

There are only 1,075 PPEs registered in Poland (as of 23 April 2015)[13], which have a total of approximately 381,000 participants (as of 31 December 2014; participation rate at a level of approx. 70%), having accumulated funds of around PLN 10.2 billion (as of 31 December 2014). This represents somewhat less than 2.5% of persons working in Poland. By comparison, the Polish Central Statistical Office has estimated that at the end of 2014 there were around 73,000 commercial companies that employed at least 10 persons, and around 341,000 commercial companies employing between 0 and 9 persons. For many years the rate of growth for the number of PPEs has been negligible - already in 2006, the number of functioning PPEs was close to 1,000. What is more, the register maintained by the KNF shows that in recent years the number of operating PPEs has been decreasing instead of increasing.

The low popularity of the PPEs has led to the introduction of two types of private pension savings – IKE (in 2004) and IKZE (in 2012) that have also not been overly popular to date (at the end of 2014, IKE membership was 824,485 persons, with 528,142 persons in IKZEs).

Studies on the Polish pension system underline that in light of economic and demographic conditions, a retirement pension system without widespread private pension plans and savings will prove insufficient to guarantee a future adequate level of retirement benefits for Polish retirees (the level of replacement rate). Further reforms are therefore required in Poland in order to develop and popularise private pension plans and savings. This is an unavoidable direction for the Polish pensions system in coming years. This is currently a hot topic in Poland; two examples are provided below.

In its 2014 report *“Poland - Country economic memorandum: saving for growth and prosperous aging*”, the World Bank presented several policy recommendations on changing the Polish pension system. These were intended to popularise private pension plans in Poland. The authors of the report propose actually an amended model of PPE. They noted that international experiences demonstrate that passive savings by earners at the bottom half of income scale can be increased through automatic enrolment pension plans; their inaction may result that most of them stay in the system.

[13] Employees’ Pension Plans register: http://www.knf.gov.pl/Images/PPE_23042015_tcm75-5913.xls, accessed on 26 April 2015.

The following amendments to a PPE are proposed: all employers should be required to enrol new employees in a PPE, into which employer contributions will be paid regularly, as well as an equivalent employee's contributions (deducted from salaries); the government may also make a contribution to the participants account to initiate their individual's savings (form of sign-on bonus or additional regular flat payments). The employee would have a specific period of time in which he or she could opt out of the plan. Contributions to the plan would be tax free for the employee, but pay outs to the contributor would be taxed as income. There would also be an equivalent system for those not in employment, but who also wish to use this scheme. The law should permit the withdrawal of the assets accumulated in a PPE before retirement for some specified purposes, e.g. acquiring a house or for medical emergencies. Moreover, part of the assets accumulated in a PPE should be blocked as pension benefits for a time after the retiree has reached the age of, say, 80-85, to ensure that the pensioner does not suffer poverty when the earlier pay outs run out[14].

In the same year, upon the initiative of the Chancellery of the President of Poland, a report was prepared by the Association of Polish Economists on *"The Supplementary Pension System in Poland – diagnosis and recommendations for change"*. The purpose of the report is to commence discussions on necessary changes to the supplementary pension insurance system in Poland and to work out a target form for the third pillar of the Polish pension insurance system[15]. This report was the subject of debate during the Public Debate Forum on "How to guarantee equitable income for old-age – the role of voluntary pension savings", held at the Chancellery of the President of Poland in January 2015[16].

Authors of the report also propose making the PPE plan mandatory, with an opt-out option for employees. Contributions would be paid by the employer and the employee (1-3% of salary each; both contributions would be taxed). The obligatory nature of the PPE would cover, firstly, employers where plans already operate and employers employing 250 or more people. The system would also cover, among others, public sector entities and persons employed under civil law contracts. After 5-10 years of operation, the system could also be extended to small and medium-sized enterprises. A fundamental novelty of the system would be the creation of so-called national occupational programs, from which the employer would select two which his employees could join.

The views expressed in this article do not represent the official standpoint of Wardyński & Partners.

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[14] World Bank. 2014. Poland - Country economic memorandum: saving for growth and prosperous aging. Washington, DC: World Bank Group, points 37 and 209 et seq., http://documents.worldbank.org/curated/en/2014/06/20291843/poland-country-economic-memorandum-saving-growth-prosperous-aging, accessed on 26 April 2015.

[15] Association of Polish Economists [Towarzystwo Ekonomistów Polskich]. 2014. The Supplementary Pension System in Poland – diagnosis and recommendations for change [Dodatkowy System Emerytalny w Polsce - diagnoza i rekomendacje zmian], http://tep.org.pl/wp-content/uploads/Raport-DSE-Towarzystwo-Ekonomist%C3%B3w-Polskich.pdf.

[16] The Chancellery of the President of Poland website: http://www.prezydent.pl/dialog/fdp/solidarne-spoleczenstwo-bezpieczna-rodzina/aktualnosci/art,32,konieczne-dalsze-zmiany-w-systemie-emerytalnym.html, accessed on 26 April 2015.

RUSSIA

QUESTION 1

What is the legal framework for private pension plans in your country?

Overview

Private pension provision

The private pension provision is provided by non-state pension funds as separate legal entities. The contract for the private pension provision is concluded between the non-state pension fund and the individuals or the sponsor (employers or other third parties). The non-state pension fund provides pension benefits to individuals.

Individuals may make contributions in favour of themselves or employers may act as sponsors by providing contributions under the rules that have been established.

When conditions of the pension benefits payments have been met, the non-state pension funds pay benefits to individuals as participants in the private pension system.

The non-state pension fund is entitled to accumulate pension contributions, to invest them in order to make a profit and then to provide pension benefits to participants.

Private pension insurance as one of the insurance options

Pension insurance is one of the options for private pension plans.

Pension insurance is provided by insurance companies under an insurance contract concluded between the insurance companies and individuals as insured persons and beneficiaries at the same time, or by the sponsor in favour of the individuals (beneficiaries).

Pension insurance as endowment life insurance can also provide additional pension benefits.

The insured risks are (i) reaching the age specified in insurance contract or (ii) dying before reaching this age.

The insurance pension benefits are to be paid by the insurance company for life or for a specified period as monthly additional pension. When the risk insured is the death of the insured person (i) the pension benefits shall be paid to the heirs if the guaranteed period has been determined; or (ii) the sum of pension contributions shall be paid to the heirs if the death occurred prior to the payment pension date.

Additional insurance contributions to the funded pension as a part of state pension

State pension in Russia consists of insurance pension and funded pension. Pension insurance is financed by obligatory contributions of an employer for the employee and shall not be placed in a special account, but only the sum of these contributions may be included.

The Government has decided not to divide the pension contributions from the employers between the insurance pension and funded pension. In 2015, all obligatory contributions from employers shall be referred only to the insurance pension.

But the opportunity to make voluntary contributions to the funded pension by individuals or employers is still provided for by the Russian law and can be used as a way of investing in future pensions.

Additional insurance contributions to the funded pension provide an opportunity to increase the state pension by voluntary additional contributions to the state pension system.

After paying the contribution, such funds become a part of all other funds accumulating in the state pension system and shall be located in a special account of the individual in the state pension system. These contributions are investment funds and the pension capital of the individuals that shall be repaid monthly as part of the state pension to individuals after reaching a retirement age.

Where the contributions are voluntary, these form a specific private pension plan in the state pension system.

All of these ways may be used to invest funds for the future. But they are not wide-spread in Russia. The main reasons for this are the instability of the Russian economy and the intention of the people to invest in other instruments to save their funds.

The lack of popularity of long-term accumulation programs in Russia can also be explained by several additional reasons: uncertainty of people in the long-term stability of the economic situation; and the small number of people that can make additional savings for a long-term period; and people not having a habit of keeping their savings for a long-term period (10-20 years). The longest planning time-frame generally does not exceed 5-6 years, which is not appropriate for private pension plans.

Legislation for private pension plans

Private pensions and retirement plans are governed by the following main statutes and regulations with regard to the ways of private pension plans:

Private pension provision

Private pension investment is regulated on the federal level by the “Federal law on Non-state Pension Funds” No 75-FZ dated 7 May 1998.

It defines the main rules for incorporation of the non-state pension funds and requirements for their business activity (assets, licensing, guarantees and others). “The Federal law on Non-state Pension Funds” No 75-FZ dated 7 May 1998 also regulates the rules of the pension contract that is the base of private pension provision, main requirements to pension programs, rules of investing funds by non-state pension funds and procedures for control of such investments.

Under this main law, the Government of the Russian Federation has enacted special regulations such as Government Regulation on “Enactment Requirements to Pension Schemes of Non-state Pension Funds that are used for Private Pension Provision” No 1385 dated 13 December 1999, Government Regulation on “Enactment the Rules of Accounting the Pension Funds by Non-state Pension Fund” No 817 dated 15 August 2014 and others.

A significant part of the legislation is administrative regulation by the Central Bank of the Russian Federation (previously the governing body was the Federal Service on Financial Markets of the Russian Federation) (the "Central Bank") that is a regulatory body which oversees, inspects and monitors the private pension sector.

Among others, the Central Bank of the Russian Federation (previously – Federal Service on financial markets of the Russian Federation) has enacted regulations on detailed requirements for accounting and reporting, internal control system of the non-state pension funds.

Private pension insurance as one of the insurance ways

The main statutory Act regulating pension insurance is the Law of the Russian Federation on the "Organisation of Insurance Business in the Russian Federation" No 4015-1 dated 27 November 1992.

It is the main Act for all forms of insurance including pension insurance. On the basis of this main statute the Central Bank is the regulatory body in insurance as well as in private pension provision and enacts other detailed regulations with respect to all forms of insurance including pension insurance.

Mostly these Acts regulate the accounting and reporting of the activities of the insurance companies, the procedure of notification about forms of insurance, licensing and other questions of control and supervising the insurance business of the insurance companies.

According to the general rules for insurance business every insurance company which has an intention to run pension insurance business must adopt the rules of pension insurance that include pension programs and all other details of pension insurance.

Additional insurance contributions to the funded pension as a part of state pension

Additional insurance contributions to the funded pension provide an opportunity to increase the state pension by voluntary additional contributions to the state pension system.

In general the funded pension as part of the state pension is regulated by "Federal Law on Funded Pensions" No 424-FZ dated 28 December 2013.

The procedure and conditions of additional contributions were stipulated in the "Federal Law on Additional Insurance Contributions to Funded Pension and State Support for Formation of Pension Capital" No 56-FZ dated 30 April 2008.

According to the aforementioned law, additional contributions can be made by employers as well as the individuals by themselves. There are no exceptions to make such contribution by one individual to another.

The aforementioned Federal law is directed to stimulate the formation of pension investments and increase the level of state pension provision and stipulates the procedure of voluntary entry into the state pension system in order to contribute additional funds to funded pension and procedure and conditions for additional insurance contributions to funded pension, additional contributions of employers as well as provision with state support for formation of pension capital.

Russian tax legislation concerning private pension plans

First of all it is important to note that under the Tax Code of the Russian Federation insurance services, as well as services of private pension provision by non-state pension funds, are not subject to taxation of VAT.

Moreover, as per corporate income tax (i) the additional contributions to the funded pension as part of the state pension system in favour of the employees and (ii) contributions made by employers under the voluntary insurance contracts (contracts of private pension provision) concluded in favour of employees with insurance companies (non-state pension funds) that have a license, are considered to be labour costs. These costs can be taken into consideration to calculate the tax base of the corporate income tax.

Russian legislation further, provides individuals and employees with tax exemptions for these contributions with regard to individual income tax.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

The Central Bank supervises and monitors private pension activity to protect the rights and interests of the participants, insured persons and other interested parties and its main objectives are to:

- adopt regulations on the pension business activity of the non-state pension funds;
- adopt the Acts on the regulation, monitoring and oversight of the non-state pension funds;
- carry out licensing of private pension provision;
- approve the pension rules of non-state pension funds;
- consider complaints (applications, references) of individuals and legal entities of the violations of the Federal legislation; and
- attract non-state pension funds, as well as their officials to administrative responsibility in the manner prescribed by federal legislation of the Russian Federation.

Russian legislation stipulates rules and requirements for the investment activity of the non-state pension funds to guarantee the safety of pension contributions.

Non-state pension funds are entitled to invest pension reserves by themselves as well as through a management company, in government securities of the Russian Federation, bank deposits and other investment objects provided by the Bank of Russia.

Also there are special rules for management companies with regard to the investing of pension reserves, rights and limitations for such investing.

At least 85% of the net income from the investment of pension reserves shall be directed to increasing the pension reserves. The same rule is passed for the pension accumulation fund.

All non-state pension funds must report on their activities to the Central Bank of Russia annually.

Moreover, each of the non-state pension funds must submit the conclusion of the actuarial valuation carried out by an actuary at the end of the year. This is an integral part of the annual report of the fund.

Pension insurance is conducted by insurance companies

The insurance business is licensed by a regulatory body and all insurance companies must be included in Register of Members of Insurance Business Activity.

Insurance companies assess the insurance risk, receive insurance premiums (premiums), generate insurance reserves, invest their assets, determine the amount of loss or damage, make insurance payments, and carry out other actions related to the performance of obligations under the insurance contract.

Each insurance company must ratify the Pension Rules that is the main document under which the insurance contract is concluded and which determines all issues of insurance such as pension plans, insurance risks, insurance premium, procedure for determination of the losses and damages, procedure for the conclusion of the insurance contract and rights and obligations of the parties.

Regulation is by the Central Bank to ensure compliance with insurance legislation, the prevention and restraint of violations of insurance legislation by the participants in the insurance relations, protection of the rights and legal interests of all interested parties and the state, and the effective development of the insurance business.

Regulation is carried out by the following methods:

1. Licensing of insurance entities and maintenance of a unified state register of insurance entities, registry associations of insurance entities;

2. Monitoring compliance with insurance legislation, including through on-site inspections of insurance entities, and reliability of their reporting, as well as providing insurers of their financial stability and solvency.

All insurance companies must provide the Central Bank of the Russian Federation with special reports which include:

- Report on the structure of assets;
- Report on insurance reserves;
- Report on solvency;
- Report on the operations of reinsurance;
- Report on the financial result relating to the type of insurance.

All reports include the whole activity of the insurance companies (including pension insurance) and the activity of all branches and subsidiaries of such insurance companies.

QUESTION 3

How are the plans governed?

Private pension provision

The non-state pension fund is regulated according to the current legislation, the Charter of the Non-State Pension Fund and Pension Rules.

The Pension Rules must be approved in accordance with the legislation of the Russian Federation by the Board of Directors of the fund and are to be registered in the manner prescribed by the Central Bank of Russia.

Private pension provision is realised on the basis of the contract on private pension provision.

This contract is concluded between the non-state pension fund and sponsor in favour of the participants and regulates the obligations of the sponsor to pay the contributions and the obligations of the non-state pension fund to pay the benefits to the participants.

A sponsor can be an employer in favour of the employee (the individual) or an individual in favour of himself.

Employers are not required to be sponsors of private pension plans. In most cases, the pension programs form part of the benefits provided by the employer. Generally, they are specified in local labour documents or in collective agreements (or other similar agreements). The employer specifies the conditions for employees and procedures for taking part in pension programs. In some cases employers can appoint special committees to co-ordinate the corporate pension provisions.

The programs of private pension provisions are offered by large state-owned companies. In private companies the programs of private pension provisions are not widespread.

Private pension insurance

There is no specific regulation for pension insurance. The pension insurance contract is concluded between the employer and insurance company in favour of the employee, but is obligatory for employers.

In practice, if the employers want to provide additional pension plans for their employees they do it by means of the private pension provision described above. Additional insurance contributions to the funded pension as a part of state pension.

Under the “Federal Law on Additional Insurance Contributions to Funded Pension and State Support for Formation of Pension Capital” No 56-FZ dated 30 April 2008 the employers are entitled to make additional contributions to the funded pension of their employees.

There is no obligation of employers to make any contributions to the funded pension for their employees. The employers are entitled to make such contributions. Such decision can be contained in local act or included in the labor contract or collective agreement between employer and employees.

In the case of the termination of the relationship between employer and employee, payments of such contributions terminate as well, starting from the moment of the termination of the labour contract.

The amount of contributions to be paid by the employer is determined on a monthly basis in respect of each employee (insured person) in favour of whom the contributions are to be paid.

Employer contributions are included in the funded pension of insured persons in whose favour such contributions are to be paid.

Additional employer contributions to the funded pension are transferred by the employer to the budget of the Pension Fund of the Russian Federation in the manner and within the timeframe established by the Federal Law "On Mandatory Pension Insurance in the Russian Federation" No 167-FZ dated 15 December 2001 in respect of payment of premiums for mandatory pension insurance.

QUESTION 4

Is there a compensation fund for pension benefits?

Private pension provision

Every non-state pension fund must create pension reserves to secure the fulfilment of its obligations under the contract on the private pension provision.

Pension reserves include reserves for covering pension benefits and insurance reserves.

Pension reserves are the accumulated cash resources owned by the non-state pension fund and aim to fulfil by the non-state pension fund its obligations under contracts on the private pension provision.

Pension reserves can be composed of:

- pension contributions;
- income from the investment of pension reserves;
- special-purpose revenue; and
- other property determined by the Board of Directors of the non-state pension fund to cover the negative result from the investment of pension reserves.

There is an obligation for non-state pension funds to keep the cash of pension reserves in credit institutions which meet the requirements specified in the legislation of the Russian Federation to the credit organisations – participants of the deposit insurance system of individuals of the Russian Federation.

The funds of pension reserves and assets, in which pension reserves are invested, cannot be levied on debts of non-state pension fund (except cases specified by Russian legislation) and other specialised depository third parties, including the insured persons and participants, they also cannot be an object of interim measures including the seizure of assets.

The Central Bank of the Russian Federation shall determine the normative standards of pension reserves for defined pension schemes of non-state pension fund.

1. Reserves for covering pension benefits

   For reserves for covering pension benefits the non-state pension fund shall open a separate bank account and special account for the securities in which the pension reserves were invested.

   In whole the normative standards of reserves for covering pension benefits are the minimal value, sufficient to cover all pension benefits.

   The normative standards of reserves for covering pension benefits are equal to paid value of pension obligations determined as contemporary value of the pension obligations under the contracts on private pension provision in force reduced to the contemporary value of the future pension contributions which shall be paid under the mentioned contracts.

   Determination of contemporary value of the pension obligations under the contracts on private pension provision in force shall be made in accordance with the methodology specified in Pension Rules of the non-state pension funds.

2. Insurance reserves

   Insurance reserves shall be formed for stability and fulfilment of the obligations to participants of the non-state pension fund. Insurance reserves shall be separately accounted.

   Normative standards of insurance reserves are determined by the non-state pension fund. Normative standards of insurance reserves must be 5% and more of the smaller values:

   - the value of the reserves for covering pension benefits at the beginning of the year; or

   - the value of the reserves for covering pension benefits at the end of the year.

   Insurance reserves can be used for:

   - renewal of the reserves for covering pension benefits in order to keep the reserves for covering pension benefits in compliance with the obligations of payment by non-state pension fund the pension benefits to participants; and

   - renewal of the reserves for covering pension benefits in accordance with the recommendation of the actuary set forth in the actuarial report.

Also the insurance reserves can be used for renewal of the reserves for covering pension benefits in case of decreasing the pension reserves as a result of their investments.

Pension insurance as one of the insurance ways

All insurance companies maintain insurance reserves to guarantee the fulfilment obligations of insurance. Insurance reserves require actuarial assessment of the obligations to pay further insurance payments under the insurance contracts and perform other insurance obligations. Insurance reserves shall be used only for fulfilment of insurance obligations.

Insurance companies are obliged to invest the reserves on the basis of diversification, liquidity and profitability of repayment. Insurance companies do not have the right to invest insurance reserves in bills of exchange of legal entities and individuals and to lend the insurance reserves, except as stipulated in Russian legislation.

Additional insurance contributions to the funded pension as a part of state pension

As part of the state pension system, reserves in respect of additional insurance contributions to the funded pension are regulated in the same way as mandatory pension insurance.

Thus, every non-state pension fund must create a pension accumulation fund to fulfil its obligations with respect to the state pension payments (and in particular concerning the additional insurance contributions to the funded pension).

A pension accumulation fund includes accumulation of sums of all pension resources owned by a non-state pension fund and it is necessary to be fulfilled by non-state fund its obligations with regard to state pension insurance including cash resources that were provided as additional insurance contributions to the funded pension.

There is no special amount of such fund, but there are obligatory cash assets of which the pension accumulation fund is composed. For example, additional pension contributions to the funded pension are a part of such accumulation fund as well as cash assets transferred to the trust fund management company in accordance with this federal law and other cash assets stipulated in Russian law or determined by the Board of Directors of the non-state pension fund in order to cover the negative result of the investment of pension assets.

The following resources shall be included in the pension accumulation fund: (i) cash resources for payments of funded part of state pension and (ii) cash resources for special pension payment that shall be provided to the insured person which (or in favour of which) the additional contributions to funded part of state pension had been made.

Pension accumulation fund and assets, in which pension accumulation fund is invested, cannot be levied on debts of non-state pension fund (except cases specified by Russian legislation) and other specialised depository third parties, including the insured persons and participants, they also cannot be an object of interim measures including the seizure of assets.

Moreover, every non-state pension fund must establish reserves of mandatory pension insurance to secure the fulfilment of the obligations to participants of the non-state pension fund including participants which (or in favour of which) the additional contributions to the funded part of the state pension had been made.

Russian legislation stipulates the value of this reserve on the base of percentage of the special indicator (accounting base).

From 1 January 2018 the reserve of mandatory pension insurance must be not less than 1% and not more than 10% from the accounting base on 31 December of every year.

The rate of annual contributions to the reserve of mandatory pension insurance cannot exceed 0,5 % of the accounting base.

In case the value of the reserve of mandatory pension insurance exceeds 10% of the accounting base on 31 December of the year, the annual contributions to this reserve for such a year are not made by the non-state pension fund.

Accounting base consists of the sum of the average net assets held in trust for all contracts of trust management, cash resources for payments of funded part of state pension and cash resources for special pension payment that shall be provided to insured person which (or in favour of which) the additional contributions to funded part of state pension had been made, and assets on account(s) as of 31 December of the year.

The reserve of mandatory pension insurance can be used for:

- guarantee renewal of the pension assets of the non-state pension funds in accordance with the Russian legislation,

- pension payments to successors of the deceased insured person in cases stipulated by the Russian law.

The reserve for mandatory pension insurance must also be separately accounted.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

The Russian pension system and the pension insurance in Russia is organised in a way that the employers are only contributors (sponsors) who pay the contributions in favour of the employees as a social benefit. They do not pay pensions when their employees retire.

In the case of insolvency of the employer, further contributions in favour of the employees are terminated and the pension is paid based on the actually transferred contributions.

All functions of accumulating the contributions and then payment of the pension are conducted by non-state pension fund or insurance companies (in case of pension insurance) and Russian law stipulates special rules in case of insolvency of the non-state pension funds and insurance companies.

All or some measures can be applied to recover the solvency of a financial organisation and shall be included in the plan of recovery of the solvency that shall be developed and accomplished by non-state pension fund and its management bodies or the interim administration (if any).

Private pension provision

For non-state pension funds that provide private pension provision the special grounds for application of these measures to prevent insolvency are stipulated, they are:

- decrease normative value of pension reserves for pension schemes with defined pension benefit for the quarter of the current year less than the amount provided for regulated body; and
- confirmation the increase of the actuarial deficit on the results of the annual actuarial valuation of the activities of non-state pension fund compared with the previous year.

In the case of the occurrence of the aforementioned grounds, the non-state pension fund must provide to the Central Bank of the Russian Federation the plan of recovery of the solvency in case at the same time there are no signs of bankruptcy. After receipt of this plan the Central Bank is entitled to appoint an interim administration to recover the solvency of non-state pension fund.

There are no special rules regarding the fulfilment of the contracts of the private pension provisions in periods of recovering the solvency, but these contracts are to be terminated from the date of the court decision under which the non-state pension fund was adjudged a bankrupt.

Within three months from the date of the arbitration court's decision on the recognition of the non-state pension fund as bankrupt and the opening of bankruptcy proceedings, the bankruptcy trustee:

1. notifies in writing investors and participants of the non-state pension fund on the adoption of a decision of the arbitration court on the recognition of non-state pension fund as bankrupt and the opening of bankruptcy proceedings, not later than thirty days from the date of adoption of the decision by the court;
2. defines the obligations of contracts on the private pension provision (including the obligations to pay the designated pensions benefits) on the information available to the non-state pension fund;
3. determines the structure of creditors whose claims are to be satisfied at the expense of pension reserves, and the amount of the bill payable;
4. determines the market value of the assets constituting the pension reserves traded on organised trading, engages an appraiser to determine the market value of other assets constituting the pension reserves and other assets that make up its own property of the fund.

Within six months starting from the date of the arbitration court's decision on the recognition of the non-state pension fund as a bankrupt and the opening of bankruptcy proceedings, the bankruptcy trustee takes all actions to provide:

1. payments or transfers to other non-state pension funds redemption sums of the participants, or transfer them as payments of premiums on insurance pension contracts concluded with insurance companies;

2. transferring of obligations for payment of lifelong private pension benefits and pension reserves to another non-state pension fund.

Pension insurance as one of the insurance ways

Insurance companies as financial organisations also meet the requirements described above.

The “Federal law on Insolvency (Bankruptcy)” specified special rules for the insolvency of insurance companies, but there are no special rules in respect of the types of insurance provided by the insurance companies. The main rules and specific rules of insolvency shall be applied to all insurance companies.

So, there are some additional cases to take measures for preventing the bankruptcy as follows:

- repeated violation of the normative correlation between the owned assets and obligations of the insurance companies in the amount specified by the regulatory body that takes place within 12 months from the date of the first violation;

- repeated violation of the requirements as to the structure of assets of the insurance company intended to recover the insurance reserves and owned assets of insurance company that takes place within 12 months from the date of the first violation;

- withdrawal of the license for insurance activities;

- suspension of the license for insurance activities; and

- limitation of the license for insurance activities of the mandatory types of insurance.

Appointment of the interim administration of the insurance companies is to be obliged in cases of withdrawal or suspension of the license for insurance activities in the following situations:

- carrying out any activities prohibited by the Russian laws and activities violating the conditions of the license for insurance activities;

- failure to comply with Russian laws regulating insurance activity in a sphere of creation and investment of the insurance reserves, investment owned cash resources, resources of any fund guaranteed the insurance compensation;

- failure to meet the requirements to provision the normative correlation between the owned assets and obligations and other requirements to financial stability and solvency of insurance companies; and

- lack of financial resources for the timely fulfilment of financial obligations and (or) the obligations to pay the mandatory fees.

In the case of a court decision on the recognition of the insurance company as a bankrupt and the initiation of bankruptcy proceedings, the policyholders are entitled to unilaterally refuse to execute an insurance contract within one (1) month from the date of notification of such decision.

In that case policyholders have a right to get back the paid insurance premium proportional to the difference between the term of initial duration of the insurance contract and the term of duration in fact, or to receive the redemption sums.

One of the measures for preventing the bankruptcy of insurance companies is the sale of the insurance portfolio of the special type of insurance or the several types of insurance to another insurance company with the preliminary approval of such a transaction by a regulatory body.

In that case an insurance portfolio includes:

- obligations under the insurance contracts (of the special type of insurance or the several types of insurance) that are not fulfilled on the date of the decision to transfer the insurance portfolio to another insurance company;

- assets that shall be used to recover the insurance reserves under the Russian legislation.

In the case of a decision to transfer the insurance portfolio to another insurance company, the policyholders and beneficiaries are entitled to claim the termination of the insurance contract that shall be transferred to another insurance company.

Also the policyholders and beneficiaries intending to terminate the insurance contract are entitled to claim the repayment of the insurance premium proportionally to the difference between the term of initial duration of the insurance contract and the term of duration in fact, or the redemption sums.

Additional insurance contributions to the funded pension as a part of state pension

Because additional insurance contributions to the funded pension have become a part of state pension some special rules for insolvency of a non-state pension fund operating in the state pension system shall be applied.

For non-state pension funds in the state pension system, the special grounds for application of these measures to prevent insolvency are stipulated, they are:

- failure to fulfil the obligation to recover the reserves for funded pensions and (or) pension accumulation fund of individuals for whom the special pension payment is established under the rules specified in Russian legislation;

- lack of reserves of mandatory pension insurance and other assets to conduct the charter activity of the non-state pension fund in order to recover cash resources on the account of individuals in cases stipulated by Russian legislation; and

- failure to perform the obligation of recovering the value of reserves of mandatory pension insurance in cases stipulated by Russian legislation.

In case of the occurrence of the aforementioned grounds the non-state pension fund shall provide to the Central Bank of the Russian Federation the plan to recover the solvency if at the same time there are no signs of bankruptcy. After receipt of this plan the Central Bank is entitled to appoint an interim administration to recover the solvency of non-state pension fund.

Federal law of the "Russian Federation on Insolvency (bankruptcy)" stipulates additional grounds to appoint an interim administration as following:

- special grounds for application of these measures to prevent insolvency in the absence of notice of the relevant circumstances;
- a ban on all or part of the operations of non-state pension fund;
- withdrawal of license for insurance activities (except cases stipulated by law); and
- initiation of the court trial of recognition of the non-state pension fund as the bankrupt.

The interim administration shall take all necessary measures to recover the lack of pension accumulation fund and to fulfil the obligations to the individuals.

Within one (1) month from the date of the appointment of the interim administration, the interim administration shall:

- make a register of obligations to the individuals in accordance with rules stipulated by the Russian legislation; and
- make a cost estimate and provide it to the regulatory body for approval.

If there are signs to recognise the non-state pension fund bankrupt the court makes such decision and initiates bankruptcy proceedings for 1 year.

The Deposit Insurance Agency shall be a bankruptcy trustee in all cases of bankruptcy of non-state pension funds operating in a state pension system.

From the date of recognition of the non-state pension fund as a bankrupt and the opening of bankruptcy proceedings:

- contracts on mandatory pension insurance shall be terminated,
- transferring the pension accumulation fund of the bankrupt non-state pension fund to another non-state pension fund is strictly prohibited (except in cases stipulated by law),
- examination of proposal of individuals to set the funded pension benefits shall be terminated.

The pension accumulation fund and pension reserves shall not be included in the bankruptcy assets.

Within two months from the date of publication of the arbitration court's decision on the recognition of the non-state pension fund as a bankrupt and the opening of bankruptcy proceedings, the Deposit Insurance Agency as bankruptcy trustee takes all action to:

- make a register of the obligations to the individuals including the claims submitted during the period of interim administration and claims submitted during bankruptcy proceedings;

- if the non-state pension fund provides the private pension provision and at the same time operates in the state pension system to run accounts separately in the register of submitted claims of creditors:

    i. obligations under the contracts on private pension provision (including obligations of awarded private pension benefits); and

    ii. the list of creditors which claims shall be satisfied at the expense of pension reserves.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

Russian legislation stipulates special rules with regard to the priority of satisfying the claims of creditors in case of insolvency (bankruptcy).

Private pension provision

Pension reserves are not included in the bankruptcy assets and shall be used only in ways stipulated by law as follows:

- payments or transfer to other non-state pension fund redemption sums of the participants, or transfer as payments of premiums on insurance pension contracts concluded with insurance companies; and

- transfer of obligations for payment of lifelong private pension benefits and pension reserves to another non-state pension fund.

The redemption sum is determined under the contracts.

If the pension reserves are sufficient to satisfy claims of participants, the obligations to participants are satisfied in the following order:

- in first priority – claims of the participants in private pension system in respect of which the obligations of the non-state pension fund to pay lifelong private pension benefits become due; these obligations shall be satisfied by means of determination and separation of the obligations of payment of lifelong private pension benefits from the pension reserves for formation the payment fund sufficient to fulfil mentioned obligations;

- in second priority – claims of payment of the redemption sum to the participants of non-state pension funds in respect of which the obligations of the non-state pension funds to pay private pension benefits within the special period become due;

- in third priority – claims of contributors and participants of non-state pension funds – individuals;

- in fourth priority – claims of contributors of non-state pension funds – legal entities;
- in fifth priority – claims of other creditors that shall be paid at the expense of pension reserves under the "Federal Law on Non-State Pension Fund" No 75-FZ dated 7 May 1998.

If the amount of pension reserves exceeds the claims of creditors mentioned above, the remaining pension reserves shall be included in the bankruptcy assets.

If the pension reserves are not sufficient to satisfy all claims of creditors, obligations to participants of the non-state pension fund are satisfied in the aforementioned order with the following features:

- in first priority among the aforementioned obligations the following claims shall be satisfied:
  - i. claims of participants of non-state pension funds in respect of which obligations to pay lifelong private pension benefits become due and which were not satisfied in accordance with rules and priority mentioned above;
  - ii. claims to pay redemption sums to participants of non-state pension funds in respect of which the obligations of the non-state pension funds to pay private pension benefits within the special period become due and which were not satisfied in accordance with rules and priority mentioned above;
- in third priority – claims shall be satisfied in the following order:
  - i. firstly – not satisfied at the expense of pension reserves claims to pay redemption sum to contributors, participants of non-state pension funds – individuals;
  - ii. secondly – not satisfied at the expense of pension reserves claims to pay redemption sum to contributors, participants of non-state pension funds – legal entities; and
  - iii. finally – claims of all other creditors.

Pension insurance as one of the insurance ways

"Federal Law on Insolvency (bankruptcy)" stipulates special rules about satisfying the claims of creditors of insurance companies. These rules are applied to all types of insurance, including pension insurance.

Claims therefore, of insured persons in respect of which obligations of insurance companies to pay insurance recovery under the contracts of life insurance with insurance risks of endowment insured persons under a certain age or period become due shall be satisfied in the first priority.

Additional insurance contributions to the funded pension as a part of state pension

Because of additional insurance contributions to the funded pension is a part of state pension special rules for insolvency of non-state pension fund operating in state pension system shall be applied.

“Federal Law on Insolvency (bankruptcy)” stipulates special rules for satisfying the claims of creditors of such non-state pension funds at the expense of pension accumulation funds and bankruptcy assets. These rules shall be applied to claims of all creditors of non-state pension funds including individuals who (or in favour of whom) the additional insurance contributions to the funded pension.

Under these rules the claims of all creditors of non-state pension funds refer to obligations of non-state pension funds to individuals that shall be determined by the bankruptcy trustee in the amount of obligations specified in the register of obligations to individuals.

Claims of individuals and their successors, the claims of the Deposit Insurance Agency obtained as a result of payment of guaranteed compensation, and claims of other creditors due to be satisfied at the expense of pension accumulation fund in accordance with the Federal Law on “non-state pension funds” shall be satisfied at the expense of the cash resources from the sale of property from the pension accumulation fund.

The claims of creditors shall be satisfied at the expense of the pension accumulation fund in the following order:

- in first priority – claims of the Deposit Insurance Agency obtained as a result of payment of guaranteed compensation;

- in second priority – claims of individuals and their successors in excess amount of guaranteed funds by means of transferring to the Pension Fund of the Russian Federation owing cash resources of the pension accumulation fund; and

- in third priority – claims of creditors of non-state pension fund due to be satisfied at the expense of pension accumulation fund in accordance with the Federal Law on “non-state pension funds”.

If the pension accumulation fund is not sufficient to satisfy all claims of mentioned creditors, these claims shall be satisfied at the expense of the bankruptcy assets in the described order with the following specifics:

1. as part of the claims of creditors of the first priority the claims of the Deposit Insurance Agency obtained as a result of the payment of guaranteed compensation and the claims of the individuals in the amount exceeding the size of guaranteed funds not satisfied at the expense of pension savings as well as claims of successors of the individuals shall be satisfied as well,

2. as part of the claims of creditors of the third priority shall be satisfied the claims of creditors of the non-state pension fund due to be satisfied at the expense of pension accumulation fund in accordance with the Federal Law on “non-state pension funds” that were not satisfied at the expense of pension accumulation fund.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

Private pension provision

Russian legislation does not specify any remedies to collect pension deficits at the expense of other than the resources of non-state pension fund.

In whole the deficit shall be recovered at the expense of internal resources (such as the positive results of investments pension reserves and others) and established insurance reserves.

Incorporators can provide their contributions to assets of the non-state pension fund to recover this deficit but it is not obligatory under the Russian law. In that case non-state pension funds can use all remedies not prohibited by law to recover the deficit of their pension reserves.

But if there are grounds to take measures to prevent the insolvency of the non-state pension fund they shall be done in accordance with the rules prescribed in the previous question.

Pension insurance as one of the insurance ways

As stated earlier, all insurance companies must meet the requirements of financial stability, conditions of investment owned assets and insurance reserves, normative correlation between owned assets and insurance obligations. This applies to all types of insurance including pension insurance.

The Law of the Russian Federation on the "Organisation of Insurance Business in the Russian Federation" stipulates that in case of failure to meet the requirement of normative correlation between owned assets and insurance obligations the insurance company shall provide the Central Bank with the plan on improvement of the financial situation.

As a part of this plan the insurance company shall comply with all measures which have to be taken to improve the financial conditions of the insurance company. There are no limits in legislation concerning measures that can be used to improve the financial conditions of the insurance company.

In that case insurance companies can use all remedies not prohibited by law to recover the deficit of their insurance reserves.

Also during the process of insolvency (bankruptcy) in case of lack or absence of assets to fulfil the obligations by the insurance company under the insurance contracts under which the compensation payments shall be made, the missing part of assets can be recovered by the professional association at the expense of resources intended to finance compensation payments in the manner and on the terms established by the regulatory body.

Additional insurance contributions to the funded pension as a part of state pension

Because of additional insurance contributions to the funded pension is a part of the state pension special rules for insolvency of non-state pension fund operating in the state pension system shall be applied.

Today there is a process of creating the system of state guaranteed fund of pension accumulation fund.

This fund is operated by the Deposit Insurance Agency of the Russian Federation and shall be compounded by contributions from the Pension Fund of the Russian Federation and non-state pension funds intended to take part in this guaranteed fund system.

In case of deficit or another lack of cash recourses to recover the pension accumulation fund this deficit can be recovered by the Deposit Insurance Agency of the Russian Federation at the expense of this guaranteed fund.

Non-state pension funds operating in the state pension system can take part in this guaranteed fund system only with special approval by the Central Bank if they meet all necessary requirements including requirements as to the quality and quantity of their assets

QUESTION 8

Are there any cross-border features of your pension regime?

There are no special rules under Russian legislation concerning cross-border features with respect to private pension provision (including additional contributions to the funded pension of state pension system) and pension insurance.

QUESTION 9

Discuss the state of defined benefit plans in your country

Private pension provision

The Russian Government plans to extend the State guaranteed system on pension reserves of private pensions. These plans shall be discussed with non-state pension funds and experts.

This system can start working not earlier than two or three years, while the legal framework is being developed.

The Russian Government has proposed the extension of the State guaranteed system to private pension plans as an additional guarantee for participants of non-state pension funds in spite of the voluntary nature of the contributions under private pension schemes.

But all measures to make private pension plans widespread and popular among individuals and employers have not had the expected effective results. Most non-state pension funds operate on the basis of resources of large and mostly state-owned companies. Employees of large corporations become a member of their private pension plans because of their corporate and employment relations.

The percentage of individuals enrolling for the private pension provision who are not the employees of a large corporation is very low. Today, in our view, there are no objective reasons why this percentage will meaningfully increase and for the system of private pension provision to become the effective instrument to save money for old age.

Pension insurance as one of the insurance ways

Today, the pension insurance provided by insurance companies is a small component of the life insurance business. And there are no real steps to improve this system and make it more guaranteed and, therefore, more popular among people.

Insurance companies try to lobby for amendments in present Russian legislation in order to become competitive with non-state pension funds in corporate pension insurance.

The Labour Ministry of the Russian Federation has confirmed that it does not have any principal objections to this concept. However, the relevant law will come into force not earlier than January 2017. The reasons for this are the different requirements as to limits on asset allocation, to organisational structure and capital, etc.

But the insurance companies and insurance experts fear that a delay in involving insurance companies in the pension system right now could cost them too much. As a result, they said that by 2017 the entire market will be large customers. Insurance companies can operate with only small and medium businesses that are paying too little attention to corporate pension plans.

In our view, in the current Russian economic situation and new pension reforms in the state pension system, people do not want to save money for the long-term by means of another legal entity such as insurance companies. The pension insurance programs are not popular among people and these vehicles do not make them more attractive. We consider that in the current situation people are concerned about their obligatory pension benefits more than searching for ways for private accumulation of funds for retirement.

Additional insurance contributions to the funded pension as a part of state pension

The Russian Government has taken steps to increase the popularity of making additional contributions to the funded pension and the public's respect for the non-state pension funds and their activity.

The Russian Government has provided the option of co-financing additional contributions to the funded pension. Under this program, individuals or sponsors in favour of individuals provide additional contributions in sum of not less than 2,000 roubles, the State provides contributions to the individuals' accounts up to 12,000 roubles per year. Enrolment into the program of state co-financing of pensions ended on 31 December 2014.

But as mentioned above, the Government has decided not to allow the division of pension contributions from the employers between insurance pension and funded pension and in 2015 all obligatory contributions from the employers shall be referred only to the insurance pension.

The Russian Government has now issued additional rules to the non-state pension funds that intend to operate in the state pension system.

Earlier all non-state pension funds were incorporated as non-commercial legal entities (non-commercial partners). The Russian Government is worried about this fact because in its opinion the non-commercial partners are not allowed to control their management bodies and their appointment as well as to bring the management bodies to responsibility in case of damages caused by their ineffective decisions.

In that case all non-state pension funds shall be reorganised as joint-stock companies. Moreover from the 1 January 2014 all non-state pension funds are closed to new contributions from individuals and their sponsors.

To regain the possibility of accumulating mandatory pension contributions into a pension accumulation fund, all non-state pension funds must meet additional requirements and, therefore, be included in the new State guaranteed system. The meeting of additional requirements and involvement in the new State guaranteed system will be confirmed by the Central Bank by means of issuing the new license.

As we can consider these requirements are extended to the state pension system and to the ability of the non-state pension fund to operate in a state pension system with mandatory pension contributions.

As additional pension contributions become part of state funded pensions, we suggest these limitations and additional requirements for the non-state pension funds will impact the option of voluntary pension planning too.

Also the Russian Government is discussing the idea of liquidating funded pensions not only for 2015 but for the whole period.

In that event, the additional contributions to the funded pension can lose their meaning in the state pension system and the increase in future pension benefits will no longer be available for individuals.

SOUTH AFRICA

QUESTION 1

What is the legal framework for private pension plans in your country?

In South Africa, 'private sector funds' and 'public sector funds', are governed by the common law, the Constitution and a number of different statutes. They are also subject to laws of general application, such as the Income Tax Act[1], the Divorce Act[2], the Maintenance Act[3] and the Financial Advisory and Intermediary Services Act[4] ("FAIS").

'Private sector funds' are obliged to register under the Pension Funds Act[5] (the "PFA") and are accordingly regulated by the PFA. Aspects of the Financial Services Board Act, the Inspection of Financial Institutions Act and the Financial Institutions (Protection of Funds) Act, also apply to these private sector funds.

The office of the Registrar of Pension Funds, which falls within the ambit of the Financial Services Board ("the FSB"), regulates and oversees the private sector retirement fund industry. The FSB is an independent institution established by statute to oversee the South African non-banking financial services industry in the public interest. Certain service providers to retirement funds, for example investment consultants, are also regulated by the FSB.

The PFA empowers the Registrar of Pension Funds (the "Registrar") by notice in the Government Gazette, to issue board notices and directives on certain issues. The Registrar may also issue circulars, however, unlike board notices and directives which have the status of subordinate legislation, circulars are an expression of the Registrar's opinion and are not binding in law. Other regulators, such as the Registrar of Financial Service Providers also issue board notices, directives and circulars. Board notices, directives, circulars as well as other information can be obtained on the FSB's website at www.fsb.co.za.

The PFA establishes a dispute resolution forum, known as the 'Office of the Pension Funds Adjudicator'. The Adjudicator is empowered under the PFA to determine pension-related disputes. Determinations issued by the Adjudicator do not have value as legal precedent but can be enforced as a civil judgment in a court of law and can accordingly be appealed to the High Court.

'Public sector funds', on the other hand, are funds to which the state contributes in its private capacity as an employer. They are thus established for employees of the State, its entities and its enterprises (such as the Government Employees Pension Fund and the Post Office Retirement Fund). Public sector funds are governed by their own statutes (such as the Government Employees Pension Law Act in the case of the Government Employees Pension Fund) and, accordingly, the PFA does not apply to public sector funds until and unless they register, of their own volition (often subject to ministerial consent) under the PFA. The licensing and approval requirements for public sector funds are thus determined by the relevant special statute, however, there is no formal prohibition on public sector funds appointing private service providers to administer them.

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1 Act 58 of 1962.
2 Act 70 of 1979.
3 Act 99 of 1998.
4 Act 37 of 2002.
5 Act 24 of 1956.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

Private sector funds are subject to regulation by the FSB, in particular, the Deputy Registrar for Pension Funds and Friendly Societies. Public sector funds, on the other hand, are subject to ministerial oversight, approvals, board appointments etc. In relation to private sector funds registered under the PFA, a third party administering such a fund must be licensed and approved as a fund administrator by the Registrar in terms of the PFA. The conditions for the approval of a fund administrator are published in Board Notice 24 of 2002. Public sector funds are regulated by the specific statute in terms of which they have been incorporated, unless they have registered under the PFA.

The PFA, read with regulation 28, regulates investments by private sector funds. Although public sector funds are not governed by the PFA, they also tend to make use of the guidelines set out thereunder. Regulation 28 deals with, among other things, the type of instruments in which funds can invest, the liquidity levels which must be maintained by a fund, and the spreading of the fund's assets in various investment vehicles. It does not prohibit private sector funds from investing in any specific asset or asset class; instead, it places restrictions on investment in specific asset classes. In this regard:

- a private sector fund must not invest or contractually commit to invest in an asset, including a hedge fund or private equity fund, where the fund may suffer a loss in excess of its investment or contractual commitment in the asset;
- a fund may engage in securities lending subject to prescribed conditions;
- a fund may invest in derivative instruments subject to prescribed conditions; and
- a fund may not acquire a controlling interest in a company.

Financial service providers, such as asset managers, have to be approved by the FSB as authorised financial service providers under FAIS in order to operate as a service provider to retirement funds. Similarly, short-term and long-term insurers are required to obtain approval from the FSB in terms of the Short-term Insurance Act[6] (the "STIA") or the Long-term Insurance Act[7] (the "LTIA"), whichever is applicable, in order to provide services to retirement funds. No person (including a foreign insurer) may render services to a retirement fund in South Africa without authorisation from the FSB.

6 Act 53 of 1998.
7 Act 52 of 1998.

QUESTION 3

How are the plans governed?

Boards of management of retirement funds, (often referred to as trustees although the term is technically incorrect), are responsible for fund governance. It is typical of private sector funds to have quarterly board meetings. Many such funds have a number of committees, typically including an Investment Committee and a Legal, Risk and Compliance Committee at a minimum. There are, however, some employer-specific funds and several bargaining council funds which are self-administered.

In relation to private sector funds, the PFA requires the board of a fund to consist of at least four board members, 50% of whom the members of the fund must have the right to elect. It further provides that the constitution of the board, the election procedure, the appointment and terms of office, the voting rights of board members, and the powers of the board and so on must be set out in the rules of the fund. The rules are accordingly approved and registered by the Registrar. The PFA furthermore requires private sector funds to furnish training to the members of the board within six months of their appointment.

The majority of retirement funds are administered on a contractual basis by third party service providers. There are, however, some employer-specific funds and several bargaining council funds which are self-administered.

QUESTION 4

Is there a compensation fund for pension benefits?

There is no compensation fund.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

Retirement funds are legal entities distinct from the employers participating in the fund, the pensioners drawing from the fund, and from the sponsors who establish the funds. The funds hold assets in their own right and a participating employer or the sponsor has no claim to these assets, except in very specific instances prescribed by statute. Thus, in the event of a participating employer or the sponsor becoming insolvent, the assets held by the fund cannot be liquidated.

Employer insolvency has no direct consequence to plan members, but since the employer ceases to contribute to the fund, the fund may be terminated / wound up in accordance with the rules of the fund. Typically, the fund will appoint a liquidator who will apply credit balances in terms of the rules of the fund or, where empowered to do so, may use his/her discretion. The Registrar of Pension Funds must approve the appointment of the liquidator.

With regard to the contributions paid to the fund by an employer, Section 98A of the Insolvency Act[8] (the "Insolvency Act") provides that, in the event of there being any free residue in the estate of the insolvent[9], it shall be applied in paying any contributions which were payable by the insolvent (immediately prior to the sequestration of the estate) in respect of any of its employees which were owing by the insolvent, in its capacity as employer, to any pension fund. The fund will thus have a claim against the insolvent estate for outstanding employer contributions. The priority of payments is provided for by the Insolvency Act.

The provisions of the Insolvency Act which apply to individuals are made applicable to companies and close corporations.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

The Insolvency Act does not make provision for a right of preference pertaining to pension deficits during insolvency. As stated above, the Insolvency Act provides that, in the event of there being sufficient free residue in the estate of the insolvent, it shall be applied in paying any contributions which were payable by the insolvent in respect of any of its employees which were owing by the insolvent to any pension fund.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

If 'pension deficits', in this context, refers to a situation whereby a retirement fund does not have sufficient assets to pay a pension to a member, a member will have contractual and / or delictual claims available against the fund. The fund may then, in turn, have a claim against the insurer of the fund if the reason for the deficit is covered by the relevant insurance policy. The plan member may also have contractual and / or delictual claims against the individual board members of the fund, the trustees of the fund or the actuaries of the fund in their personal capacity. Further, in the event of a deficit, the fund itself may have contractual and / or delictual claims against the actuaries of the fund, the administrators of the fund, or the trustees of the fund.

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8 Act 24 of 1936, as amended.

9 The Insolvency Act, in turn, in Section 2 defines 'free residue' as the portion of the estate which is not subject to any right of preference by reason of any special mortgage, legal hypothec, pledge or right of retention.

QUESTION 8

Are there any cross-border features of your pension regime?

Generally, the law which governs pension funds in South Africa is restricted in its application to pension fund organisations registered in South Africa. Section 2(4) of the PFA provides that the provisions of the PFA (with certain exceptions) do not apply in relation to a pension fund if the head office of the association which carries on the business of that fund, or, as the case may be, of every employer who is a party to such fund, is outside the Republic, if:

- the Registrar is satisfied that the rules of the fund applicable to members resident in the Republic are not less favourable than those applicable to members resident outside the Republic, taking into consideration differences in the conditions of service;
- the Registrar is satisfied that adequate arrangements exist for ensuring the financial soundness of the fund; and
- the fund furnishes such security as the Registrar may from time to time require for the payment of any benefits which may become payable to members resident in the Republic who are South African citizens, or otherwise satisfies the Registrar that it will be able to pay such benefits.

As mentioned with respect to the regulatory framework above, Regulation 28 allows pension funds to make investments based abroad. These are known as “offshore allowances”. The nature and processes of these investments remain governed and bound by South African pension regulations and law despite their being extra-territorial.

QUESTION 9

Discuss the state of defined benefit plans in your country

In the private sector there has since the 1990’s been a shift from defined benefit funds to defined contribution funds. The majority of private sector retirement funds today are defined contribution funds, although some may retain defined benefit elements. Most public sector retirement funds are still defined benefit funds or have significant defined benefit components.

SPAIN

QUESTION 1

What is the legal framework for private pension plans in your country?

The main rules governing Spanish pensions are found in the Pensions Act (Royal Legislative Decree 1/2002) (the "Pensions Act") and its implementing Regulations (Royal Decree 304/2004 and Order EHA/407/2008) (the "Pension Regulations").

Pension plans are social welfare institutions of a contractual nature which govern, by means of certain specifications, the relations between the personal elements involved, their rights and obligations. They are voluntary and their benefits, which are private in nature, can be supplementary or not, but in no case can they replace those received from the Social Security system.

Pension plans, depending on the parties they include, can be of several types:

- Individual – those plans whose sponsor, who does not make contributions, is one or more financial-type entities and whose recipients are any individual.
- Associated – those plans whose sponsor, who does not make contributions, is any association or trade union, with the recipients being their associates, members or affiliates.
- Employment-related – those plans whose sponsor is any entity, corporation, company or society and whose recipients are their employees. These plans consist of contributions from the sponsors and from the recipients, as the case may be.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

Pension funds are created subject to administrative authorisation from the Ministry of Finance, in a public deed executed by the sponsor, management and depository entities and are recorded at the Commercial Registry and Special Administrative Registry established for this purpose.

In order for a pension plan to be established, the financial contributions from sponsors and recipients are immediately and mandatorily deposited to a standing account for the plan in a pension fund, the balance of which will be used to pay the benefits deriving from executing the plan.

Prior to the creation of the fund, the sponsor must apply for administrative authorisation for the project from the Directorate General for Insurance and Pension Funds.

Pension funds are managed by a management entity and supervised by a supervisory committee. If the fund forms part of just one employee pension plan, the supervisory committee for the plan will perform the functions of the fund's supervisory committee.

The assets of the pension funds will be invested according to criteria on risk profile, profitability, diversification and investment periods suitable for this purpose.

Pension fund management entities must audit and publish their annual accounts within the time periods established by law. The Ministry of Finance can require, as an exception, that external audits be performed, and can collect accounting and statistical data on the management entities and pension funds managed by them, in relation to their inspection and protection duties.

Management entities must provide information to the recipients and beneficiaries of the pension plans, at least quarterly, on the performance and status of their financial rights within the plan, as well as on any other aspects which may affect them.

The custody or deposit of the securities and financial assets contained in the pension funds corresponds to a pension fund depository entity established in Spain. These can be credit entities which fulfil the legal requirements for this and which are recorded at a special registry of the Ministry of Finance.

As for administrative control, the Ministry of Finance is responsible for the administrative regulation and supervision of compliance with regulations. In addition, the Directorate General for Insurance and Pension Funds can order the inspection of pension fund depository entities to ensure that they are properly complying with the regulations governing pension plans and pension funds.

QUESTION 3

How are the plans governed?

The plan must contain rules on the constitution and operation of the supervisory committee, which must mandatorily carry out the following tasks:

- supervise the fulfilment of the specifications for all matters regarding the rights of recipients and beneficiaries;
- select the actuary in charge of rendering the services necessary for the execution of the plan;
- propose and agree on any amendments to benefits, contributions and other issues regarding the plan; and
- represent the collective interest of recipients and beneficiaries in all matters related to the pension plan.

The supervisory committee must have equal representation in terms of the employer and employees, although a different distribution of representatives can be established if agreed in the applicable collective bargaining agreement, provided that the representation of the sponsor and the recipients is guaranteed in any event. The specifications establish the rules for electing the members of the supervisory committee, which must comply with the provisions established by law.

QUESTION 4

Is there a compensation fund for pension benefits?

In the event of insolvency of the pension plan promoter, there is no guarantee fund that covers pension plans.

Pension plans are excluded from the Salary Guarantee Fund (Fondo de Garantía Salarial or FOGASA), which is an autonomous body attached to the Ministry of Employment and Social Security. Its function is to guarantee that workers receive their salaries, as well as severance payments or indemnification for termination of the labour relationship which are outstanding due to the employer going bankrupt or entering insolvency proceedings.

Pension plans are not covered by the Credit Institution Deposit Guarantee Fund (*Fondo de Garantía de Depósitos de Entidades de Crédito*) either, the object of which is to guarantee deposits in cash or securities or other financial instruments in credit institutions.

Nevertheless, account should be taken of the reference to the insolvency of the management or depositary entity of pension plans made in Legislative Royal Decree 1/2002, of 29 November, which approved the restated text of the Pension Plan and Pension Fund Regulation Act. Article 23.3 thereof states that insolvency proceedings of the management or depositary entity will lead to the cessation of management or deposit of the fund by the entity in question. In the case of the management entity, the management will be provisionally entrusted to the depositary entity. If the entity that ceases to operate is the depositary, the financial assets and cash of the fund will be deposited at the Bank of Spain. In both cases, the fund will be dissolved unless a new management or depositary entity is appointed within one year. Article 34.3 of the same Act, according to the wording approved by Act 20/2015, of 14 July, which comes into force on 1 January 2016, establishes that when a judge declares that a pension fund management or depositary entity is in insolvency proceedings, that person will immediately notify the Directorate General for Insurance and Pension Funds of the decision and it can ask the insolvency judges for information on the status and progress of the insolvency proceedings that affect pension fund management and depositary entities.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

Pension rights cannot be enforced unless any of the legal requirements for such enforcement take place (e.g retirement, complete incapacity to work, death of beneficiary, long term unemployment, serious illness).

However, should the employer be declared insolvent, the employee (beneficiary of the pension rights), would be entitled to displace the pension rights to its next employer, only if this new employer allowed such displacement. If this new employer refused to take hold of the pension plan, the sponsor would be registered as a "suspended sponsor", but the beneficiary would still keep such condition without profiting from the contributions that the sponsor used to make.

Another scenario would be if the insolvent company was acquired by a third party. In this case, the law does not foresee any limitation for this new employer to subrogate in the former sponsor's position, if the pension plan permits it.

In any case, the insolvency proceeding of the employer / sponsor does not entitle him to recover the contributions that he has made on behalf of his employees, and such sums cannot be acknowledged as part of his estate.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

The Spanish Insolvency Act does not foresee any special right of the employees for pension deficits. This makes sense given that the insolvency of the employer / sponsor does not constitute a cause to recover the contributions that have been made up to that moment.

It must be said, however, that in case it is the employee who is declared insolvent, his pension cannot be seized to pay back his other debts.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

In the case of the insolvency proceeding of the employer, the beneficiary would not see his pension rights harmed, with regards to the contributions made so far.

QUESTION 8

Are there any cross-border features of your pension regime?

Pursuant to the provisions of Directive 2003/41/EC of 3 June 2003 on the activities and supervision of institutions for occupational retirement provision, employee pension funds authorised and registered in Spain can form part of pension plans for employees sponsored by companies established in other EU Member States.

In addition, employee pension funds authorised or registered in other Member States can form part of pension plans sponsored by companies established in Spain.

Cross-border activities require that the pension fund be authorised by the competent authority of the Member State of the pension fund.

The integration of each plan into the corresponding employee pension fund will require prior compliance with the communication procedures between the pension fund and the supervisory authorities of the home and host Member States, which are established by law.

Cross-border activities involving employee pension funds must be carried out pursuant to the labour and employment legislation of each host Member State.

Spanish pension plans operated through pension funds registered in another Member State must comply with the provisions of Spanish social and labour legislation and, if applicable, any provisions established in the applicable collective bargaining agreement in this regard.

The Pensions Act sets forth what those provisions of Spanish social and labour legislation are. The details are below.

- All pension commitments of employers vis-à-vis employees must be formalized through a pension plan or insurance agreements;

- Pension plans must comply with some basic principles: non-discrimination, individual capitalization (taking into account financial actuarial and capitalization systems), irrevocability of the contributions made by the sponsor, attribution of consolidated rights to the recipients and financial rights to the beneficiaries, and compulsory inclusion of contributions made into a pension fund;

- The pension plan can only be terminated under certain circumstances established by the Pensions Act: (A) inability to comply with the above-mentioned basic principles; (B) lack of functioning of the supervisory committee; (C) lack of compliance with the requirements imposed by the Directorate General for Insurance and Pension Funds in an intervention plan in case the pension plan does not meet Spanish requirements; (D) non-compliance with any amendment necessary for the plan as a result of an actuarial review; (E) lack of recipients or beneficiaries for a period longer than one year; or (F) dissolution of the sponsor of the plan (unless such dissolution is as a result of a merger or complete assignment of assets, in which case the assignee or merging company will subrogate the position of sponsor of the plan);

- The specifications of the plan must mandatorily include: (A) the identification of the type and form of the plan (e.g. individual, associated or employment-related plan; DB or DC plan); (B) the rules for the incorporation and functioning of the supervisory committee; (C) financing system; (D) inclusion in a pension fund; (E) definition of the benefits and rules to establish their amount, including whether or not the benefits are adjustable and the means to make this adjustment; (F) the rights and obligations of recipients and beneficiaries, covered contingencies and causes which give rise to the right to receive the benefits; (G) causes which allow the recipients to modify or suspend their contributions; (H) rules regarding the inclusion and removal of recipients; (I) requirements for amendments to pension plans and procedures for following up to that effect; and (J) causes of termination of the plans and rules for their winding-up;

- Any employee with at least 2 years of seniority, regardless of the classification of their employment contracts, may adhere to the pension plan (a shorter grace period may be established); and

- All pension plans must comply with the mandatory rules established by the Pensions Act on the contingencies which may be covered (retirement, dependence, death, permanent occupation-specific or all-work disability); and the calculation of the relevant benefits.

QUESTION 9

Discuss the state of defined benefit plans in your country

The public Spanish Social Security system, associated with the Welfare State, has come to guarantee that citizens' needs at the time of their retirement are covered, for the most part, by the public pension fund, which is not the case in other countries where the public system is less protective.

However, maintaining this high public coverage in Spain is beginning to become unsustainable, mainly due to two factors: a demographic problem and the current economic crisis situation.

The lower birth rate and the increase in life expectancy have created an inverted pyramid with a high elderly population at the top. The active population is fewer than the number of pensioners, and as a result, the income cannot maintain the growth of expenses.

The economic crisis has worsened the problem, with a rise in unemployment to unsustainable rates, with expenses increasing and income from contributions decreasing.

As a result, Spain's Social Security system could become unsustainable, and for that reason, several reforms have been made to the State pension system over the past few years, in an attempt to ensure the system's survival and to reorganise the public accounts. These are measures which are already pushing retirement age back and setting higher Social Security contribution rates in order to be entitled to full benefits.

It is precisely in this context where pension plans appear, not as a formula to substitute Social Security benefits, but to supplement them. In light of the foreseeable drop or decrease in public pensions, private pension schemes are becoming the back-up which would permit an individual to maintain their same lifestyle upon retirement. For this reason, increasing numbers of citizens are contributing to private pension plans, with the conviction that access to a retirement without hardship requires saving through these private plans.

The Spanish Government has been encouraging the creation of private pension plans, applying tax measures which act as incentives to this private savings mechanism.

By virtue of the tax reform which entered into force on 1 January 2015, pension plans have undergone several changes, in terms of both their contributions and their redemption.

The tax reform has introduced measures to benefit the holders of pension plans and pension funds, giving them a 30% reduction on their maximum fee and the possibility of redeeming the economic rights after 10 years.

Until 31 December 2014, a reduction could be applied to the tax base for the contributions made, provided that the overall total for the year did not exceed the amount of 10,000 euros or 12,500 in the case of persons over the age of 50 years, up to a maximum of 30% (or 50% for plan holders over age 50) of the sum of their net employment earnings and earnings from economic activities received individually during the year.

As anticipated, the January 2015 reform limits the contributions which can be made to a pension plan to 8,000 euros per year, and up to a maximum of 30% of the sum of the individual's net employment earnings and earnings from economic activities, eliminating the higher limit which existed before for plan holders over age 50.

Meanwhile, Spanish Act 26 / 2014 amends the Regulations on Pension Plans and Pension Funds, permitting early redemption after contributions have been made for 10 years, although, in the case of contributions made prior to 31 December 2015, the money cannot be taken out of the plan until January 2025.

The reform maintains the possibility of applying a 40% reduction to the redemption in the form of capital for those contributions made prior to 2007, although it introduces a note of caution whereby this only applies if the money is withdrawn from the pension plan during the year when the insured contingency occurs, or during the following two years.

A transitional regime is expected to apply to contingencies occurring between 2011 and 2014, in which plan holders have eight years as from the date of their retirement in which to redeem their pension plan and apply said tax benefit, and to those cases in which the contingency occurred prior to 2011, in which they can apply the reduction if they recover the money prior to 31 December 2018.

SWEDEN

QUESTION 1

What is the legal framework for private pension plans in your country?

The Swedish pension system is generally divided into three different parts; the national retirement pension, the occupational pension, and the voluntary private pension. The first part is funded by the government and the two latter parts constitute the private pension system.

The national retirement pension

The national retirement pension from the Swedish Pension Agency consists of income pension, premium pension and guarantee pension. The income-based pension is the main component of the national pension system and is based on total earnings throughout life. Income includes salaries, sickness benefits, unemployment benefits, etc. The premium pension is also based on lifetime earnings. It is placed in pooled funds and everyone may choose his or her own specific funds. The guarantee pension is aimed to guarantee pensions for those who have had little or no income from work in their lifetime. It is linked to the price base amount calculated annually by Statistics Sweden. The size of the guarantee pension depends on how long the individual has lived in Sweden. The legal framework for the national retirement pension is the Social Insurance Code (Sw. Socialförsäkringsbalken).

The occupational pension

The occupational pension generally has its origin in the collective agreement which has been executed by the employer. The pension can also be based on individual agreements between the employer and the employee. The occupational pension originating from the collective agreement is governed by the conditions in that collective agreement. The pension plans are usually financed by the employer. However, there are also agreements that state that the individual shall make contributions.

The employer is obliged to pay a pension contribution in addition to the salary.

The pension contributions to a defined pension plan are tax deductible for the employer. The tax rules can be summarized as below. Please note that these rules are very extensive and technical in nature.

In order for an employer to deduct pension costs, certain criteria must be met:

(i) The pension must be secured by:

- payment of a premium to a pension insurance,
- a reservation in the company's balance sheet in combination with a credit insurance, a state or municipal guarantee or a similar guarantee,
- transfer of funds to a pension foundation, or
- transfer of funds to a foreign insurance institute that is considered equal to a pension foundation.

(ii) In order for pension costs to be deducted, the pension must not exceed a certain percentage of the employee's yearly salary. The main rule is that the deductible pension may not exceed 35% of the employee's pension or 10 price base amounts per employee. The amounts are calculated for each individual employee. The deduction may be calculated on the salary during the fiscal year or the previous fiscal year.

- Deductible pensions are not subject to normal social security contributions but to a special social security tax of 24.24%, deductible as a business expense.

- If a pension is not secured, the deductions will be made when the company pays the pension.

The voluntary private pension

The voluntary private pension is a supplement, a top-up, to the other parts of the national pension system. This part of the pension is funded by the individual. The individual can invest in stocks and mutual funds within the pension account. The individual pays return tax on the account value on January 1 each year. The size of the return tax depends on the previous year's average government borrowing rate. In addition to the private pension savings account, the individual can also get a pension insurance. A pension insurance is a separate saving and is combined with an insurance.

Tax deduction

The individual can make deductions each year in the tax return for the amount of savings the individual has put into the private pension savings. The amount that the individual may deduct has been reduced over the years. As from January 1, 2015 the deduction has been lowered from 12,000 SEK per year to 1,800 SEK per year. After 2016, the deduction system will be completely abolished. To avoid double taxes from 2016, the individual will have to choose another plan for the voluntary private pension. Some of the options available today for alternate voluntary private pension plans are direct savings in funds or shares, ordinary savings accounts and investment savings accounts. The investment savings account is a new form of savings account as of January 1, 2012. It is a free account where the individual can save in funds, shares and other securities. The individual pays an annual tax based on the total value of the savings account.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

The Swedish Pensions Agency has the overall responsibility for pension plans and also administers the national pension and provides information about the pension system to employees and retirees. The Swedish Social Insurance Inspectorate supervises the Swedish Pensions Agency, and conducts its administration with due process and efficiency.

The private part of the pension in Sweden is normally placed in a pension plan handled by an insurance company. Insurance companies need to comply with certain regulations to ensure the value of the pension plans. For instance, the value of the insurance companies' assets need to be substantially larger than the companies' liabilities. Insurance companies are supervised by Sweden's financial supervisory authority who receives reports from the insurance companies once every four months. The reports include status on the equity, assets, liability and other relevant information.

QUESTION 3

How are the plans governed?

Under the Swedish pension system, the employer is obliged to pay a pension contribution alongside the salary. The pension contribution is part of the premium pension and is generally paid to an insurance company, either directly or via a fund manager. The insurance company manages the plan and monitors the plan value.

Since the pension is linked to the individual, the employee or retiree can choose to participate in the governance of the pension plan. The employee can choose which fund to place his or her pension in, or hire a fund manager to do so in his or her place. In case an individual does not make an election, the government or the insurance company will place the pension in a general plan.

QUESTION 4

Is there a compensation fund for pension benefits?

All retirees in Sweden are guaranteed a minimum of pension benefits, the so-called guarantee pension. The benefits differ depending on how long a person has lived in Sweden and if the retiree receives pension benefits from a former employer. The guarantee pension is funded by the government.

An important part of the pension benefits derive from the employer who makes pension contributions for its employees. Normally, the pension benefits are regulated by a collective agreement between the employer and a labour union. To ensure the pension benefits, several of the labour unions in Sweden as well as the largest business federation, the Confederation of Swedish Enterprise, have created a guarantee fund. The purpose of the guarantee fund is to compensate the employees if their employer becomes insolvent. The fund is administered by Alecta, a co-operative that specializes in occupational pensions, and is supervised by the Swedish Financial Supervisory Authority. The fund is limited to only cover companies with a collective agreement. In order for the guarantee fund to be used, the employer must be declared bankrupt.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

There is no enforcement of the pension rights if the employer becomes insolvent. Therefore there is no regulatory body involved. If the employer becomes insolvent, there are limited means for the employees to enforce their pension benefits.

The employee's claim on pension in the employer's bankruptcy has a right of priority in the bankruptcy, but only with respect to pension accruals for a period of six months before and six months after the bankruptcy petition was received by the district court, according to The Right of Priority Act paragraph 12, subparagraph 5 (Sw. *Förmånsrättslagen)*. However, the Right of Priority Act only applies to direct pension claims. Direct pension is an agreement between the employer and the employee where the employer is bound to pay capital insurance with a promise of pension to the employee. Direct pension has priority in case of the employer's insolvency and is guaranteed by the Salary Guarantee Act (Sw. *Lönegarantilagen*).

It is more common that the employee's pension is secured under the regulations in the Pensions Obligations Vesting Act (Sw. *Lagen om tryggande av pensionsutfästelsen m.m*). The most common solution to guarantee the employee's pension entitlements is through the insurance under the collective agreements. The consequence of pensions insured under the Pensions Obligations Vesting Act is that pension claims seldom occur under the Right of Priority Act, which means that it is difficult for the insurance company to collect an amount in the bankruptcy. In case of an employer's insolvency, the insurance company collects information on the salaries to estimate each employee's pension benefits. If the insurance company cannot collect all relevant information the insurance company will estimate a lump sum that will be paid to the employee. The insurance company will then have a claim in the employer's bankruptcy. Under the current pension system in Sweden, there is no strategy for when an insurance company becomes insolvent. The insurance companies are supervised by Sweden's financial supervisory authority.

In the rare case that the debtor (that is the employer) has not secured the pension commitment through an insurance, but by a pension trust, it should be noted that under the Bankruptcy Act (Sw. *Konkurslagen*), the employee does not have any right of payment from the employer when the employee can receive the promised pension from the trust.

Moreover, the pension benefits provide some protection in case of the personal insolvency of the employee. The pension benefits from the national retirement pension cannot be subject to a seizure. However, the private pension can be seized if the pension has been saved for a shorter time than 10 years, or if the annual contribution is significantly larger in a particular year as compared to other years. If any of these circumstances are at hand, the private pension could be seized if the employee becomes insolvent. If a person becomes insolvent after retirement, the pension benefits could be seized if the retiree receives more than a minimum standard.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

See answer under question 5.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

There are no specific remedies to collect in respect of pension deficits. However, general remedies that are applicable in insolvency matters are available against the board members and the shareholders.

The board and the shareholders have no personal liability for the obligations of the company. However, there is a protection for the equity in the company. Creditors and others should always ensure that the company has a share capital of at least 50,000 SEK. The board has a responsibility to monitor and ensure that the assets of the company do not fall below half the value of the registered share capital. If this happens, the board is obliged to prepare a balance sheet for liquidation purposes which should contain a plan to restore the company's equity. If the company continues its business without restoring the share capital, the board members could face personal liability. Representatives and shareholders with knowledge of the situation could also face personal liability.

Furthermore, the board and the shareholders risk facing personal liability if the court decides to pierce the corporate veil. Under Swedish case law[1] three factors are taken into account when piercing the corporate veil:

- a limited number of the owners of a business entity have failed to maintain arm's length relationships with the owners' business;
- the business does not have an independent administration; and
- the business entity is significantly undercapitalized (capitalization requirements may vary based on the nature and location of the business).

1 See e.g. NJA 1947 s. 647, NJA 1975 s. 45, and NJA 1982 s. 244.

Another possibility is if the employer sells or transfers the business to another company before the insolvency. The buying company would then take over the employees as well as the business. The new employer has the option to voluntarily take over the responsibilities regarding salary and pension prior to the takeover from the previous employer.

QUESTION 8

Are there any cross-border features of your pension regime?

In Sweden, the pension is linked to the individual who owns the rights to his or her pension. If a person chooses to emigrate from Sweden after retirement, he or she will still be able to collect the Swedish pension. This is valid for all sorts of pension benefits, including income pension and private pension. However, in order to receive the guarantee pension there is a requirement that the individual resides in an EU or EEC member state or in Canada. In order to collect the pension while residing in another country, the Swedish Pension Agency will need to receive a *life certificate* that proves that the individual is alive and lives in the country of residence. The *life certificate* needs to be attested to by the government in the country of residence. If a person resides abroad that pension will pay a reduced tax amount in Sweden.

If the individual has retired, the pension benefits in Sweden will not be affected by the previous employer's insolvency as the pension benefits are handled by the Swedish Pension Agency and/or an insurance company.

In case of the employer's insolvency, the pension benefits are sometimes protected by the Salary Guarantee Act, see answer under question 5. The Salary Guarantee Act also applies in cross-border situations within the EU and EEC. If a person resides in Sweden but has an employer who faces insolvency proceedings in another country, he or she can contact the Swedish Enforcement Authority to receive salary guarantee, e.g. salary and pension benefits. If a person resides in another country, but has an employer who is located in Sweden, he or she can contact the Swedish Enforcement Authority to receive relevant information of the bankruptcy.

As stated above, the Salary Guarantee Act has certain limitations. If the employee has a claim on the employer, the employee will have to report the claim to the administrator who is handling the bankruptcy of the employer. The main duties of the administrator are to promptly look after the assets of the bankruptcy estate. This includes assets that are located abroad.

There is no regulated protection in case of an employer's insolvency outside the EU or EEC.

QUESTION 9

Discuss the state of defined benefit plans in your country

It is difficult to foretell what the future holds for the defined pension plans. Some collective defined pension plans are likely to be phased out in favor of defined benefit plans, but there are still defined benefit solutions. Many private employees who are born 1978 or earlier and who are covered by a collective agreement are covered by a large collective defined benefit pension plan.

Furthermore, there are changes being made to the administration of the guarantee fund. In the future, the administration of the fund will be handled by an independent foundation instead of Alecta. The aim is to separate the fund from Alecta thus ensuring the value of the fund for the years to come. The fund will continue to be supervised by the Swedish Financial Supervisory Authority.

THE NETHERLANDS

QUESTION 1

What is the legal framework for private pension plans in your country?

The Dutch pension system – general overview

As in many other European countries, the Dutch pension system consists of three pillars: (1) the state pension ("AOW"), (2) the supplementary collective pensions, and (3) the private individual pension products that individuals can arrange for themselves. These three pillars determine the pension amount that a person will receive after retiring, and can be summarised as follows:

First pillar: AOW

The AOW is governed by the Algemene Ouderdomswet (*General Old Age Pensions Act*). As compared to other countries, the Dutch state pension provides only a portion of the total amount of retirement benefits. The AOW provides basic income, the amount of which is linked to the statutory minimum wage and depends on the individual circumstances of the recipient (e.g. composition of family, dependants, home situation)[1]. Every person who has lived or worked in the Netherlands between the age of 15 and their retirement age has a state pension and a right to AOW benefits. The retirement age (the moment a person starts receiving the AOW benefits) has recently been raised from 65 to 67. For individuals born after 1 January 1955, the retirement age is 67. Beginning in 2022, the retirement age will be linked to the general life expectancy. AOW benefits are funded by contributions that are paid by people younger than the retirees (*pay-as-you-go*). AOW obligations and benefits are not addressed in this article.

Second pillar: supplementary collective pension

The second pillar consists of collective pension schemes, which are typically arranged between employees and their employer ("Employer"). Due to the relatively limited nature of the first pillar, the amounts received through the second pillar constitute an important part of the Dutch pension system.

Collective pension schemes in the Netherlands are most commonly administered by a pension fund or, alternatively, by an insurance company. Under Dutch law, pension funds are legal entities and operate separately and independently from the Employer. As a result, pension funds generally are not directly affected if an Employer faces financial difficulties.

There are three different types of pension funds: (i) sectoral pension funds *(bedrijfstakpensioenfondsen)*, which constitute approximately 75% of the pension assets in the Netherlands, (ii) company pension funds *(ondernemingspensioenfondsen)*, and (iii) occupational pension funds *(beroepspensioenfondsen)*, that is, pension funds that are mandatory for specific groups of independent professionals.

The second pillar is financed by capital funding: from the contributions that scheme members paid for in the past and from the investment return on those contributions. Collective pension schemes in the Netherlands are the subject of this article.

1 For an indication of the cap on AOW benefits, see: http://www.svb.nl/int/en/aow/hoogte_aow/bedragen/index.jsp

Third pillar: supplementary individual pension

The third pillar is formed by individual pension products. Individual pensions are mainly used by the self-employed and by employees in sectors without a collective pension scheme. Employees may privately purchase products in the third pillar to meet their additional requirements, often taking advantage of tax benefits. Private individual products are not addressed in this article.

Collective pension schemes and the Dutch Pensions Act

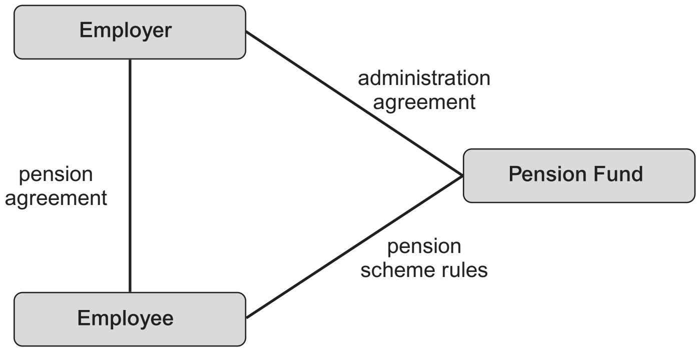
The Dutch Pensions Act (*Pensioenwet,* "Pw") manages collective pension schemes that are governed by sectoral and company pension funds. This contribution focusses on the Pw. The Act concerning Compulsory Membership of an Occupational Pension Scheme (*Wet verplichte beroepspensioenregeling, "WVB"*) applies to occupational pension funds.[2]

The Pw's primary goal is to preserve and secure the accumulated pension rights of employees. This goal is most clearly manifested in article 23 Pw, which stipulates that an Employer must transfer (*onderbrengen*) the pension rights of its employees to an external entity. Because of the obligation to transfer a pension scheme to a pension provider, the pension assets of former employees are shielded from the Employer's entrepreneurial risk (*ondernemingsrisico*). With this, pension capital cannot be used by the Employer for purposes unrelated to pensions. Thus, capital intended for pension distributions, which has already been transferred to a pension fund, is usually not lost if an Employer becomes bankrupt.

Typically, collective pension schemes are employment-based and as such, they are arranged between Employer, employee and an independent external pension fund. The legal basis of a collective pension scheme consists of a pension agreement (*pensioenovereenkomst*) in which the Employer and employee agree upon the conditions of the pension. The pension agreement is commonly included in individual employment agreements or in the collective bargaining agreement (*collectieve arbeidsovereenkomst*). Only rarely will the pension agreement be a separate agreement. After entering into a pension agreement with the employee, the Employer delegates the execution of the pension agreement to a pension provider (article 23 Pw). Arrangements between the Employer and the pension provider about the execution of the pension plan (premium contribution, indexation, etc.) are included in the administration agreement (*uitvoeringsovereenkomst*). The relationship between the pension provider and the employee is governed by the pension scheme rules (*pensioenreglement*), which in turn are determined by the provisions in the pension agreement and the administration agreement. The pension scheme rules stipulate the individual pension rights and pension obligations of an employee in regard to the respective pension fund.

2 Due to the limited role of occupational pension funds in the Dutch pension system, the WVB will not be expanded upon separately.

This triangular relationship can be depicted as follows:



Three forms of pension agreements

As stipulated by article 10 Pw, three types of pension schemes are possible and their differences are characterised by whether they focus on defined benefits, capital or contributions.

In the first type of plan, the defined benefit scheme (*toegezegd-pensioen-regeling*), the employer and employee agree upon a benefit of a defined amount that the employee will receive as from a defined age. The defined benefit plan places both the investment risk and the risk of a change in life expectancy with the pension fund. For defined benefit plans, a final pay scheme (*eindloonregeling*) used to be the norm in the Netherlands. However, today the career average system (middelloonregeling) is the most common type of defined benefit plan.

In the second type of scheme, the defined capital scheme (*toegezegd-kapitaal-regeling*), only the amount of capital that will be available on the date of retirement is defined. On the date of retirement, the defined capital will be converted into pension benefits against rates determined at that time. A defined capital scheme places the investment risk with the pension fund. However, during this period of accumulation, this risk of a change in life expectancy remains with the employee, as only at the retirement date does the conversion rate become known.

The third type of scheme, the defined contribution scheme (*toegezegde-bijdrage-regeling*), places both the investment and life expectancy risk with the employee. In this type of agreement, only the amount of the contribution is determined and, as a result, the amount of the final pension benefit is unknown. As a result, the employee bears the entire risk. Different varieties of defined contribution plans exist where some or all of this employee risk is insured.

Defined benefit schemes are currently being phased out of the Dutch pension system. Defined capital is already a rare occurrence. Defined contribution schemes currently make up the bulk of pension agreements of the current working population. However, as far as the current generation of (soon-to-be) retirees is concerned, a substantial part of these pensions is accumulated under defined benefit schemes.

Interaction with the Dutch tax regime

As previously stated, in the Netherlands an Employer must transfer the pension rights of his employees to a pension fund. Pension funds are legally independent entities and operate separately from the Employer. Pension funds are treated as separate taxpayers from Employers; as a result, a pension fund's (negative) investment performance cannot result in any Employer tax deductions. Further, Dutch pension funds have a preferred tax position and effectively are tax exempt in the Netherlands (or, more precisely, are taxed against a zero percent rate).

However, as the Dutch government encourages accumulation of pension through tax incentives, general tax advantages do exist for employee pension contributions. Within a scheme's specific limits (see below), the accumulation of pension is tax exempt. This means that tax is not levied on an Employee's contribution towards his or her pension, or on the growth of his or her pension via the pension fund's investment performance (article 11:1(c) of the Wage Withholding Tax Act 1964, *Wet op de loonbelasting 1964*). Pension benefits are only taxed when they are paid out and received as income by a retiree. This is called the reversal rule (*omkeerregel*). Income received after retirement is taxed at a lower rate than the rates that apply to income earned during working life, thus making the accumulation of pension funds financially attractive.

General limits on second pillar pension plans

The reversal rule effectively results in a government subsidy and, as such, it is somewhat politically controversial. This has resulted in placing limits on the advantages of second pillar pension accumulation.

Today, the aim of collective pension schemes in the Netherlands is for an employee to accumulate 75% of his or her career-average wage as a second pillar pension (aside from what is possible in first pillar AOW benefits) in a forty-year time span. For the most part, the limits on the accumulation of collective pension schemes are of a fiscal nature. As longs as a pension scheme stays within these limits, no tax is levied on the accumulation of pension.

The maximum accumulation rate differs according to the type of pension scheme the employee participates in. It should be noted that the maximum accumulation rates have been lowered as of 1 January 2015 (Witteveen regime). Generally, the total accumulated pension rights cannot surpass an employee's final earned wage. Additionally, as of 1 January 2015, the fiscal benefits on pension accumulation are limited to a pensionable wage with a maximum of EUR 100,000.

We stress that these limits apply only to the part of an employee's wage from which he or she derives second pillar pension contributions. This portion excludes the part of an employee's wage from which his or her pay-as-you-go contributions towards the first-pillar AOW are collected. This excluded amount is known as the AOW-franchise.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

Two regulatory bodies exist in the Dutch pension system: the Dutch Central Bank (*De Nederlandse Bank,* "DNB") and the Dutch Authority for the Financial Markets (*Autoriteit Financiële Markten,* "AFM"). DNB and AFM are supervising authorities and do not adjudicate individual disputes (article 152 Pw).

DNB and requirements regarding financial position of pension funds

DNB examines the financial position of pension funds (*prudentieel toezicht*). DNB assesses whether pension funds are financially healthy and whether they can be expected to fulfil their financial obligations in the future.

The requirements for the financial position of pension funds in the Netherlands are set out in the Financial Assessment Framework (*Financieel Toetsingskader,* "FTK"), which is part of the Pw (articles 125a-150). In keeping with the FTK, a pension fund must always have sufficient assets available to pay out the accumulated pension benefits of its contributors.

Additionally, the FTK sets criteria for pension funds' coverage ratio (*dekkingsgraad*), that is, the ratio between the assets of a pension fund and the pension benefits to be paid out in the future (obligations). Under the FTK, a pension fund must value its assets and liabilities at fair value. Importantly, the FTK stipulates that liabilities must be discounted at the risk-free interest on the capital markets (*ultimate forward rate*). For each pension fund liability, there is a "dot" on the swap curve that matches the duration of that particular liability. If the discount rate decreases, a pension fund needs more assets today in order to be sure it can generate sufficient investment returns to pay a projected amount of benefits in the future. Since 2008, the risk-free rate has decreased to a historically low level of currently around 1.7% (2015).

In the case of a funding shortfall (as outlined in article 132 Pw), a pension fund must notify DNB and submit a recovery plan (article 138 Pw). In the recovery plan, the fund should explain how the coverage ratio will regain the required level within ten years. Recovery plans have to be actualised every 12 months.

Lastly, article 134 Pw provides an emergency "safety valve", on the basis of which pension claims can be cut back. If, in light of the applicable FTK, a pension fund has inadequate assets compared to its current obligations and this situation has not improved after the recovery period, the pension fund can decrease pension rights to bring pay-outs into line with its existing capital. This ensures that at any given time, a pension fund does not have more obligations than it can fulfil with its existing capital. Therefore, it is generally believed in the Netherlands that pension funds are not susceptible to bankruptcy.

Conduct supervision

The AFM monitors the conduct of pension funds (article 151 Pw). The obligation of pension funds to periodically inform employees on the accumulation and growth of their pension rights is supervised stringently (articles 38-51 Pw).

QUESTION 3

How are the plans governed?

Pension funds are separate entities in the Netherlands and are governed by their own independent boards. As of 1 July 2014, the Pw (as amended based on the *Wet versterking bestuur pensioenfondsen,* "Pension Fund Governance Act"), provides for five types of governance models: the joint model, the independent model, and three mixed one-tier board models.

Joint and independent models

In the joint model, the board consists of representatives from the three stakeholder groups: (i) the Employers, (ii) employees, and (iii) pension beneficiaries. The employee and beneficiary representatives together hold the same number of seats as the employer representatives. It is possible to add two seats on the board for one or two independent directors who do not directly represent stakeholders in the fund. In the joint model, the supervision of the board is exercised by a permanent supervisory board consisting of independent members. For a sectoral pension fund, the supervisory board is mandatory; a company pension fund may instead opt for annual visitation by a visitation committee.

In the independent model, the board includes at least two independent professional board members. They are ''independent'' in that they do not directly represent any pension fund stakeholders. In this model, supervision is structured in the same way as in the joint model.

Mixed models

The mixed board models are all varieties of a one-tier board model, where both executives and non-executives have seats on the board. There are three types: (i) the independent mixed board, with both the executive and the non-executive members being independent (not directly representing stakeholders), (ii) the joint mixed board, where the executive directors are representatives of the three stakeholder groups (again, plus the option of one or two external directors) and the non-executive directors are independent persons, and (iii) the inverse mixed model, where the executive directors are independent professional directors, and the non-executive directors are representatives of the three stakeholder groups.

In each type of the mixed board model, there are at least three non-executive directors. These directors are charged with the supervision of the executive directors. The chairman has to be a non-executive director. In addition, in the inverse mixed board, the chairman may not be a representative of the pension fund stakeholders; this means that the number of non-executive directors in the inverse mixed model is at least four.

The joint mixed board model and the inverse mixed model have an accountability body (*verantwoordingsorgaan*) which fulfils the external supervisory role. The board is accountable to this body with regard to the board's policy and how the policy is conducted, and the accountability body may express its views on this. The accountability body also has advisory rights, and it may initiate appeals and corporate inquiry proceedings before the Enterprise Chamber of the Amsterdam Court of Appeal. The accountability body consists of employee and pensioner representatives, and – if all stakeholder groups agree – employer representatives. As the three stakeholder groups are not represented on the board in the independent mixed board model, this model also includes a stakeholder body (*belanghebbendenorgaan*). The powers of the stakeholder body are similar to those of the accountability body, but the range of issues in which they may advise is wider. In addition, the stakeholder body is granted certain rights of consent, which the accountability body lacks.

QUESTION 4

Is there a compensation fund for pension benefits?

The Dutch government believes pension funds should not be susceptible to bankruptcy, which is reflected in the stringent financial framework pension funds have to comply with, and their options in case of a shortfall (see Question 2). Considering this stringent regulation and strict supervision, there is no compensation or guarantee fund for pension liabilities in the Netherlands.

However, the Dutch government could face member state liability under European Union law, more precisely Directive 2008/94/EC. According to article 8 of the Directive 2008/94/EC, member states must ensure that the necessary measures are taken to protect the interests of (former) employees at the date of the onset of the Employer's insolvency in respect of rights conferring on them immediate or prospective entitlement to old-age benefits. In its 2007 Robins-ruling, the European Court of Justice ("ECJ") declared that, in light of article 8 Directive 2008/94/EC, national provisions of an EU member state in which a minimum of 49% of all accumulated pension rights are not safeguarded do not adequately protect these rights[3]. Subsequent to the Robins case, in 2013 the ECJ decided in the Hogan case that the Irish government had inadequately protected the interests of (former) employees when merely 16 to 41 percent of the accumulated pension remained after the insolvency of an Employer[4].

As stated above, it is unlikely that an employee in the Netherlands would face a pension deficit of more than 50%. Nevertheless, it can still be concluded that the outcome of Directive 2008/94/EC and its case law provides a theoretical minimum for employees with a pension that falls under the Dutch pension regime.

[3] ECJ 25 January 2007, C-278/05 (Robins v Secretary of State for Work and Pensions), paragraph 57.

[4] ECJ 25 April 2013, C-398/11 (Hogan v Minister For Social And Family Affairs, Ireland), paragraph 53.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

In the Netherlands, employees receive their pension rights regardless of the insolvency of a (former) Employer, as their contributions have been transferred to an independent pension provider, which is separate from the Employer. The Pw also stipulates that all claims must be fully funded. The combination of these factors means that under Dutch law, in principle, accumulated pension rights are protected from Employer bankruptcy.

As regards the Employer's unfulfilled former and future obligations, in "inability of payment" (*betalingsonmacht*) situations, the Dutch Employee Insurance Agency (*Uitvoeringsorgaan Werknemersverzekeringen*, "UWV") will take over some of the Employer obligations and will continue to pay wages for a designated period of time. This also includes the Employer's obligation to pay pension contributions.
Under article 61 in conjunctions with article 64 of the Unemployment Benefits Act (*Werkeloosheidswet,* "WW") an employee whose Employer has been declared bankrupt is entitled to payment of any outstanding amounts relating to the employment relationship between the Employer and the employee that are owed to third parties.
In a situation where the employee loses pension claims because of the Employer's non-payment of the pension fund contribution, the UWV will fund these pension contributions. UWV will make payments relating to outstanding / unpaid amounts as described above that relate to a period of no longer than one year prior to the inability of payment. It is currently unclear whether the UWV's obligation to take over outstanding contributions includes contributions that have been withheld by an Employer from wages, but have not been paid to the pension fund. If and in as far as the UWV pays out amounts to employees, it subrogates to the claims of the employees against the employer, including the right to be preferred to other creditors.

Finally, the WW, the statute that stipulates these guarantees, does not only apply to bankruptcy proceedings. It also applies to suspension of payment proceedings and situations in which the Employer can demonstrate severe financial difficulties.

Consequences of non-payment of pension contributions

If pension contributions cannot be paid from the insolvent estate, the absence of pension contributions has no effect on the pension if the pension plan is being administrated by a pension fund. The "no contribution, no pension" principle does not apply to pension funds. As long as the pension fund has resources, an employee's accumulated pension rights will stay intact. If the pension plan is administrated by an insurance company, the build-up claims can be reduced. In that case, the rules for conversion into a paid-up policy (after notification of payment arrears) as set out in articles 29 Pw and article 39 WVB apply.

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

The bankruptcy of an Employer in itself does not release it from its obligations, contractual or otherwise, to make employer contributions and fulfil its pension obligations towards its employees. Contributions have to be made until a pension plan is terminated or until employees of the bankrupt entity are dismissed. In the case of bankruptcy proceedings, most employment agreements are usually terminated by the bankruptcy trustee. Generally, termination of an employment agreement leads to termination of participation in the pension scheme[5]. As described earlier, under Dutch law it is rare for a major pension rights deficit to remain through bankruptcy. However, it is possible for some claims to exist.

Typically, two types of claims remain in bankruptcy: (i) a claim from the employee against the Employer with respect to the outstanding payment of the employee's contribution to the pension fund, which has already been withheld from wages, and (ii) the claim from the pension fund against the Employer with respect to the Employer's unpaid contribution. The claim mentioned under (i) is considered back wages and is therefore a preferred claim as stipulated by article 3:288(e) of the Dutch Civil Code (*Burgerlijk Wetboek*). The claim mentioned under (ii) does not constitute back wages and, thus, is not a preferred, but an ordinary claim.

Furthermore, if an Employer is declared bankrupt, a distinction is made between (i) claims dating from the period leading up to the date of the bankruptcy, and (ii) claims dating from after the adjudication of the bankruptcy. The claims under (i) are, in principle, claims that can be submitted in the bankruptcy proceedings (*verifieerbare vorderingen*), which can be preferred or ordinary claims. The claims mentioned under (ii) are in principle claims on the bankrupt estate (*boedelvorderingen*).

From the date bankruptcy is declared, the wages and the Employer contribution debts (*premieschulden*) related to the employment contract become estate claims, as long as the employment agreement continues after bankruptcy (art. 40 Bankruptcy Act). The contribution debts include the payable Employer pension contributions.

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

Should the matter be in regards to a sectoral pension fund, Dutch law provides for specific grounds for directors' liability for unpaid pension premiums (article 23, *Wet verplichte deelneming in een bedrijfstakpensioenfonds 2000,* Sectoral Pension Funds (Obligatory Membership) Act 2000, "Wet Bpf. 2000"). The managing board of the employer that is participating in a sectoral pension fund must report any expected inability to pay pension contributions to the sectoral pension fund. Should the managing

[5] The conditions of an individual employee's pension scheme (as set out in the pension agreement) is leading and can stipulate whether the scheme can be voluntarily continued by the Employer which, if so, is responsible for making the required contributions.

board timely report this inability to pay, the board members are in principle only liable if it can be assumed that the inability to pay the premium is the consequence of manifestly improper management occurring within the three years prior to the notification of the inability to pay (article 23, section 3 Wet Bpf. 2000). Should the managing board fail to do so in a timely manner, it is presumed that non-payment is attributable to the directors. This presumption can only be rebutted by a director who plausibly demonstrates that the absence of a timely notification / report of the inability to pay cannot be attributed to him (article 23, section 4 Wet Bpf. 2000). Liability based on article 23 Wet Bpf. 2000 is a liability towards the sectoral pension fund. If the relevant pension fund is not a sectoral pension fund – but, for example, a company pension fund – director liability does not apply.

Liability for pension deficits can also be based on different, more general, grounds such as guarantees issued by the shareholder or unlawful acts by the directors and / or shareholders. In practice, director liability towards employees has been assumed if the company (employer) has deducted pension premium from the employee's salary, but has not made the related contributions to the pension fund.

QUESTION 8

Are there any cross-border features of your pension regime?

The Dutch pension regime has many cross-border features, of which a part is based on the EU Directive 2003/41/EC on the activities and supervision of institutions for occupational retirement provision (the "Pensions Directive 2003")[6]. This includes provisions regarding: the law applicable to the pension agreement and the administration agreement (and the applicability of national social and labour legislation), outsourcing, execution and regulatory supervision. We do not elaborate on these types of cross-border features, as they fall outside the scope of this book.

As described in Question 7, the Dutch pension regime has legislation imposing directors' liability for unpaid pension premiums under certain circumstances. The Pw has special provisions regarding the joint and several liability for contributions regarding unpaid pension premium by employers located outside the Netherlands, with respect to sectoral pension funds. This legislation provides that either of the following is jointly and severally liable for such contributions: (i) the "leader" (*leider*) of a permanent establishment in the Netherlands, (ii) the permanent representative of such "leader" located in the Netherlands, or (iii) the person in charge of the business conducted in the Netherlands (article 22 Wet Bpf. 2000).

We note, perhaps superfluously, that since pension funds in the Netherlands are separate legal entities, the Dutch pension regime does not need and has thus not implemented any long-arm legislation that imposes liability on foreign corporate group members for the pension deficits of companies located in the Netherlands, as is the case in, for example, the United States and England.

6 Part of the Pension Directive 2003 was modelled after the Dutch pension regime, for which reason implementation did not require drastic amendments to the Dutch pension regime.

QUESTION 9

Discuss the state of defined benefit plans in your country

In 2013, many pension funds had to lower the pensions of participants. In order to prevent this from happening again and to create more certainty with respect to pensions, new legislation was implemented in 2015. Although pension funds are struggling to maintain sufficient buffers, partially due to low interest rates, retirement income security is generally considered to be secure.

The State Secretary for Social Affairs and Employment (*staatssecretaris van Sociale Zaken en Werkgelegenheid*) has announced that further steps in pension reform will follow, and progress is being made with respect to the draft bill general pension fund (*wetsvoorstel algemeen pensioenfonds*), which aims at implementing a general pension fund (*algemeen pensioenfonds,* “APF”) in the Netherlands. An APF is a new type of pension fund. The characteristic of the APF is that it can split off separate capital for the diverse pension schemes administered by the fund. With this, the Dutch legislature would accept an exception to the “prohibition on ringfencing” as meant in article 123 Pw.

UNITED KINGDOM

QUESTION 1

What is the legal framework for private pension plans in your country?

Structure of private pension plans in the UK

Private pension plans in the UK are provided under two broad structures, “Personal Pension Plans” and “Occupational Pension Schemes”.

Personal Pension Plans

Personal Pension Plans have historically been set up by an Independent Financial Advisor on an individual’s behalf. The arrangements are usually known as “insured” or “contract” schemes whereby the individual pays into a pooled investment fund directly from their banks.

There are a large number of investment fund products on the market each with different risk characteristics to suit different personal circumstances (e.g. such as the age of the individual). These are structured to a predefined risk and return criteria and essentially pool the funds of their members to purchase investments. The members therefore purchase “units” in the fund through their contributions.

The UK government has, in recent years, sought to address what it considered was an increasing reliance on the State Pension Scheme[1] to provide for retirement. In 2001, the UK government introduced legislation to oblige employers to provide their employees with access to a new type of pension arrangement called “Stakeholder Pension Schemes”. These are essentially a type of Personal Pension Plan that are designed to be a simpler and cheaper option than existing Personal Pension Plans on the market, making it feasible for employees to contribute as little as £20 per month. They are aimed at employees who do not have access to an Occupational Pension scheme or a Personal Pension Plan.

Contributions are paid after the deduction of income tax but, where the plan is an “approved”[2] scheme, the investment fund managers are able to reclaim tax on the individual’s behalf and pay this into the fund on top of the direct contribution.

As Personal Pension Plans are largely arrangements entered into by individuals outside of their employment, the remainder of this chapter focuses on Occupational Pension Schemes.

Occupational Pension Schemes

Occupational Pension Schemes are set up by an employer on behalf of its workforce. These are structured with the assets held separately to those of the employer (usually in a Trust) and can be defined benefit or defined contribution.

1 The State Pension Scheme provides a capped weekly pension, is part funded by the UK government and part funded by individuals through “National Insurance “ contributions.

2 Approved by Her Majesty’s Revenue and Customs for tax purposes under the Finance Act 2004.

The UK Government introduced further measures to tackle the aforementioned reliance on the State Pension Scheme under the Pensions Act 2008. This introduced the requirement for employers to automatically enroll employees into a qualifying pension scheme[3] unless the employee opts out. This requirement was an evolution on the previous legislation (which was therefore phased out) requiring employers to provide employees with access to Stakeholder Pension Schemes.

Given that this would force considerable set up costs on employers that did not have access to a qualifying scheme, the UK Government set up NEST[4] as a qualifying pension scheme employers can enroll their employees into. However, employers may be able to use an existing Occupational Pension Scheme or Stakeholder Pension Scheme, if it met the qualifying criteria under the auto enrolment legislation.

Overview of UK legal framework

The UK operates under three separate legal jurisdictions (England and Wales, Scotland and Northern Ireland). However, the majority of key legislation relevant to retirement benefit provision is nearly identical across all three legal jurisdictions.

Legislation is introduced either as an Act of the UK Parliament or through Statutory Instruments that have been made under the authority of an Act of the UK Parliament.

The main legislation that governs Occupational Pension Schemes can be summarised under two main strands: pension specific legislation and trust law, we outline both below.

Pensions specific legislation

UK pensions legislation has evolved considerably over the last 20 years to improve pension plan governance following a number of high profile pension funding scandals.

The current form of the legislative framework was introduced through the Pensions Act 2004. A number of other Acts and Statutory Instruments have also been introduced since then but the Pensions Act 2004 remains the main legislation by which Occupational Pension Schemes are now regulated and governed.

Trust law

As most Occupational Pension Schemes are Trusts, trust law is also a key legislative feature of pensions provision and is a complex legal area. Trust law has evolved over a significant period of time and encompasses primary legislation such as Acts of the UK Parliament (and rules made under them), under common law established by a body of legal cases and, more recently, supplemented by regulatory guidance issued by the Pensions Regulator.

The primary aspect of Trust law relates to the regulation of a Trustee's duties and behaviour with an overriding duty to act in the interests of the beneficiaries of the trust. This means that Trustees must avoid a conflict of interest and not profit from the trust and distils into specific duties such as a duty to act impartially, a duty to not benefit themselves and duty to act with reasonable skill and care.

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3 Needs to meet a number of minimum requirements, depending on the scheme type, such as minimum contribution levels, benefit levels etc.

4 National Employment Savings Trust.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

Overview

The Pensions Act 2004 established the Pensions Regulator as the UK regulator of Occupational Pension Schemes, replacing its predecessor the Occupational Pensions Regulatory Authority.

The Pensions Regulator is an independent arm of the Department for Work and Pensions and regulates largely through issuing Regulatory Guidance notes and Codes of Practice. However, it also has far reaching powers to enable it to fulfil its statutory objectives[5].

Its powers are, broadly, to enable it to investigate, remedy and act against avoidance. For example, it can intervene where it considers members' benefits are at risk (see Question 7 later) but can also prohibit a person from being a trustee of a pension scheme where it deems they are not "fit and proper" to do so.

The Pensions Ombudsman in an independent organisation set up under the Pension Schemes Act 1993 and funded by the Department of Work and Pensions to deal with complaints by members in respect of either Personal Pension Plans or Occupational Pension Schemes. Decisions made by the Pensions Ombudsman are binding on both parties.

Reporting

Occupational Pension Plans have a range of mandatory reporting requirements:

Audited annual financial statements

Under the Occupational Pension Schemes (Requirement to obtain Audited Accounts and a Statement from the Auditor) Regulations 1996, all Occupational Pension Plans require audited financial statements produced annually unless they are exempt[6].

The financial statements need to include a statement from the trustees as to whether they are prepared in accordance with the Statement of Recommended Practice "Financial Reports of Pension Schemes[7]" and must be audited by an independent firm of registered auditors.

Members can request a copy of these financial statements but there are otherwise no requirements for these financial statements to be published or filed. However, many trustees typically send their members a copy of the accounts or publish them on a dedicated website as part of transparent governance.

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[5] To protect members' benefits, promote and improve good administration, reduce the risk to the Pension Protection Fund, maximise employer compliance and minimise any adverse impact on sustainable employer growth from achieving the requirements of Part 3 of the Pensions Act 2004 (Scheme funding).

[6] Typically schemes with less than 12 members.

[7] As amended from time to time.

Strictly speaking, the trustees need to have obtained signed, audited financial statements within seven months of the scheme's financial year end. However, the Pensions Regulator will not normally require the trustees to inform them of a breach of this requirement provided that the signed, audited financial statements are received within a "short" period of the deadline.

Scheme Annual Return

Trustees are required to submit a Scheme Annual Return to the Pensions Regulator which outlines a range of information in respect of the scheme, its funding and membership.

Scheme Specific Valuation

All defined benefit Occupational Pension Schemes require a Scheme Specific Valuation preparing every three years.

This valuation is prepared by the scheme's actuary and outlines the extent to which members' accrued benefits are funded.

The trustees work with the scheme's actuary to determine the required level of prudence of the valuation assumptions based on a number of factors, the most important of which is the trustee's assessment of the sponsoring employer's ability to underwrite the funding of the scheme[8].

To the extent that this valuation highlights a deficit in funding, the sponsoring employers are required to fund the deficit and the trustees will negotiate with them an appropriate, affordable deficit recovery plan.

If the scheme remains open to the future accrual of benefits, the scheme's actuary will also recommend the level of contributions required from members and the employers to fund future benefits based on current market conditions and actuarial guidance.

QUESTION 3

How are the plans governed?

Trust structure

As explained earlier, Occupational Pension Schemes are structured as trusts and managed by a board of trustees. The Board comprises individuals appointed by both the employer and elected by the plan's members for a fixed period of time. After this period, they can stand for re-election if they wish but others may be nominated to stand against them.

The trustees manage the scheme in accordance with its constitution, its "Trust Deed and Rules" and with UK legislation. These rules stipulate a range of matters including the number of trustees required and the split between employer and member nominated trustees.

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[8] Known as the "employer covenant".

General administration of the plan

In addition to the Trust Deed and Rules, the trustees will also have a number of other policy documents which they use to guide their day to day decision making such as the "Statement of Investment Principles" and the "Statement of Funding Principles".

Contributions are usually made by the employee (as a deduction from their pay) and by the employer. The combined contributions are then paid across to the scheme and must be received no later than the 19th of the month[9] following the month in which the deduction is made from the employees' pay.

The trustees will then be responsible for investing the scheme's funds in line with the Statement of Investment Principles, which ensures they balance the requirements of getting the best return for the members whilst reflecting the right amount of investment risk given the membership profile and funding position of the scheme.

With larger schemes, decision making is often delegated to sub-committees of the main trustee board such as a valuation sub-committee or investment sub-committee.

Role of advisers in plan governance

The trustees' management of a modern day Occupational Pension Scheme requires the navigation of complex funding, investment and legal issues. As the majority of trustees are usually employees or former employees of the business, they rarely have the necessary skills to be able to make all decisions without the assistance of a range of professional advisors. Some of these are outlined below.

Scheme actuary

The actuary's role is a formal, personal appointment to the scheme. The actuary is responsible for modelling and monitoring the overall funding position of the scheme and is required to formally sign off the Scheme Specific Valuation and any associated recovery plan every three years.

Investment managers

Investment management is a complex area and whilst the trustees have overall responsibility for managing the scheme's funds in line with its Statement of Investment Principles, they will appoint a professional investment manager to advise them on investment strategy and risk and deal with the day to day management of the scheme's investments.

Scheme lawyer

As explained earlier, the pensions legal framework is complex and as such, the trustees will retain a lawyer that specialises in pensions law to advise them on the myriad of legal issues that arise.

Scheme administrators

The day to day management of Occupational Pension Schemes is often delegated to a specialist firm of scheme administrators who have the systems to manage accounting, payroll, administration and scheme enquiries.

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9 22nd of the month where paid electronically.

Scheme auditor

As explained earlier, all Occupational Pension Schemes require their financial statements to be audited by a registered[10] auditor and for them to have been signed within eight months of the plan's financial year end.

Other advisors

On top of the above key advisors, the increasing complexity of scheme management results in trustees requiring the services of a myriad of other advisors including fiduciary managers, trustee secretarial services and employer covenant advisors.

The role of the Independent Trustee

Despite the support from specialist advisors, trustees remain ultimately responsible for making appropriate judgements when decision making. Key decisions on the funding, governance and structure of an Occupational Pension Scheme will often require a negotiation with the sponsoring employer, placing a number of the trustees, many of whom remain employed by the sponsoring employer, in a potential position of conflict given their duties under trust law.

This has seen an increase in the number of schemes which have appointed an Independent Trustee to the board. These professional trustees have significant pensions experience gained from previous roles as investment managers, actuaries, lawyers or chartered accountants. As the Independent Trustee usually has considerably more pensions experience, they will often Chair trustee meetings and lead negotiations with the sponsoring employers.

QUESTION 4

Is there a compensation fund for pension benefits?

The Pension Protection Fund overview

The Pensions Act 2004 established the Pension Protection Fund, an independent statutory fund, to provide compensation to members of eligible defined benefit occupational pension schemes in the event of a qualifying insolvency event of the sponsoring employer.

The Pension Protection Fund is funded through an annual levy paid by all UK defined benefit pension occupational schemes. The levy comprises two elements, the Scheme based levy (calculated by reference to the scheme's deficit[11]) and the Risk Based Levy (calculated by reference to the insolvency risk of the employer[12]). The levy is structured in such a way as to be geared towards those schemes which bear a higher risk of compensation being payable by the Pension Protection Fund (c.80% of the total levy is generated from the Risk Based Levy).

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[10] A registered auditor is a firm that undertakes regulated audit work and that is registered with a recognised supervisory body (Institute of Chartered Accountants in England and Wales, Institute of Chartered Accounts of Scotland, Association of Chartered Certified Accountants, Chartered Accountants Ireland and Association of Authorised Public Accountants).

[11] Calculated on a basis set out by s.179 of the Pensions Act 2004.

[12] Calculated based on Experian insolvency risk tables for each employer produced for the Pension Protection Fund.

Pension Protection Fund compensation is payable when certain conditions are met, primarily that:

- The sponsoring employers have entered a qualifying insolvency event[13]; and

- The plan has a deficit, when calculated under the basis set out under s.143 of the Pensions Act 2004, at the relevant date of the insolvency.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor

Notification of insolvency

The insolvency office holder must, within 14 days of the qualifying insolvency event (or, if later, the date on which they first becomes aware of the existence of the defined benefit occupational pension scheme) issue a notice of their appointment in the prescribed form[14] to each of the Pension Protection Fund, the Pensions Regulator and the trustees of the scheme. In practice, however, this is sent electronically to the Pension Protection Fund who then escalates the notice to the Pensions Regulator and the trustees of the scheme on behalf of the office holder.

This notification allows each party to take the necessary steps to fulfil their obligations as regards the scheme.

Pension Protection Fund assessment period

Once the Section 120 notice is received and validated by the Pension Protection Fund, provided the entry criteria are met, the scheme enters an "assessment period".

During this period, which is a maximum of two years, the Pension Protection Fund works with the trustees to review the accuracy of data held in respect of the scheme's members and the scheme's assets. Following the conclusion of the assessment period, the Pension Protection Fund takes over the scheme's assets and liabilities.

During the assessment period, the trustees will continue to manage the day to day activities of the scheme, under the supervision of the Pension Protection Fund. However, benefits are paid at a level which would be payable as compensation by the Pension Protection Fund (see below).

However, once the Section 120 notice has been received and validated, the Pension Protection Fund takes over the rights of the scheme as a creditor of the sponsoring employer such as the rights to prove as a creditor, the right to vote at creditors' meetings, negotiating compromise agreements and representing the creditors as a member of a creditors' committee.

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[13] Set out under the Pension Protection Fund (Entry Rules) Regulations 2005. For corporate employers, the qualifying insolvency events are Administration, Administrative Receivership, Creditors' voluntary winding up, Winding up by the Court, Creditors' Voluntary Arrangement but excludes Members' voluntary winding up and Schemes of Arrangement. For individuals that are employers, the qualifying insolvency events are Bankruptcy, Individual Voluntary Arrangements.

[14] A Section 120 notice, pursuant to Section 120 of the Pensions Act 2004.

The compensation payable

Once the scheme has been accepted, the Pension Protection Fund pays compensation to the scheme's members. Only certain members[15] of the failed scheme will receive their full benefit entitlement with the remaining members receiving 90% of their entitlement, subject to an overall compensation cap[16].

The involvement of the Pensions Regulator

On receipt of the Section 120 notice, the Pensions Regulator may consider appointing an Independent Trustee if it is deemed appropriate (for example where the scheme does not already have a trustee with the requisite experience of assessment periods), will investigate any moral hazards of the sponsoring employer and use its powers to sanction, where requested by the Pension Protection Fund (for example, where the trustees do not comply with legislative requirements).

QUESTION 6

Are there any special priorities for the pension deficit in an insolvency?

Preferential claim

Schemes have a preferential claim in the sponsoring employer's insolvency for any unpaid employee contributions[17] relating to benefit accrual in the four months preceding the insolvency event.

Preferential creditors are paid in priority to any holders of a floating charge but after the costs of the insolvency have been paid (including the remuneration of the office holder).

Unsecured claim

As explained previously, the Pension Protection Fund assumes the right to prove as a creditor in the insolvency of the sponsoring employer. However, any amounts due to the scheme over and above the preferential claim referred to above will rank as an unsecured claim, unless the scheme benefits from some security over the sponsoring employer's assets.

The scheme's unsecured claim will generally comprise the full past service deficit of the scheme[18], any unpaid employer contributions (relating to benefit accrual and past service) and any unpaid employee contributions which relate to payroll periods more than four months prior to the date of the insolvency appointment.

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[15] Generally members who are at or above the scheme's normal retirement age, are in receipt of a survivor's pension or in receipt of an ill health pension.

[16] Cap is £36,401.19 from 1 April 2015 with an age related adjustment factor applied.

[17] Depending on the scheme, in some circumstances, the employer contributions may also be preferential.

[18] Calculated in accordance with Section 75 of the Pensions Act 1995.

The scheme's unsecured claim will not have any special priority. However, in many cases, it is likely that the scheme is the single largest unsecured creditor in the insolvency and as such, will have considerable influence in voting on resolutions at creditors' meetings (for example, voting on the basis of the officeholder's remuneration).

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

Overview of the Pension Regulator's powers

The Pensions Act 2004 provides the Pension Regulator with a range of powers to enable it to protect the benefits of members of Occupational Pension Schemes.

These powers allow the Pensions Regulator to investigate schemes, remedy problems when identified and to act against avoidance. This latter category relates to what are commonly known as the Pension Regulator's "moral hazard" powers, of which there are two as outlined below.

Financial Support Directions

A Financial Support Direction requires an entity connected to the sponsoring employer to put in place financial support for the scheme. This support can be in a number of forms (e.g. a cash payment, a guarantee or simply one or more of the connected entities accepting joint and several liability for the scheme's funding).

The Pensions Regulator will only issue a Financial Support Direction against the connected entity if the sponsoring employer is either a service company or is "insufficiently resourced[19]" and where the Pensions Regulator considers it reasonable to do so given the circumstances of the case. Typically, the Pensions Regulator will look to the degree of connectivity the entity has to the sponsoring employer and the extent to which it received any benefit from the sponsoring employer.

Contribution Notices

A Contribution Notice requires payment to be made to a defined benefit occupational pension scheme by an individual or entity connected with a sponsoring employer where that individual or entity was party to an act or deliberate failure to act that has resulted in a "material detriment" to the likelihood of accrued scheme benefits being paid.

The Pensions Regulator will only issue a Contribution Notice if it believes that the "statutory defence" has not been met and it is reasonable to impose liability on the individual or entity in the circumstances of the case. The Pensions Regulator has six years from the date the act or failure to act took place to issue a Contribution Notice.

The "statutory defence" is that the individual or entity gave due consideration to the extent to which the act or failure to act would have given rise to the material detriment, took all reasonable steps to eliminate or minimise the potential detriment and at the time of the act or failure to act, the individual or entity, given the circumstances of the case, could reasonably conclude that the act or failure to act would not detriment, in a material way, the likelihood of accrued scheme benefits being paid.

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[19] Typically where its assets are less than 50% of the scheme's deficit measured on the basis set out in Section 75 of the Pensions Act 1995.

A Contribution Notice may also be issued against an entity that fails to comply with a Financial Support Direction.

The Clearance Procedure

When a Group undertakes a major corporate transaction (for example a disposal of part of its business or a refinancing) which involves either directly or indirectly a sponsoring employer of a defined benefit pension scheme, there is a risk that this is perceived to have had a material detriment to the likelihood of accrued scheme benefits being paid and therefore opens up the possibility of the Pensions Regulator using its moral hazard powers.

In order to avoid this risk, the Group could opt to use the voluntary "Clearance Procedure" to obtain confirmation from the Pensions Regulator that it would not seek to use its moral hazard powers after the transaction takes place.

Whilst receipt of a Clearance Statement may reduce the post transaction risk, it has some challenges. Firstly, it will require the support of the trustees, many of whom are likely to work in the business and as such, presents confidentiality issues. Secondly, it may add to the timescales to complete the transaction due to the need to consult with the trustees (who do not necessarily meet regularly) and the time required for the Pensions Regulator to complete its assessment of the transaction.

Furthermore, the transaction must be completed on materially the same terms and structure as that presented in the Clearance Application otherwise the Clearance Statement will not be effective.

Examples of the Pensions Regulator exercising its moral hazard powers

The Pensions Regulator has stated that it will only use its moral hazard powers when it is reasonable and appropriate to do so and as such, there are only limited examples. Some high profile cases where the Pensions Regulator has exercised its moral hazard powers are below.

Sea Containers Limited

The Pensions Regulator issued its first Financial Support Direction against Sea Containers Limited, the Bermudan parent of the sponsoring employer of two UK defined benefit pension schemes. This followed several of the trading entities in the group entering US Chapter 11 bankruptcy proceedings. The issuing of the Financial Support Direction was on the basis that the UK sponsoring employer had close connections with its Bermudan parent which had received considerable benefits from the sponsoring employer prior to the Chapter 11 proceedings commencing.

Lehman Brothers / Nortel Networks

These were two separate, high profile cases regarding the status of a Financial Support Direction issued after the commencement of insolvency proceedings.

In both cases, the Pensions Regulator issued Financial Support Directions against various entities in the group of companies to which the UK sponsoring employers belonged. This was on the basis that the Pensions Regulator determined that it was reasonable for these entities to put in place financial support for the associated defined benefit schemes given the circumstances of those entities. The respective schemes had significant deficits (£130m and £2.1bn for the Lehman Brothers and Nortel schemes respectively).

In both cases, the Financial Support Directions were issued after the commencement of insolvency proceedings in the target entities. As a consequence of this, the High Court (and, later, the Court of Appeal) held that the amount of required support under the Financial Support Directions ranked as an expense of the insolvencies of the entities issued with the Financial Support Directions. This would have resulted in these amounts ranking ahead of the remuneration of the insolvency office holder and any secured creditors and would therefore have considerable implications for the pensions, other stakeholders and the insolvency process generally.

However, the Supreme Court (the highest court in the UK) overturned the previous decisions and established that amounts due to defined benefit schemes under Financial Support Directions (and Contribution Notices) rank as provable, unsecured debts rather than as an expense of the insolvency.

Michel Van De Welde

The Pensions Regulator issued a contribution notice against Michel Van De Welde, the parent company of Bonas UK Limited. This followed Michel Van De Welde purchasing Bonas UK Limited through a “pre-pack administration” via a newly formed subsidiary and was on the grounds that the process used to purchase Bonas UK Limited minimised the price paid for the business and resulted in the pension scheme liability being abandoned.

QUESTION 8

Are there any cross-border features of your pension regime?

As explained earlier, the UK pensions regime covers pension schemes operated in the three legal jurisdictions in England and Wales, Scotland and Northern Ireland.

Entities registered overseas often operate UK divisions that operate occupational pension schemes and as such, may be sponsoring employers and therefore subject to the legal framework in the same way as UK registered entities. Under UK law, only sponsoring employers have a legal obligation for their respective occupational pension schemes, even where they sit in a Group.

However, other entities in the Group may fall under the scope of the Pension Regulator’s moral hazard powers by virtue of being connected parties, even where they are overseas. The Pensions Regulator has endeavoured to exercise its moral hazard powers against overseas registered entities with mixed success, with only the Sea Containers case reaching a conclusion with the Bermudan parent ultimately putting in place an agreed financial support structure for the UK based pension scheme.

QUESTION 9

Discuss the state of defined benefit plans in your country

Divergence from defined benefit

Over the last 20 years, the increased risk and cost of defined benefit occupational pension arrangements has resulted in them gradually losing their place as employers' preferred method of retirement benefit provision.

As a consequence of this, many defined benefit occupational pension schemes have closed to new entrants and to future accrual and as such, remain as legacy liabilities to the sponsoring employers, largely disconnected from the employee benefit structure of the business.

The main factors behind these changes are outlined below.

Deterioration in funding

In the 1990's, a number of factors arose which resulted in a sharp deterioration in the funding position of defined benefit pension plans as a consequence of an increase in scheme liabilities.

Firstly, UK interest rates started to fall from their historical peaks of c.15% in 1990 to c.6% by 2000. This resulted in lower discount rates driving considerably higher present values of scheme liabilities.

Secondly, the Pensions Act 1995 introduced the requirement for pensions in payment to be increased in line with inflation.

Finally, there have been significant improvements in mortality rates resulting in members receiving pensions for longer.

Changes in accounting standards

Changes in accounting standards[20], requiring increased disclosure and the recognition of scheme deficits on the balance sheets of sponsoring employers, this caused considerable issues to businesses due to the commercial and financial implications of recognising previously off balance sheet obligations.

Complexity and cost

Defined benefit occupational pension schemes have seen increased regulation in order to protect members' benefits. Furthermore, there is increased complexity, particularly in group situations where there could be a number of legacy defined benefit pension schemes that have transferred with businesses acquired by groups.

This increased complexity has driven increased costs, particularly given the number of advisors that are now required by trustees as well as the sponsoring employers themselves to navigate the complexities.

[20] Initially with the introduction of the UK Financial Reporting Standard 17 – Retirement Benefits, fully introduced by 2005.

The future for defined benefit schemes

With the phasing out of defined benefit arrangements, the provision, by employers, of retirement benefits is now mainly focussed on defined contribution arrangements, whether through new occupational pension schemes or group personal pension plans.

Employers with legacy defined benefit schemes are increasingly putting in place strategies to exit their schemes (replacing them with defined contribution arrangements) leaving them as legacy liabilities being repaid over a period of time.

Furthermore, employers are also putting in place complex funding structures to manage the risk and cost associated with scheme deficits. Solutions such as asset backed contribution arrangements, where a special purposes vehicle is set up to hold an income generating asset for the benefit of the scheme, and the provision of security being provided over company assets are becoming more commonplace as employers seek to mitigate the risks associated with legacy defined benefit schemes.

Private sector vs public sector

The divergence from defined benefit pension arrangements has been more acute in the private sector, primarily due to the fiduciary duty of directors to protect and enhance shareholder value. Furthermore, the private sector has seen a reduction in the influence of unions, primarily due to the evolution of the UK private sector away from unionised activities.

The culture of the public sector is such that defined benefit pension provision has largely been protected from the changes seen in the private sector, with most public sector organisations still providing a defined benefit pension scheme to new and existing employees.

However, in recent years, austerity measures have forced public sector organisations to revisit their pension arrangements to address short term budget cuts and the longer term ambition to eliminate the fiscal deficit and may now offer career average benefits rather than final salary benefits.

However, the public sector remains heavily unionised and has faced challenges in steps recently put in place to mitigate the longer term risks of retirement benefit provision. As such, it is likely to take a considerable time for the public sector to be more closely aligned to the private sector whereby pension provision is largely through defined contribution arrangements.

UNITED STATES OF AMERICA

QUESTION 1

What is the legal framework for private pension plans in your country?

In the U.S., federal law - the Employee Retirement Income Security Act of 1974 ("ERISA") and the Internal Revenue Code (the "IRC"), together with case law interpreting ERISA and the IRC - governs the establishment, maintenance, and termination of private, defined benefit pension plans, as well as the rights and duties of the sponsoring employers and the participants and beneficiaries of such plans[1]. ERISA and the IRC prescribe the contribution and funding obligations for defined benefit pension plans[2]. ERISA and the IRC also define the liabilities that arise due to the termination of a defined benefit pension plan or an employer's withdrawal from a pension plan[3].

ERISA generally contemplates two types of retirement plans. A "defined contribution plan" provides an individual account for each participant, and the amount of any participant's retirement benefits depends on the contributions to the account and subsequent additions - principally, earnings on the contributions[4]. Thus, when a participant retires, he or she is entitled only to what has been accumulated in that account. While employers often agree to make contributions to this kind of plan, there is no requirement that they do so, nor do they make any commitment to a participant of any particular level of retirement benefit[5].

A "defined benefit plan," on the other hand, is a retirement plan where the participant is promised retirement payments based on a defined formula, often taking into account the length of his or her service and salary. The employer that sponsors a defined benefit plan must ensure that there is enough money in the plan to cover the aggregate benefit promises made to the employees. In order to enforce this funding requirement, ERISA imposes specific minimum funding standards on the sponsors of defined benefit pension plans[6].

1 The IRC only governs certain tax-qualified pension plans, which are exempt from taxation. See I.R.C. §§ 401, 501. The IRC requirements for tax-qualified pension plans are parallel to the requirements found in Title II of ERISA.

2 ERISA §§ 302-305, 29 U.S.C. §§ 1082-1085; I.R.C. § 412.

3 ERISA § 4062, 29 U.S.C. § 1362; ERISA § 4068, 29 U.S.C. § 1368; ERISA § 4201, 29 U.S.C. § 1381.

4 See ERISA § 3(34); 29 U.S.C. § 1002(34).

5 The insurance program established under Title IV of ERISA, see Section 4, infra, does not cover "defined contribution" plans and certain other qualified plans.

6 See ERISA §§ 302-304, 29 U.S.C. §§ 1082-1084; I.R.C. §§ 412, 430.

This chapter focuses on "qualified" defined benefit pension plans[7]. Defined benefit pension plans are delineated further into multiemployer plans and single-employer plans[8]. "Multiemployer" plans are collectively bargained plans to which two or more unaffiliated employers contribute[9]. A "single-employer" plan is a plan maintained by one employer or by two or more employers in the same "controlled group[10]".

Plan as separate entity

Defined benefit pension plans are treated as separate entities from the plan's sponsors and participating employers. Assets in qualified pension plans must be kept separate from the employer's general assets. A plan may be maintained through one of a number of vehicles. One method is to establish a trust agreement with a bank or similar institution. The trust then holds the plan assets and invests it, and the employer does not have access to the funds. A plan may also be maintained with an insurance company through allocated (e.g., for defined contribution plans) or unallocated (e.g., for defined benefit plans) accounts. If an allocated arrangement is used, separate accounts are established for each plan participant prior to retirement, and total contributions are divided among participants. Under an unallocated arrangement, a pool of funds is established and benefits are paid from it.

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7 A "qualified" plan is one that is described in Section 401(a) of the Internal Revenue Code. In a qualified plan (often referred to as "tax-qualified"), a participant's accrued benefit must become 100 percent vested immediately upon plan termination, to the extent then funded. If a partial termination occurs in such a plan, for example, if an employer closes a particular plant or division that results in the termination of employment of a substantial portion of plan participants, immediate 100 percent vesting, to the extent funded, also is required for affected employees. The most common types of qualified plans are defined contribution plans (e.g., 401(k) plans, profit sharing plans, employee stock ownership plans (ESOPs), simplified employee pension plans (SEPs), and savings incentive match plans for employees of small employers (SIMPLEs)) and defined benefit pension plans. "Nonqualified" plans, by contrast, are plans that are not required to satisfy most of the requirements of ERISA or the IRC that are imposed on tax-qualified plans. Nonqualified plans are unfunded, unsecured promises by an employer to the key employee to pay compensation at a specific time or upon a specific event in the future. A nonqualified plan is a contract between the employer and the key employee for the payment of these future benefits.

8 *See* 29 U.S.C. §§ 1002(37).

9 *See* ERISA § 4001(a)(3), 29 U.S.C. § 1301(a)(3). Contributions to a multiemployer plan are then pooled into a pension fund that is administered by a trust. Multiemployer Plans are regulated under ERISA and the Multiemployer Pension Plan Amendments Act of 1980 ("MPPAA"), 29 U.S.C. § 1381 *et seq.*, which was enacted as an amendment to ERISA to fill a statutory gap with respect to employers who withdrew from and ceased participation in a multiemployer plan. *See generally PBGC v. R.A. Gray & Co.*, 467 U.S. 717, 722-23 (1984), *superseded by statute on other grounds*, Pub. L. No. 98-369, § 558, 98 Stat. 494, 899 (1984).

10 *See* ERISA § 4001(a)(15), 29 U.S.C. § 1301(a)(15). The official definition of a single employer plan is "any defined benefit plan . . .which is not a multiemployer plan." This, however, translates into plans maintained by one employer or by employers in the same controlled group.

Tax treatment

The tax treatment accorded to qualified defined benefit plans provides incentives both for employers to establish such plans and for employees to participate in them. In general, employer contributions to defined benefit plans are immediately deductible expenses for the employer. An employer may not, however, make contributions to the plan above a certain limit (i.e., excess contributions) without incurring an excise tax penalty. Similarly, interest, dividends, and investment gains or losses are not taxable to the employer. At the participant level, participants do not pay taxes on employer contributions, investment income, or capital gains of retirement plan assets until they receive benefits. While most private-sector defined benefit plans do not require participant contributions, employees have traditionally paid taxes on their own plan contributions in the year such income was earned.

QUESTION 2

Are the plans regulated by a government authority or any other independent authority?

The Pension Benefit Guaranty Corporation ("PBGC") guarantees benefits and regulates the termination of defined benefit pension plans in the U.S. Established with the enactment of ERISA in 1974, PBGC is a wholly owned U.S. government corporation and was modeled after the Federal Deposit Insurance Corporation[11]. In addition to the powers specifically enumerated in ERISA (including the power to appear in any court, state or federal, through its own counsel), PBGC has the powers conferred on a nonprofit corporation under District of Columbia law. PBGC collects insurance premiums from employers that sponsor insured pension plans, earns money from investments, and receives funds from pension plans it takes over.

The PBGC's statutory mandate is to (a) encourage the continuation and maintenance of private-sector defined benefit pension plans, (b) provide for the timely and uninterrupted payment of pension benefits to participants in PBGC-insured plans, and (c) maintain pension insurance premiums at the lowest levels consistent with its other obligations[12]. The PBGC guarantees payment of pension benefits (up to a limit) earned by more than 42 million workers and retirees who participate in more than 24,400 private-sector defined benefit pension plans[13]. Historically, the PBGC limited its role with respect to ongoing underfunded plans, and stepped in only upon the termination or expected termination of such plans. As a result of changes to ERISA and the IRC, and Congressional oversight, the PBGC has increased its involvement with companies that sponsor underfunded defined benefit pension plans.

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11 The PBGC's Board of Directors consists of the Secretaries of Labor (who is the Chair), Treasury and Commerce. Since statutory amendments were enacted in 2006, its chief executive officer is the Director, who is appointed by the President with the advice and consent of the U.S. Senate.

12 *See* ERISA § 4002(a)(1)-(3), 29 U.S.C. § 1302(a)(1)-(3).

13 *See* FY 2015 Congressional Budget Justification–Pension Benefit Guaranty Corporation 13, http://www.pbgc.gov/Documents/Budget-CBJ-2015.pdf.

In addition, the Internal Revenue Service (the "IRS") enforces the tax qualification and minimum funding requirements of defined benefit plans[14]. The Department of Labor enforces the fiduciary duty provisions of ERISA[15].

Benefit accruals

ERISA requires that plans use one of three alternative formulas to determine the minimum speed at which defined benefit pension benefits accrue to participants. These formulas used to determine final retirement benefits include: (1) flat-benefit formulas, which include a flat-dollar amount for every year of service recognized under the plan; (2) career-average formulas, which provide a benefit at retirement equal to a percentage of the career-average pay, multiplied by the participant's number of years of service; and (3) final-pay formulas, which bases benefits on average earnings during a specified number of years at the end of a participant's career (usually five years), multiplied by the number of years of service.

Once vested, a participant's benefits generally cannot be revoked[16]. ERISA and the IRC require single-employer plans to adopt vesting standards for the employee's accrued benefits at least as liberal as the two following schedules: full vesting after five years, with no vesting prior to that time (known as "cliff vesting"), or graded vesting of 20 percent after three years of service and an additional 20 percent after each subsequent year of service, until 100 percent vesting is reached at the end of seven years of service[17].

Funding requirements

To ensure that defined benefit pension plans have sufficient assets to pay benefits when participants retire, ERISA and the IRC set minimum funding standards. Defined benefit plan sponsors assume an obligation for paying an agreed-to future benefit. If the pension fund earns a lower-than-expected rate of return, the participating employer(s) will need to make additional contributions to pay the promised benefits.

In general, sponsors of defined benefit plans are required to make contributions for a given year sufficient to fund benefits accrued during that year, plus certain administrative expenses of the plan (referred to as a plan's "normal cost"). The sponsor may also have to cover a portion of the amortized cost of benefits that employees have earned in the past (known as "accrued benefits"), if prior contributions and earnings have not been sufficient to cover those costs[18].

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14 *See* ERISA §§ 302-304, 3002, 29 U.S.C. §§ 1082-1084, 1202; I.R.C. §§ 412, 430.

15 *See* ERISA §§ 404-409, 29 U.S.C. §§ 1104-1109.

16 ERISA and the IRC contain a so-called "anti-cutback" rule, which generally prohibits plan amendments that eliminate or reduce "accrued benefits," a term that has been interpreted to include the right to receive certain forms of benefits such as a lump-sum payout. *See* ERISA § 204(g), 29 U.S.C. § 1054(g); I.R.C. § 411(d)(6).

17 ERISA § 203(a), 29 U.S.C. § 1053(a); I.R.C § 411(a).

18 ERISA §§ 302-303, 29 U.S.C. §§ 1082-1083; I.R.C. §§ 412, 430.

The funded status of a defined benefit pension plan is determined each year by the plan's actuary and is reported on an annual basis on the plan's Form 5500 annual report. Underfunding occurs when the actuarial value of a plan's vested accrued benefits (the promised future benefits that participants have earned a right to receive) exceeds the value of the plan's assets. These calculations are influenced by various assumptions (investment rate of return, mortality, contribution hours, etc.) and by the level of benefits promised to participants. For example, if the plan does not meet its investment return assumption or has less than anticipated employer contributions, an imbalance may result and unfunded vested benefits may be created or increase. Trustees of a plan are obligated to be prudent in their decisions of the various assumptions to use in maintaining the plan, so trustees may change assumptions from time to time, which could increase or decrease unfunded liability.

ERISA and the IRC set out a complicated process for evaluating whether a plan must contribute more than normal cost. That is because measuring at any point in time whether a defined benefit plan will eventually have sufficient assets to cover accrued benefits requires various actuarial assumptions about how the balance between the plan's assets and liabilities may change in the future. These assumptions include judgments about future investment earnings on the current assets, as well how the benefit liabilities may be affected by such items as future employee compensation, employee turnover, and how long pensioners might live. Because these assumptions cover decades of future experience, it is inevitable that there will be both positive and negative variances between the assumptions and the plan's actual experience. Because short term fluctuations in earnings or interest rates could have devastating financial implications if companies had to make up actuarial losses immediately, plan sponsors are permitted to amortize any funding shortfall over time – generally a period of seven years[19].

Under this regime, a defined benefit single-employer plan may be "underfunded," "fully funded," or "overfunded," depending on the market value of its assets compared to the actuarial calculation of its current and future benefit liabilities. Indeed, a plan may be fully funded or overfunded for certain purposes under ERISA and the IRC and underfunded for other purposes at the same time because the law requires different actuarial funding assumptions for different purposes. For example, where a plan is amortizing an actuarial loss, the plan may be "fully funded" for purposes of determining whether the sponsor must make a contribution in a particular year, yet "underfunded" in the sense that there would not be enough money to pay all the benefits if the plan terminated immediately because there would not be enough time to make up the actuarial loss that is being amortized. Congress recently recognized that many plans are underfunded on a termination basis but not liable for immediate contributions and began requiring plan sponsors to perform special funding calculations to determine whether a plan is at risk of default on any or all of its liabilities. Congress then imposed various consequences if the plan falls below the 80 percent funding level using the actuarial assumptions in the general funding rules, or below 70 percent using a series of special "at-risk" actuarial assumptions[20]. One of these consequences is that certain underfunded plans are prohibited from paying out benefits on an accelerated basis.[21]

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[19] I.R.C. § 430(c); 29 U.S.C. § 1083(c).

[20] ERISA § 303(i), 29 U.S.C. § 1083(i); I.R.C. § 430(i).

[21] *See* ERISA § 206(g)(3), 29 U.S.C. § 1056(g)(3); I.R.C. § 436(d)(3).

Single-employer plans

The Pension Protection Act of 2006 (the "PPA") significantly overhauled the minimum funding requirements of single-employer defined benefit pension plans[22]. Under the new funding requirements, all single-employer defined benefit plans have a new funding target of 100 percent of plan liabilities. In general, the minimum required contribution is equal to the target normal cost plus a seven-year amortization of unfunded liability, less any permissible credit balances[23]. Normal cost is the cost of benefits earned on account of service performed during the current year. Past service liability is liability for benefits earned on account of service rendered before the current year, but which has not yet been covered in the plan[24]. The PPA also creates a separate category for "at-risk" plans and increases required contributions for at-risk plans by increasing the target normal cost and the funding target.

Multiemployer plans

The funding rules for multiemployer plans differ from the funding rules for single-employer plans. Plan contributions to multiemployer defined benefit pension plans are made by employers that are subject to a collective bargaining agreement. The employer's contribution amount is generally determined through negotiations with the applicable labor organization and fixed in the collective bargaining agreement. All contributions are pooled in a common fund that pays for plan benefits. Investment earnings increase the size of the common fund. Substantially underfunded multiemployer plans are required to adopt funding improvement plans or rehabilitation plans that are designed to either restore the multiemployer plan or fully funded status or, at the very least, delay insolvency. Unlike with single-employer plans, the PBGC does not take over multiemployer plans. Instead, the PBGC makes loans to insolvent multiemployer plans in amounts sufficient to enable the plans to make payments in respect of guaranteed benefits.

PBGC premiums

When a covered defined benefit pension plan terminates without sufficient assets to pay promised benefits, the PBGC ensures payment of a minimum level of benefits. Sponsors of covered plans are required to pay annual premiums to the PBGC to fund the insurance programs. The PBGC charges a flat-rate premium for single and multiemployer plans and an additional variable-rate premium for single-employer plans. The per-participant flat premium rate for plan years beginning in 2015 is $57 for single-employer plans (up from a 2014 rate of $49) and $26 for multiemployer plans (up from a 2014 rate of $12). For plan years beginning in 2015, the variable-rate premium (VRP) for single-employer plans is $24 per $1,000 of unfunded vested benefits (up from a 2014 rate of $14), subject to a VRP cap for 2015 of $418 times the number of participants[25].

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22 *See* ERISA § 206(g)(9)(B), 29 U.S.C. § 1056(g)(9)(B); I.R.C. § 436(j)(2).

23 ERISA § 303(a), 29 U.S.C. § 1083(a). If the value of plan assets is at least equal to the value of benefit obligations, no funding shortfall exists and shortfall amortization installments are not required.

24 Past service liability can rise when the plan is initially adopted and it is to cover current employees' past service or when the plan is later amended to raise benefit levels retroactively.

25 Pension Benefit Guaranty Corporation–Premium Rates, http://www.pbgc.gov/prac/prem/premium-rates.html.

QUESTION 3

How are the plans governed?

Under ERISA, the plan sponsor is the person who establishes or maintains the plan. In a single-employer plan, the plan sponsor will be the employer; however, in the case of a multiemployer plan, the plan sponsor is generally a board of trustees[26]. Frequently, the plan sponsor serves in more than one capacity with respect to the plan: it is the entity that decides to adopt a plan in the first place and determines what benefits will be provided (the "settlor") and, once the plan is established, it will direct the plan activities as the named fiduciary and / or serve as the plan administrator.

When the plan sponsor wears multiple hats, however, it may be difficult to determine the capacity in which it is functioning when it performs certain activities (i.e., whether it is acting as the plan sponsor or a fiduciary at the time). Indeed, not all decisions that affect a plan are fiduciary actions. Some courts have described some of them as "settlor" or "plan sponsor" functions and have refused to hold the plan sponsor responsible as a fiduciary for those actions and their consequences[27]. A number of cases involving single-employer plans under ERISA have focused on where one draws the line between settlor and fiduciary functions. For instance, the courts have concluded that the acts of establishing or amending an employee benefit plan or deciding to modify or terminate a plan are considered to be settlor functions[28]. However, the implementation of a settlor decision may involve fiduciary functions. Although this is clearly the rule for single-employer plans covered by ERISA, courts are divided as to whether actions taken by a joint board of trustees of a multiemployer plan fall neatly into the same settlor / fiduciary categories[29].

ERISA permits the PBGC to become the statutory trustee of single-employer plans that are involuntarily terminated by the PBGC and, in practice, the PBGC is ordinarily appointed as the statutory trustee of such terminated plans.

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[26] ERISA § 3(16)(B), 29 U.S.C. § 1002(16(B). As discussed *supra*, a multiemployer plan is a collectively bargained plan, which under § 302(c) of the Taft-Hartley Act, 29 U.S.C. § 186, must be administered by a joint board of trustees consisting of equal representatives of management and labor unions. The trust document states how many trustees will govern the plan and how they are appointed or elected.

[27] An important limitation on fiduciary status is found in the language of ERISA § 3(21)(A), 29 U.S.C. § 1002(21)(A), which provides that a person is a fiduciary only "to the extent" he performs one of the defined fiduciary functions. *See Pegram v. Herdrich*, 530 U.S. 211, 226 (2000) ("In every case charging breach of ERISA fiduciary duty . . . the threshold question is not whether the actions of some person employed to provide services under a plan adversely affected a plan beneficiary's interest, but whether that person was acting as a fiduciary (that is, was performing a fiduciary function) when taking the action subject to complaint.").

[28] *See, e.g., Lockheed Corp. v. Spink*, 517 U.S. 882 (1996) (even though an employer acts as a fiduciary when it administers a pension plan, it is not acting in a fiduciary capacity when it decides to create, amend, or terminate such a plan)); *Beck v. PACE Int'l Union*, 551 U.S. 96, 101 (2007) (plan sponsor and its directors had no fiduciary liability where it chose to terminate plan, without considering merger with another plan, as "[i]t is well established in this Court's cases that an employer's decision *whether* to terminate an ERISA plan is a settlor function immune from ERISA's fiduciary obligations," and merger is not a permissible form of termination); *Malia v. General Elec. Co.*, 23 F.3d 828, 833 (3d Cir. 1994) ("[Fiduciary] duties do not attach to business decisions related to modification of the design of a pension plan and in such circumstances the plan sponsor is free to act 'as an employer and not a fiduciary'" (citation omitted)).

[29] *Compare Deak v. Masters, Mates & Pilots Pension Plan*, 821 F.2d 572, 577-78 (11th Cir. 1987) (amending the plan is a fiduciary function) *with Walling v. Brady*, 125 F.3d 114, 117-18 (3d Cir. 1997) (amending the plan is not a fiduciary function, even when amendments are adopted by the multiemployer plan trustees).

QUESTION 4

Is there a compensation fund for pension benefits?

Yes. As discussed above, when a covered defined benefit pension plan terminates without sufficient assets to pay promised benefits, the PBGC ensures a minimum level of benefits. The PBGC funds this insurance program with premiums paid by employers maintaining covered plans (at the rates set by the PBGC), and with assets in terminated plans, amounts recovered from employers that terminate underfunded plans, and investment earnings[30]. The PBGC maintains two separate funds to pay the minimum level of benefits, one that funds guaranteed benefits under single-employer plans, and a second that funds guaranteed benefits under multiemployer plans.

QUESTION 5

How are pension rights enforced in an insolvency of the employer / sponsor?

Single-employer plans

Under ERISA, single-employer pension plans may be terminated "voluntarily" by the plan administrator, or "involuntarily" by the PBGC. The statutory termination procedures set forth in ERISA are exclusive, regardless of whether the plan sponsor is in bankruptcy.

Voluntary terminations are initiated by the plan administrator and are either "standard terminations" or "distress terminations[31]". Because a plan administrator may cause a standard termination of a pension plan only if (among other things) the plan contains sufficient assets to pay all accrued benefit liabilities, standard terminations rarely occur in the insolvency context[32]. ERISA also permits an employer to voluntarily terminate an underfunded defined benefit pension plan if the plan qualifies for a "distress termination[33]." To qualify for a distress termination in bankruptcy, the following four requirements must be satisfied:

- The employer must have filed its chapter 11 petition as of the proposed termination date;
- The chapter 11 cases must not have been dismissed as of the proposed termination date;
- The debtors must timely submit to the PBGC their request that the bankruptcy court terminate the plan; and

[30] ERISA § 4006, 29 U.S.C. § 1306. For a general discussion of the PBGC insurance program, *see Pension Benefit Guar. Corp. v. LTV Corp.*, 496 U.S. 635, 636-39 (1990).

[31] ERISA § 4041(b) and (c), 29 U.S.C. § 1341(b) and (c).

[32] A plan administrator effecting a standard termination must provide for the payment to plan participants of all accrued benefits. Typically, the employer will use the assets of the plan to purchase annuities providing such benefits from an insurance company. ERISA § 4041(b)(3)(A), 29 U.S.C. § 1341(b)(3)(A).

[33] ERISA § 4041(c), 29 U.S.C. § 1341(c).

- The bankruptcy court must find that, "unless the plan is terminated, the debtors will be unable to pay all their debts pursuant to a plan of reorganization and will be unable to continue in business outside the reorganization," and approve the termination[34].

In either a standard or distress termination, 60 days before the proposed termination date the employer must give to each "affected party" (including, among others, each plan participant or beneficiary, any employee organization representing participants, and the PBGC) a notice of its intent to terminate the plan[35]. Both standard and distress terminations are subject to confirmation by the PBGC that all statutory requirements are satisfied. As discussed above, the termination of a plan is not a "fiduciary decision" such that an independent fiduciary does not need to be appointed to decide if a plan should be terminated.

"Involuntary terminations" are initiated by the PBGC. PBGC may institute proceedings to terminate a plan whenever it determines that:

- The plan has not met the minimum funding standards, or the IRS has issued a notice of deficiency with respect to an excise tax on accumulated funding deficiencies[36];

- The plan will be unable to pay benefits when due[37];

- The plan has made a lump-sum payment to a participant who is a substantial owner of the sponsoring company[38]; or

- PBGC's possible long-run loss with respect to the plan may be expected to increase unreasonably if the plan is not terminated[39].

Importantly, in an involuntary termination under ERISA, the PBGC's ability to terminate the plan is not restricted by any provision in a union's collective bargaining agreement[40]. Nor does the PBGC need to consult with a union before terminating a plan[41]. Under the distress termination provisions of ERISA, on the other hand, a plan sponsor cannot terminate a plan if it would violate the terms of a collective bargaining agreement[42]. Following a distress or involuntary termination, the plan sponsor and its affiliates (the "controlled group") become jointly and severally liable to the PBGC for the underfunded amount.

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34 A debtor may satisfy its burden of proving that it cannot pay its debts pursuant to a plan of reorganization by showing that, without terminating the pension plan, it cannot obtain necessary financing. *See In re Wire Rope Corp. of Am.,* 287 B.R. 771, 778 (Bankr. W.D. Mo. 2002).

35 ERISA § 4042(c)(3)(A)(i), 29 U.S.C. § 1342(c)(3)(A)(i).

36 ERISA § 4042(a)(1), 29 U.S.C. § 1342(a)(1).

37 ERISA § 4042(a)(2), 29 U.S.C. § 1342(a)(2).

38 ERISA § 4042(a)(3), 29 U.S.C. § 1342(a)(3).

39 ERISA § 4042(a)(4), 29 U.S.C. § 1342(a)(4).

40 *See In re UAL Corp.*, 428 F.3d 677, 680-81 (7th Cir. 2005).

41 *See id.* at 683 ("[The settlement agreement] simply provided for PBGC to initiate a review to determine whether PBGC should terminate the plan under § 1342 – an administrative process that is *wholly* separate from § 1341(c) and unrestrained by the terms of collective bargaining agreements.").

42 ERISA § 4041(a)(3), 29 U.S.C. § 1341(a)(3).

Multiemployer plans

As discussed above, in contrast to a single employer plan, a multiemployer plan is a collectively bargained plan maintained by more than one employer, usually within the same or related industries, and a labor union. When an employer withdraws from an underfunded multiemployer plan, ERISA provides that the employer is liable for its allocable share of the plan's unfunded vested benefits, which liability is referred to under ERISA as the employer's "withdrawal liability[43]". Even where an employer's withdrawal liability is discharged during bankruptcy proceedings as a prepetition obligation, non-debtor members of the debtor's controlled group remain liable for any unpaid withdrawal liabilities.

The PBGC-insurable event for a multiemployer plan is cash-flow insolvency, in which event the plan must seek financial assistance from PBGC[44]. The insurable event for a single-employer plan, by contrast, is termination of the plan at a time when the plan's assets are insufficient to pay benefits at the guaranteed level[45].

Termination premium

ERISA Section 4006(a)(7), a provision added by the Deficit Reduction Act of 2005, generally requires an employer to pay the PBGC a "termination premium" following termination of an underfunded U.S. tax-qualified pension plan sponsored by the employer[46]. Upon termination, a "premium" is imposed on the plan sponsor equal to $1,250 per participant for each of the 3 years after the plan is terminated. The premium is enforceable by a PBGC lien. In the case of a chapter 11 reorganization, the premium is payable following emergence. While most pension claims are considered to be prepetition claims, some courts have held that these termination premiums become an obligation of the employer upon emergence from bankruptcy. Accordingly, at least in some circuits, such termination premiums are not subject to discharge in bankruptcy, at least where the employer reorganizes rather than liquidates[47].

Statutory liens

If a plan sponsor's aggregate delinquent minimum funding contributions exceed $1 million, a statutory lien in favor of the plan is imposed on all assets of the sponsor and any other member of the sponsor's controlled group[48]. The lien is treated as a tax lien[49]. The lien attaches automatically to "all property and rights to property" of the plan sponsor[50], but is not effective against "holder[s] of . . . security interest[s]" in the sponsor's assets until the lien is properly recorded[51]. Thus, the PBGC's lien will not prime security interests that were perfected before the PBGC gave proper notice of its liens[52].

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43 *See* ERISA § 4201, 29 U.S.C. § 1381.

44 *See* ERISA § 4261, 29 U.S.C. § 1431.

45 *See* ERISA § 4022, 29 U.S.C. § 1322; PBGC Op. Ltr. 91-1 (Jan. 14, 1991).

46 ERISA § 4006(a)(7), 29 U.S.C. § 1306(a)(7), as amended by the Deficit Reduction Act of 2005 § 8101(b), Pub. L. No. 109-171. The Pension Protection Act of 2006 made this provision permanent. PPA § 401(b)(1), Pub. L. 109280, 120 Stat. 780, 922 (2006).

47 *Pension Benefit Guar. Corp. v. Oneida Ltd.*, 562 F.3d 154, 157–58 (2d Cir. 2009).

48 *See* ERISA § 303(k), 29 U.S.C. § 1083(k); I.R.C. § 430(k).

49 *See* ERISA § 303(k), 29 U.S.C. § 1083(k); I.R.C. § 430(k).

50 I.R.C. § 6321. Although the statute does not say so explicitly, case law establishes that the PBGC's liens attach to after-acquired property. *See Glass City Bank v. United States*, 326 U.S. 265, 267 (1945).

51 I.R.C. § 6323(a). The procedures for recording such liens are set forth in IRC section 6323(f). *See* I.R.C. § 6323(f).

52 *See United States v. McDermott*, 507 U.S. 447, 449 (1993) (tax liens "do not automatically have priority over all other liens"); *Rodeck v. United States*, 697 F. Supp. 1508, 1510-11 (D. Minn. 1988) (a tax lien has priority over the interests enumerated in IRC section 6323(a) "if notice of the lien was filed before the [competing interestholder] perfected her interest").

In bankruptcy, the PBGC may not assert or take any action to perfect liens after the petition date against debtor entities due to the automatic stay in bankruptcy, but the stay does not automatically prevent the PBGC from perfecting liens against non-debtor entities in the sponsor's controlled group[53]. It is less clear whether existing PBGC liens attach to property acquired after the petition date[54].

Excise taxes for missed contributions

The IRS can also impose an excise tax equal to 10% of the missed contributions of all plan years remaining unpaid as of the end of any plan year ending with or within a taxable year[55]. If the excise tax is not paid by the close of the taxable period, the IRS can impose an additional excise tax equal to 100% of the missed contribution[56].

QUESTION 6

Are there special priorities for pension deficits in an insolvency?

The PBGC typically asserts that its claims against a plan sponsor or any member of the "controlled group," as described below, are entitled to priority in bankruptcy. However, most courts have held that only a portion of unpaid postpetition contributions are entitled to priority as an administrative expense under Section 507(a)(2) of the Bankruptcy Code, and that a portion of unpaid contributions attributable to the 180-day period preceding the bankruptcy filing are entitled to fifth priority for contributions to employee benefit plans under Section 507(a)(5) of the Bankruptcy Code. The balance of PBGC's claims, to the extent allowed in the bankruptcy case, are generally treated as prepetition general unsecured claims.

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[53] *Cf.* 11 U.S.C. § 362.

[54] Section 552(a) of the bankruptcy code provides that, subject to section 552(b), "property acquired by the estate or by the debtor after the commencement of the case is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case." 11 U.S.C. § 552(a). Section 552(b) provides an exception for security agreements that grant the lender a security interest in "proceeds, products, offspring, or profits." *Id.* § 552(b). By its terms, section 552(a) does not apply to PBGC liens because PBGC liens are not "lien[s] resulting from any security agreement." *Id.* § 552(a); *see also In re Avis*, 178 F.3d 718, 721 (4th Cir. 1999) (noting that the bankruptcy code is silent on the attachment of statutory liens to property acquired after the petition date). Several courts have therefore concluded that "tax liens generally survive bankruptcy and, being nonconsensual, are not cut off by the operation of 11 U.S.C. § 552(a)." *In re Se. R.R. Contractors, Inc.*, 235 B.R. 619, 622 (Bankr. E.D. Tenn. 1996). But other courts take the contrary view. *In re Avis*, 178 F.3d at 722-23 (section 362(a)(5) of the bankruptcy code prevents the perfection of tax liens on property acquired by the estate after the petition date).

[55] I.R.C. § 4971(a)(1).

[56] *Id.* § 4971(b)(1).

Termination

If a single-employer defined benefit pension plan is terminated in bankruptcy at a time when it is underfunded, the plan sponsor and the members of its "controlled group" may be liable for the full amount of the underfunding. In addition, plan sponsors are required to fund single-employer defined benefit plans by making statutorily-required minimum funding contributions and pay annual insurance premiums to the PBGC. The PBGC therefore may assert a claim in bankruptcy to recover an amount equal to the (i) termination liability with respect to an underfunded pension plan, (ii) liability for a failure to satisfy minimum funding requirements and associated excise taxes, and (iii) liability for unpaid PBGC premiums. Courts have accepted the PBGC's argument that under ERISA, once a plan has been terminated, the PBGC has the sole and total right to recover against employers for pension plan underfunding and participants have no right to make claims against their employers for benefits under terminated plans[57].

Withdrawal

An employer that withdraws from participation in a multiemployer plan may do so either in a complete withdrawal[58] or a partial withdrawal[59]. In the multiemployer plan context, following the triggering withdrawal event, the administrator of the multiemployer plan must take affirmative steps to collect the outstanding obligations from the withdrawing employer by: (1) determining the amount of liability, (2) notifying the employer of the liability, and (3) collecting the liability[60]. The law sets out various allocation formulas that a plan can use for determining an employer's withdrawal liability. In addition, other methods can be approved by the PBGC.

Priority

Ordinarily, claims relating to U.S. pension obligations constitute prepetition contingent claims in a bankruptcy case. Indeed, numerous courts have addressed the question of whether the claim would be deemed a prepetition claim even though the claims themselves did not crystallize until after the filing of the petition. Nonetheless, most courts that have ruled on this issue have held that such claims are prepetition claims[61].

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57 *See* 29 U.S.C. § 1362; *see also United Steelworkers of Am. v. United Eng'g, Inc.*, 52 F.3d 1386, 1390 (6th Cir. 1995); *Int'l Ass'n of Machinists and Aerospace Workers v. Rome Cable* Corp., 810 F. Supp. 402, 407-08 (N.D.N.Y. 1993); *In re Lineal Group, Inc.*, 226 B.R. 608, 613-14 (Bankr. M.D. Tenn. 1998).

58 *See* ERISA § 4202, 29 U.S.C. § 1382.

59 To ensure that employers who gradually reduce their contributions to a multiemployer plan do not escape withdrawal liability, ERISA has rules under which a partial cessation of the employer's obligation to contribute could trigger liability. *See* ERISA **§** 4205, 29 U.S.C. § 1385; ERISA § 4206, 29 U.S.C. § 1386; ERISA § 4208, 29 U.S.C. **§** 1388.

60 *See* 29 U.S.C. §§ 1381, 1391.

61 *See, e.g.*, *McFarlin's*, 789 F.2d at 103-04 (withdrawal liability from a multiemployer pension plan not considered to arise from postpetition transactions with the debtor, but rather arising from the prepetition creation of the pension plan; and thus are not considered administrative expense claims to the extent that the missed contributions were attributed to prepetition labor); *In re Crane Rental Co.*, 334 B.R. 73, 76-77 (Bankr. D. Mass. 2005) (withdrawal liability is a prepetition claim); *In re CD Realty Partners*, 205 B.R. 651, 659 (Bankr. D. Mass. 1997) (same); *In re Westmoreland Coal Co.*, 213 B.R. 1, 15 (Bankr. D. Colo. 1997) (plan trustees hold an unmatured, unliquidated claim for future pre-funding premiums); *In re Great Ne. Lumber & Millwork Corp.*, 64 B.R. 426, 428 (Bankr. E.D. Pa. 1986) (withdrawal liability not entitled to administrative priority); *In re Pulaski Highway Exp., Inc.*, 57 B.R. 502, 507 (Bankr. M.D. Tenn. 1986) (liability and amount may be contingent and unliquidated, but "such uncertainties do not defeat the existence of prepetition claims for benefits which accrued prior to withdrawal"); *In re Silver Wheel Freightlines, Inc.*, 57 B.R. 476, 478-79 (Bankr. D. Or. 1985) (withdrawal liability constituted contingent prepetition claim); *but see In re Marcal Paper Mills, Inc.*, 650 F.3d 311, 319-21 (3rd Cir. 2011) (holding that a company in chapter 11 bankruptcy that withdraws from a multiemployer pension plan will incur administrative expense liability for such portion of the withdrawal liability attributable to work performed during the postpetition period).

Generally, in order for a claim to be accorded administrative expense priority, the bankruptcy court must find that the debt both (1) arises from a transaction with the debtor in possession and (2) is beneficial to the debtor in possession in the operation of the business[62]. In In re Chateaugay Corp., the Bankruptcy Court for the Southern District of New York determined that although a pension plan was terminated postpetition, the PBGC's claim for termination liability was not based on a postpetition transaction with the debtor in possession; rather, LTV's obligation was of a prepetition nature and did not directly benefit the estate[63]. In other words, even though the event triggering the debtor's liability (i.e. the termination of the plan) occurred postpetition, the liability still arose from employees' prepetition service in consideration for participation in LTV's pension plans[64]. Moreover, the pension plan termination induced no employees to perform work benefiting the postpetition estate. In fact, most of the pension obligations were already owed to retirees[65]. Accordingly, the court held that the postpetition termination of the pension plans "did not transform the PBGC's contingent prepetition claims into postpetition claims[66]".

As stated above, bankruptcy courts apply a two-part test to determine if a claim is entitled to administrative expense status. First, the obligation in question must stem from a transaction with, and induced by, the postpetition debtor in possession, rather than the prepetition debtor. Second, the obligation for which administrative expense status is sought must have directly benefited the estate. Applying this test, courts generally hold that a fraction of the PBGC's claims are entitled to administrative expense priority. That fraction is equal to the portion of unfunded contributions (i) due postpetition and (ii) directly attributable to the postpetition labor of the employees in the pension plan (i.e. the so called "normal cost" contribution)[67]. To be clear, the administrative expense priority portion of the claim is limited to the value of benefits earned during the pendency of the bankruptcy case as measured by the plan's "normal cost[68]". In other words, for employees who have been earning benefits for many years and are still working at the company, only the portion of underfunding that the actuaries determine is related to pension benefits earned on account of postpetition labor is considered to be "normal cost" and entitled to administrative expense priority.

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[62] *In re Jartran, Inc.*, 732 F.2d 584, 587 (7th Cir. 1984) (quoting *Cramer v. Mammoth Mart, Inc.* (In re Mammoth Mart, Inc.) 536 F.2d 950, 954 1st Cir. 1976) (internal quotation marks omitted).

[63] *LTV Corp. v. PBGC* (In re Chateaugay Corp.), 115 B.R. 760 (Bankr. S.D.N.Y. 1990), *vacated by consent order*, No. 89 Civ. 6012 (KTD), 90 Civ. 6048 (KTD), 1993 WL 388809 (S.D.N.Y. June 16, 1993).

[64] *In re Chateaugay Corp.*, 115 B.R. at 773-775.

[65] *Id.* at 775-776.

[66] *Id.* at 775; *see also PBGC v. LTV Corp.* (In re Chateaugay Corp.), 87 B.R. 779, 797-798 (S.D.N.Y. 1988) (PBGC claims based on prepetition conduct of debtors; postpetition termination merely rendered contingent claims fixed; analogizing claims for termination liability to withdrawal liability owed to multiemployer plan (citing *McFarlin's*, 789 F.2d at 101, 103)), *aff'd sub nom. PBGC v. LTV*, 875 F.2d 1008, 1019 (2d Cir. 1989) (prepetition labor, not postpetition termination of plan, gave rise to termination liability), *rev'd on other grounds*, 496 U.S. 633 (1990) (PBGC could restore terminated plan); *see also In re Finley, Kumble, Wagner, Heine, Underberg, Manley, Myerson & Casey*, 160 B.R. 892, 898-99 (Bankr. S.D.N.Y. 1993) (PBGC claim constituted "the paradigmatic prepetition contingent claim" and "is a general unsecured claim except to the extent that [the] Pension Trustee can prove, by a preponderance of the evidence, that the necessary funding contributions pertained to and encouraged postpetition labor by Debtor's employees"); *PBGC v. Sunarhauserman, Inc.* (In re Sunarhauserman, Inc.), 126 F.3d 811, 818-19 (6th Cir. 1997) (holding that administrative expense priority will only be granted for that portion of the claim that relates to benefits earned during the postpetition period).

[67] *In re Chateaugay Corp.*, 115 B.R. at 776-778.

[68] *In re Finley*, 160 B.R. at 898-99 ("prepetition contingent claim for minimum funding contributions ... is a general unsecured claim except to the extent that [the] Pension Trustee can prove, by a preponderance of the evidence, that the necessary funding contributions pertained to and encouraged postpetition labor by Debtor's employees").

As discussed above, in the context of chapter 11 reorganizations, some courts have determined that termination premiums are obligations of the post-emergence entity. Conversely, most courts have held that excise taxes imposed by the IRS in respect to missed contributions are "penalties" and so have treated them as prepetition general unsecured claims rather than priority tax claims[69].

QUESTION 7

Are remedies to collect in respect of pension deficits available against parties or entities other than the employer?

Yes. ERISA provides for joint and several liability against the plan's participating employer(s) and each member of the employer's "controlled group". In addition, ERISA provides remedies if the principal purpose of any person in entering into any transaction is to evade liability to which they would be subject under Title IV of ERISA.

Controlled group liability

ERISA provides that each member of a "controlled group", consisting of the employer and each trade or business under common control with the employer, is jointly and severally liable for the following:

- Multiemployer plan withdrawal liability;
- Single-employer pension termination liability;
- Minimum funding obligations; and
- PBGC premiums, including termination premiums.

Defining the controlled group is therefore important when analyzing defined benefit pension plan issues in bankruptcy because some liabilities under ERISA and the IRC extend to the debtor's controlled group members. "Trade or business" is not defined under ERISA, but a company engaged in a trade or business must be involved in the activity with (i) the primary purpose of making income or profit; and (ii) continuity and regularity[70]. For these purposes, a trade or business is generally considered to be under "common control" with a contributing employer if:

- The trade or business owns, directly or indirectly, a controlling interest (generally, an 80 percent or greater interest) in the contributing employer[71];

[69] *See United States v. Reorganized CF&I Fabricators, Inc.*, 518 U.S. 213 (1996) (excise taxes under I.R.C. § 4971(a), are penalties, and therefore not entitled to priority as a "tax" under section 507(a)(8)(E) of the Bankruptcy Code. 11 U.S.C. § 507(a)(8)(E)).

[70] *See Comm'r v. Groetzinger*, 480 U.S. 23, 35 (1987). Practitioners traditionally had operated under the assumption that private equity funds characterized as passive investment vehicles do not fall under the definition of a "trade or business." In 2007, the PBGC Appeals Board ruled that a private equity fund was a "trade or business," and, therefore, was liable for the pension liability of one of its portfolio companies. In 2013, the First Circuit adopted an "investment plus" test and determined in Sun Capital that a private equity fund was engaged in a "trade or business" and could be held jointly and severally liable for the pension obligations of its portfolio companies. *See Sun Capital Partners III, LP v. New England Teamsters & Trucking Indus. Pension Fund*, 724 F.3d 129 (1st Cir. 2013).

[71] *See* 29 U.S.C. § 1301(a)(14)(A); 29 C.F.R. §§ 4001.2, 4001.3(a)(1); 26 C.F.R. §§ 1.414(c)–1, 1.414(c)–2.

- The contributing employer owns, directly or indirectly, a controlling interest in the trade or business; or

- A parent organization which is a trade or business (or, in certain cases, an investor group consisting of five or fewer individuals, trusts or estates) owns, directly or indirectly, a controlling interest in both the contributing employer and the trade or business[72].

In other words, PBGC (or the plan administrator in the context of multiemployer plan withdrawal liability[73]) does not need to prevail on veil-piercing or alter-ego theories to hold controlled group members jointly and severally liable.

Transactions designed to avoid or evade liability

As originally enacted, ERISA did not contain any provision specifically dealing with liability for evasive transactions. Congress twice amended ERISA to make clear that evasive or sham transactions should not defeat ERISA liability, first in enacting ERISA Section 4212(c), 29 U.S.C. § 1392(c), applicable to multiemployer plans, and then in enacting ERISA Section 4069, 29 U.S.C. § 1369, applicable to single-employer plans. Congress enacted ERISA Section 4212(c) in 1980 to "require plan sponsors, employers, and courts to disregard sham transactions structured to avoid or evade liability, just as the PBGC is expected to disregard sham transactions in the enforcement of the current law[74]". Similarly, in later enacting ERISA Section 4069, Congress stated that:

> "a transaction intended to avoid liability should be disregarded for Title IV liability purposes. It has always been the intent of the law that solvent employers who benefit from work performed in return for pension promises, pay for those pension benefits rather than shift that cost to other companies which fund plans that pay PBGC premiums[75]".

Single-employer plans

In addition to the ability to pursue any member of the plan sponsor's "controlled group", PBGC also has the ability to impose liability on predecessor plan sponsors and members of the predecessor's "controlled group" for terminated single-employer plans. Section 4069(a) of ERISA, 29 U.S.C. § 1369, provides that if (1) a principal purpose of any person in entering into any transaction is to evade liability to which such person would be subject under Title IV and (2) the transaction becomes effective within five years before the date of the termination of a plan on which such liability would be based, then such person and the members of such person's controlled group (determined as of the termination date) shall be subject to liability under Title IV

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[72] *See* ERISA § 4001(a)(14)(A), 29 U.S.C. § 1301(a)(14)(A); 29 C.F.R. §§ 4001.2, 4001.3(a)(1); 26 C.F.R. §§ 1.414(c)–1, 1.414(c)–2.

[73] The MPPAA provides for withdrawal liability in the event that an employer withdraws from a multiemployer plan. Under the MPPAA, an employer who withdraws from a Multiemployer Plan becomes liable on the date of withdrawal for its proportionate share of the Multiemployer Plan's unfunded vested liability. In the event of a complete withdrawal, the employer is required to make payments to satisfy its vested, but unfunded, obligations to the plan beneficiaries. This obligation, commonly referred to as "withdrawal liability," was created to dissuade employers from withdrawing from multiemployer plans.

[74] Joint Report of the Senate Committee, 126 Cong. Rec. S10,117 (daily ed. July 29, 1980).

[75] H.R. Rep. No. 99-241 (II), at 55 (1985), *reprinted* in 1986 U.S.C.C.A.N. 685, 713.

in connection with such termination as if such person were a contributing sponsor of the terminated plan as of the termination date[76].

Section 4069 of ERISA was "the first statutory provision in ERISA expressly to impose liability on predecessor plan sponsors for terminated single-employer plans[77]". Prior to enacting Section 4069 of ERISA, a federal district court held that a predecessor employer is liable when it transfers a pension plan that later terminates when: (1) the employer intended to evade pension obligations and (2) the transferee that assumed responsibility for the plan had little chance to succeed economically[78]. Section 4069 of ERISA therefore codified the district court's ruling with one important change: Congress replaced the second prong of the test, that the transferee had no reasonable chance of fulfilling the pension obligations it had assumed, with the temporal requirement that the plan terminate within five years of the date the transaction became effective[79].

Multiemployer plans

Similarly, if a principal purpose of a transaction is to evade or avoid withdrawal liability in the context of a multiemployer plan, such liability may be imposed as if the transaction had not occurred (i.e., even if the entity left the controlled group in the transaction[80]). Several cases have applied ERISA Section 4212(c) to impose withdrawal liability[81]. Other cases have held that ERISA Section 4212(c) did not apply despite the avoidance of

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[76] *See* ERISA § 4069, 29 U.S.C. § 1369. Section 4069(a) of ERISA provides as follows:

> "If a principal purpose of any person in entering into any transaction is to evade liability to which such person would be subject under this subtitle [29 U.S.C. §§ 1361-1371] and the transaction becomes effective within five years before the termination date of the termination on which such liability would be based, then such person and the members of such person's controlled group (determined as of the termination date) shall be subject to liability under this subtitle [29 U.S.C. §§ 1361-1371] in connection with such termination as if such person were a contributing sponsor of the terminated plan as of the termination date. This subsection shall not cause any person to be liable under this subtitle [29 U.S.C. §§ 1361-1371] in connection with such plan termination for any increases or improvements in the benefits provided under the plan which are adopted after the date on which the transaction referred to in the preceding sentence becomes effective".

[77] *PBGC v. White Consol. Indus., Inc.*, 998 F. 2d 1192, 1197 (3d Cir. 1993).

[78] *See In re Consol. Litig. Concerning Int'l Harvester's Disposition of Wis. Steel*, 681 F. Supp. 512, 525-27 (N.D. Ill. 1988).

[79] *PBGC v. White Consol. Indus., Inc.*, 215 F.3d 407, 414 (3rd Cir. 2000) (noting that, unlike the test adopted by the district court, Section 4069 of ERISA "does not require, as an independent element, proof that the new sponsor lacked a reasonable chance of succeeding").

[80] ERISA § 4212(c), 29 U.S.C. § 1392(c).

[81] *See, e.g.*, *Santa Fe Pac. Corp. v. Central States Se. & Sw. Areas Pension Fund*, 22 F.3d 725, 729 (7th Cir. 1994) (where a parent sold a trucking subsidiary in a leveraged buyout and the purchaser went broke a year later, withdrawal liability could be assessed against the parent; the court acknowledged that for reasons unrelated to withdrawal liability the parent wanted to get rid of the subsidiary, but by choosing a stock sale as opposed to an asset sale in part to avoid withdrawal liability, it showed that a major purpose was to avoid withdrawal liability); *Sherwin-Williams Co. v. N.Y. State Teamsters Conference Pension and Retirement Fund*, 969 F.Supp. 465 (N.D. Ohio 1997), *aff'd*, 158 F.3d 387 (6th Cir. 1998); *SUPERVALU, Inc. v. Board of Trustees of Sw. Pa. & W. Md. Area Teamsters & Emprs. Pension Fund*, 500 F.3d 334, 341-42 (3d Cir. 2007) (agreement with union to terminate obligation to contribute to fund in return for lump sum severance pay and wage premiums was a transaction that had a principal purpose to evade or avoid withdrawal liability and therefore must be disregarded).

withdrawal liability[82]. Courts have on occasion found individuals liable under ERISA Section 4212(c) for participating in a scheme to evade or avoid liability even though multiemployer withdrawal liability generally only applies to the employer[83]. The multiemployer provision, ERISA Section 4212, does not have the five-year "look back" limitation contained in the analogous single-employer provision, ERISA Section 4069[84].

Personal liability

When Trans World Airlines ("TWA") filed for bankruptcy in 1992, the proposed plan of reorganization would have severed an individual investor's controlled group affiliation with TWA leaving little recourse for PBGC in its attempts to remedy the underfunding of the pension plans. In response, PBGC announced its intent to terminate the pension plans before the reorganization plan could be confirmed and pursue TWA and the individual investor for the more than $1 billion in alleged underfunding. As a result of this threat, a settlement was reached between TWA, the unions, the investor, and PBGC to prevent termination and alleviate the underfunding. Relevant settlement provisions included:

- The investor would loan TWA $200 million;
- An investor-related entity would sponsor the plans, thus making the investor responsible for making the minimum funding contributions;
- TWA would issue $300 million in notes to make part of the annual plan contributions;
- PBGC would not terminate the plans and would release TWA and the investor from all future termination liability, except for what was agreed to in the settlement;

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82 *See, e.g.*, *Cuyamaca Meats, Inc. v. San Diego & Imperial Cntys. Butchers' and Food Emprs.' Pension Trust Fund*, 827 F.2d 491, 499-500 (9th Cir. 1987) (an employer proposal during collective bargaining that was motivated at least in part by a desire to minimize withdrawal liability, namely, that it cease making contributions to multiemployer plan and contribute to individual retirement accounts instead, could not be disregarded by the union as a transaction to evade or avoid liability under § 4212(c), since the offer was a candid reaction to the change in financial status of the pension funds and posed no threat to the financial stability of the fund); *Dorn's Transp., Inc. v. Teamsters Pension Trust Fund of Phila. & Vicinity*, 787 F.2d 897, 902-03 (3d Cir. 1986) (overturned arbitrator's decision, and held that where a buyer bought a company in a stock purchase, there was no withdrawal liability imposable on the buyer as a result of the sale since it was a mere change in form under ERISA, particularly since both the buyer and the seller had identical collective bargaining agreements; with respect to ERISA § 4212, the court held that even though the seller may have known it was evading liability, since the buyer was unaware of the circumstances avoidance of liability could not be a principal purpose of the transaction); *Trustees of Teamsters Pension Trust Fund of Phila. & Vicinity v. Fed. Express Corp.*, No. 86-304, 1995 WL 791371, at *6 (D. Del. Dec. 27, 1995) (primary purpose of employer's sale of interest in subsidiary that ceased making pension plan contributions when it filed for bankruptcy 14 months after sale date was not to evade withdrawal liability, where there were plausible reasons for structuring as stock sale rather than asset sale).

83 *IUE AFL-CIO Pension Fund v. Herrmann*, 9 F.3d 1049, 1056 (2d Cir. 1993) (ERISA §§ 4212(c) and 4301 can be read together to impose liability on individuals even though they are not employers, if they participated in a scheme to evade or avoid withdrawal liability); *Bd. of Trustees, Sheet Metal Workers' Nat'l Pension Fund v. Illinois Range, Inc.*, 186 F.R.D. 498, 201-02 (N.D. Ill. 1999) (owner of company who sold company in a scheme where buyer would go bankrupt, could be liable under §§ 4212(c) and 4301 for evading and avoiding withdrawal liability).

84 ERISA § 4221(g), 29 U.S.C. § 1401, added by the PPA, relieves an employer in certain narrowly defined circumstances of the obligation to make withdrawal liability payments until a final decision in the arbitration proceeding, or in court, upholds the plan sponsor's determination that the employer is liable for withdrawal liability based in part or in whole on ERISA § 4212(c), 29 U.S.C. § 1392(c).

- At the investor's request, PBGC would terminate the plans if a "Significant Event" (as defined by the settlement) occurred; and

- If a Significant Event requiring termination occurred, the investor's liability to PBGC would be limited to $240 million.

PBGC ultimately terminated the TWA plans in 2000 and the settlement agreement was upheld by the DC Circuit[85].

QUESTION 8

Are there any cross-border features of your pension regime?

Extraterritorial application

ERISA does not expressly address whether controlled group liability extends to entities based outside of the U.S. In a 1997 advisory opinion letter (the "1997 Opinion Letter"), the PBGC took the position that non-U.S. entities who are under "common control" with a U.S. employer may be included within the employer's controlled group[86]. The PBGC expressed the view that imposing liability on non-U.S. controlled group members did not implicate the extraterritorial application of ERISA where the events triggering the liability occurred in the U.S., but further noted that it would reach the same conclusion even where extraterritorial application was implicated[87].

While the PBGC acknowledged in the 1997 Opinion Letter that there existed a presumption against extraterritorial application of U.S. laws absent clear congressional intent to the contrary[88], the PBGC reasoned that the purpose behind ERISA's controlled group principle was to prevent business owners from avoiding liability by fractionalizing their business operations or otherwise organizing their activities so as to avoid the liability provisions of ERISA, and that this purpose would be "ill-served" by limiting controlled group liability to U.S. entities. Accordingly, the PBGC determined that the controlled group liability provisions of ERISA were intended to have extraterritorial application[89].

Liens against non-US entities

PBGC believes that its statutory liens may be asserted extraterritorially[90]. Case law addressing the ability of the PBGC to obtain and enforce a lien against non-U.S. entities recognizes that a court must first address whether the court has personal jurisdiction over the defendant non-U.S. entity. A court may find two types of personal jurisdiction: (i) general (or all-purpose) jurisdiction and (ii) specific (or case-linked) jurisdiction.

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[85] *Allied Pilots Ass'n v. PBGC,* 334 F.3d 93 (D.C. Cir. 2003).

[86] PBGC Op. Ltr. 97-1 (May 5, 1997), *available at* http://prbc.gov/documents/oplet/97.1.pdf.

[87] *Id.*

[88] *See, e.g.*, *EEOC v. Arabian Am. Oil Co.*, 499 U.S. 244, 248 (1991) ("It is a longstanding principle of American law 'that legislation of Congress, unless a contrary intention appears, is meant to apply only within the territorial jurisdiction of the United States.'" (citation omitted)).

[89] PBGC Op. Ltr. 97-1, *supra* n.81.

[90] Internal Rev. Manual § 5.12.2.11 (revised Feb. 1, 2007).

General jurisdiction generally requires a higher level of business activity in the United States than typically results from a non-U.S. company's ownership of a U.S. subsidiary. When a non-U.S. defendant maintains such continuous and systematic contacts with the United States that it is essentially "at home" in the United States, general jurisdiction exists and a U.S. court can hear any and all claims against the defendant[91]. In contrast, specific jurisdiction may apply where (1) the non-U.S. defendant has purposely directed its activities at the U.S. and (2) the claim arises out of the activities directed at the U.S.

In *PBGC v. Satralloy, Inc*.[92], a federal district court held that in order to adjudicate whether a PBGC lien is properly assertable against a non-U.S. company, the PBGC must establish the minimum contacts necessary for the court to have personal jurisdiction over the defendant, i.e., the party against whom the PBGC is asserting the lien[93]. The court dismissed the claims by the PBGC for lack of personal jurisdiction, stating that being a controlled group member, by itself, did not amount to sufficient minimum contacts to establish personal jurisdiction[94]. The court subsequently reconsidered its decision, and found that the dismissal was improper as to one of the parties because the PBGC made a prima facie case for personal jurisdiction when it asserted that the non-U.S. company acted through a U.S. agent[95]. The court remanded the case for rehearing on the issue of jurisdiction over the non-U.S. company, noting that, while a parent-subsidiary relationship is not, in and of itself, sufficient to establish personal jurisdiction, such relationship may serve as a basis for jurisdiction if the subsidiary acts as the "alter ego" of the parent.

In a more recent Seventh Circuit Court of Appeals case, *GCIU-Employer Retirement Fund v. Goldfarb Corporation*[96] (*Goldfarb*), a multiemployer pension plan sought to collect withdrawal liability payments from a non-U.S. entity that was a member of the same controlled group as the withdrawing employer. In considering whether to dismiss the claim for lack of personal jurisdiction, the Seventh Circuit held that a non-U.S. parent's ownership of a majority of the contributing employer's stock was insufficient to establish the minimum contacts necessary for personal jurisdiction[97].

Jurisdiction over non-U.S. entities (*Asahi* Tech)

In a recent decision, the U.S. District Court for the District of Columbia determined that a non-U.S. corporation, having acquired a company with the knowledge that the target maintained a significantly underfunded defined benefit pension plan, had sufficient contacts with the United States to allow the court to exercise personal jurisdiction over the non-U.S. entity in an action brought by PBGC to recover liabilities associated with the underfunded pension plan. Following that determination[98], *Asahi* Tec Corporation (*Asahi*), the non-U.S. (Japanese) corporation that acquired U.S. based Metaldyne Corporation (Metaldyne) in 2007, announced a settlement of its long-running dispute with the PBGC regarding the 2009 termination of Metaldyne's significantly underfunded defined benefit pension plan.

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91 *See Daimler AG v. Bauman*, 134 S. Ct. 746, 761 (2014) (citing *Goodyear Dunlop Tires Operations, S.A. v. Brown*, 131 S. Ct. 2846, 2851 (2011)).

92 No. C-2-90-0630, 1992 U.S. Dist. LEXIS 22829 (S.D. Ohio July 16, 1992).

93 *Id.* at *6-7.

94 *Id.* at *14.

95 *PBGC v. Satralloy, Inc.*, No. C-2-90-0630, 1993 U.S. Dist. LEXIS 21422, at *13 (S.D. Ohio Aug. 6, 1993).

96 565 F.3d 1018 (7th Cir. 2009).

97 *Id.*

98 *PBGC v.* Asahi *Tec Corp.*, 979 F. Supp. 2d 46, 57 (D.D.C. 2013).

Although the *Asahi* court did not address the extraterritorial enforceability of any judgment obtained under ERISA, the court did find that it had personal jurisdiction over *Asahi* with respect to the PBGC's claims and that, notwithstanding *Asahi*'s status as a non-U.S. entity, *Asahi* was liable for unfunded benefit liabilities under ERISA Section 4062 and for termination premiums under ERISA Section 4006 by virtue of being a member of a controlled group that included Metaldyne.

The *Asahi* district court determined that *Asahi* had directed its activities at the United States by acquiring Metaldyne with prior knowledge of the pension liability issues, and that this was sufficient to establish personal jurisdiction over *Asahi*. In finding personal jurisdiction over *Asahi*, the district court highlighted the fact that *Asahi* had hired a U.S. company to conduct due diligence on Metaldyne for the specific purpose of identifying Metaldyne's pension plan obligations, and the court cited additional evidence showing that senior officers of *Asahi* were aware of both the underfunded status of the Metaldyne plan and of the potential for controlled group liability.

The *Asahi* district court also determined that the PBGC's claim was based on *Asahi*'s status as a controlled group member, which resulted from its acquisition of Metaldyne, and that the PBGC claim against *Asahi* therefore arose out of the activities that *Asahi* had directed at the United States. The court distinguished the Seventh Circuit's *Goldfarb* decision by noting that in that case, "liability had to have been triggered by some act of the defendant," i.e. the decision to withdraw from a multiemployer plan, whereas in *Asahi* liability was controlled by "mere ownership at the time of termination[99]". This distinction is unpersuasive, however, because in both cases the liability of the non-U.S. entity arose as a result of it being a member of the same controlled group as the entity whose action (the withdrawal from the multiemployer plan in *Goldfarb* and the termination of the single employer plan in *Asahi*) resulted in the original liability upon which the controlled group liability was based. The *Asahi* district court disagreed with the *Goldfarb* court's test for determining personal jurisdiction, criticizing the Seventh Circuit's ruling that specific jurisdiction exists against a non-U.S. defendant only where the action "*directly* arise[s] out of the specific contacts" between the defendant and the forum state as imposing "a more stringent test than the one required by the Supreme Court[100]".

Having found personal jurisdiction over *Asahi*, the district court held that *Asahi* could be held liable on a controlled group theory for both unfunded pension liabilities and termination premiums. The *Asahi* district court therefore implicitly determined that such liabilities may be imposed on non-U.S. members of a controlled group.

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[99] *PBGC v. Asahi Tec Corp.*, 839 F. Supp. 2d 118, 128 (D.D.C. 2012).
[100] *Id.*

QUESTION 9

Discuss the state of defined benefit plans in your country

Since the passage of ERISA, there has been a steady trend away from defined benefit pension plans in favor of defined contribution plans, such as 401(k) plans, which are not guaranteed by PBGC and in which the employee, rather than the employer, bears the investment risk. Over the past three decades, there has been a more than 75 percent decline in the number of PBGC-covered plans. We expect the decline in the number of PBGC covered plans to continue.

One innovative step being taken to preserve multiemployer plans is the adoption of “hybrid” multiemployer plans. In a hybrid multiemployer plan, an employer completely withdraws from multiemployer plan (incurring withdrawal liability in an agreed-to amount) and agrees to “reenter” as a “new employer” in a separate pool. The new and old employer pools are treated separately. We expect this trend to continue in the context of multiemployer plans.

Member Associations

American Bankruptcy Institute
Asociación Argentina de Estudios Sobre la Insolvencia
Asociacion Uruguaya de Asesores en Insolvencia y Reestructuraciones Empresariales
Association of Business Recovery Professionals - R3
Association of Restructuring and Insolvency Experts
Australian Restructuring, Insolvency and Turnaround Association
Bankruptcy Law and Restructuring Research Centre, China University of Politics and Law
Business Recovery and Insolvency Practitioners Association of Nigeria
Business Recovery and Insolvency Practitioners Association of Sri Lanka
Canadian Association of Insolvency and Restructuring Professionals
Canadian Bar Association (Bankruptcy and Insolvency Section)
Commercial Law League of America (Bankruptcy and Insolvency Section)
Especialistas de Concursos Mercantiles de Mexico
Finnish Insolvency Law Association
Ghana Association of Restructuring and Insolvency Advisors
Hong Kong Institute of Certified Public Accountants (Restructuring and Insolvency Faculty)
Hungarian Association of Insolvency Practitioners
INSOL Europe
INSOL India
INSOLAD - Vereniging Insolventierecht Advocaten
Insolvency Practitioners Association of Malaysia
Insolvency Practitioners Association of Singapore
Instituto Brasileiro de Estudos de Recuperação de Empresas
Instituto Brasileiro de Gestão e Turnaround
Instituto Iberoamericano de Derecho Concursal
International Association of Insurance Receivers
International Women's Insolvency and Restructuring Confederation
Japanese Federation of Insolvency Professionals
Korea Restructuring and Insolvency Practitioners Association
Law Council of Australia (Business Law Section)
Malaysian Institute of Certified Public Accountants
National Association of Federal Equity Receivers
Nepalese Insolvency Practitioners Association
NIVD – Neue Insolvenzverwaltervereinigung Deutschlands e.V.
Non-Commercial Partnership Self-Regulated Organisation of Arbitration Managers "Mercury" (NP SOAM Mercury)
Recovery and Insolvency Specialists Association (BVI) Ltd
Recovery and Insolvency Specialists Association (Cayman) Ltd
Recovery and Insolvency Specialists Association of Bermuda
REFor – The Insolvency Practitioners Register of the National Council of Spanish Schools of Economics
Restructuring Insolvency & Turnaround Association of New Zealand
Russian Union of Self-Regulated Organizations of Arbitration Managers
Society of Insolvency Practitioners of India
South African Restructuring and Insolvency Practitioners Association
The Association of the Bar of the City of New York
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ISBN: 978-1-907764-19-6