



Revision of the annual  
guaranteed rate of return

# Revision of the return guarantee

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## How it was...

- Sponsor had to guarantee a minimum rate of return on contributions made to the pension plan
- Guarantee embedded in the Belgian social and labor law
- Active plan members
  - Guarantee on employee contributions → **3,75%**
    - Applicable to both DB & DC schemes
  - Guarantee on employer's (sponsor) contributions → **3,25%**
    - Only applicable to DC or cash balance plans
    - First 5 years in the plan → guarantee = annual inflation with max. 3,25%

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## How it was...

- Deferred plan members
  - 0% return guarantee
- In theory the guarantee only has to be funded
  - For pension funds at effective payment (at retirement, decease, transfer of pension provisions)
  - In practice prudence imposes continuous funding for insured plans
- Interest rates have dropped substantially
- Insurance vs. Pension fund industry
  - Belgium: pension plans mostly via insurance contracts
  - If legal guarantee > offered insurance annual guarantee: hard for employers to find insured solution for the legal return guarantee:
    - contributions will rise
    - plans are cancelled
    - Employer bears the financial risk →use pension fund

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## Reform law of 18/12/2015

### ➤ Changes:

- No difference anymore between return guarantee on employer/employee contributions
- Fixed rate replaced by a floating rate with annual adaptation, minimum 1,75% and maximum 3,75%

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## Law 18 December 2015

### **Floating annual return guarantee**

- Linked to the observed 10y yield of Belgian Government bonds
- Formula: yield = x % of the average yield of 24 months on June 1st
- 2016 + 2017: x = 65%
  - 2018 + 2019: x = 75% if ok by BNB
  - From 2020: x = 85%

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**Law 18 December 2015**

## **Floating annual return guarantee**

- Round to closest multiple of 0.25%
- If new calculation differs more than 0.25% from former return guarantee: adaptation applicable from January 1st
- Min 1,75% - max 3,75%
- FSMA communicates the new return guarantee before Dec 1st

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**Law 18 December 2015**

## **Application revised return guarantee**

- Different application depending on
- Type of pension institution
- Type of contractual obligation to the sponsor

“Horizontal” or “vertical” methodology

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**Law 18 December 2015**

## **Application revised return guarantee**

- Horizontal method to be used by
- Institutions that offer guarantee until pension age (term of the contract) → most existing insured plans
- Revised return guarantee only applicable to pension contributions made after return revisions

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**Law 18 December 2015**

## **Application revised return guarantee**

- Vertical method
- All other pension institutions and plans without contractual term guarantee
- Revised rate of return applicable to existing provisions and new contributions

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## **Difference between the social and labour law guarantee and the (maximum) contractual guarantee by insurance companies**

Social guarantee = guarantee of employer to employee. Employer has to recognize its liability in the balance sheet of the company

Contractual guarantee = guarantee of pension institution to employer/employee

Consequence:

If social guarantee > contractual guarantee: employer at risk for difference – provisions on balance sheet

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## Calculation method

-Average yield 10y Be Gvt bond (1/6/2013-1/6/2015): **1,7113%**

- $0,65 \times 1,7113\% = 1,1123\%$

-round next 0,25% = **1%**

- $\text{Min}(\text{Max}(1\%; 1,75\%); 3,75\%) = 1,75\%$

Possibilities:

- 1.75%
- 2.00%
- 2.25%
- 2.50%
- 2.75%
- 3.00%
- 3.25%
- 3.50%
- 3.75%

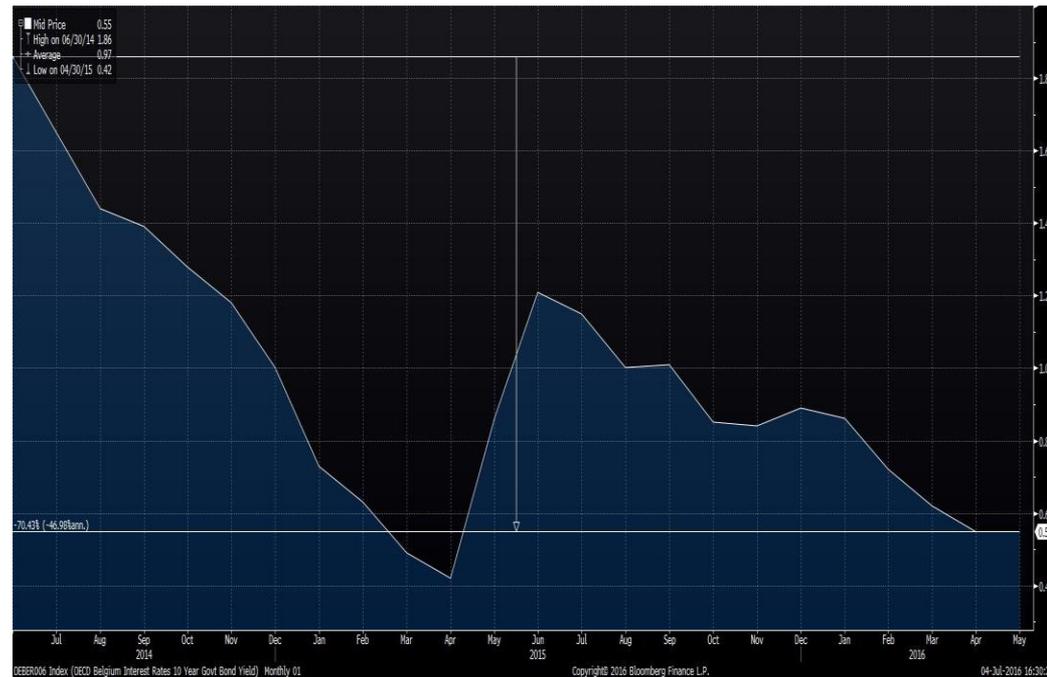


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## Calculation update 1/6/2016

- Current guarantee: 1,75%
- Average yield 10y B Gvt Bond (01/06/2014-01/06/2016): **0,97%**
- $0,65 \times 0,84\% = \mathbf{0,6305\%}$
- Round to nearest multiple of 0,25% = **0,75%**
- $\text{Min}(\text{Max}(0,75\%; \mathbf{1,75\%}); \mathbf{3,75\%}) = \mathbf{1,75\%}$
- If the new guarantee <  $\mathbf{1,75\% + 0.25\%}$ : no change



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## Evaluation

### ➤ Pro:

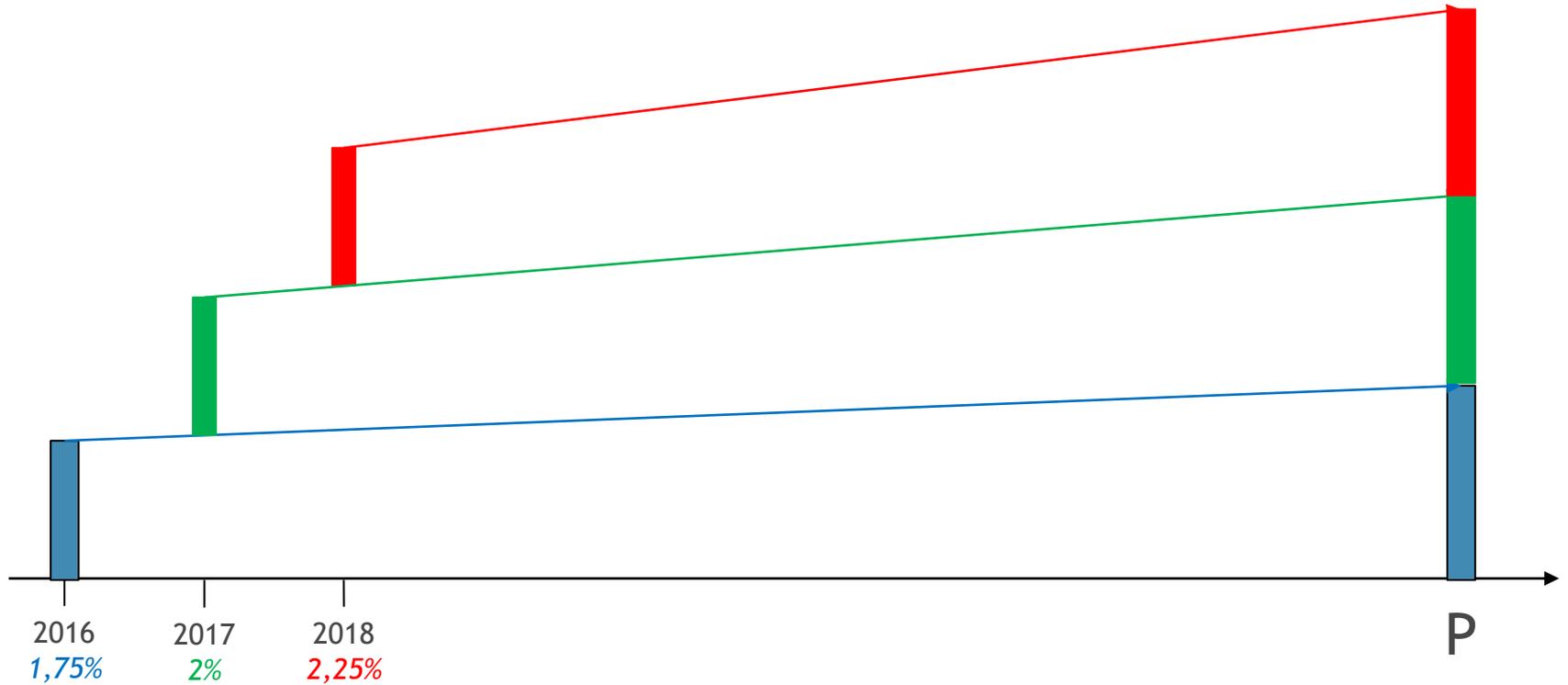
- Guarantee function of market situation
- Guarantee for plan members to build up a min.

### ➤ Contra:

- Relevance of a long-term guarantee in a low interest environment
- Use of reference to lending money to the Belgian government?
- Backwards looking calculation to be applied to future payments?

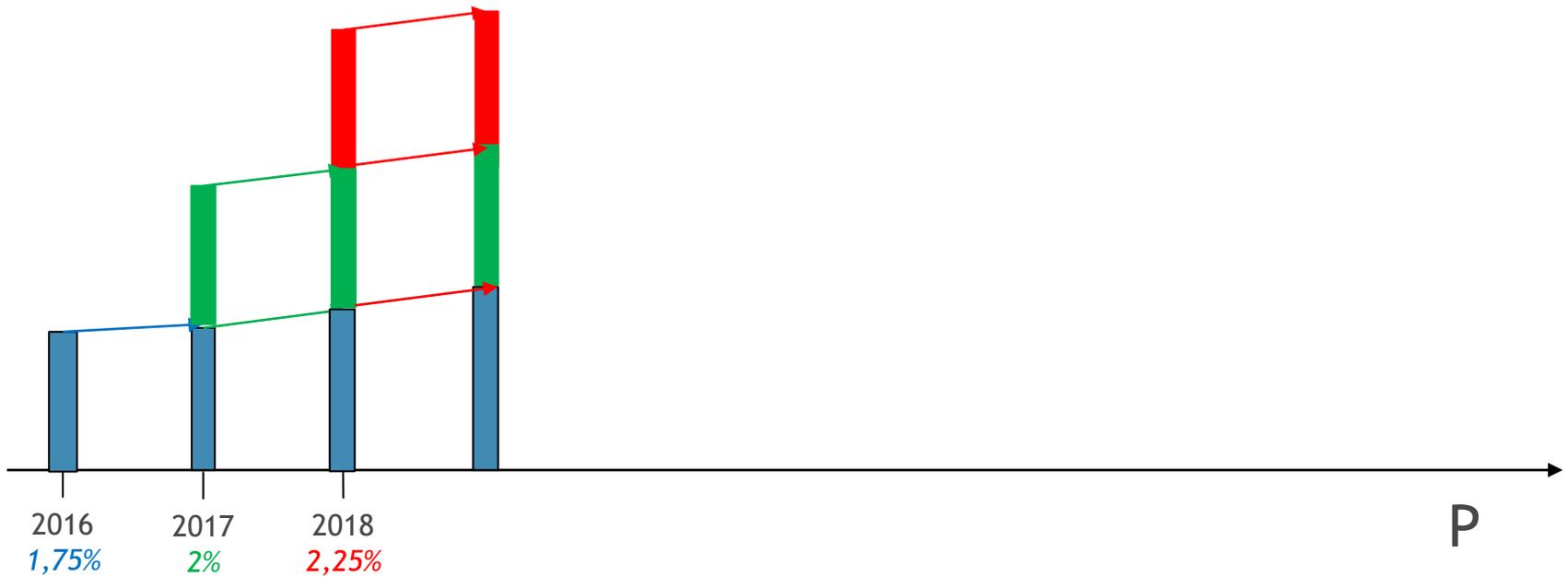
# Horizontal and vertical method

## Horizontal method



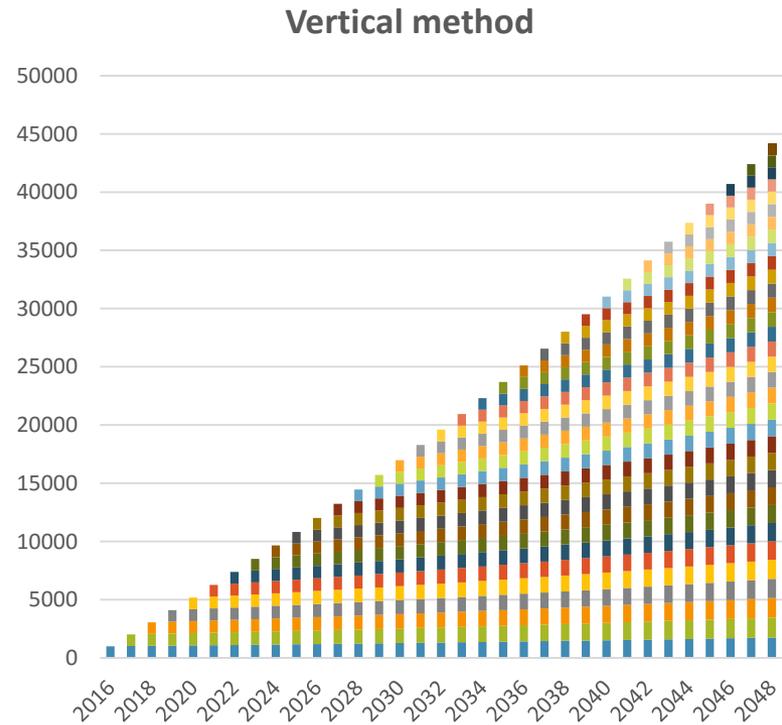
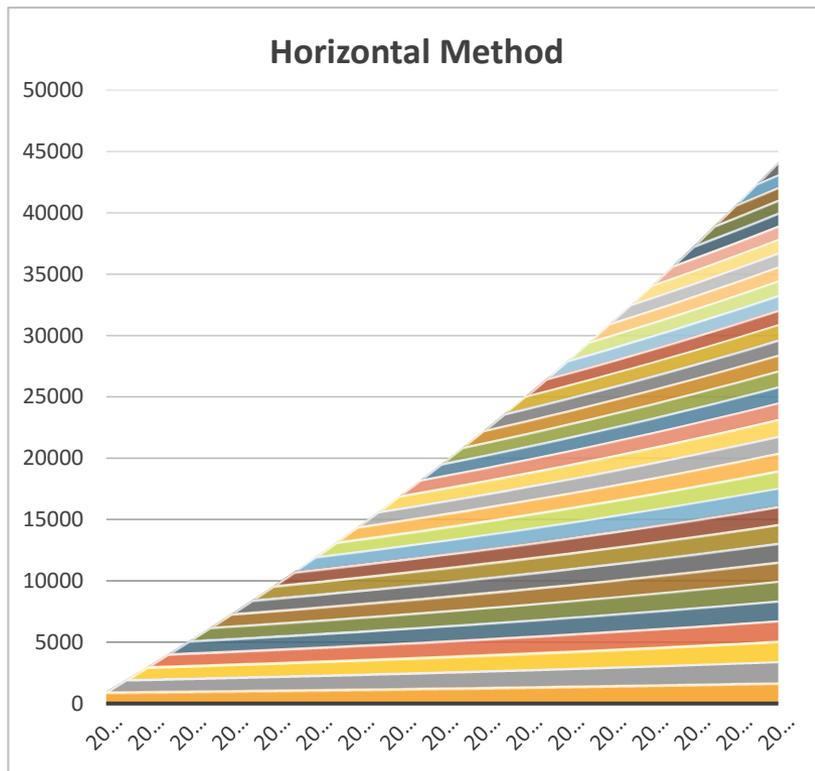
# Horizontal and vertical method

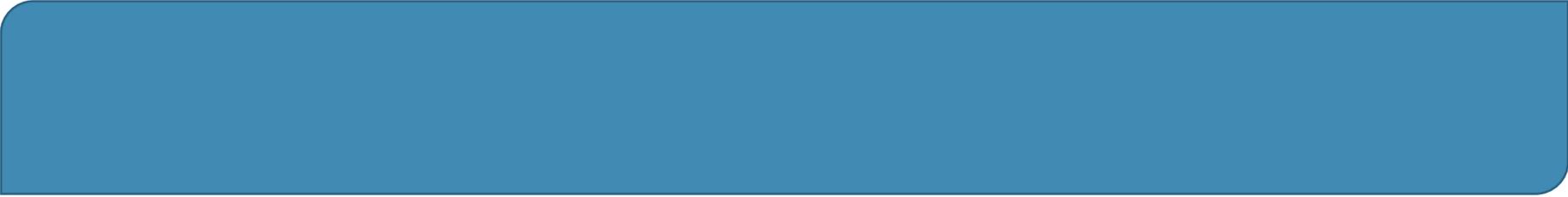
## Vertical method



# Horizontal and vertical method

35j, wp=67, B=1000, i=1,75%





# Results Belgian stress tests

# EIOPA stress tests

- Intention to perform stress testing every 2 years
- Universe of funds: to be determined by local regulators
  - Selection of funds so that min 50% of AUM is covered
  - Mainly the largest funds are selected
  - 13 funds selected by regulator, 3 participated voluntarily (16 funds total)
- <> QIS (or QA) which are studies in order to see the impact of a changing solvency regime (not stress scenario's)

# Methodology and Results

- Starting point : baseline scenario (scenario “as is”) under both NBS (local pensions GAAP) and HBS (holistic balance sheet, renamed ‘common methodology’)
- Difference: actualisation rate used to calculate NPV of liabilities – common methodology imposes current market rates (based on swap curve cfr SII)
- In general, liabilities +24% in HBS compared to NBS
- Is there underfunding under NBS or/and HBS in the current situation?
- BE shows 138% FR under NBS and 107% FR under HBS
- BE starts with relatively high level of overfunding
  
- All results on aggregated basis – individual fund situations may vary

# Stress tests

- 2 adverse market scenario's + longevity scenario
- Probability of the events set to 0.5% (or 99.5% certainty)
- Adverse market scenario's contain both:
  - Asset prices drop
  - Interest rates fall
- Impact in value of investments and value of liabilities! (interest rates drop, liabilities rise)

## NBS

- BE after stress still above 100% of NBS FR
- In general, scenario 2 less impact then scenario 1 in NBS terms
  - Why? Liability discount rates! Scenario's only impact investments under NBS.

# Stress tests

## HBS

- Scenario 1 impacts mainly assets only, while scenario 2 impacts heavily both assets and liabilities under HBS!
- Effect of scenario 2 larger than scenario 1 due to impact on discount rates in liabilities
- BE: scenario 1 increase of 3% in liabilities and decrease of 22% of assets (FR HBS 82%) ; scenario 2 6% increase in liabilities and 11% decrease in assets (FR HBS 90%)
- A lot of conditional benefits
- Reasons:
  - Asset mix relatively balanced
  - Discount rates not too high
  - High level of funding
  - Bigger funds in sample (mostly better funded/managed funds) – individual cases may vary

# Tom Mergaerts, CEO Amonis

- Tom is currently CEO at Amonis, the largest Belgian pension fund aimed at the medical sector. Amonis manages € 1,8 bln for about 27.000 plan members, mostly self-employed
- Tom has studied applied economics and holds master degrees in economics, financial economics and actuarial and financial modelling. He is also Level II candidate in the CAIA program
- Tom is qualified actuary and member of the council of the Belgian Actuarial Society IA|BE, board member of the Belgian pension association PensioPlus and member of the Dutch actuarial association