Maastricht
Law

Faculty of Law
Working Paper series

2020/02

Pan-European Personal Pension Product: on its need, tax-treatment and obstacles

by Pim Mertens

Maastricht University

Pan-European Personal Pension Product: on its need, tax-treatment and obstacles

Pim Mertens

Abstract: The European pension market is very diverse, generally insufficiently sustainable and inefficient. This paper examines the recent PEPP Regulation and its evolution in more detail, observes the tax problems and seeks a solution to the tax problems. The PEPP is introduced to strengthen and integrate the European pension market. The PEPP is designed as a transparent, simple and cost-efficient pension product, which can be offered across borders by many European pension providers. However, both pension and tax policy are national competencies, which put pressure on the PEPP. This paper observes that during the legislative procedure a less ambitious and 'European' Regulation was developed. It is concluded that a more ambitious plan regarding to taxation is necessary in order to make PEPP a success. The tax problems arise from the diversity of tax regimes and can best be remedied by optional tax harmonisation. This 'fiftieth' tax regime for PEPPs should be designed as 'lightly' as possible and introduced step by step. A necessary and fundamental start is harmonising the tax admissible providers and the principle of compensating vessels.

Keywords: Pensions, European integration, Taxation, EU policy and competency, Cross-border mobility

Table of contents

1. Introduction ... *3*

2. Pan-European Personal Pension Product ... *3*

a. Background of the proposal ... 3

b. The Regulation ... 6

3. Tax treatment of personal pensions in the EU ... *12*

a. The Recommendation and the EU powers regarding taxation ... 12

b. Case-study: the Netherlands ... 13

c. Arising tax problems due to diversity ... 17

4. Solutions on the tax treatment of PEPP ... *20*

a. Status quo is not enough ... 20

b. Tax policy options ... 23

c. Optional harmonisation and its implementation ... 26

Conclusion ... *32*

1. Introduction

Pension is a hot-topic, both on national as European level. A pension system is not adequate enough due to diminishing returns and low interest rates, while it is also not sustainable due to increasing ageing and dejuvenation. Most national governments and social partners are working on reforming and improving their pension systems via negotiations and legislative measures.[1] Despite the fact that pension design is a national matter, the European Commission (hereafter: EC) is also working on the sustainability and adequacy of pensions. On the 29th of June 2017, the EC has put forward a proposal[2] for a pan-European personal pension product (hereafter: PEPP). On the 25th of July 2019, the official text is published in the Official Journal of the European Union[3] as Regulation (EU) 2019/1238 of the European Parliament and of the Council of 20 June 2019 on a pan-European Personal Pension Product (PEPP) (hereafter: Regulation). The PEPP has to deal with several factors, such as the ageing population and strengthening of the European internal market.

However, research has shown that the tax facilitation of pension savings has a major impact on the success of pension savings.[4] Since Article 114(2) of the Treaty on the Functioning of the European Union (hereafter: TFEU) stipulates that taxation is an autonomous competence of the EU Member States, the tax facilitation of the PEPP may be compromised. The PEPP is accompanied by a Recommendation on the taxation of PEPP[5], but is not of binding nature. This article investigates the tax issues arising around a true European pension product, as the PEPP and how policy could deal with this. Before the obstacles and solutions are identified, the paper starts with elaborating the Regulation, its aims and relevant changes compared to the proposal.

2. Pan-European Personal Pension Product

a. Background of the proposal

The proposal of the EC is based on the report of the European Insurance and Occupational Pensions Authority (hereafter: EIOPA) of 2016[6], recommending a European personal pension

---

[1] See for example OECD, *Pension Adequacy Report 2018*, vol. 1, OECD Publishing: Paris; European Foundation for the Improvement of Living and Working Conditions, *Social partners' involvement in pension reform in the EU,* Dublin 2013.

[2] European Commission, *Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on a pan-European Personal Pension Product (PEPP)*, COM(2017) 343.

[3] Official Journal of the European Union L 198/1

[4] Ernst & Young, *Study on the feasibility of a European Personal Pension Framework* (FISMA/2015/146(02)/D), 2017, DOI: 10.2874/342225.

[5] European Commission, *Commission Recommendation on the tax treatment of personal pension products, including the pan-European Personal Pension Product,* C(2017) 4393 final.

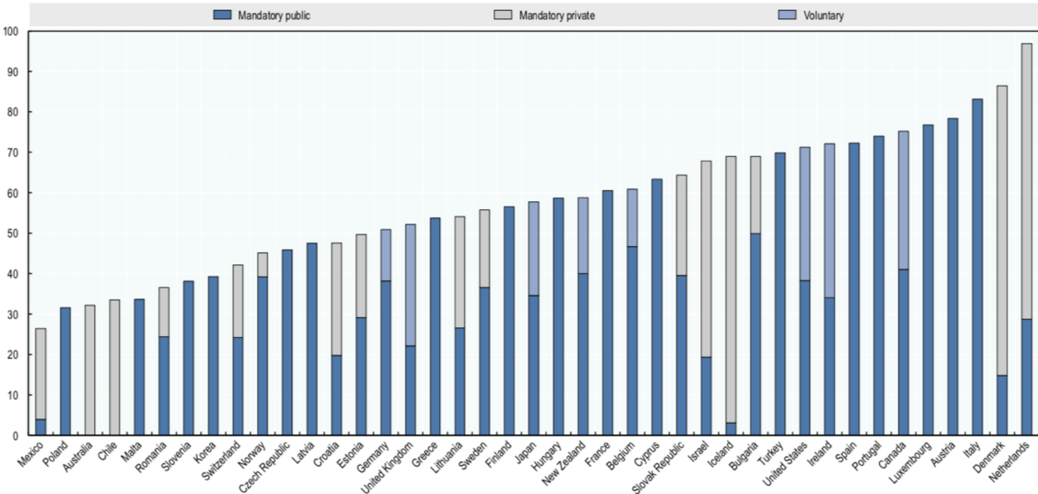
[6] European Insurance and Occupational Pensions Authority, *EIOPA's advice on the development of an EU Single Market for personal pension products (PPP)*, EIOPA-16/457, EIOPA: Germany, Frankfurt 2016.

product. The lines of thought are the same and can be brought back to two reasons: the pension adequacy in Europe and the integration of the European market.

The pension systems of the European Member States are very different. Each system originates from and is shaped by the specific social, cultural, economic and historical circumstances of a Member State. Pension policy is therefore seen as a national matter for the Member States.[7] Nevertheless, pension systems are generally designed along the same lines as those of the World Bank. In its report, the World Bank advocates a pension system with three pension pillars.[8] For adequacy and sustainability, the pension pillars combine the pay-as-you-go system and the funded system. In the pay-as-you-go system, the pension benefits of current pensioners are financed by the current tax/contribution payers, which is done by means of the basic pension in the first pillar. The basic pension is usually obtained from the government on the basis of residency, independent or dependent on an employment history and is therefore drawn from public finances. In addition, in the second and third pillars, private savings are made, according to the funded scheme, in order to limit the pressure on public finances. In the funded scheme, pension benefits are covered by own contribution payments and the returns on them. The second pillar consists of the supplementary pensions, arranged between employer and employee, while the third pillar contains the private pension savings of an individual.

The diversity of pension policies can be seen, among other things, in the relative size, and even the presence, of the different pension pillars, which differ significantly from one Member State to another.

Table 1 Breakdown of average replacement rate by pension pillar



[7] European Commission, *White Paper: an agenda for adequate, safe and sustainable pensions,* COM(2012) 55 final, p. 8.
[8] World Bank, *Averting the Old Age Crisis,* Oxford University Press: 1994. DOI:10.1596/0-8213- 2970-7.

As table 1[9] shows, the total pension income in many Member States still rely mostly of the public pension benefit. In many Member States, funded pillars are underdeveloped or even absent. One result of this is that only 27% of European residents participate in a pension product.[10] Given the ageing society, the sustainability and adequacy of pension systems are under stress. The so-called *pension gap*, the difference between the replacement rate of a pension scheme and an adequate replacement rate[11], is across Europe around €2,010 billion.[12] Given the expectancy that the global old-age dependency ratio will only increase, an increase in funded pension savings is essential as these are less vulnerable for this risk. The PEPP could and should help the total pension savings in Europe, calculated by Ernst & Young with €700 billion by 2030.[13] With the PEPP, the EC takes its shared responsibility in strengthening the national pension systems, following on from the IORP Directive[14] and the recommendations in the Green- and White Paper[15].
Second incentive for the EC for its proposal lies in the previous mentioned diversity of pension systems. The capital markets, such as the pension market, are highly fragmentated, which hampers the internal market and does not fully exploit the freedom of capital and free movement of workers. By introducing a European pension product, the integration and European freedoms should be improved.

The PEPP is proposed on the basis of Article 114 TFEU, which allows the EC to adopt regulations and directives to strengthen the internal market, in the case of the PEPP the internal market for pensions. The legislative method chosen is a regulation. A regulation is directly applicable and binding in all Member States, according to Article 288 TFEU. According to the EC, a regulation is a more appropriate legislative instrument than a directive, because its direct effect can achieve faster market penetration and thus contribute directly to the current problems. In addition, interaction with national legislation is undesirable, because the EC has a European approach to pension saving and also wants to strengthen the European market. The PEPP must therefore be a truly European product, so that no national differences can arise. The PEPP

[9] As retrieved from OECD, *Pensions Outlook 2018*, OECD Publishing: Paris, 2018, p. 19.
[10] European Commission, *Commission launches a new pan-European personal pensions label to help consumers save for retirement*, press release, June 2017.
[11] What is considered adequate is often based on the OECD average and is a pension income between the 60 and 75 percent of the former income.
[12] Aviva, *Mind the Gap, Quantifying the pension savings in Europe,* September 2016, p. 6.
[13] Ernst & Young, 2017, p. 258-259.
[14] Directive (EU) 2016/2341 of the European Parliament and of the Council of 14 December 2016 on the activities and supervision of institutions for occupational retirement provision (IORPs)
[15] COM(2010) 365 & COM(2012) 55

should also complement national pension systems and not replace them. A regulation, 'above' or 'in addition' to national law, is therefore an appropriate instrument.

Despite its noble and clear purpose, the PEPP has not been warmly welcomed by all Member States and questionable by some stakeholders. As national policy area, national governments are very distrustful of European intervention in pensions systems. Therefore, the final version of the Regulation, as adopted by the European Parliament (hereafter: EP) and the Council, has some major differences compared to the initial proposal of the EC.[16] The Committee on Economic and Monetary Affairs (hereafter: ECON) with rapporteur Sophie in ‘t Veld has been responsible for all the amendments. Some striking or interesting amendments will be highlighted in the next paragraph, dealing with the Regulation.

b. The Regulation

Due to the direct effect of the Regulation, it is also referred to as a second or 29th regime.[17] The regime for the PEPP is therefore a separate regime on top of the national systems of the 28 European Member States. Under this regime, the characteristics of pension products under the umbrella of the PEPP will be standardised.[18] All matters not regulated by the Regulation shall comply with the relevant and applicable sectorial Union law and national laws.[19]

Definitions and provision

Firstly, the different definitions are standardised in Chapter I of the Regulation. For example, the Article 2(2) of the Regulation stipulates that a PEPP is 'a long-term savings personal pension product, which is provided by a financial undertaking eligible according to Article 6(1) under a PEPP contract, and subscribed to by a PEPP saver, or by an independent PEPP savers association on behalf of its members, in view of retirement, and which has no or strictly limited possibility for early redemption and is registered in accordance with this Regulation’. The definition of a 'personal pension product' is diverse across Europe[20] which is why Article 2(1) of the Regulation also standardises this definition at EU level for the PEPP. It should be a product that is voluntarily agreed between the saver and an entity, that provides a complementary income after retirement through capital accumulation and should therefore have

[16] Or stripped as Karel Lannoo in K. Lannoo, *PEPP: How to kill an EU proposal*, IPE June 2019.
[17] EIOPA, 2016, p.73.
[18] Article 1 of the Regulation.
[19] Article 3 of the Regulation.
[20] EIOPA, 2016, p. 10.

an explicit retirement objective and only limited benefit possibilities for retirement. Especially after the amendments made by the Council[21] an additional section is included that states that the PEPP is not a statutory nor a supplementary pension product.[22] This is an important addition, because under the initial proposal a discussion is possible whether a PEPP could be offered by an employer as supplementary pension product to his employees.[23] The supplementary pension, as result of collective bargaining between national social partners, is seen as an important national competency and thus not an area for European intervention.

A PEPP saver is defined as any individual and therefore includes not only employees, but also the self-employed, the unemployed, the disabled and students.[24] Next to standardising the registration, manufacturing, distribution and supervision of the PEPP, the Regulation stipulates in Article 4 what minimally should be in the provisions relating to the PEPP contract, such as explicitly specifying the characteristics of the default investment option, a description of the alternative investment options, the coverage of biometric risks (or not), the forms of benefits and the conditions and costs for the portability service and change of investment option.

Chapter II elaborates on authorisation and authorised PEPP providers, i.e. regulated financial undertakings. Regulated financial institutions include banks, insurers, institutions for occupational pensions qualifying under the IORP Directive (the so-called IORPs) and investment firms.[25] In particular, the provision that IORPs are authorised PEPP providers has led to many amendments. IORPs have a special position in pension systems such as those in the Netherlands, since the Dutch pension funds qualify as IORPs. Certain collectively agreed pension schemes may be made mandatory at sectoral level by the legislator upon request. This infringes the freedom of the employer and employee to enter into a pension agreement and the freedom of the employer to choose a pension provider, as these are predetermined. This is in principle contrary to European competition law, as the government grants a pension fund a monopoly position with regard to a mandatory pension scheme. However, this infringement is justified in view of the social importance of pension schemes in the Netherlands, as ruled by the European Court of Justice (CJEU) on Article 106(2) TFEU in the *Brentjens* case.[26] This

[21] Council of the EU, *Regulation on Pan-European Pension Product – Mandate for negotiations with the European Parliament*, 2017/0143 (COD), nr. 9975/18.
[22] Article 2(2)(c) of the Regulation, but also added in section a.
[23] E.g. J. Van Zanden, 'Het PEPP: is er nog een pijler op te trekken?', *PensioenMagazine* 2017/34.
[24] Article 2(3) of the Regulation.
[25] Article 5(1) of the Regulation.
[26] CJEU 21 September 1999, C-115/97 and C-117/97.

implies that the pension fund must be assigned a specific task: the implementation of that mandatory scheme. "Pension funds are only authorised to execute pension agreements arising from an employment relationship, the so-called second pillar pension schemes", according to the Explanatory Memorandum to the Pensions Act.[27] Section 5.3 of the Dutch Pensions Act (PA) supervises this demarcation of duties for pension funds. For example, it prohibits ancillary activities[28], such as personal pension products, and the pension assets must be separated financially per group[29]. Allowing IORPs with such a demarcation of tasks to offer a PEPP can stress the legitimacy of the (quasi-)obligation.[30] The amendments therefore call for the removal or restriction of or a Member State option in allowing IORPs as PEPP providers.[31] Ultimately, the final text of the Regulation allows IORPs to be a PEPP provider, which pursuant to national law are authorised and supervised to provide also personal pension products and all assets and liabilities for PEPPs are separated from other retirement provisions and no transfers are possible. In practice, IORPs that fall under the demarcation of tasks such as the Dutch pension funds will not be able to offer a PEPP.[32] Nevertheless, it is debatable whether it excludes all pension institutions operating in the second pillar[33] from the PEPP.[34] The Dutch Pension Premium Institution (PPI) does not fall under the scope of the legal demarcation of tasks, can ringfence pension capital and thus might offer a PEPP. Literature is not very clear.

In contrast with the EC proposal, the final Regulation states that authorised institutions should apply for registration of a PEPP to the national competent authorities.[35] Again, a strong lobby of the Member States, among others certainly the Netherlands, became visible here. In the initial proposal EIOPA had the full authorisation role, for the purpose of safeguarding the European character. The role of EIOPA in the final Regulation is limited to only keeping track of the central public register of PEPPs, after being notified by the competent authorities. If added to

[27] *Kamerstukken II* 2005/06*,* 30413*,* nr. 3, p. 66.
[28] Activities other than pensions, see Article 116 PA.
[29] Article 123 PA.
[30] As stressed in L. Blom, "PEPP vult nationale pensioenstelsels aan, maar verstoort deze ook", *Tijdschrift voor Pensioenvraagstukken* 2018/2.
[31] See Committee on Economic and Monetary Affairs, *DRAFT REPORT on the proposal for a regulation of the European Parliament and of the Council on a Pan-European Personal Pension Product (PEPP),* 2017/0143(COD) and *AMENDMENTS 176-486 on the proposal for a regulation of the European Parliament and of the Council on a Pan-European Personal Pension Product (PEPP),* 2017/0143(COD), PE621.054; Council, 2018.
[32] In the Netherlands also already on the basis that it is for pension funds not possible to ringfence pension capital, see Article 123 PA.
[33] This is the pension pillar of the supplementary pension products.
[34] Compare the views on the Premium Pension Institution of H. Van Meerten & A. Wouters, Can a Dutch IORP offer a PEPP?, *Cross Border Benefits Alliance, Europe Review*, July 2018, p. 8-32; and L. Blom, 2018.
[35] Article 6 of the Regulation.

the central public register, the authorisation applies throughout the EU. This shows that the PEPP is in fact nothing more than a kind of 'quality label' for pension products. Once a pension product, whether newly developed or already existing, meets the requirements of the Regulation and is registered in EIOPA's register, it constitutes a PEPP.[36]

Cross-border provision and portability

Chapter III ensures the cross-border offer and portability of PEPPs. Since the PEPP is introduced for fostering cross-border movement of both people, services and capital, this is one of the core chapters of the Regulation. PEPP providers are subject to the freedom of establishment to provide services within Europe, i.e. PEPP providers may establish themselves anywhere in the EU and offer their PEPPs to all European residents.[37] With Article 15 the final text has somewhat limited this power limited compared to the initiative proposal, in order to ensure that only those IORPs which have national competence to administer personal pension products can operate across borders. Before an IORP can offer a PEPP to a PEPP saver in another Member State, the Member State of the PEPP saver must inform the Member State of the IORP of the admission. A period of 10 working days is set for this purpose. Article 16 empowers the Member State in which the PEPP is offered and executed (the PEPP saver's Member State) to take additional measures if the PEPP provider does not act in line with the applicable laws and regulations. These amendments also clearly comes from the wishes of the Member States, as they are introduced in the text of the Council's mandate.[38]

PEPP savers should also be able to enjoy complete freedom through the portability service provided for in Article 17 of the Regulation. A PEPP saver can move to another Member State without this affecting his PEPP. PEPP savers can continue to contribute to their PEPP account with the same PEPP provider. All the benefits and incentives (tax facilitation) granted and enjoyed by the PEPP saver are retained. In order to achieve this, PEPP providers should create national sub-accounts for each Member State where they and their customers are active. Within these national sub-accounts, the PEPP is structured according to the national provisions, including tax provisions, of the Member State in which the PEPP saver contributes, has contributed or will contribute.[39] The proposal of the EC therefore obliges PEPP providers to

[36] Article 9 of the Regulation.
[37] Article 14 of the Regulation.
[38] Article 11a and 11b of Council of the EU, 2018.
[39] Article 19(1) of the Regulation

create such a sub-account for all Member States in which their customers have lived, are living or will live within three years of the entry into force of the Regulation. This requirement is, in view of feasibility, watered down to the minimum requirement of at least two Member States.[40] In the absence of a sub-account in the Member State where a PEPP saver moves to, the PEPP provider is obliged to inform the PEPP saver about the right to switch to another PEPP provider and facilitate this at no cost and no delay. The PEPP saver can also choose to continue contributing to the last sub-account opened, regardless of where the PEPP saver is living.[41] However, the PEPP provider is obliged by Article 20(4) to offer personal recommendations in the case new sub-accounts might be more beneficial.

The national sub-accounts is also an important element for a policy area that 'Brussels' has limited power on: taxation. By stating that a sub-account must comply with the relevant national rules, included tax law, the Regulation makes sure that the PEPP will qualify for national tax facilities regarding to the accrual, capital gains and decumulation. Table 2 shows how the sub-accounts within a PEPP will look like in the situation of a PEPP saver with sub-accounts in the Netherlands, Belgium and Germany within the same PEPP at the same PEPP provider.

Table 2: Functioning of sub-accounts

General rules of the PEPP Regulation		
Dutch sub-account	***Belgian sub-account***	***German sub-account***
Accrual and decumulation according to, amongst others, Dutch tax law	Accrual and decumulation according to, amongst others, Belgian tax law	Accrual and decumulation according to, amongst others, German tax law

Noteworthy was the right of the PEPP saver under the EC proposal to transfer accrued pension rights/pension assets from one sub-account to another under the former Article 16. This part of the portability right has been deleted in the final text, as it already was no part in the proposal of the Council.

In addition, the switching service[42] is not only limited to the situation of relocation with no sub-account available, but can also be done at the request of the PEPP saver after at least five years from the conclusion of the PEPP contract. The rules for this are set out in Chapter VII of the Regulation. The value transfer of pension assets can take place both domestically and across

[40] Article 18(3) of the Regulation.
[41] Article 20(3) and 20(5)(b) of the Regulation.
[42] The right of the PEPP saver to switch from PEPP provider, Article 53(1) of the Regulation.

borders, but must remain within a PEPP with the same sub-accounts opened. Value transfer to products other than the PEPP is therefore not possible. Furthermore, the costs that can be charged for the switching service are capped by Article 54 of the Regulation. The switching service is not obligatory for PEPP providers in the case of already receiving lifetime annuities during the decumulation phase[43] and in the case of subsequent switching, the PEPP provider is allowed to offer the switching service. Many amendments have been tabled to change the frequency of the switching service, as the EC started with a right to witch after ever five years after the last switch. The expected costs and administrative hassle have overturned this provision.

Information and governance requirements

Chapters IV and V of the Regulation regulate governance requirements and the provision of information from PEPP providers to potential, current and former PEPP savers. The information requirements and documents are precise and detailed in the Regulation to ensure that it is a transparent product and appropriate to personal circumstances. In advance there should be a Key Information Document[44] handed to the potential PEPP saver and during the accrual and decumulation phase an annual PEPP Benefit Statement[45]. The investment rules are according to the 'prudent person' rule and thus should be in line with the best interests of the PEPP saver. The PEPP offers PEPP savers a certain freedom in investment options, capped at six according to Article 42(1). One of these is a mandatory default investment option, the so-called Basic PEPP. The Basic PEPP should be a safe product with a basis of a guarantee on the capital. Further and more extensive treatment of these provisions on information and investments goes beyond the scope of this paper and will therefore not be further elaborated.

Benefit possibilities are set out in Chapter VIII of the Regulation. However is directly stated in Article 57(1) that the national conditions regarding to the decumulation phase apply on a national sub-account. These conditions include the minimum pension age and the forms of payments. The Regulation obliges the PEPP provider to offer at least one of the benefit forms: annuities, lump sums, withdrawals (lump sum) or combinations of the three. The choice can be made by the PEPP saver for each sub-account one year before and at the start of the decumulation phase and when making use of the switching service. The PEPP provider has the

[43] Article 52(2) of the Regulation. This is probably because of the high (actuarial) costs for the PEPP provider.
[44] Section II of Chapter IV of the Regulation.
[45] Section IV of Chapter IV of the Regulation.

important task her to inform the PEPP saver about the financial implications of changes in payment form.[46] As later will be shown, the tax consequences can be huge.

Finally, Chapter IX divides the supervisory tasks between EIOPA and the national authorities, in which we again see a smaller role for EIOPA compared to the proposal of the EC. Chapter X describes the breaches, the possible sanctions and the procedure to be followed and Chapter XI contains the final provisions, such as the processing of personal data and the power of the EC to adopt delegated acts.

3. Tax treatment of personal pensions in the EU

a. The Recommendation and the EU powers regarding taxation

The Regulation regulates the PEPP. However, Member States' national laws and regulations continue to play an important role for the PEPP. For example, it is clear from the previous paragraph that the Regulation does not prescribe everything as mandatory, but also retains freedom of choice for the Member States and the PEPP providers. These include, for example, the conditions governing pension accrual (additional conditions such as age limits may still be set at national level), the forms of payment and minimum or maximum contributions. In addition, the Regulation does not at all refer to taxation with regard to the PEPP. Direct taxation falls within the national policy domain of the Member States and, according to Article 114(2) TFEU, cannot be harmonised by a regulation of the EP and the Council. Only if there is unanimity among all European Member States can taxation be harmonised at European level.[47] Nonetheless, the EC has taken several actions in order to remove tax obstacle to cross-border pension provision[48], fostering the EU internal market, and more recently its Communication of 15 January 2019[49] on gradually moving from unanimity voting to the ordinary legislative procedure[50]. However, given the unlikeliness of harmonisation of the tax treatment of personal pensions and the importance of tax facilitation for pension savings, the Regulation has

[46] Article 59(2) of the Regulation.
[47] Article 115 TFEU.
[48] Such as its Communication in European Commission, *Communication from the Commission to the Council, the European Parliament and the Economic and Social Committee - The elimination of tax obstacles to the cross-border provision of occupational pensions*, COM/2001/0214 final; and the infringements procedures that can be found on: EC, *Pension taxation,* https://ec.europa.eu/taxation_customs/individuals/personal-taxation/pension-taxation_en.
[49] European Commission, *Communication towards a more efficient and democratic decision making in EU tax policy,* COM(2019) 8 final.
[50] Which is explained on: https://ec.europa.eu/taxation_customs/taxation/decision-making-eu-tax-policy_en.

introduced national sub-accounts within a PEPP and the EC has provided the proposal with an additional Tax Recommendation[51], that has been adopted by the EP on 4 April 2019.

In the Tax Recommendation the Member States are remined on the fact that *"The national treatment principle, stemming from Articles 21, 45, 49, 56 and 63 of the Treaty on the Functioning of the European Union and interpreted by the Court of Justice of the European Union, applies to PEPP savers. Therefore, it should be possible for a PEPP that is objectively comparable to a PPP marketed in a given Member State to benefit from the same tax relief granted to the PPP in that Member State. This also applies if the PEPP is provided by a provider from another Member State."*[52] Here the EC is addressing the important case-law of the ECJ that dictates that a Member State cannot treat an insurance product, that meets the national requirements of the Member State, from other Member States, differently than national insurance products. The Tax Recommendation also goes further by requesting the Member States to undertake active tax policy actions. There are three approaches suggested: (1) analysing existing tax incentives for personal pension products and assessing their effects; (2) granting the same tax relief to PEPP as to national products, even in the case PEPP does not meet all criteria; (3) granting a specific tax relief to PEPP, harmonised at Union level, to be laid down in a multilateral tax agreement between Member States.[53] In a draft report of Sophie in 't Veld, also the option for a subsidy or premium to PEPP savers in the form of a fixed amount or percentage has been suggested.[54]
As a result, the EC and the EP try to make Member States aware of the importance of pension saving and cooperation, but cannot impose enforceable requirements, other than where there is an obvious case of discrimination. This can be troublesome in a very fragmented landscape of personal pension products and tax facilities in Europe.

b. Case-study: the Netherlands

To get a better understanding of the functioning of the PEPP in national pension systems, this paragraph will look into the Dutch system, how the PEPP fits in it and what obstacles possibly arise.

---

[51] European Commission, *Commission Recommendation on the tax treatment of personal pension products, including the pan-European Personal Pension Product,* C(2017) 4393 final.
[52] Consideration 8 of the Tax Recommendation.
[53] Article 2 of the Tax Recommendation.
[54] Committee on Economic and Monetary Affairs, *DRAFT REPORT on with recommendations to the Commission on tax treatment of personal pension products, including the pan-European Personal Pension Product*, 2018/2002(INL).

With the final text of the Regulation, a PEPP must be placed within the third pillar of the Dutch pension system.[55] Since the Regulation does not foresee in all requirements and leaves a lot of room for national law. The market for third pillar pension product in the Netherlands is dominated by insurers and banks, but, as stated before, not an area for pension funds given their demarcation of tasks. The third pillar falls out of the scope of the PA, the law that regulates the pension domain between employee, employer and pension provider.[56] However, given the major role played by insurers and other financial institutions, the Act on Financial Supervision (Wft) is of great importance. No specific product regulation applies here.[57] Supervision is exercised by the Dutch Central Bank and the Authority for Financial Markets. The personal pension products in the Netherlands are mainly annuities, whether it is an annuity insurance, an annuity savings account or annuity investment rights. The PEPP and its characteristics as laid down in the Regulation do fit within this Dutch legislative framework. The rules regarding to tax facilitation are more strict however.

Taxation

The tax facilitation of personal pension products and its conditions are laid down in Section 3.7 of the Dutch Income Tax Act 2001 (IB). The tax treatment is based on the EET-principle: the premium is tax deductible, the capital gains are untaxed at the level of the provider and the pension benefit is taxed[58].

First of all, for tax facilitation there must be pension gap, which is mentioned in Article 3.124(1)(a) and 3.126a(1) IB. The Dutch government aims at facilitating a pension income of 75 percent of the average income during the accrual phase. The tax system is designed to facilitate upon this replacement rate and is also referred to as 'compensating vessels': the tax facilitation in the third pillar 'breathes' with the benefits in the first and second pillars.[59] For tax facilitation in the third pillar there has to be a pension gap. This results in detailed, but also complex, regulations regarding the calculation of the permitted annual contribution deduction. What one should know is that the maximum annual premium base[60] is €110.111 (2020), 13,3 percent of the premium base will be tax facilitated and the deduction is further limited by the

[55] As I elaborated thoroughly in the Master Thesis ‘Een fiscaal gefaciliteerd Pan-Europees Persoonlijk Pensioenproduct: ook voor Nederland?’, but also in H. Van Meerten & A. Wouters, De PEPP-verordening. Pensioenfondsen: Quo vadis?, *NtER* 2019, nr. 3-4.
[56] As can be found in the definitions of Article 1 PA.
[57] *Kamerstukken II* 2017-18, 22 112, nr. 2434, p. 16.
[58] In principle regardless the deductibility of the premium paid, Article 3.100(1)(b) IB.
[59] G. Dietvorst, Proposal for a pension model with a compensating layer, *EC Tax Review,* 144, 2007.
[60] The premium base is the income for box 1.

AOW franchise (the fictive annual accrual of AOW) of €12.472 and the pension accrual in other pension provisions.[61] Thus the maximum annual deduction is €12.986.[62] Above the cap on the premium base, there is a possibility for a so-called net-annuity that is facilitated by the TEE-principle. Both the net-annuity and the complex rules regarding to the annual contribution deduction will not be further elaborated as it falls out of the scope of this case-study

Secondly, in addition to the complex calculation of the allowed premium deduction, the IB has additional tax requirements with regard to the annuity. For example, Article 1.7(1)(a) IB requires in the definition of an annuity that the payments must be fixed and periodic, end at the latest upon death, cannot be redeemed or surrendered and can formally or actually lead to security. This shows that an annuity can be lifelong (old-age annuity) as well as periodic, but cannot take place in a lump sum payment. An old-age annuity must take effect no later than five years after retirement age.[63] With regard to a temporary annuity, the conditions are that the minimum payment period is five years, the annual payment is limited to a maximum of €22.089 (2020) and the payments do not start earlier than the pensionable age but also not later than five years after the pensionable age.[64]

Thirdly, Articles 3.126 and 3.126a(2) IB determine who the pension providers admitted for tax purposes are. In short, these are in the Netherlands-based and registered life insurers, pension funds, foreign pension funds in the event of continuation of an existing scheme and a foreign provider designated by the Minister for insurance annuities and banks, investment institutions/companies and foreign institutions designated by the Minister for bank savings and annuity investment rights. Noteworthy is the fact that to be designated by the Minister, foreign pension providers should commit themselves to providing information to the Netherlands and have to provide security for taxation or accept liability.

Finally, Article 3.133 IB contains a list of 'prohibited transactions' (e.g. redemption) which result in direct taxation. This is subject to 20 percent revision interest.[65] In the highest tax

[61] Article 3.127(3) IB.
[62] 13,3% over €110.111 minus the AOW franchise of €12.472. For full explanation see A. Bollen-Vandenboorn, *Pensioen en de belangrijkste toekomstvoorzieningen*. Den Haag, Netherlands: SDU 2020, p. 494 and further.
[63] Article 3.125(1)(a) IB.
[64] Article 3.125(1)(b) IB.
[65] Article 30i(1)(b) in conjunction with Article 30i(2) of the General Income Tax Act.

brackets this can total to 71,75 percent.[66] Value transfer of pension capital is in principle also seen as redemption and thus heavily taxed. However, an exception is made, among other things, in the event that the annuity is continued under another, similar, right.[67] For this, however, the previously listed tax requirements must again be met.

In the event of emigration, the Netherlands would like to retain its right to levy tax on pension entitlements. In principle a protective tax assessment on the economic value of the accrued pension entitlements (the premiums for which tax deductions have been granted and the return on these premiums) is imposed, but in the situation where there is a tax treaty between the Member States only the premiums for which tax deductions have been granted are taken into account.[68] The protective tax assessment is postponed for ten years, which is subsequently waived without the postponement being revoked. However, in the event of improper transactions (e.g. redemption and lump sum), benefits unduly received are taken back as negative expenses for income provisions.

PEPP in the Netherlands

Since the PEPP will not be treated differently than national personal pension products[69], the PEPP must comply with these rules above for fiscal facilitation. However, since the national sub-accounts within a PEPP should be designed according to, amongst others, the tax law, the PEPP would be fiscally facilitated in the Netherlands. Therefore, the maximum annual contribution deduction would be €12.986, the gains would be exempt and the benefits would be taxed where the Netherlands have the taxing rights.[70] Furthermore, the retirement age must be set according to the rules in the PEPP contract, in the case of a PEPP with periodic payments these should be for at least five years and especially the fact that no lumpsum within a PEPP is allowed are important.

However, there are some major concerns, especially in the perspective of cross-border provision and mobility. First of all, fiscal facilitation is dependent of the eligibility of the provider, in this case the PEPP provider. As shown, foreign PEPP providers should be

[66] E. Schouten, 'Fiscale behandeling van het PEPP: wordt het EET of TEE?, *Weekblad voor Fiscaal Recht* 2017/231, 2017a, par. 3.6.
[67] Article 3.134(1) IB.
[68] Article 3.136(1) IB and Article 3.136(2) IB.
[69] *Kamerstukken II* 2017-18, 22 112, nr. 2434, p. 17.
[70] In cross-border perspective, the bilateral tax treaties will determine who is entitled to tax.

designated by the Minister and meet certain criteria. Especially because of the additional information and liability obligations, foreign providers often do not request to be designated. Currently there are only three foreign providers for personal pension products designated.[71] This prevents foreign PEPP providers from offering their PEPP in the Netherlands and, the other way around, prevents Dutch PEPP savers to sign a PEPP with a foreign PEPP provider.

Secondly, in the case cross-border pension capital transfer, such as happens with PEPP in the case of a cross-border switching service, the criteria of Section 3.7 IB have to be met again in order to have no taxation and revision interest. The problem here is that the receiving foreign provider should be designated and the national legal framework of the receiving Member State must not have conflicting regulations. Already on the basis, again, of the permissible provider, the cross-border pension capital transfer will very likely result in direct taxation and a levy of revision interest. In practice, therefore, a tax-free, cross-border value transfer will not occur very often.[72]

Lastly, emigration of a PEPP saver to another Member State could lead to a protective tax assessment including a levy of revision interest on the tax advantages enjoyed within a Dutch sub-account. As long as in the Dutch sub-account for which tax advantages are granted no improper, forbidden transactions happen, the postponement of ten years will ultimately be revoked. However, this arrangement is administratively aggravating and burdening, again, the (feeling of) freedom of a PEPP saver.

c. Arising tax problems due to diversity

In previous section is shown how a PEPP would fit and function in one Member State, the Netherlands, however earlier is shown that the European pensions market is very diverse, as pensions are a national policy area. Exclusive national tax competence also means that PEPP has to deal with different tax regimes. The differences in taxation stem from:[73]

- System diversity: a tax system provides for the tax treatment of the pension contribution paid, the return on pension capital and the final pension benefit. For example, a pension

[71] *Overzicht aangewezen buitenlandse pensioenfondsen en lijfrente aanbieders,* retrievable on: https://www.belastingdienst.nl/wps/wcm/connect/bldcontentnl/themaoverstijgend/brochures_en_publicaties/overzicht_aangewezen_buitenlandse_pensioenfondsen_en_lijfrente_aanbieders.
[72] A. Bollen-Vandenboorn, 2020, p. 485.
[73] H. Van Meerten & N. Hooghiemstra, *PEPP – Towards a Harmonized European Legislative Framework for Personal Pensions*, June 2017, http://dx.doi.org/10.2139/ssrn.2993991.

premium may be deductible from taxable income for wage tax and/or income tax purposes (or not), the returns on the pension assets deposited with the pension provider may be exempt (or not) and the pension benefits may be taxed (or not). The combination of these three tax options results in the tax system: EET, ETT, TEE or even EEE and TTT;

- Differences in legal requirements for tax facilitation: tax facilities are often granted under conditions set out in the tax law. For example, conditions can be set with regard to certain characteristics of the pension product (such as the pension age included, the method of payment and the premium level) and the pension provider. However, tax legislation differs from one Member State to another and therefore also these legal requirements.

With regard to the first difference, system diversity, the EC states that the EET system is most commonly used within Europe.[74] However, this observation is mainly based on the tax facilitation of supplementary pensions in the second pillar. The tax framework of personal pension products sometimes differs from the 'general' one. Table 3 shows the various tax systems for *voluntary* personal pension products.

Table 3: Main tax systems for voluntary personal pension products[75]

TAX SYSTEM	EU MEMBER STATES
EET	Finland, Ireland, Luxembourg, the Netherlands, Poland, Slovenia, Spain, United Kingdom, Romania
TEE	Estonia, Czech Republic, Greece, Hungary, Lithuania
ETE	Cyprus, Latvia
ETT	Denmark, Italy, Sweden
TET	Austria, Belgium, Croatia, France, Germany, Malta, Norway, Portugal
EEE	Bulgaria, Slovakia

In addition, the legal differences with regard to tax facilitation are even more significant. After studying the cross-border pension problems, Starink and Van Meerten[76] came to the conclusion that a pension product, which qualifies under more than one of the national fiscal facilitation

[74] European Commission, *Communication from the Commission to the Council, the European Parliament and the Economic and Social Committee - The elimination of tax obstacles to the cross-border provision of occupational pensions*, COM/2001/0214 final, p. 6.
[75] Derived from OECD, *Financial incentives for funded private pension plans,* OECD Publishing: Paris, 2019, p. 5-6. Please see this publication for full overview of tax treatment per private pension plan (e.g. occupational, mandatory).
[76] H. Van Meerten & B. Starink, “De belemmeringen voor een interne markt voor bedrijfspensioenvoorziening”, *SEW: Tijdschrift voor Europees en Economisch Recht*, 187(10), 2010, p. 388-398.

requirements of a Member State, does not exist. By way of illustration, Dutch tax law only facilitates pension products with lifelong and periodic annuities and thus explicitly prohibits the possibility of a lump sum payment. On the other hand, Belgian tax law does not provide for such an obligation of lifelong annuities or a prohibition of lump sum payments. A lump sum payment is even tax facilitated more advantageously than a lifelong annuity due to the lower tax rate at the time of payment.

On top of this, there are often several personal pension products per Member State. There are also differences in legal requirements for personal pension products on a national level. More specifically, there are 49 different personal pension products (and legal requirements) in Europe.[77] The legal requirements for tax facilitation of pension products are therefore very diverse. This diversity of tax regimes constitutes a major barrier to the PEPP. Due to the lack of a harmonised tax definition of a personal pension product, it is not possible for the EC and EP to design the PEPP in such a way that it falls within the scope of all national tax rules and therefore all tax facilities.

The freedoms of the TFEU ensure that cross-border pension contributions and benefits should be treated equally to national cases, as confirmed by the CJEU in *Safir*[78] and *Bachmann*[79]. This means that a pension contribution and/or benefit from or to another Member State should not be treated more unfavourably if national requirements for tax facilitation are met. It is precisely here that the differences in legislation and regulations with the freedom of capital and labour are suspended. The requirements for tax facilitation in national legislation and regulations are strongly focused on national pension products. As a result, foreign pension products (and pension providers) often do not qualify for tax facilities under the legislation and regulations. This is not seen as discrimination against cross-border situations, as domestic situations must meet the same conditions. Nevertheless, this effectively hinders cross-border pension movements and administration.

A second de facto obstacle to the freedoms of the TFEU, and cross-border pension movements, are the tax requirements for cross-border value transfer and emigration which are often very strict in order to maintain the taxing rights by Member States. From the Dutch case it becomes

[77] Ernst & Young, 2017, p. 9.
[78] ECLI:EU:C:1998:170
[79] ECLI:EU:C:1992:35

clear that the requirements ensure that, with some exceptions[80], no cross-border value transfer can actually take place without any noise from a tax point of view[81] and therefore tax and revision interest will be levied at the time of value transfer. As set out in its White Paper, the EC is combating such tax obstacles. However, this is a long and difficult path and will not be foreseen in the near future, as the Dutch case again shows.[82] Together it can therefore be concluded that the European pension market is not (yet) free of obstacles, which also affects the PEPP.

4. Solutions on the tax treatment of PEPP

a. Status quo is not enough

The solutions in the status quo consists of the Tax Recommendation and the creation of national sub-accounts within the PEPP, as described in the previous paragraph. However, the solutions still leave fiscal problems.

First of all, the Recommendation urges the European member states to apply their most advantageous tax facilitation to the PEPP and to exchange best practices. This addresses both the diversity of tax systems and the differences in legal requirements. In a previous Communication[83], the EC explicitly preferred an EET system at European level. With the recommendation, the EC therefore hopes to encourage the member states to adopt such a European system. This EET system will then apply to the PEPP regardless of national tax requirements, if the Recommendation as a whole is followed by the Member States. However, as indicated above, the Recommendation is not binding on the Member States and therefore this solution is entirely dependent on the willingness of the Member States. In all probability, this willingness does not exist in all Member States, for example the Netherlands that attaches great value to fiscal sovereignty.[84] This will make it unlikely that the system diversity and differences in tax requirements for the PEPP will be resolved at European level.

A second EC solution for taxation is the national sub-accounts within the PEPP. This particularly addresses the second problem of the different tax facilitation requirements, as each

---

[80] There are some exceptions made in the Decree of 9 October 2015, nr. DGB2015/7010M, *NTFR* 2016/862. See A. Bollen-Vandenboorn, 2020, p. 454-457 for the full elaboration on these conditions.
[81] A. Bollen-Vandenboorn, 2020, p. 485.
[82] See the infringements procedures of the EC against the Netherlands of July 2018 and November 2019.
[83] EC, 2001, p. 20.
[84] A motion has been adopted, which addresses and confirms the importance of fiscal sovereignty: *Kamerstukken II* 2019-20, 21 501-07, nr. 1654.

sub-account should be designed according to the national tax law. The sub-accounts thus qualify the PEPP under all the different tax rules, regardless of where the PEPP provider and the PEPP saver are located within the EU. In this way, tax facilities are granted in most European member states and the PEPP saver can 'carry' his/her PEPP anywhere, as the sub-accounts do not have to take out another national pension product after moving.

Nevertheless, differences in tax requirements may still mean that the PEPP is not facilitated (equally) everywhere and portability is disappointing in practice. Think, for example, of the providers allowed for tax purposes within Dutch legislation and regulations. Because of the additional information and liability obligations, foreign providers often do not request to be designated. A PEPP saver who moves to the Netherlands and, as a PEPP provider, has a non-appointed provider, will not be able to benefit from tax facilities and will still have to rely on the national pension products for tax facilitation. The compartmentalisation does not remedy such situations. The compartmentalisation does also not solve the fact that non-appointed foreign PEPP providers cannot offer a tax-facilitated PEPP in for example the Netherlands. Both facts do, however, reduce the attractiveness of the PEPP for savers and hinders the aim for enhancing the internal market by improvement of cross-border mobility and provision.

In addition, the Regulation also states that PEPP savers may transfer the accrued pension assets from a PEPP provider to another with the switching service. However, this may lead to taxation and/or, in the case of the Netherlands for example, revision interest. These provisions of value transfer between PEPP providers by a switching service are therefore a nice aim of the European legislator for full portability within the EU, but in practice will more often run into tax problems and therefore not expected to be used much.

Another possible problem that the European legislator leaves open is the 'Pensionista problem', which involves tax arbitrage by (wealthy) pensioners.[85] The different tax systems can be misused to create an artificial EEE system. During the build-up phase, wealthy residents in a Member State with an EET system can save in a PEPP and thus defer taxation. Towards retirement age, the 'pensionistas', and their pension capital for example by the switching service, move to another Member State, which has a TEE or TTE system. In accordance with Art. 18 OECD Model Tax Convention, most tax treaties grant the right of taxation to the State of

[85] H. Van Meerten & N. Hooghiemstra, 2017, p. 84 and onwards.

residence, i.e. the Member State to which the 'pensionista' has moved.[86] As a result, pension benefits also remain untaxed. Some Member States with, or even without, a TEE/TTE system promote such an arbitrage possibility through additional advantageous tax concessions. For example, despite having a TET system (see Table 3), Portugal offers an additional tax credit to non-ordinary Portuguese residents: *resident não habitual* (hereafter: NHR).[87] The NHR scheme is specifically designed to attract pensioners and talented or rich individuals to Portugal. With regard to pension benefits, the NHR scheme for a long time provided a full tax exemption for foreign pensions for a period of ten years. After the 2020 State Budget Law, this tax exemption has been replaced by a special tax rate of 10%. For this NHR scheme, the pensioner must become a Portuguese resident and not have been subject to tax in Portugal for the previous five years.

Tax treaties can combat and prevent such arbitrage by including a withholding tax clause, as was done in the Netherlands-Portugal and Netherlands-Belgium tax treaties. Contrary to the general allocation of taxing rights to the state of residence[88], this clause also grants the right of taxation to the source state (in this case, the Netherlands), if less than 90% of the pension benefits are taxed by the state of residence and the accrual is fiscally facilitated by the source state. However, such a provision often does not occur in existing tax treaties, in addition to the fact that a tax treaty does not exist in all situations. Negotiations to include such a provision are expected to be difficult, as both negotiating parties wish to have the right to tax.[89] Therefore, it is unlikely that the Pensionista problem will be solved in the foreseeable future through this route.

For the sake of completeness, I would like to mention the Pensionista problem, which could also prevent the opposite: double taxation.[90] Because this is due to system differences, a tax treaty does not provide for this and thus an artificial TTT system can arise.

---

[86] B. Starink, *Belastingheffing over particulierpensioen en overheidspensioen in grensoverschrijdende situaties,* Tilburg University 2015 (doctoral thesis).
[87] Novo Banco SA, *I wish to benefit from a favourable tax regime in Portugal*, 2018, retrieved from https://www.novobanco.pt/site/cms.aspx?labelid=taxbenefitseng; E. Verdegaal, Kan ik belastingvrij met pensioen in Portugal?, *NRC.nl*, 2015, retrieved from https://www.nrc.nl/nieuws/2015/01/10/kan-ik-belastingvrij-met-pensioen-in-portugal-1454761-a594004.
[88] Based on Article 18 or 21 of the OECD Model Tax Convention.
[89] European Federation for Retirement Provision, *The EFRP model for pan-European pensions*, 2003, retrieved from https://www.pensionseurope.eu/system/files/2003-10%20-%20EIORP%20report.pdf.
[90] EIOPA, 2016, p. 59.

Finally, the national sub-accounts will very likely create additional administrative burdens for the PEPP provider. In addition, the sub-accounts of the PEPP providers require knowledge of the various national laws and regulations, which may also lead to additional costs. This additional burden may result in increased costs for the PEPP providers and thus make the PEPP more expensive than the initial idea behind the PEPP. After all, the initial idea behind the PEPP is to bring a more cost-efficient pension product onto the European market.[91] Also, the intended competition will be less intense, because some (small) pension providers are not willing or able to bear the additional costs and/or do not possess the necessary knowledge.

In conclusion, it can be said that the solutions proposed by the sub-accounts and the Recommendation are not sufficient to eliminate the fiscal problems surrounding the PEPP. The Recommendation is too non-committal and therefore not a realistic solution. The sub-accounts try to deal more effectively with the diversity of tax regimes, but still cannot prevent national tax differences from impeding portability and cross-border pension provision and administration. In addition, possibilities for tax arbitrage such as the Pensionista problem remain open. Finally, compartmentalisation is counterproductive to the objectives of the PEPP (simple, cheap and high degree of competition).

Given the European nature of the PEPP and the fiscal problems, unilateral action by the Member States will not be sufficient.[92] Rapporteur Sophie in 't Veld therefore states in her Working Document that a European approach to taxation is necessary.[93] A balance must be found here between the fiscal autonomy of the Member States on the one hand and freedom of movement in combination with a functioning PEPP on the other.[94]

b. Tax policy options

In his book 'The Economics of International Integration' Robson describes three broad categories of international policy options: integration, harmonisation and coordination.[95] These

[91] Consideration 16 of the Regulation, see also the caps on costs.
[92] EC, 2001.
[93] EC, 2018.
[94] E. Schouten, Oplossingen voor fiscale obstakels voor een Europees personal pension framework? *Weekblad voor Fiscaal Recht*, 2017/111, 2017b.
[95] P. Robson, “The Economics of International Integration”, *Routledge, 4 edition*: December 17, 1998.

three categories, particularly harmonisation, can be further subdivided as Schouten[96] does in his overview of existing literature.[97] Four possible tax policy options have been identified:

- Full harmonisation: tax rules would be set at European level. The Member States comply with these European rules and thus give up their tax autonomy. This is also referred to as fiscal integration by Robson;
- Minimum harmonisation: only minimum rules are set at the European level. In addition, the national laws and regulations of the Member States continue to exist and apply. However, the Member States are obliged to implement the European minimum rules, which may lead to more far-reaching and stricter rules. This is usually done in the form of a Directive at European level;
- Optional harmonisation: the Member States once again retain their fiscal autonomy and national laws and regulations. At the European level, however, rules are also laid down which apply as a second regime next to the national rules. A pension provider can opt for the European regime or the national rules;
- Mutual recognition: Member States retain their full fiscal autonomy, but are obliged to recognise the various foreign pension products under their own rules. As a result, all foreign pension products, and the PEPP, qualify under the various national rules. Robson places this under coordination.

Three of these four policy options are not promising. Full tax harmonisation, integration, obviously solves all tax problems for the PEPP. Even if there was only a harmonised tax relief for the PEPP, that would lead to the fact that the tax treatment of PEPP in all Member States will be the same, as a single European framework applies. However good this may sound, the more utopian this idea is, as acknowledged in the Tax Recommendation and its evaluation.[98] As mentioned earlier, Member States must agree unanimously on European tax matters. The Member States are probably not prepared to give up their tax autonomy, and this will not lead to unanimity in favour of full harmonisation or a fully harmonised framework for PEPP.[99] In line with this observation, minimum harmonisation would also not be an appropriate policy option. Also under this option, Member States would have to cancel part of their tax autonomy,

---

[96] E. Schouten, 2017b, p. 6.
[97] See also P.J.G. Kapteyn & P. Verloren van Themaat, Het recht van de Europese Unie en van de Europese Gemeenschappen, Deventer: Kluwer 2003, pp. 268-269.
[98] EC, *Follow up to the Parliament non-legislative resolution on the tax treatment of pension products, including the pan-European Personal Pension Product (PEPP),* SP(2019)433, p. 2.
[99] See for example the reaction of the Dutch government on not treating PEPP differently from national pension products.

i.e. at the level of minimum rules. Furthermore, it can be expected that the national translation of the minimum harmonisation by Member States will once again ensure a diversity of rules.[100]

In addition, Fry and Eichenberger indicate in their article[101] that policy options such as full harmonisation and minimum harmonisation may be, and are likely to be, inefficient due, inter alia, to political distortions. This means that, by losing or reducing their regulatory power, policymakers can respond less or not at all to the societal needs of their country. Policies and rules are therefore rather not in line with citizens' preferences. This counterargument for full and minimum harmonisation based on national customisation weighs heavily within the pension domain. As explained earlier, pensions and its taxation are a national matter because they arise from the specific social, cultural, economic and historical circumstances of the various Member States and also play a different role within the relevant society. In addition, the EC in its Ageing Report and earlier in the Tax Communication[102] refers to the importance of fiscal policies on pensions for the sustainability of public finances. Indeed, ageing populations mean fewer people in work (and therefore tax revenues) and more pension expenditure. National policymakers must have the freedom to use taxation for public finances. Centralising fiscal pension policy from Member State to EU is therefore undesirable in view of the potential welfare losses in national policies.

Mutual recognition is also not promising in the foreseeable future. After all, it takes a great deal of time and effort for all European member states to implement mutual recognition either bilaterally or unilaterally. Some tax treaties already have a non-discrimination clause, which provides the same tax facilitation for foreign pension products that qualify in the other Member State.[103] Didden concluded and defended this so-called pension contribution provision as best solution to battle tax problems of cross-border pensions in his doctoral thesis.[104] This could be an important solution for PEPP as well in the form of mutual recognitions, as it will lay down that PEPPs and its PEPP providers will be tax facilitated in all Member States. However, the inclusion of such a clause in all tax treaties in the EU takes a lot of time, as these (re)negotiations

---

[100] Schouten, 2017b, p. 7.
[101] B. Frey & E. Eichenberger, To Harmonize or to Compete? That's not the Question, *Journal of Public Economics* 60, p. 335-349.
[102] EC, *The 2018 Ageing Report Economic & Budgetary Projections for the 28 EU Member States (2016-2070)*, Institutional Paper 079, ISSN 2443-8014, p. 7; EC, 2001, p. 20.
[103] An optional clause in paragraph 37 on Article 18 of the OECD Commentary on the Tax Model Convention.
[104] B. Didden, *Cross-border qualification problems: between social security and supplementary pensions*, Maastricht: ProefschriftMaken 2019.

take time. This conflicts with the objective of achieving rapid market penetration (see also the argument of the EC for opting for a Regulation). In addition, mutual recognition, and thus the solution for taxation, relies on bilateral efforts and goodwill, which is also not in line with the desired multilateral approach by the EC to facilitate pension market integration and intensified competition.

This leaves optional harmonisation as a fiscal policy option. Optional harmonisation will ensure that Member States arrive at a European tax regime for the PEPP. This tax regime, like the Regulation itself, will apply as a 'fiftieth' regime (second regime) alongside the (49) existing national tax regimes. The European tax regime will therefore not interfere with the national tax regimes. With this observation, the optional harmonisation can be seen as a simple solution that represents a compromise between the fiscal autonomy of Member States and the realisation of a successful European pension product that can intensify the pension market.

c. Optional harmonisation and its implementation

This section will discuss the various factors that the optional harmonised tax regime for PEPP (hereafter: PEPP regime) could include in more detail and will follow with its implementation.

Tax admissible providers

One of the fiscal conditions may be that the pension provider must be admitted or qualified, as is the case in the Netherlands. Foreign pension providers are often confronted with additional requirements and therefore often do not engage in cross-border activities. This hinders the intended competition and the portability of the PEPP. It is important that the PEPP regime therefore regulates which pension providers are fiscally allowed to implement the PEPP. This will of course be in line with the authorised PEPP providers as under Article 5 of the Regulation. If Member States agree to harmonise this for the PEPP, a single European PEPP market may emerge. Obstacles, such as those imposed by the Netherlands in the form of additional requirements, will after all be removed, as a result of which providers throughout Europe will be able to offer their PEPP and PEPP savers will be able to move undisturbed from Member State to Member State and remain with their own PEPP provider. As pointed out above, this is important in order to achieve competition and simplicity and thus a simple and inexpensive pension product, which will benefit the pension savings of EU citizens.

In addition, such additional information requirements or barriers are out of date and unnecessary. The Common Reporting Standards (CSR) already require financial institutions (pension institutions) to provide information, such as account holder data, to tax authorities on an annual basis. For the PEPP, this means that PEPP providers have to report to the tax authorities of their PEPP savers.[105] In addition, the PEPP regime may also lay down reporting provisions as set out in Section 5 of Chapter IV of the Regulation. Liability claims are also, in principle, unnecessary for the PEPP, as the national tax authority already has the power under the Regulation to recover any benefit granted in the event of improper use.[106]

Product requirements

The diversity of tax rules means that different requirements are imposed on the PEPP. In addition to the previously discussed admitted pension provider, one can think of the pension age, the form of benefit, the pension provider and, as in the case of the Netherlands, the demonstrable pension gap and its difficult calculation. As previously shown, this means that foreign pension products do not qualify for facilitation and cross-border value transfers could hindered. It also obliges PEPP providers to compartmentalise and collect tax knowledge, which entails administrative costs and costs relating to gathering all expertise.

The PEPP regime can harmonise tax product requirements with respect to the PEPP. This can be done both at the front and the back: the requirements regarding the accrual phase of the PEPP can be harmonised (e.g. the contractually agreed pension age/term and the level of tax deduction) and the requirements regarding the benefit phase of the PEPP can be harmonised (e.g. minimum age, benefit possibilities and level). Harmonisation of the requirements for the accrual phase for entitlement to facilitation is initially the most important aspect here. Indeed, this will make most contributions to the PEPP fiscally easier in Europe, given that most Member States and annuities have EET treatment.[107] In addition, the contribution deduction can be capped by means of a maximum deduction or in the form of a pension shortfall (the principle of compensating vessels, as in the Netherlands). The latter, in particular the deductibility on the basis of the pension deficit, can also provide a solution to tax arbitrage, such as the Pensionista problem. In this way, PEPP savers cannot save untaxed indefinitely and postpone taxation undesirably. In my view, however, the main advantage of harmonised requirements for the

[105] E. Schouten, 2017a, p. 6.
[106] Article 58(4) of the Regulation and the powers of the national authorities are laid down in Article 62 and 63.
[107] Ernst & Young, 2017, p. 261: 22 out of 28 Member States, 37 out of 49 national pension products.

accrual phase is that the compartmentalisation as proposed by the EC is no longer necessary from a fiscal point of view.

<u>Tax system</u>

The PEPP regime can also harmonise the tax system. As a result, the tax facilitation of the PEPP would be the same across Europe. As the majority of Member States and pension products have an EET treatment, the move to an EET system for the PEPP seems obvious. The advantage of a harmonised EET system is that the maximum incentive to save in a PEPP is provided everywhere, since according to the OECD calculations, the present value of the tax benefit is the highest in this system.[108] This promotes the success of the PEPP, certainly in those countries where no or less facilitation is yet taking place, and thus the realisation of higher pension savings in Europe. A potential disadvantage of the EET system is that tax arbitrage is possible because the tax claim can only be redeemed in the benefit phase. Note that the Pensionista problem (an artificial EEE system) is solved by this harmonisation, as the PEPP can no longer be subject to a TEE system.

A second disadvantage comes from the perspective of national public finances. A harmonised EET system may cost too much, since the premium deduction reduces tax revenues. This argument certainly applies to those Member States that do not yet have an EET system. Both counterarguments can be met and limited by limiting the deductibility of premiums on the basis of a demonstrable pension gap or a certain ceiling, as the case-study of the Netherlands shows. This would eliminate the EET facilitation above a certain amount, thus reducing tax arbitrage and financial costs until a certain maximum.

As an alternative, Schouten mentions the TEE system in his article.[109] The great advantage of the TEE system is its simplicity. By shifting taxation from the benefit phase to the accrual phase, the direct financial impact on Member States' public finances is limited and there is no room for the outlined Pensionista problem (an artificial EEE system). In addition, the portability and portability of the PEPP is ensured: Member States do not have tax claims, allowing pension capital to move undisturbed (without protective tax assessments, exit taxes) from one Member State to another. Finally, a TEE system ensures that less importance can be attached by Member

---

[108] OECD, *OECD Pensions Outlook 2016*, OECD Publishing, Paris 2016. http://dx.doi.org/10.1787/pens_outlook-2016-en.
[109] E. Schouten, 2017a.

States to the fiscal conditions for facilitation. After all, there is no tax claim on the accrued pension capital. However, as the OECD calculations showed the TEE system is less advantageous than the EET system, which may reduce the decline and success of the PEPP. In addition, the highlighting of tax revenues on pension assets conflicts with the recommendations of the EC in its Ageing Report and Communication.[110] Indeed, due to an ageing society, taxation of pension benefits is an important source of income. Finally, the TEE system is also intended to prevent unrestricted tax-free saving (tax arbitrage), which again also could be limited by the introduction of ceilings or a pension gap.

A proposal for implementation

A PEPP regime, in which all tax aspects are harmonised, solves all the tax problems and thus facilitates a single market for PEPP and its goals of enhanced competition, transparency and portability. In this case too, however, the tax autonomy of Member States is likely to prevent such a PEPP regime. In addition, this conflicts with the view that PEPPs should not be given a more advantageous or different position than national pension products. Finally, on a comparable topic, that of capital income taxes, Tanzi and Bovenberg indicate in their study on the European economic integration and harmonization of capital income taxes that tax harmonisation always should take place as specifically as possible.[111] The arguments for specific harmonisation are again based on efficiency. A uniform one-size-fits-all tax regime creates welfare losses, given the diversity between Member States and taxes as policy area within a society. The pension domain in particular requires a certain degree of customisation, again consider the recommendations in the Ageing Report.

Nevertheless, a specific optional harmonisation will also effectively infringe the fiscal autonomy of Member States, namely with regard to (some) tax rules for the PEPP. Schouten therefore rightly points out that 'this regime should be as 'light' as possible'.[112] The PEPP regime should require little or no effort on the part of the Member States, should have little budgetary impact and should not give the appearance of being treated differently. As a result, Member States are more likely to accept a PEPP regime. Therefore, Tanzi and Bovenberg came to the conclusion in their study on harmonisation of capital income taxes that a step-by-step approach

[110] EC, 2018; EC, 2001.

[111] V. Tanzi & L. Bovenberg, Is There a Need for Harmonizing Capital Income Taxes Within EC Countries?, *IMF Working Paper 90/17,* 1990.

[112] E. Schouten, 2017a, p. 5.

is the best route to European harmonisation.[113] As far as capital gains tax is concerned, they recommend starting with a harmonised tax base for capital gains tax and extending from there, if desired, for example, with a minimum tax rate. This step-by-step approach ensures, on the one hand, that Member States are more inclined to agree to such a fiftieth regime and, on the other hand, that a step-by-step assessment can be made as to whether further harmonisation is necessary or whether the current level is specific enough.

If these two recommendations are combined, it can be concluded that the PEPP regime can harmonise the tax aspects step by step, if desirable, and each step should be as 'light' as possible. I see a proposal for a step-by-step implementation of the PEPP regime as follows:

Step 1: the absolute minimum to guarantee the PEPP objectives

As a first step, the absolute minimum must be determined. These are the fiscally permissible pension providers and the principle of compensating vessels. The previous section has shown that this enables providers to operate anywhere in Europe and PEPP savers to enjoy the characteristic portability of the PEPP undisturbed. This is very important because the idea behind the PEPP can be realised: through competition and economies of scale, make the personal pension market more efficient and cheaper and thus encourage pension saving. This minimum requires little from the Member States. As explained in the previous section, any information and liability provisions are already guaranteed in the EU or by the Regulation.

The principle of compensatory vessels is already applied in countries such as the Netherlands and the United Kingdom.[114] In this context, the third pillar functions as a means of closing the pension gap remaining after pension accrual in the first and second pillars.[115] Fiscal facilitation depends on the policy replacement ratio (such as the 70% in the Netherlands) and the benefits already accrued in the first two pillars. As a result, the pension target of the PEPP is made more explicit and the scope for tax arbitrage is restricted. Staats is critical of the principle of compensating vessels, according to which the third pillar can never replace the first and second pillars, but can only supplement them as an ultimum remedium.[116] In the case of the PEPP, on the contrary, this observation is a major advantage: it strongly emphasises the PEPP's objective

[113] V. Tanzi & L. Bovenberg, 1990.
[114] H. Van Meerten & N.Hooghiemstra, 2017, p. 12-14.
[115] G. Dietvorst, 2007.
[116] G. Staats, *Personal Pensions in the EU,* Tilburg University, 2014 (doctoral thesis).

of complementing national pension systems and not replacing them or going to replace them. The PEPP regime as a 'compensating vessel' thus ensures, on the one hand, that the PEPP is not seen as a means of tax arbitrage and, on the other hand, that it does not replace national pension and tax systems but complements them. This can be beneficial to the acceptance and cooperation of Member States.

Step 2: Harmonisation of the PEPP tax definition

In line with the recommendation of Tanzi and Bovenberg, the next step is a harmonised tax base: a PEPP definition. Van Meerten and Hooghiemstra conclude in their paper that such a PEPP definition for tax purposes is necessary to bridge the diversity of tax rules.[117] Without this harmonisation, it would not be possible to create a European 'passport' for the PEPP in the tax sense, as the PEPP has to meet different requirements per Member State. However, by harmonising the PEPP definition in a tax sense, a single product will be created that can use a European passport for tax purposes. This will solve the problems previously mentioned arising from the different national tax requirements for personal pension products. In addition, the PEPP administrators opting for this regime only need to know the tax rules of the PEPP regime in order to work across Europe, if an EET/ETT/EEE system is in place, in a tax-facilitated way. This ensures the portability of the PEPP even without the compartments from a tax perspective, which benefits the main features of the PEPP: simplicity, transparency and inexpensive.

In order not to give Member States the feeling that the PEPP is treated more favourably than national personal pension products and to keep the step 'light', only the fiscal requirements for the accrual phase can be harmonised.[118] In practical terms, this means standardizing when a PEPP qualifies for tax facilitation, if the Member State has an EET system. Benefit options and conditions will therefore remain the same as national alternatives, depending on national laws and regulations. Ernst & Young concludes in its study that harmonisation of the requirements for the accrual phase could easily be achieved. After all, the national differences in the requirements for the accrual phase are less extensive than differences in the requirements for the benefit phase.[119] Finally, in principle, this step does not have any major budgetary consequences, as only those Member States that already facilitate the premium are 'affected' by this harmonisation.

[117] H. Van Meerten & N. Hooghiemstra, 2017, p. 46 and onwards.
[118] J. Van Zanden, 2017.
[119] Ernst & Young, 2017, p. 261.

Step 3: Harmonisation of the tax system

A more far-reaching harmonisation in the PEPP regime is the provision of a uniform tax facility for the PEPP. The advantages and disadvantages of the EET and TEE systems have already been discussed. A TEE system has been recommended earlies, since such a system is the 'lightest', given the budgetary implications and the safeguarding of the tax claim of the facilitating Member State.[120]

In view of the fact that a substantial proportion of the Member States have an EET system, it is strange, in my opinion, to transform it into a TEE system for the PEPP. After all, step 2 qualifies the PEPP for the EET system, which provides a greater tax benefit for pension savings and is better suited to an ageing society. Harmonisation of the tax system towards TEE within the PEPP regime therefore has undesirable consequences. Nevertheless, an EET system as a PEPP regime is too expensive for Member States without an EET system or any facility and will meet with opposition.

A compromise between Schouten's motives for a TEE system and the desire for an EET system could possibly be found in Dutch practice: the capping limit. The PEPP regime can be designed with an EET regime up to a certain maximum. This maximum can be set on the basis of income, as in the Netherlands, or the contribution can be absolutely capped. Setting the level of this capping limit is a national competence, allowing member states to respond to their budgetary scope and pension targets. A TEE system applies above the capping limit.

Finally, in addition to an EET or TEE system, the option of a 'matching contribution system' is put forward, whereby for each euro of contribution to the PEPP there is a certain amount (less than one euro) of tax credit.[121] This, too, is an intermediate step between the 'too expensive' EET system and the TEE system.

5. Conclusion

This paper has dealt with the PEPP Regulation, its evolution and the identification and solution to the tax obstacles it is faces with. The PEPP is introduced as European pension product that

[120] Schouten, 2017a, p. 5.
[121] H. Van Meerten & N. Hooghiemstra, 2017, p. 91.

should strengthen the national pension savings, and thus the sustainability and adequacy of national pension systems, and facilitate European integration of pension markets, and thus the cross-border mobility and provision. The Regulation standardizes the characteristics of the PEPP and therefore it is concluded that PEPP is a ‘quality label’ for personal pension products. After examining the Regulation and the legislative changes compared to the initial proposal of the EC, it can be concluded that the PEPP received a less European character and is less ambitious. Changes as a greater role for and influence of national supervisory authorities and governments instead of at European level with EIOPA, is slightly eroding the European character and safeguarding the standardised characteristics of PEPP. Furthermore, by limiting the scope of eligible providers, the portability possibilities and switching services, the potential for facilitating cross-border mobility and provision and strengthening of competition and efficiency are weakened.

The Regulation does not deal with the tax-treatment of PEPP, but has included national designed sub-accounts and a Tax Recommendation. This paper concluded that the tax obstacles stemming from the great diversity of tax regimes (system and requirements) cannot be solved sufficiently by the national sub-accounts and Tax Recommendation. The tax obstacles make tax arbitrage possible and makes the PEPP less able to function in terms of provision, competition, transparency and portability. The main problem is that the national competency regarding to taxation stands in the way of a single market. These problems can be solved by different levels of harmonisation, as discussed in the paper. After analysing these levels, it is concluded that optional tax harmonisation is the most efficient and feasible option, as regime next to the national tax regimes. Within this PEPP regime the different tax aspects to be harmonised and the extent to which they solve the tax problems and thus facilitates a single market for PEPP are discussed. A PEPP regime can solve all tax obstacles, resulting from diversity in tax systems and tax requirements. However, since direct taxation is a national policy domain, the paper recommends a step-by-step implementation, where the steps should be as ‘light’ as possible. The first and fundamental step of the PEPP regime would be harmonising the tax admissible providers and implementing the principle of ‘compensating vessels’. This will allow PEPP providers, as specified in the Regulation, to operate on a tax-facilitated basis everywhere. Competition and European viability, and thus the objective of the PEPP, are safeguarded. The PEPP as a 'compensating vessel’ guarantees the explicit pension objective of the PEPP and its complementary effect on national pension systems. This provides a sufficient basis on which to subsequently take the suggested follow-up steps.