New Dutch Pension Act on 1 July 2023

Major reform of pension system

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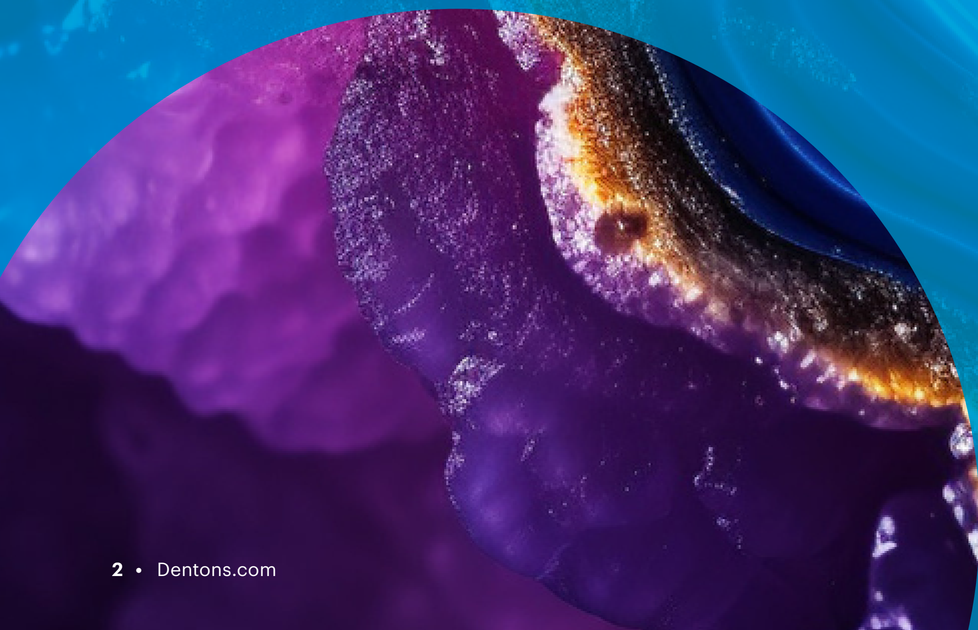
Introduction

On May 30, 2023 the Dutch Senate adopted the new Dutch Pension Act to reform the Dutch pension system, (**the Act**) which comes into effect on July 1, 2023. This change impacts every employer with a pension scheme in place. In practice, all pension arrangements with employees and contracts with pension providers will need to be renewed. In this alert we provide you with an overview of the most important reforms to the Dutch pension system and recommended steps forward for employers. For those not yet familiar with the current Dutch pension system, we begin with a brief explanation.



Dutch pension system

The current Dutch pension system consists of three pillars that together determine the pension amount a person will receive after retirement:

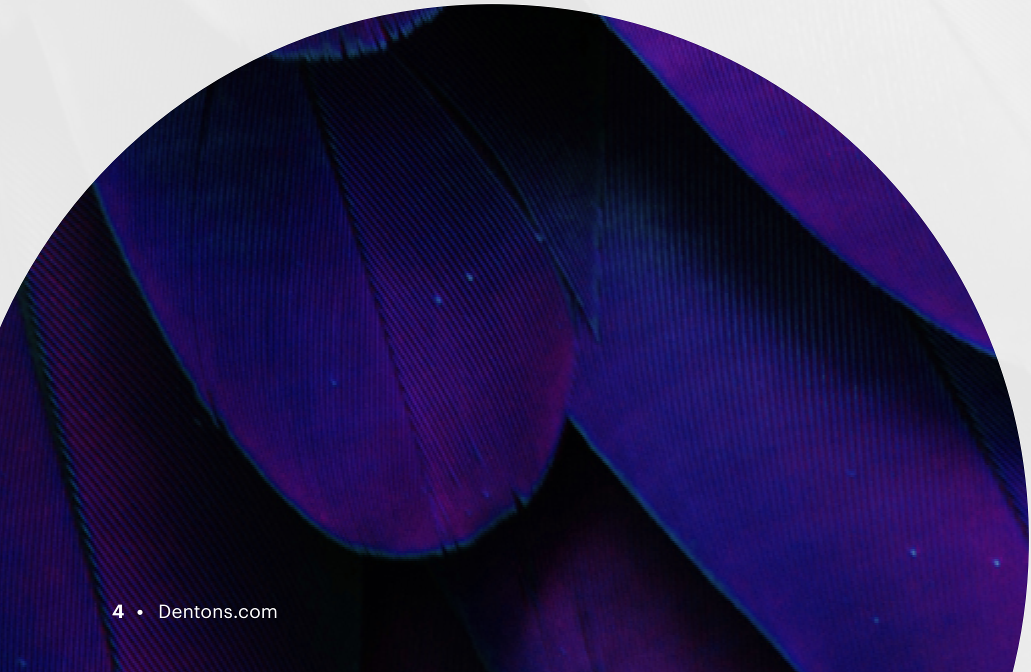
1. State pension (in Dutch, *AOW*) – a pension benefit paid to people upon reaching the current retirement age of 67 and funded by contributions paid by younger people; also known as a "pay-as-you-go" system;
2. Supplementary collective pension – occupational pension, arranged through employment;
3. Private individual pension products – arranged by individuals on their own.

The collective pension schemes under the second pillar are arrangements between employers and employees and are commonly administered by pension funds. These are generally funds for a specific industry – most of these have been made mandatory, company or for a group of people working in a specific sector. Alternatively, insurance companies may administer the pension scheme. These schemes are funded by capital funding – the pensions are financed by contributions paid in the past as well as the investment return on those contributions.

At present, the Dutch Pension Act allows for three types of pension schemes: (1) a defined benefit scheme (either a final pay scheme or a career average scheme), (2) a defined capital scheme, or (3) a defined contribution scheme. The defined benefit schemes are being phased out of the Dutch pension system, and defined capital schemes are already quite rare. Defined contribution schemes (either in full or combined with characteristics of other schemes) are becoming more common for employees, but the current generation of retirees mostly still have defined benefit schemes.

Purpose of the reform

The Dutch government wishes to reinvigorate the pension system since, among other reasons, low interest rates and the aging Dutch population are putting pressure on the system, resulting in higher costs and a reduction in pension benefits. The increase in self-employment and other forms of flexible labor are also having an impact on the Dutch pension market, as fewer people now participate in pension plans. The purpose of the new system is to provide for the accrual of a pension as part of an individual pension capital, combined with the benefits of collective risk-sharing. Defined benefits are no longer possible. The Dutch government intends to abolish the system of average premiums whereby one premium is paid for each individual, regardless of age. It wants to introduce a premium tailored to the individual circumstances and allocated to the individual pension capital, which is probably the most essential element of the new pension system.



Main elements of the new Dutch pension system

There is a lot to say about this new pension system but, from the perspective of the employer and briefly stated, the main elements of the Act are:

- **Contribution based** – Pension accrual is only possible based on a defined contribution scheme, and the pension assets are managed and invested collectively for all participants. Parties can no longer agree on a defined benefit pension scheme. This means that the new pension system will be contribution-based.
- **Three new types of schemes** – The Act introduces three new types of defined contribution schemes: (i) a solidarity contribution scheme, (ii) a flexible contribution scheme and (iii) a contribution-capital scheme (only for pension insurers). The main difference between the three options is the level of the participants' involvement to the investments of the contributions and collective risk sharing by using a reserve in the event of disappointing returns on investments. For a more detailed description per scheme please see below.

    1. The "**solidarity contribution scheme**" (in Dutch: *solidaire premieovereenkomst*) is a new concept. It is characterized by a collective investment policy1 for at least the excess returns for active, former and future participants in the scheme. Accrual takes place by way of an individual pension capital that is combined with the benefits of collective risk-sharing (e.g. through spreading of financial ups and downs and a solidarity reserve);

2. The "**flexible contribution scheme**" (in Dutch: *flexibele premieovereenkomst*) currently exists under the name "collective variable pension"—a contribution scheme with collective risk sharing among employees. This scheme is characterized by a separate accrual and benefit phase, whereby at retirement date an accumulated individual pension capital is converted into, or used for, a lifetime benefit. The investment policy is designed on the basis of specific investment mixes per age cohort (life-cycles). Upon retirement, participants can also opt for a variable pension by continuing investments after retirement begins. This is already allowed under the Premium Schemes Improvement Act (in Dutch: Wet verbeterde premieregeling) and will thus be continued under the new system with some improvements.

3. With the **contribution-capital scheme** (in Dutch: *de premie-uitkeringsovereenkomst*) participants can – up to 15 years before the Dutch state pension (in Dutch: AOW) retirement age – request to use the accrued capital to purchase guaranteed fixed (or partly fixed) lifetime pension benefits that are to be paid upon retirement. Future pension accrual (i.e. accrual during the 15 years up to retirement) can be taken into account when purchasing the pension benefits. Consequently, the risks will be for the account of the insurance company from the moment of purchasing the fixed pension benefits. This scheme can only be offered by pension insurers and cannot be administered by pension funds, since insurance companies can guarantee a nominal pension.

- **Age-independent contributions** – most defined benefit pension schemes have age-dependent (flat rate) pension contributions, which are no longer allowed. The current average pension accrual will be transformed to a degressive pension accrual by adopting **age-independent** pension contributions only. Exceptions will apply to net pension and voluntary top-up. This may also have consequences for existing defined contribution schemes, i.e. amendment may be necessary, but again exceptions apply for existing defined contribution schemes on 30 June 2023 and defined benefit plans administered by an insurance company amended to an age-based defined contribution plan prior to 1 January 2028.

- **Minimum entry age** – the starting age in pension schemes will be lowered from 21 to 18 as per 1 January 2024.
- **30% tax** – the tax limitation will no longer be on pension accruals, but on the contributions. The proposed maximum contribution for retirement and partner's pension is 30 percent of the pensionable base.
- **Net pension** – the Act treats net pensions (i.e. pension accruable on salary above €128,810 as from January 1, 2023 that can be put in private individual pension products, which people arrange for themselves) almost equal to pensionable salary (i.e. under that amount). For instance, this means that the same tax limitation (i.e. 30 percent) will apply, but it is corrected with a net factor. For net pensions, the obligation of flat rate pension contributions does not apply.
- **Transition plan** – when transitioning to the new pension scheme, employers should prepare a transition plan, which takes account of substantial consequences related to converting accrued pensions into the new pension scheme (in Dutch: *invaren*) and of adequate compensation to employees in the event the change is to their detriment. Suggestions for financing this transition include a temporary increase in contributions, using temporary financial buffers, a lump sum from the employer in the solidarity reserve, etc.
- **Partner pension** – partner pensions, which are paid out upon death after retirement, will be brought in line with current market-practice: Up to a maximum of 70 percent of retirement benefits can be converted into a partner pension. Partner pensions paid out upon death before retirement will be on a risk-basis only with a maximum of 50 percent of the pensionable salary, regardless of years of service, and until three months after participation in the scheme would have ended. The definition of partner definition will be made uniform, as fewer people are choosing to marry, opting instead for a registered partnership or living together only.

What to do and when?

- Start early, preferably now, and consider this a project!
- Review your current pension arrangements with employees, the agreement with the pension provider and the renewal date of such agreement;
- Involve both your legal counsel and pension broker (if any) to start investigating renewal requirements, possibilities and implementation actions;
- Remember that implementation also comprises changing employee documentation containing the arrangements with regard to the pension and not only the agreement with the pension provider, as the employee documentation forms the basis for the pension arrangement. This may require the employees' individual consent;
- Involve the works council (if any) at an early stage, as the works council's endorsement will be required over both the change in pension scheme as the establishment of the transition plan.

30 June 2023

Deadline to amend defined benefit plans at pension funds to an age-based defined contribution plan.

1 July 2023

New pension plans need to be contribution based and age-independent.

1 January 2025

Deadline to submit transition plan if pension provider is pension fund.

1 October 2027

Deadline to submit transition plan if pension provider is an insurance party.

1 January 2028

Deadline transition – only contribution based pension schemes are allowed, except for a few exceptions.

Please note that when your company is participating in a company or a mandatory industry-wide pension fund, whether or not (also) on the basis of a pension arrangement in a collective labor agreement, different actions may be required than those set out above. Usually social partners, i.e. the employer and employee organizations, collectively negotiate the new pension arrangement.

We would be happy to assist you in (all of the phases of) this process, and we can always provide more information to you or your HR teams about this subject.

Contact

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CSBrand-119508-BrochureaboutnewDutchPensionAct-02—27/06/2023