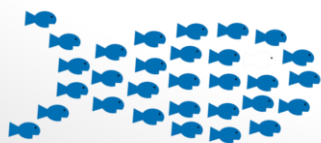




Better Finance response to the OECD Public consultation on Core Principles of Private Pension Regulation

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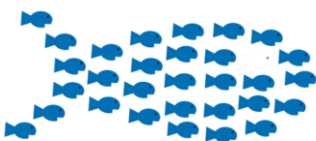




Introduction

Better Finance, the European Federation of Investors and Financial Services Users is the only dedicated representative of financial services users at European level. It counts more than fifty national and international members and sub-member organizations in turn comprising about 4.5 million individual members. Better Finance acts as an independent financial expertise center to the direct benefit of the European financial services users (shareholders, other investors, savers, pension fund participants, life insurance policy holders, borrowers, etc.) and other stakeholders of the European financial services who are independent from the financial industry.

Better Finance is the most involved European end user and civil society organisation in the EU Authorities' financial advisory groups, with experts participating in the Securities & Markets, the Banking, the Occupational Pensions and Insurance and Reinsurance Stakeholder Groups of the European Supervisory Authorities; and in the EC Financial Services User Group. Its national members also participate in national financial regulators and supervisors bodies when allowed. For further details please see our website: www.betterfinance.eu



We write in response to your request for comments on the Draft Recommendation of the Council on the Core Principles of Private Pension Regulation released in July 2015. We appreciate the efforts of the Working Party on Private Pensions and the Council of the Organisation for Economic Cooperation and Development to try to improve the world's pension systems.

This our response to the revision of OECD's "Core Principles of Private Pension Regulation", and especially about Section 4.16 of the draft Core Principles:

1. Section 4.16 of the Core Principles discourages investment in employer stock, such as with employee stock ownership plans in the U.S.A. (ESOPs), as not providing sufficient diversification.

That section contends that:

"Self-investment by those undertaking investment management of pension funds should be prohibited or, where appropriate safeguards exist, strictly controlled. Investment in the assets of the plan sponsor, in parties related or affiliated with the governing body of pension fund, the pension entity or pension fund management company should be prohibited or strictly limited to a prudent level so as to ensure diversification (e.g. 5 percent of the pension fund assets) or otherwise avoid undue risks or costs to members. When the plan sponsor, the pension entity or the pension fund management company belong to a group, investment in entities belonging to these same groups should also be limited to a prudent level of diversification, which may be a slightly higher percentage (e.g. 10 percent of the pension fund assets)."

2. Preliminary comment

Employee share ownership is nowadays one of the last remainders of economic democracy where the real economy stakeholders are also the direct co-owners of the economy and can exercise their voting rights. It should be therefore encouraged instead of the reverse. Indeed, overall direct individual ownership of the equity of



listed companies has been decreasing dramatically over the last decades¹. In parallel, “agency” ownership now flourishes with financial intermediaries (dealing with “other people’s money”) getting in control (voting rights) of an increasing part of listed equity. This is the main explicative factor for the current insufficient long term “shareholder” engagement” and related corporate governance issues.

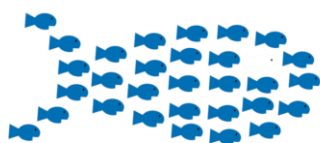
Nowadays, Employee ownership is one of the rare opportunities for citizens to get basic education on equity and share ownership., as retail financial intermediaries have mostly dropped promoting direct share ownership in favor of “packaged” products such as mutual funds and life insurance, which generate much more fees and commissions from them.

This being said, it is of course not advisable to concentrate one’s savings into one’s employer’s equity: there should be a limit set with regard to the total amount of long term savings per person that one can hold in company stock via employer-sponsored schemes.

3. We believe that the new OECD guidelines could have a negative impact for employee share ownership as a whole, actually not only for employee share ownership but for the economy of OECD countries in general if they followed your recommendation of a complete ban of self-investment of company pension funds in the shares of the own company. These new principles seem inappropriate to the employee share ownership phenomenon.

4. Employee share ownership is the result of employees' investments in shares of their company. Over the last thirty years, employee share ownership has developed strongly in Europe. In some figures: Today, 86% of large European companies have

¹ See in particular the research published by the European Commission at the request of the Financial Services User Group (FSUG) on « Who owns the European economy? », 2013
http://ec.europa.eu/finance/finservices-retail/docs/fsug/papers/1308-report-who-owns-european-economy_en.pdf



employee share plans, the number of employee shareholders was multiplied by 10, reaching 10 million people and a total investment of 301 billion Euro in 2014 ².

5. Employee share ownership is generally promoted by concrete public policies in most developing countries nowadays. Indeed, a well-conducted employee share ownership policy brings beneficial results in terms of productivity, profitability, economic growth and employment. As formulated, the OECD project poses an unfortunate threat to this policy choice.

6. The principle of Diversification applies to employee share ownership as to any other financial investment. It is illustrated by the aphorism "do not put all eggs in one basket." In this light, we can also indicate that employee share plans are generally characterized by voluntary membership and by investment limits depending on the employee's remuneration level. We do not agree in any case with a prohibition of self-investment of company pension funds, but instead to a maximum percentage of assets of the company long term and pension funds invested in the company's equity or bonds. **We deem the proposal from OECD of 5% (10% in case of investments in entities belonging to these same groups) as a much too low ceiling.** We would like to make OECD aware that a sufficient diversification level could be possible with even higher proportions of self-investment, depending on the composition of the rest of the pension fund portfolio and cannot be set in isolation of the rest of the employees' personal long term savings. This depends mostly on the correlation of the performance and risk of those other assets within the portfolio. These should be, ideally, invested in companies from different economic sectors than the own company from the company pension plan, ideally with a high diversification which could be achieved through "wide", total market index funds or investment funds of other type ideally with a low annual management fee.

² Annual Economic Survey of Employee Ownership in European Countries in 2014, European Federation of Employee Share Ownership, Brussels, 2015.



7. Employee share ownership is not just a financial investment. It also has the character of an industrial investment. This character is most evident when the employees' stake reaches 100% of the company's capital, which is the typical case of employee share ownership in SMEs³. However, it is also present, although more incidentally, to the minority employee share ownership in large companies.

8. If the aphorism of eggs and basket frequently applies to the diversification of financial investments, another aphorism applies better to industrial investment: "The bird lays all eggs in the same nest"⁴. By concentrating its eggs in one nest, the bird manages security by the particular care that this choice allows. So is it also for employee share ownership as an industrial investment. Employee share schemes are usually supported by communication programs and financial information and they are recognized as a powerful tool for economic and financial education for employees, and thus, for risk control.

9. When the OECD project considers employee share ownership in its sole dimension of financial investment, omitting that of industrial investment, it makes a unilateral choice. This simplistic position ignores the complexity of employee share ownership. It is therefore inappropriate.

10. This positioning is in line with the movement of "*financialization*" that tends to obscure industrial or "real" considerations. About employee share ownership, this positioning is clearly at odds with the economic policy choices of many OECD countries that advocate a return to "real" economy considerations rather than purely financial.

³ Majority employee share ownership is also found in medium and large companies: In Europe, there are over 300 companies of this type in 2014.

⁴ Among the few exceptions, the example of the cuckoo is well known. It must be said: Employee share ownership is not a cuckoo.



11. Furthermore, if one merely has to consider employee share ownership in its sole dimension of financial investment, it is appropriate to apply the same diversification rules that apply to all forms of financial investment. There is therefore no reason to grant specific treatment as does the OECD project. This discrimination is not justified. The negative signal it sends about employee share ownership is inappropriate.

As a conclusion, the overwhelming body of evidence suggests that encouraging employee share ownership is a proven and effective means of improving the retirement security of employees and the economy as a whole. Therefore, we urge the WPPP to recognize the benefits of encouraging employee share ownership by correcting the Draft Principles in this sense.