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Newsletter of the Geneva State Pension Fund (*CPEG*) January 2017

Message from the President

Since our last issue in June 2016 the risk of a cut in the technical rate has become a reality due to persistently low interest rates and the long-term financial equilibrium of your Fund is no longer guaranteed.

In October 2016 the accredited expert at the CPEG accordingly advised the Committee to cut the technical rate by 0.5% and to reduce future benefits to currently employed insured members by around 20%. The pensions of current retirees are protected by the federal law and cannot therefore be reduced.

As the Committee is obliged to adjust the benefits in line with the level of contributions stipulated in the cantonal law, it followed the recommendations of the accredited expert and must consequently adopt a set of structural measures to restore the long-term financial equilibrium.

At this stage, the Committee announced a preliminary measure which involves raising the pivotal age from 64 to 65 for the standard benefits plan and from 61 to 62 for the hardship plan. This measure will come into effect on 1 January 2018. It represents a benefit reduction of around 5%, i.e. around a quarter of the total cuts of 20% that must be made in order to comply with the recommendation by the accredited expert.

Other measures are undergoing an in-depth analysis and will be announced during the first half of 2017 for implementation this time on 1 January 2019 at the earliest.

In order to give you a full picture of the situation, we will dedicate most of this issue to presenting the challenges that face the Fund with regard to its long-term financial equilibrium. In the following four pages you will also find articles about the reduction in the technical rate, raising the pivotal age by one year and the other structural measures which the Committee will have to decide.

While you are awaiting the publication of the next *CPEG INFO* at the end of the first half of 2017, you will be able to keep up to date by means of the news published on our website or by means of our newsletters. Do not hesitate to subscribe on our website www.cpeg.ch (Practical information > Newsletter).

The Committee is fully aware of the pain that the new measures which are addressed in this issue will cause the insured members who are currently in employment. Please be assured that the Committee will do everything in its power to ensure that the burden is distributed equally between the generations of active insured members as far as possible.

Lastly, we wish to draw your attention to the fact that 2017 is the year in which the first renewal of the term of office of your Fund management bodies will take place. This electoral process using an e-voting system, which is a first for the CPEG, is explained to you on page 7.

Pierre Béguet,
President of the CPEG
until 31 December 2016

Cut in the technical rate and recommendations by the accredited expert at the Fund

The technical rate is the interest rate that is used in the annual valuation of all the Fund's future liabilities in respect of its active and retired insured members (see general article on the technical rate, *CPEG INFO* of June 2016, pp. 6-7).

The Committee made the decision to cut the technical rate from its current 3% to 2.5% as at 31 December 2016. It is consequently following the recommendation of its accredited expert, who himself takes account of the advice of the Swiss Chamber of Pension Fund Experts (*CSEP*).

It should be borne in mind that this new cut comes after two successive cuts that were made at the end of 2012 (from 4.5% to 3.5%) and at the beginning of 2014 (from 3.5% to 3%). This situation had not been foreseen when the CPEG was created. It is largely due to the introduction of negative interest rates by the Swiss National Bank and to persistently low interest rates.

The cut to 2.5% at the end of 2016 is due to increased liabilities of CHF 1.45 billion in respect of the active and retired insured members, which led to a corresponding reduction in the coverage ratio (of around 4 points). This effect is purely mechanical and has no bearing on the quality of the Fund's asset management. This cut consequently exacerbates its situation with regard to insufficient capitalisation.

In his expert report of October 2016, the accredited expert at the CPEG justified his recommendation to cut the technical rate by emphasising the necessity of implementing structural measures that will affect the retirement benefit plan with the aim of restoring the financial equilibrium of the Fund in the medium and long term.

Recapitalisation measures: changes to the General Regulations

The CPEG Committee has included a list of recapitalisation measures in the General Regulations for implementation if the Fund were to experience a temporary shortfall (i.e. its assets would no longer enable it to meet its obligations in terms of the coverage ratio)[1].

The main measure involves holding a recapitalisation account. This measure slows down the increase in vested benefits and consequently reduces the future pensions of active insured members. The recapitalisation measures stipulated in the General Regulations are temporary and may be reversed if the financial health of the Fund permits. The measures do not alter the retirement benefit plan.

The amendments to the General Regulations (Article 62A et seq.) entered into force on 1 January 2017, but **they will not be activated unless necessary**, namely if the Fund were to undergo recapitalisation. **This is not the case at present** as the Fund ended its financial year 2016 with a performance of around 5% and a coverage ratio of approximately 57% (based on the technical rate of 2.5%), thereby complying with the statutory requirements in this respect.

[1] We would point out that the CPEG Regulations (Article 29) also specify a measure which provides for the collection of a maximum temporary additional contribution of 1%, half of which is paid by the employer and half by the insured member for 4 years maximum.

Glossary

Pivotal age: retirement age stipulated in the plan (in 2017, 64 years of age for the standard plan and 61 years of age for the hardship plan, and from 2018, 65 years of age and 62 years of age respectively), with no reduction in pension benefits.
Early retirement: optional retirement from 58 years of age with a reduction of 5% to 6% for each year of early retirement based on the pivotal age.
Pension objective: pension entitlement after 40 years of contributions (currently corresponds to 60% of the last insured salary, namely around 50% of the last OASI salary).
Technical rate: interest rate used to calculate the Fund's liabilities in respect of the active insured members (calculation of the leaving benefits) and in respect of the retired members (calculation of the capital required to pay the pensions).
Coverage ratio: relation between the net assets of the Fund divided by its liabilities in respect of all its insured members (active and retired).
Long-term financial equilibrium: equilibrium which the Fund is obliged to ensure with the aim of achieving a coverage rate of 80% as at 1 January 2052. Until then, its growth path must adhere to 6 stages, which are defined in the CPEG Regulations. Its first stage is scheduled for 1 January 2020, the date on which it must achieve a coverage ratio of at least 60%.

Painful but necessary structural measures

In order to guarantee the long-term financial equilibrium of the CPEG, the accredited expert of the Fund recommends implementing structural measures that fall within the competence of the Committee. These measures involve reducing payments by changing the retirement benefit plan. These measures may only affect those insured members who are currently employed as the pensions of current retirees are protected by the federal law (accrued entitlement).

Raising the pivotal age

The Committee is legally bound to adjust benefits in line with the available funds. Hence, the Committee made the first authoritative decision in November 2016: raising the pivotal age. This means that future retirees will have to work for around one additional year to receive an equivalent pension. Insured members who wish to take early retirement at the previous pivotal age (64 and 61 years of age respectively) will of course still be able to do so, subject to a 5% reduction in their benefits.

When the Committee made this decision it took account of the consequences for Fund members. The Committee found that although this measure obliges insured members to work for around one additional year, at this stage it has the advantage of not changing the pension objective in the current retirement benefit plan (60% of the last insured salary, i.e. around 50% of the last OASI salary for 40 years of contributions).

This measure will come into effect on 1 January 2018 (see **Numerical Examples**, p. 4). Insured members aged 58 and over who wish to take advantage of the current plan with the previous pivotal age will be obliged to retire with effect from 30 November 2017 at the latest. They may ask the Fund for comparative forecasts from now on.

The other insured members will be notified in due course in 2017.

It is an authoritative decision that will firstly have to be presented to the meeting of representatives and will then lead to a formal decision in 2017 (see Next Steps, p. 5).

Other measures under consideration

Raising the pivotal age only accounts for a quarter of the changes that are required to offset the cut in the technical rate from 3% to 2.5% and to guarantee the financial equilibrium in the medium and long term according to the latest studies. Other measures will be required and are undergoing an in-depth analysis, including a reduction of the annuity rate, a calculation of pension benefits based on an increase in the early retirement reduction factors or even a reduction of benefits for the children of retirees or disability benefits as well as the potential transitional regime that will be required to implement them.

The consideration of these measures will lead to a decision by the Committee at the end of the first half of 2017. These measures that will supplement the raised pivotal age will enter into force on 1 January 2019 at the earliest, notably to enable the Fund to provide the persons concerned with information that will assist them in making the right decisions.

The Committee is fully aware of the painful effects that these measures will have on its insured members. The Committee will do everything in its power to ensure that the burden is distributed equally between the generations of active insured members as far as possible.

The scale of these structural measures could be reduced by additional funding (contributions, capitalisation). However, this funding is not within the remit of the Committee, but requires a legislative amendment which falls under the sole remit of the Grand Council (see Who decides what? p. 5).

Recapitalisation measures and structural measures: what is the difference?

The Fund is subject to two periodic audits to monitor its financial equilibrium:
- an annual audit, when the accounts are closed, which determines whether the Fund has a temporary deficit as at 31 December of a given year;
- an audit of the long-term financial equilibrium which is conducted every 3 years at least on the basis of an actuarial appraisal which reveals any structural financial disequilibrium.

In the event of a temporary deficit, the Fund Committee must implement **recapitalisation measures**. They are essentially temporary and may even be reversed if the financial health of the Fund so permits and do not affect the retirement benefit plan as such.

In the event of a (structural) long-term financial disequilibrium, the Committee must implement **structural measures**. They are not temporary and have a permanent impact on the retirement benefit plan.
With regard to the CPEG, the actuarial appraisal undertaken by our expert in 2016 revealed a medium and long-term structural financial disequilibrium which was exacerbated by the cut in the technical rate from 3% to 2.5%. Unless the Committee implements structural measures, the Fund will be unable to continue on its growth path and satisfy the legal requirements.
However, on an annual basis at the end of 2015 and at the end of 2016, the Fund is not in a temporary state of disequilibrium and consequently does not have to implement recapitalisation measures.

The next steps for the CPEG

Below is the schedule for the next steps, which was correct at the time of going to press.

From January to April 2017: meetings of the Fund's management bodies together with the accredited expert to specifically address the structural measures:
- consideration of the additional structural measures that are necessary to restore the financial equilibrium;
- consideration of potential transitional measures to accompany such measures;
- preparation of the report on the long-term financial equilibrium for the *ASFIP* (Cantonal Supervisory Authority for Foundations and Pension Schemes - Geneva) and the political authorities.

18 May 2017: **an extraordinary meeting of representatives** is convened to provide preliminary information on the measures selected by the Committee and the details of their implementation (transitional arrangements).

May - June 2017: the Committee formally adopts the structural measures.

1 January 2018: entry into force of the raised pivotal age.

1 January 2019 (at the earliest): entry into force of other structural measures.

Notifications to employers and insured members

We will continue to provide employers and insured members with regular updates through our newsletters and the news published on the website, including:

End of June 2017: publication of *CPEG INFO*, which will provide explanations of the structural measures that are adopted and their effects, the transitional measures and in particular their effective date. The insurance certificate will be dispatched together with the *CPEG INFO*.

From September 2017 onwards: various communication initiatives will be organised in association with the employers to explain the measures adopted by the Committee and their implementation.