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Issues note on the treatment of individual pension trusts

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At the October 2023 meeting of the Advisory Expert Group (AEG) on National Accounts, the treatment of individual pension trusts was discussed, based on the example of such trusts in Australia[1]. The AEG noted the recommendation to treat arrangements similar to those in Australia for self-managed superannuation funds as social insurance type of schemes. However, the AEG also requested the editorial team to refine the proposal after looking at similar arrangements in other countries and considering carefully the potential impact on the accounts of this extension of the boundary for social insurance schemes. This issues note contains such a further elaboration, now also reflecting the arrangements in the United Kingdom and the United States.

Introduction

1 In some countries, the government provides the opportunity to establish individual pension trusts. Here, the question arises whether these individual pension trusts qualify as social insurance. Treating these funds as social insurance has a significant impact on the recording. If they are considered as social insurance, any contribution to the fund, including the investment income on the accumulated funds, would qualify as (imputed) social contributions, while payments out of the accumulated assets would be recorded as social benefits. The liabilities of the trusts and the related assets of households would be recorded as pension entitlements.

2 On the other hand, if the trusts are not considered as social insurance type of schemes, a significant part of the trusts, i.e., the ones which only have one individual or family as beneficiary, would be consolidated within the households sector, unless the trusts is resident in an economy different from the beneficiary. Trusts with multiple beneficiaries would be considered as separate institutional units to be classified as captive financial institutions, while the assets of the households would be recorded as equity. Furthermore, the contributions to the funds would not be recorded as social contributions but as financial investments in either the accumulated assets, or as financial investments in the equity of the trusts in the case the trusts are treated as separate institutional units. Any contributions made by employers for the benefit of their employees would not qualify as employers' actual contributions, but as part of wages and salaries which are subsequently invested in the trust.

[1] See agenda item 12 of the 24th meeting of the AEG, "Note on resolution of outstanding issues" (SNA/M3.23/12).

3 This issues note discusses the treatment of individual pension arrangements in three countries: Australia, the United Kingdom and the United States. For each of these countries, the main features as well as the recording of the relevant schemes are presented, including the main rationale for the recording of such schemes. In the final section, recommendations are put forward for consideration by the AEG.

Australia

4 In Australia, the government introduced compulsory superannuation schemes in 1991, with the idea to provide income in retirement to supplement or replace reliance on the general pension provided by government. A specific part of this policy was the Superannuation Guarantee Act 1992, which created an obligation for employers to pay a portion of employees' income to superannuation funds. Around 1999, once again under government encouragement, saw the creation of self-managed superannuation funds (SMSFs). The initial idea of SMSFs was for the self-employed to establish and manage funds for their retirement (as they would not have employers contributing to their pension funds on their behalf). However, currently many groups of individuals as well as small business have SMSFs. All superannuation funds, including SMSFs, must elect to be regulated under the Superannuation Industry (Supervision) Act 1993, to receive concessional taxation treatment on contributions. SMSFs can have a small number of members (maximum of 6). Generally, the trustees of the funds are the beneficiaries of the fund. SMSFs are regulated by the Australian Taxation Office. Nowadays, superannuation assets amount to 3.5 trillion Australian Dollars, of which 25% relates to SMSFs.

5 Looking at the defining criteria for treating arrangements as social insurance, the individual pension trusts could be looked upon as social insurance, because they provide "insurance" against social risks. Furthermore, one of the three conditions for delineating social insurance, as listed in paragraph 9.67 of the 2025 SNA, can be considered as being met, in this case the second one: "*The scheme is a collective one operated for the benefit of a designated group of workers, whether employees or self-employed persons, which may also include persons temporarily without employment, participation being restricted to members of that group".* In the case of trusts set up by employees, also the third condition may be met: "*An employer makes a contribution (actual or imputed) to the scheme on behalf of an employee, whether or not the employee also makes a contribution*".

6 Importantly, paragraph 9.77 of the 2025 SNA makes clear that arrangements do not necessarily have to be compulsory. Encouragement may be sufficient: "*Social insurance schemes are essentially schemes in which workers are obliged, or* ***encouraged****, by their employers or by general government to take out insurance against certain eventualities or circumstances that may adversely affect their material well-being or that of their dependants*". In a similar vein, paragraph 9.75 of the 2025 SNA states the following: "*Social insurance schemes must be organized collectively for groups of workers or be available by law to all workers or designated categories of workers.* ***They may range from***

***private schemes arranged for selected groups of workers employed by a single employer, private schemes organized for selected groups of self-employed persons, to social security schemes covering the entire labour force of a country**. Participation in such schemes **may be voluntary** for the workers concerned, but it is more common for it to be obligatory*". (In both cases, bolding by the author).

7 However, it should also be noted that in the case of voluntary schemes, to which employers do not make contributions, additional criteria have to be applied, to differentiate them from individual type of insurance policies. This is especially relevant in the case of schemes for self-employed persons. Here, a new paragraph (9.79) has been included in the 2025 SNA: "*Schemes providing social benefits may also be established for groups of self-employed persons. When organized by government, as part of a broader arrangement, such schemes would typically qualify as social insurance. If government is not directly involved, the default option is to not treat such types of schemes as part of social insurance, unless **the schemes are collective arrangements which provide policies, for certain industries or professions, with a strong resemblance to similar arrangements organized by employers or government. These schemes may, or may not, be encouraged by government; in the former case, this would strengthen the case for a classification as social insurance.** In addition, to qualify as social insurance, **generally separate institutional units should be established, which are subject to regulation or supervision in line with or similar to other social insurance schemes**. In the case of pension-related schemes, an additional criterion for the qualification as social insurance is that **accumulated contributions are set aside for retirement income**".* (Bolding by the author)

8 In general, it is argued that the criteria listed in the above paragraph are met for individual pension trusts such as the ones established in Australia, also in the case of trusts set up by self-employed and other self-managed schemes. From an individual's point of view, the purpose of a SMSF is the same as that of other pension funds, except that the individual has full control over the investment decisions. Furthermore, the rules and regulations (and taxation) that apply to pension contributions to and payments from SMSFs are no different in principle to employer or industry superannuation funds. In this respect, one could also argue that the rules and regulations for the operations of SMSFs are very different from the case of an individual who simply buys shares, property, etc. on their own account as an alternative to having superannuation assets.

United Kingdom

9 In the UK, there are various types of pension plans. Most of the workplace related pensions are provided through an employer, but in some cases – particularly for multi-employer occupational schemes and group personal pensions (GPPs) provided by insurance corporations – the employer only facilitates a collective scheme and contributes to it. In addition, there may be individual personal pensions, typically provided by insurance corporations.

10 In general, the workplace related pension plans are considered to meet the criteria of social insurance, in the sense that the schemes are collective and the employer makes a contribution. In this respect, it should be noted that all workplace related pension schemes in the UK are voluntary, so the criterion that participation in the scheme is mandatory is not met. Even in the case of the government's auto-enrolment programme membership is voluntary, because people are entitled to opt out of the collective pension scheme if they wish.

11 The UK situation is somewhat different from the Australian example. For example, in the case of the self-employed persons, where in Australia SMSFs are used, in the UK, there is no special provision, and self-employed persons generally use personal pension plans. It should be noted that there is no obligation in this case – it is a matter of personal choice. There is no direct equivalent of Australian SMSFs.

12 The UK does not consider individual personal pensions as part of social insurance. Instead, individual personal pensions are classified as part of life insurance. In line with ESA 2010, the majority of these personal pensions are treated as individual life insurance. On the other hand, as noted in the above, group personal pensions provided on a collective or obligatory basis, or where an employer makes a contribution, are classed as pensions even if they are provided by life insurers.

13 The UK's Prudential Regulation Authority (PRA) regulates the insurers providing personal pensions (both workplace pensions and individual pensions). These data are collected via Solvency II regulatory data. From these data, the UK ONS is able to separately identify defined benefit and defined contribution individual personal pensions.

14 More generally, the UK does not have a strong preference regarding the treatment of the above pension plans, although they do not see strong reasons for changing the current treatment.

United States

15 The individual pension trusts, as observed in Australia, are very similar to individual retirement accounts (IRAs) in the United States. There are several types of individual retirement accounts, which are financial vehicles for individuals to save for retirement outside of an employer-sponsored plan or the government social security pension plan. IRA plans are available to both those who are not covered by an employer plan and to those who want to augment their retirement savings in addition to their employer-sponsored plan.

16 The U.S. tax code imposes limits on the contributions to these types of plans as well as rules that determine if contributions can be made with pre-tax dollars. Earnings on the plans are not taxed until withdrawn in the future. Again, the tax code sets the rules for how the funds can be withdrawn, including any penalties that may result from early

withdrawal (before age 59 ½) or failure to withdraw required minimum distributions once an individual reaches a certain age. Once an investor reaches age 59 ½, there are no restrictions to how the funds can be withdrawn for traditional IRAs; retirement is not necessary.

17 These plans are treated in the U.S. national accounts in the same way as any other type of individual investment plan. The assets remain in the household sector and distributions from these plans are not captured in the transfer income account. The primary reason for this treatment seems to be the individual nature of the pension arrangements. Although the government clearly encourages these pension arrangements by providing restricted tax incentives to individuals when establishing an IRA, there seems to be no additional characteristics which qualify these schemes as collective arrangements which could be considered as part of social insurance.

General reflections

18 It is not that straightforward to lay out common criteria between the various pension arrangements in the form of individual pension trusts and the like that qualify as social insurance versus those that qualify as (individual) life insurance or individual investment plans.

19 More generally, it can be stated that the application of various criteria for considering a scheme as social insurance, or not, are not truly discriminatory. The payments made under the schemes mentioned in this issues note would generally qualify as social benefits. Furthermore, social insurance schemes do not necessarily need to be mandatory for the participants, participation may also be on a voluntary basis.

20 It all comes down to whether the schemes can be looked upon as collective schemes, or not. In this respect, it is clear that schemes which are purely voluntary and where the "encouragement" by the government is restricted to providing, for example, tax incentives, cannot be considered as social insurance. The same holds for certain groupings of people who join together to get a discount on individual types of schemes.

21 However, such a statement does not provide any positive criteria for distinguishing social insurance type of schemes. This would come down to providing further clarity about the concept of what exactly constitutes a "collective" arraignment. In the case of the Australian arrangements for individual pension trusts for employees, the contributions by the employer represent a clear criterion for considering them as part of social insurance; it is also explicitly mentioned as one of the qualifying criteria in the 2025 SNA (carried over from the 2008 SNA). However, that does not solve the question of how to classify similar schemes to which an employer does not make any contributions. The schemes being very similar to the ones with contributions from employers makes a case for considering them as social insurance as well. Here, similarity should be defined by reference to the exact

arrangements and regulations in place, including the supervision of the schemes, as spelled out in paragraph 9.79 of the 2025 SNA.

22 All in all, it does not seem necessary to change the current guidance in the 2025 SNA. One may only want to add a reference to individual pension trusts and similar arrangements, in the sense that such arrangements may also qualify as social insurance provided the general criteria for social insurance are met.