One of the biggest triumphs of the post-war social accord between labour and capital has been the enormous expansion of old age pensions. In the United States and in several European countries, labour unions successfully bargained for workplace pension plans after the Second World War, while employers embraced these fringe benefits to circumvent post-war wage freezes and attract skilled workers. Workplace pensions thus began to complement existing state provisions for retirement income, such as the State Pension Insurance (Gesetzliche Rentenversicherung, 1889) in Germany or Social Security in the United States (1935), as well as personal pension products offered by the financial services industry. Today, workers’ accumulated pension savings constitute one of the largest concentrations of capital in the world: more than $36 trillion in 2016.¹

The enormous growth in pension capital during the post-war period is not just a function of increased participation. It is also driven by the investment of pension contributions in global financial markets. Traditionally, most pension schemes have been financed on a pay-as-you-go (PAYG) basis, whereby current pensions are paid from current contributions. In those schemes, benefit levels are dependent on the number of people contributing to the scheme and the size of their contributions. In funded pensions systems, on the contrary, contributions are invested in financial markets, and pensions are paid from the return on investment. Funded pensions – whether state, workplace or personal pensions – have therefore become the preferred policy option to cope with demographic pressures and budgetary strains.² As a result, citizens’ retirement income has become tied to fluctuations in financial markets.

Citizens’ increased reliance on financial markets for their old age pensions is part of an aspect of capitalist development, known as financialisation.³ Financialisation refers to an interconnected set of macro-, meso- and micro-social processes that...
Financialisation and the Pension System in the United States and the Netherlands

contribute to «the increasing role of financial motives, financial markets, financial actors and financial institutions» in today’s political economies. At the macro-level, financialisation is associated with new patterns of capital accumulation, whereby the profitability of non-financial firms is increasingly derived from financial sources instead of the production of goods and services. At the meso-level, financialisation is linked to the maximisation of shareholder value as a guiding principle of corporate behaviour. At the micro-level, financialisation refers to the mass consumption of financial products and services, introducing the disciplinary logics of financial markets into citizens’ daily lives. Taken together, the term financialisation thus encapsulates the growing influence of the financial world on the non-financial sectors of the economy and society.

Processes of financialisation, however, have not affected all countries equally. They have been most pronounced in the Anglo-American political economies, where financialisation processes unfolded against the institutional backdrop of highly developed stock markets. Where such institutional proclivities are absent, such as in the bank-based systems of the European continent, financialisation has been more limited. Still, studies have shown that pressures from foreign investors and the changing preferences of domestic political and economic elites have triggered the financialisation of these political economies as well. Germany and France are often mentioned in this regard as cases in point. But the stock market is not the only institutional arena through which financialisation proceeds. Financial products such as home mortgages or capital-funded pensions are other driving forces behind the financialisation process, even in political economies without a highly developed stock market. Taking into account various forms of finance thus paves the way for

a more variegated understanding of financialisation and its impact across advanced political economies.

In this article, the financialisation of the pension system will be further explored. The focus will be on workplace pensions, or the second pillar of the pension system, rather than on state pensions (first pillar) or personal pensions (third pillar). Two distinct points will be argued. First, the cases of the United States and the Netherlands will be presented to show how the financialisation of the pension system has occurred in two political economies with different institutional frameworks. Both the American and the Dutch pension systems stand out internationally for their high degrees of capitalisation and the absence of substantive investment restrictions for pension funds. The two countries differ, however, in the ways in which they have achieved these outcomes. American pension funds began to actively invest their assets according to the tenets of modern portfolio theory as early as the 1950s, while the Dutch funds remained committed to fixed-income asset classes until the late 1980s. In addition, the capitalisation of the American pension system was combined with an individualisation of workplace pension schemes, whereas collective risk-sharing persists in the Netherlands. In both political economies, the pension system is thus highly financialised, yet, the process of financialisation has proceeded along different historical paths and within different institutional contexts.

Secondly, it will be argued that the financialisation of the pension system is accompanied by its own political dynamics. At various points in time, different groups of actors (employers, labour unions, financial professionals) have made claims over the growing concentration of pension assets invested on behalf of employees. Such claims have resulted in a complicated politics of ownership and control. Here, particular emphasis is given to the role of the state. Until the late twentieth century, pension funds invested their assets predominantly in government securities. This arrangement worked to the benefit of both parties: pension funds could invest in relatively safe assets that generated stable returns, while the state had access to reliable long-term investors, who could relieve financial burdens and, in some cases, even serve as «financiers of last resort». For some time, then, public finance was closely intertwined with the finance of (private) pensions.

As the article will illustrate, the relationship between public debt and pension savings has changed in the last quarter of the twentieth century. Due to changing notions of prudence and the booming stock markets of the 1980s and 1990s, corporate equity is now the dominant investment category for many pension funds. Investment in government securities is no longer a matter of course. With increasing size has also come a growing assertiveness on the part of pension funds. As large

institutional investors, pension funds hold considerable financial stakes in corporations and other investment targets. Since the 1990s, fund managers have increasingly leveraged these ownership stakes and pushed for changes in corporate policy, particularly in the area of corporate governance. Governments have not been immune to these pressures: scholarship shows how large investors, including pension funds, circumvent the democratic process by making their investments provisional upon political reforms. These dynamics raise important questions regarding the legitimacy and accountability of pension funds as not just financial, but also political institutions.

The outline of this article is as follows. Part 1 will present three indicators of the financialisation of the pension system: a high degree of capitalisation, a predominance of investment in corporate equities and other «riskier» asset classes, and a shift from defined benefit (DB) to defined contribution (DC) pensions. An overview of ten OECD countries shows how degrees of financialisation differ across political economies. Parts 2 and 3 continue to explore these institutional varieties by analysing the different pathways towards financialisation of the American and Dutch pension systems. A particular focus will be on the interrelationship between private pensions and public debt. The final section of the paper will present some concluding remarks on the complex politics of ownership and control with regard to the enormous concentration of assets accumulated in pension funds as a result of financialisation.

1. The Financialisation of the Pension System – A Comparative View

Financialisation in the area of public and private pension provision is commonly associated with three interrelated developments. First is citizens’ increased reliance on international financial markets as funding source for their old-age pensions. In this regard, we can distinguish between two types of pension schemes. PAYG (pay-as-you-go) pensions are paid from current contributions. For these types of schemes, the demographic composition of the workforce is particularly important: in ageing societies, fewer active workers contribute to the pensions of a growing number of retirees. Pension schemes are capital-funded, when workers' contributions are invested in financial markets and pensions are paid from the returns these investments generate. Rather than being fully reliant on the payment of pension contributions, capital-funded schemes depend on good investment performance in order to ensure the continued funding of workers’ pensions.

As populations are ageing across the OECD, governments have tried to lower citizens’ reliance on PAYG pensions and instead introduce more elements of capital funding in their pension systems. In many countries, reduced benefits and stricter eligibility criteria for state pensions (e.g. a higher retirement age) have been accompanied by policies aimed at stimulating workplace and personal pension savings. Since the 1990s, policy-makers have passed various legislative reforms to increase the size of the second pillar by creating new types of workplace pension schemes (United Kingdom) or financing vehicles (Germany). In some cases, auto-enrolment has been introduced in order to promote participation in voluntary schemes (United States, United Kingdom). Policy-makers have also tried to stimulate participation in personal pension schemes by providing tax incentives (France, Italy) and state subsidies (the German Riester pensions). Finally, some governments have created reserve funds to support PAYG state pensions. The French Fonds de réserve pour les retraites (FRR) and the Canada Pension Plan Investment Board are cases in point. The growing importance of capital funding has greatly benefited the financial services industry, tasked with investing funded pension assets in global financial markets.

A related development associated with financialisation is a shift in the way in which pension assets are invested. Pension assets used to be invested predominantly in fixed-income assets classes (e.g. government and corporate bonds), which generated a predictable and guaranteed return. Conventional wisdom held that pension contributions should only be invested in «safe» asset classes, because employees’ retirement income depended on the return they generated. Such conventional wisdom was supported by quantitative investment regulations, which detailed the maximum percentage of the portfolio dedicated to a particular asset category. Since the 1950s, however, financial professionals have increasingly rejected the idea that a particular asset class is inherently risky. Instead, they adjust the risk level of the entire portfolio of investments to the preferences of the investor. The investment

strategies adopted by pension funds, for instance, will be geared towards the long term, taking into account the future liabilities of the fund (asset-liability management). Legally, these investment practices are reflected in the prudent person rule, which ties the prudence of an investment to the conduct of the investor rather than the outcome of the investment itself.\textsuperscript{20}

The new investment practices described above reflect the growing acceptance of modern portfolio theory. Modern portfolio theory (MPT) is associated with scholars such as Harry Markowitz, who first developed these ideas in 1952. Although first adopted in the United States during the 1950s, in later decades financial professionals in other political economies have also begun to invest according to its central tenets, as the case study of the Netherlands will show. MPT revolves around two main ideas. First is the idea that diversification of assets within the portfolio minimizes the risk of loss. Here, modern portfolio theory makes a distinction between different types of risk: market risk applies to all securities, while nonmarket risk is specific to a particular investment (e.g. a corporation or an industry). By diversifying investments, one can lower the portfolio’s exposure to nonmarket risk. Second is the idea that financial markets work efficiently (the efficient market hypothesis), so asset prices reflect their true value. Investors can therefore never «beat the market»: instead, investors should try to represent the whole market in their portfolio.\textsuperscript{21} Taken together, both ideas – the need for diversification and the efficient market hypothesis – have incentivized financial professionals to invest as broadly as possible, incorporating different asset categories and adopting a passive investment strategy, for instance by investing in index funds.\textsuperscript{22}

A final development associated with the financialisation of pensions is the shift from defined benefit (DB) pension schemes to defined contribution (DC) pension schemes. DB pensions guarantee a particular outcome at retirement, for instance 70 per-cent of the average salary enjoyed during a beneficiary’s career. If the investment return falls short of achieving this outcome, the plan sponsor is responsible for making up the difference. Sponsors can do so by making a lump sum payment or by raising contribution levels. DC pensions, on the contrary, are schemes with fixed contribution rates, but variable outcomes at retirement. The height of the pension is based on the investment returns accumulated during the beneficiary’s career. As a result, the actually enjoyed pension can vary substantially. If investment perfor-

\textsuperscript{20} McCarthy et al., «Investment Preferences and Patient Capital».


mance is poor, the beneficiary will receive a lower pension than expected (and vice versa). In DC pension schemes, the financial risk is thus shifted from the sponsor to the beneficiary. DC pensions are common in the Anglo-American countries, as well as in a number of European countries (e.g. Denmark). 23

It should be noted that the shift from DB to DC schemes does not necessarily reflect financialisation. After all, both DB and DC pension contributions are commonly invested in financial markets. What sets DC schemes apart from DB pensions, however, is that many DC schemes incorporate some possibility of self-investment, meaning that the beneficiary himself can make decisions regarding the investments of his contributions. Self-investment is not restricted to workplace or personal DC schemes. Since 2000, for instance, Swedish citizens select their own funds to invest a percentage of their statutory pension contributions (the Premium Pension). 24 Self-investment requires substantial financial literacy on the part of the beneficiary, a skill that many citizens do not possess. For that reason, UK-policy-makers have provided citizens with limited investment choices, when they introduced new workplace DC schemes in 2010 as part of the National Employment Savings Trust (NEST). In Sweden, citizens may choose one of 800 commercial funds or one of the four government default funds. 25 Such government-imposed restrictions aim to reduce the risk to which beneficiaries are exposed.

Taken together, the three developments described above point to a fundamental shift in the way in which retirement income is provided to citizens in advanced political economies. In addition to the broad shift from state responsibility for pension provision to the private sector, we are witnessing a transfer of risk from the collective to the individual and from the sponsor (the employer) to the beneficiary (the employee). It should be noted, however, that financialisation has not affected all pension systems equally or at the same time. The United States, for instance, was an early adopter of modern portfolio theory, with fund managers increasing their investment in «riskier» asset classes such as corporate equities as early as the 1950s. Yet in a country like the Netherlands, fund managers did not adopt similar investment practices until the 1980s. In other European political economies, such as Finland and Germany, qualitative and quantitative restrictions on certain asset categories (e.g. hedge funds, real estate, foreign assets) remain in place today. Table 1


shows the degree of capitalisation of the pension system; the presence of legal limits on investment in particular asset classes and the importance of DC pension schemes for ten OECD countries.²⁶

**Table 1: Indicators of Pension Financialisation in 10 OECD Countries in 2015**

<table>
<thead>
<tr>
<th>Country</th>
<th>Pension fund assets as % GDP</th>
<th>Legal limits on investment in asset classes?</th>
<th>DC as % pension fund assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>Canada</td>
<td>83,4</td>
<td>No</td>
<td>2,3¹</td>
</tr>
<tr>
<td>Denmark</td>
<td>44,9</td>
<td>Yes</td>
<td>93,3</td>
</tr>
<tr>
<td>Finland</td>
<td>49,4</td>
<td>Yes</td>
<td>0</td>
</tr>
<tr>
<td>France</td>
<td>0,6</td>
<td>Yes</td>
<td>100</td>
</tr>
<tr>
<td>Germany</td>
<td>6,6</td>
<td>Yes²</td>
<td>0</td>
</tr>
<tr>
<td>Netherlands</td>
<td>171,4</td>
<td>No</td>
<td>5</td>
</tr>
<tr>
<td>Sweden</td>
<td>8,9</td>
<td>Yes</td>
<td>–</td>
</tr>
<tr>
<td>Switzerland</td>
<td>123,2</td>
<td>Yes</td>
<td>0</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>99,2</td>
<td>No</td>
<td>32</td>
</tr>
<tr>
<td>United States</td>
<td>79,4</td>
<td>No</td>
<td>441</td>
</tr>
</tbody>
</table>

¹ Workplace plans only ² Pensionskassen only

Source: See Note 26.

The Anglo-American political economies show the highest degree of financialisation of the pension system, as do the European countries with longstanding traditions of funded pension plans (the Netherlands and Switzerland): in these political economies, two or more indicators are present. Pension financialisation is low in traditional Bismarckian pension systems, such as Germany or France, where relatively generous state pensions have prevented the development of strong second and third pillars. At the same time, the table shows that financialisation is by no means an all-or-nothing phenomenon. Both the Netherlands and Switzerland display exceptional degrees of capitalisation, but have low scores on the presence of DC schemes. The opposite is the case for France, which has low capitalisation but shows a dominance of defined contribution pension plans. Only Germany shows almost no sign of financialisation, although recent studies indicate that such processes are taking place in the third rather than the second pillar of the pension system.²⁷ Financialisation is thus a matter of degree.


²⁷ Schmähl, «Germany’s New Pension Policy».
What explains the outsider position of the Netherlands and Switzerland among the European political economies? Both pension systems have a long history of funded, occupational pensions, predating the Second World War. Participation in these occupational schemes is mandatory for large groups of employees. As a result, both pension systems are characterized by high levels of capitalisation. Both countries also score low on the presence of DC pension schemes. However, these numbers may hide actual developments in both pension systems. In Switzerland, occupational pensions are technically defined contribution schemes. Yet, due to the presence of a legally mandated minimum benefit, the Swiss schemes are often classified as defined benefit according to international accounting standards. The reverse applies to the Netherlands: here occupational pension schemes tend to be formally defined as benefit schemes. However, due to the presence of various mechanisms to reduce the eventual benefits of the schemes (including a reduction in pension entitlements in the case of underfunding), the schemes tend to operate as hybrid DB-DC schemes. The exceptional position of both political economies therefore seems to apply predominantly to the high levels of capitalisation and less so to the nature of the pension schemes.

In short, the financialisation of the pension system is reflected in the shift from PAYG to funded pensions in various OECD countries. Additional developments include the adoption of modern investment practices by pension professionals as well as the shift from DB to DC pension plans. Still, our preliminary exploration of pension financialisation in ten OECD countries reveals that not all political economies are affected equally: both the Anglo-American and the continental European political economies with longstanding traditions of funded pension systems show higher degrees of financialisation than other countries. Moreover, whereas the financialisation of the pension system started as early as the 1950s in the United States, it did not affect other funded pension systems such as Switzerland and the Netherlands until the 1980s and is a much more recent phenomenon in political economies with a large PAYG component such as Germany and France.

It is suggested here that the specific pathway a country takes depends on the institutional framework on which the existing pension system is built. In the following two sections, this institutional diversity will be further analysed by comparing and contrasting two cases of highly financialised pension systems: the United States and the Netherlands. Here I build on the Varieties of Capitalism (VOC) approach, which classifies political economies into two broad categories. Liberal Market

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29 P.A. Hall / D. Soskice (eds.), *Varieties of Capitalism*. 
Financialisation and the Pension System in the United States and the Netherlands

Economies (LMEs) are characterized by highly developed financial markets and deregulated labour markets, among other institutional traits. Coordinated Market Economies (CMEs), on the contrary, rely on bank-based rather than market-based finance and generally have a stronger presence of trade unions in highly regulated labour markets. As a result, we would expect more financialised pension systems in LME’s than in CME’s. The remainder of this article will show, however, that this expectation does not hold true when comparing the pension systems of the United States (LME) and the Netherlands (CME). On this point, the current article builds on other scholarship critical of the VOC approach.

2. Financialisation in a Liberal Political Economy – The United States

American workplace pension plans date back to the late nineteenth century, when railroad companies such as American Express first instituted pension plans for their employees. Large manufacturing firms, most notably Carnegie Steel in 1901, followed suit around the turn of the century. Most of these early pensions, however, had strict eligibility criteria and pay-out of benefits was often uncertain. It was not until 1929 that workplace pension first became a contractual right within the Kodak pension scheme. Even then, only a few hundred workplace pension schemes were in existence in the United States. The introduction of Social Security benefits in 1938 had a positive effect on the spread of workplace pensions, as employers hoped to avoid further legislation by offering private benefits. Wartime profit taxes, a few years later, had a similar effect: employers could circumvent such taxes by diverting profits into employee benefit plans. In a tight labour market, workplace pension plans became an alluring means to attract qualified workers and avoid unionisation.30

In 1949, the National Labor Relations Board (NLRB) ruled that employers were obligated to bargain over pensions with unions. The ruling followed the large strike wave of 1945/46, during which unions in the automobile and steel industries, among others, demanded pensions for their members. In 1945, John L. Lewis and the United Mine Workers (UMW) had negotiated a new PAYG pension fund for the coal industry. A few years later, the United Automobile Workers (UAW) union was the first to demand, and win, fully funded pension schemes.31 A few years later, a new kind of pension plan was introduced at General Motors. Unlike most other occupational pension plans at the time, the GM plan was fully funded and managed by professional money managers. Its assets were invested in the stock market, still considered speculative at the time. However, not more than 5 per cent of the assets could be invested in a single company’s stock, including that of the sponsoring


31 McCarthy, Dismantling Solidarity; Sass, The Promise of Private Pensions; O’Barr / Conley, Fortune & Folly.
employer. By adding these rules of diversification, the risk of investing in corporate equities would be reduced.\(^{32}\)

These novel ideas regarding diversification and risk quickly became the new norm for the investment of pension assets. Figure 1 shows the asset allocation of U.S. private pension plans between 1950 and 2014. Whereas fixed-income assets such as Treasury securities and corporate bonds still dominated fund portfolios in the 1950s, these asset classes became less popular in later decades. Instead, corporate equities and, from the 2000s onwards, mutual funds began to dominate private funds’ investment portfolios. State and local government pension funds deviated from these investment practices for much of the second half of the twentieth century. These funds continued to invest predominantly in government securities – Treasury securities, agency securities and municipal securities – until the 1960s, before switching to corporate bonds. Only in the 1990s did public funds reach a similar level of equity investments as the private pension funds.\(^{33}\)

Underlying the shift to the «riskier» asset classes were changes in the notion of prudence that guided fund managers’ investment behaviour. For most of the pre-war period, prudent investment was defined as an «absence of speculation». Speculative behaviour was associated with investment in particular asset classes, such as corporate equity. In 1931, for instance, equities were considered «not investments at all. They are speculation».\(^{34}\) This notion of prudence was anchored in legal statutes at the state level that contained lists of safe – and thus permissible – investments, predominantly fixed income securities. Still, between 1940 and 1970, many state statutes were replaced by a prudent man rule, which held that a plan fiduciary is «to observe how men of prudence, discretion and intelligence manage their own affairs, not with regard to speculation, but with regard to the permanent disposition of their funds».\(^{35}\) Qualified investment restrictions were thereby replaced by a notion of prudence tied to the process of making investment decisions rather than the assets’ perceived level of risk.\(^{36}\)

33 The data presented in figures 2 and 3 are the author’s own calculations, based on the Federal Reserve Board’s Flow of Fund Accounts (multiple years). The data in figure 2 apply to both DB and DC private pension funds. The total assets for each year were computed by taking the total financial assets for each year minus the claims of the pension fund on the sponsor (the unfunded liabilities). Board of Governors of the Federal Reserve System, «Flow of Funds, Balance Sheets, and Integrated Macroeconomic Accounts. Historical Annual Tables», Financial Accounts of the United States (Washington, DC, 2015), www.federalreserve.gov/releases/z1/20160609/data.htm, accessed July 10, 2017.
35 Cited in Longstreth, Modern Investment Management, ii–12.

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34 This notion of prudence was

Source: See Note 33
Alongside changing notions of prudence, both in practice and in legal norms, new ideas regarding risk began to develop from the 1960s onwards. Modern portfolio theory (MPT) held that risk was not inherent to a particular asset class, such as equities or real estate, but should be assessed in light of the whole portfolio. Moreover, mirroring Wilson’s earlier ideas on diversification, its theorists believed the risk of loss could be reduced if the portfolio consisted of different types of securities.\(^{37}\) In 1974, both the prudent man rule and the central tenets of modern portfolio theory were codified in the Employee Retirement Income Security Act (ERISA). ERISA stated that prudence was expressed by acting as a prudent man «in a like capacity and familiar with such matters» would do, namely «by diversifying the investments of the plan» to minimize the risk of loss.\(^{38}\) In addition to regulating pension investments, the legislation imposed strict funding rules and personal liability for plan trustees.\(^{39}\) ERISA applied only to private pension trusts. However, after its passage, many states also incorporated its standards of prudent behaviour into their state statutes. By 1996, only ten states were still using «legal lists» of permissible investments.\(^{40}\)

Since ERISA’s passage, periodic debates on the nature of prudent investment have taken place among various groups in the political economy.\(^{41}\) To financial professionals, prudent investment equalled the maximisation of return. According to them, realizing the highest possible retirement benefits constituted a social good in itself. To make any other consideration when investing pension assets would be a distraction from achieving this benefit. Financial professionals also maintained that financial return was the only objective measurement of investment performance. To add other considerations to the investment decision would introduce subjectivity to the decision process, something that could only lead to a lesser investment performance. Finally, they feared that adding non-financial considerations to the investment decision would tamper with the overall efficiency of capital markets, as they would no longer operate in a free market where risk determined the height of investment returns. As one financial professional stated before the U.S. Congress: «If they are good investments, they will attract capital from people such as ourselves without having to concern themselves with ancillary questions, subjective questions, such as the social consideration.»\(^{42}\)

\(^{37}\) Begleiter, The Prudent Investor; Langbein, «The Uniform Prudent Investor Act».


\(^{39}\) Wooten, The Employee Retirement Income Security Act; Leibig, «You Can’t Do That With My Money».


\(^{41}\) On conflicting notions of prudence in the United States, see Montagne, «Investing Prudently».

\(^{42}\) Testimony of Harrison V. Smith, executive vice president, Morgan Guaranty Trust Company, before the Subcommittee on Citizens and Shareholders Rights and Remedies, of the Committee on the Judiciary, United States Senate, Hearing on
Labour unions, however, have argued that pension assets should not be invested in ways that would hurt workers’ jobs and livelihoods. In 1980, the Industrial Union Department (IUD) of labour federation AFL-CIO conducted a study on the investment of private pension funds. It found that American pension assets ($565 billion in 1979) were not always invested in workers’ best interests. In the previous decade, employer-managed plans had only realized a 4.3 per cent rate of return, well below the 5.9 per cent rate of return for the S&P stock index and below the inflation rate. Moreover, pension assets were often invested in non-union firms or in firms that had moved production overseas. According to Jacob Sheinkman, president of the Amalgamated Clothing and Textile Workers Union and initiator of the IUD study, «Labor loses twice from current pension fund management. In the short run, benefits may be threatened by an inadequate rate of return, and in the long run our own money works to take away our jobs and diminish our overall well-being». Sheinkman thus argued for a more comprehensive notion of prudence that would also take into account the broader social and economic consequences of pension fund investments for American workers.

Employers, meanwhile, believed that they should benefit from pension funds’ performance in the financial markets. Between 1980 and 1989, many American employers used a loophole in ERISA to capture some $20 billion in excess pension assets, affecting more than 2 million workers. Employers used the recovered capital for different purposes. United Airlines, for instance, used the $962 million gained from its pension termination for the purchase of 25 Boeing 737s, while the American Red Cross terminated its pension plan «to use much of the money for related benefits and humanitarian causes». As one corporate officer stated in 1984: «Management saw this essentially unproductive money sitting there and thought it should be put to better use. The officers of a company, after all, have a dual fiduciary duty – to stockholders as well as to employees.» Policy-makers in turn responded to these various claims by insisting that assets could only be invested for the «exclusive benefit» of providing pension benefits, although subsequent interpretations have proved to be more fluid. As a result, a clear legal norm of prudence has failed to develop.

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43 On this debate, see Leibig, «You Can’t Do That with My Money».
49 Montagne, «Investing Prudently».
Another unintended consequence of ERISA has been the growing popularity of defined contribution (DC) pension schemes. Prior to the passage of ERISA, very few employers offered DC pension schemes. ERISA and subsequent legislation, however, made DC pensions more attractive than DB pensions. Minimum funding standards, personal liability for underfunding and mandatory insurance through the Pension Benefit Guaranty Corporation raised the costs of DB pensions. Employees experienced the disadvantages that they could not carry over their pension rights from a DB plan when changing employers. The portability of DC pension proved an advantage in a labour market in which employees no longer worked for one employer for the duration of their careers.\(^5\) In 1978, a new section 401(k) was added to Internal Revenue Code, which allowed employers and employees to make pre-tax contributions to their DC retirement plans. The 401(k) plans proved highly popular among employers and many of them began to replace their DB pension schemes with the new plans. As a result of these developments, the number of private sector workers with a DB pension dropped from 74 per cent of all participants in 1975 to 29 per cent in 2014.\(^5\)

Today, the United States is home to some of the largest pension funds in the world. The Federal Retirement Thrift, the California public employees funds (CalPERS and CalSTRS), and the New York State Common are all in the top-20 of largest pension funds, with almost $1 trillion in assets under management between them. Boeing ($101 billion), IBM ($96 billion) and General Motors ($82 billion) count as the largest single-employer funds in the United States.\(^5\) With sheer size has also come a growing assertiveness on the part of these funds: as major shareholders in American corporations, public and multi-employer pension funds in particular have tried to influence corporate managers’ decision-making – a phenomenon Clark and Hebb have called «corporate engagement».\(^5\) The authors link the emergence of pension fund activism to the propensity to invest in index funds, which prevents them from divesting from a single corporation when dissatisfied with its performance. Corporate engagement may take the form of proxy voting during annual shareholder meetings or private dialogue with corporate executives. It is often aimed at improving corporate governance procedures or related to the corporation’s social responsibility.\(^5\)

Pension funds’ engagement also extends to the public sector. Urban revitalisation projects, for instance, have become an increasingly popular investment object.

\(^{54}\) Van der Zwan, «Contentious Capital». 

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for U.S. pension funds. Financed by special purpose vehicles rather than government bonds, such projects promise relatively stable rates of return while supporting local communities. State and local governments have welcomed these investments, as growing public debt in the wake of the 2008 financial crisis has reduced their ability to fund such projects. Outside the United States, however, pension funds’ public involvement has attracted more controversy. Large American pension funds are wielding their clout over foreign governments to make their financial system more «investor-friendly», which often means modelling it after the American financial system with its strong protections for minority shareholders. The threat of divestment can place a lot of undue pressure on governments in need of FDI, particularly in developing countries. Susanne Soederberg has called this phenomenon «the new conditionality» of global investment, drawing parallels with the often restrictive lending conditions imposed on developing countries by the Washington Institutions.

The growing economic and political clout of America’s pension funds, however, hides the fact that more than half of private industry workers and around 20% of public sector workers do not participate in a workplace pension plan to begin with. Those who do, have seen their savings dissipate as a result of the financial crisis. It is estimated that the financial crisis has led to a loss of at least $1 trillion for private sector DB plans and $1 trillion in public sector plans. Meanwhile, many state and local governments like Illinois, New Jersey and the city of Chicago are confronted with underfunded pension plans and limited fiscal means to make additional contributions. It is estimated that around fifteen states will exhaust their state pension fund assets before the year 2025.

Financial market volatility, however, is not the sole factor contributing to the growing precarity of retirement provisions in the United States. The declining power of labour unions has been proposed as a major factor behind the declining participation in workplace pensions. Workplace pensions have traditionally been most widespread in sectors with high union membership, such as the manufacturing industries. As membership has declined in those sectors as a result of job loss – due to economic contractions or to conscious efforts by employers to replace unionized workers with non-union labour –, participation in workplace pension schemes

56 S.M.Jacoby, «Principles and Agents».
57 S.Soederberg, Corporate Power and Ownership.
has dropped as well.\footnote{Sass, The Promise of Private Pensions.} Labour’s role in the administration of old age pensions has always been limited. The Taft-Hartley Act of 1948 restricted the unions’ role in the governance of private pensions to multi-employer pension funds. ERISA’s emphasis on the maximisation of return, moreover, has prevented the labour movement from directing pension fund assets towards social investment goals.\footnote{Van der Zwan, «Contentious Capital»; McCarthy, Dismantling Solidarity.} As the following section will show, the American case stands in stark contrast with the Netherlands in this regard, where labour unions continue to have a strong role in collective bargaining and managing pension funds.

### 3. Financialisation in a Coordinated Political Economy – The Netherlands

Like the United States, the Netherlands has a mature three-pillar pension system. The first pillar consists of a flat-rate public pension, called the AOW (Algemene Ouderdomswet), for which all those residing in the Netherlands between 15 and 65 years of age qualify. Most Dutch employees – around 96 per cent of the labour force – also participate in a workplace pension scheme provided by their employer. The high participation rate in the second pillar can be explained by the fact that workplace pension schemes are (quasi-)mandatory for most employers and employees. Together with the state pension, workplace pensions account for about 95 per cent of retirement income. As a result, the third pillar, consisting of voluntary personal pensions, has stayed relatively small in the Netherlands.\footnote{Anderson, «The Netherlands».}

The Dutch pension system stands out internationally. In 2015, Dutch workers’ accumulated pension savings stood at 171.4 per cent of GDP, the highest of all OECD countries.\footnote{OECD, Pension Markets in Focus, 9.} High capitalisation can be attributed to the large size of the second pillar, which is fully funded and predates the PAYG-financed state pension by more than half a century. Dutch workplace pensions date back to the late nineteenth century, with a pension scheme for civil servants in place as early as 1814. Although workplace pensions were still relatively rare prior to the Second World War – only 7.5 per cent of working individuals in 1938 participated in an occupational pension scheme – employers began to offer better fringe benefits to avoid the government-imposed wage freezes during the post-war period. Legislation mandating participation in multi-employer funds from 1947 onwards and the introduction of the AOW in 1957 further ensured that most Dutch employees would receive a pension after retirement.\footnote{Anderson, «The Netherlands»; M. Haverland, «Another Dutch Miracle? Explaining Dutch and German Pension Trajectories», in: Journal of European Social Policy 11 (2001), 308–323; E. Nijhof, «Pensions and Providence: Dutch Employers and the Creation of Funded Pension Schemes», in: Enterprise & Society 10 (2009), 265–303.}

Dutch pension funds have faced few investment restrictions. The first piece of legislation that explicitly dealt with pension funds’ investments – the 1952 Pension
and Savings Funds Act – required fund managers to invest their assets in «a solid manner». The Act did not provide a substantive definition of the term «solid», but it was generally understood that single investment categories could not be excluded.65 A monitoring system of post-hoc governmental oversight in combination with transparency rules was set up to oversee the implementation of the solid investment rule. There was one important exception: to protect employees against the risk of the lack of diversification, single-employer funds were not allowed to invest more than 5 per cent of their portfolios in the sponsoring enterprise. This system of pension investment regulation remained virtually unchanged until the introduction of the prudent person rule in 2006, when Dutch legislation was adjusted to EU Directive 2003/41/EC.66

Until the late 1980s, most Dutch pension funds refrained from active portfolio management and invested predominantly in fixed-income assets: government and corporate bonds, direct long-term loans (predominantly to local governments), and mortgages. Only a small part of the portfolio was invested in corporate equities. While industry-wide pension funds invested predominantly in the public sector, company pension funds dedicated most of their assets to the private sector.67 These investment practices reflected the prevailing idea among social partners and policy-makers alike that pension fund assets should be invested as safely as possible, with minimum investment risk, so as not to jeopardize the benefits that ultimately needed to be paid out to the beneficiaries. Still, more restrictive investment regulation to protect workers’ pension savings was not deemed necessary. When the Pension and Savings Funds Act was revised in 1972 and 1980, for instance, the government concluded that a change to the solid investment rule would result in «an unnecessary restriction of investment freedom».68

Dutch pension funds’ asset mix began to change in the late 1980s. The percentage of the portfolio invested in direct loans decreased, while investment in bonds and shares grew to almost 40 per cent by the end of the decade (see Figure 3).69 Moreover, as assets began to grow, the domestic economy became too small to

65 Article 15, Pension and Savings Funds Act. The Act does require that pension funds include a statement on investment policy in their statutes. This means that individual funds are free to set investment restrictions themselves.
67 Author’s calculations based on Pensioen- en Verzekeringskamer, Financiële Gegevens Pensioenfondsen, Apeldoorn, multiple years.
69 Numbers in this table underestimate investment in corporate equity and overestimate investment in fixed-income assets, because public pension fund ABP – which was subject to different investment restrictions until the late 1980s (see below) – is also included in these data.
Several factors account for these changes. Increased participation and higher wages in the post-war period meant an increase in pension funds’ liabilities. Pension funds gradually shifted their investment portfolios towards corporate equity, as the booming stock markets of the 1980s and 1990s promised higher returns. As assets began to increase, moreover, fund management became more complex and pension fund boards increasingly outsourced asset management to external money managers, who followed the central tenets of modern portfolio theory. Pension funds’ more assertive investment practices were further supported by the strict performance standards imposed by the regulator. Pension funds are required to have a minimal solvency rate of 105 per cent of liabilities. Funds that do not achieve this

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70 Pensioenen Verzekeringskamer, Financiële Gegevens Pensioenfondsen; CBS, «CBS Statline».
71 Leading the way were the single-employer funds of large corporations such as Shell, Philips or Unilever, who began to model their investment strategies after Anglo-American institutional investors.72

72 Several factors account for these changes. Increased participation and higher wages in the post-war period meant an increase in pension funds’ liabilities. Pension funds gradually shifted their investment portfolios towards corporate equity, as the booming stock markets of the 1980s and 1990s promised higher returns. As assets began to increase, moreover, fund management became more complex and pension fund boards increasingly outsourced asset management to external money managers, who followed the central tenets of modern portfolio theory. Pension funds’ more assertive investment practices were further supported by the strict performance standards imposed by the regulator. Pension funds are required to have a minimal solvency rate of 105 per cent of liabilities. Funds that do not achieve this
solvency rate risk intervention from the regulator and, for multi-employer pension funds, a suspension of the mandatory extension that ensures participation by all employers within their industry.

Public sector pension fund Algemeen Burgerlijk Pensioenfonds (ABP) has held a special position within the Dutch pension system. For almost seventy years, the fund served as the Dutch state’s lender of first resort. A special committee within the Department of Finance determined ABP’s investment policy. From its creation in the 1920s until the late 1980s, ABP was required to invest predominantly in over-the-counter government debt. ABP benefitted from this arrangement by receiving higher interest rates than it would receive in bond and stock markets, while the Dutch Treasury secured easy access to capital. In anticipation of a common European market in financial services, ABP’s investment restrictions were gradually lifted from the 1980s onwards until the fund was fully privatized in 1996. ABP’s investment practices quickly began to resemble those of other Dutch funds: its equity investments increased from 8 per cent of the portfolio in 1993 to 39 per cent in 2000. In addition, its investments abroad grew to 24 per cent of its portfolio in 1998.

Today, ABP is the third largest pension fund in the world.

Without direct control over ABP, Dutch policy-makers have had to resort to other means to direct pension fund investments towards politically desirable goals. When in 1989, for instance, the third Ruud Lubbers administration (1989–1994) was faced with a record high public deficit, it threatened to impose a 40-per-cent-excise-tax on any pension assets exceeding liabilities after five years if pension funds would not adjust their investment strategies to the government’s political agenda. It thus pushed Dutch pension funds to increase their investments in domestic «good causes», such as housing or environmental projects. In recent years, the Mark Rutte government (2010–2012, 2012–2017) has been actively seeking pension fund investments in domestic home mortgages in order to revive the housing market after the financial crisis. To gain the pension industry’s support for a national investment vehicle that would issue mortgage bonds, the National Mortgage Institution (Nationale Hypotheekinstelling), the government had to promise full acceptance of the risk. Similar guarantees have been provided for pension fund investments in large infrastructure projects.


76 The Rutte administration eventually abandoned the plan for a National Mortgage Institution in September 2015, after the European Commission deemed the governmental guarantees a form of unauthorized state support for the banking sector.

The financialisation of the Dutch pension system has therefore occurred in the context of a coordinated market economy with a high degree of self-governance for the social partners. Pension schemes are part of collective bargaining by employers and labour unions, while pension funds are managed by bipartite boards with equal representation given to employers and labour unions.\(^7\) Although Dutch pension funds have outsourced most of their asset management to external investment firms, the pension fund boards remain responsible for setting the overall investment policy of the fund. Although employers were the first to favour investment in asset classes with higher returns to reduce pension costs, labour unions have similarly embraced such investments from the mid-1990s onwards, despite initial reluctance. The possibility to maintain generous pensions at little or no cost to the employee ultimately rendered even the risky stock market legitimate in the eyes of organized labour. Dutch unions have also led the way in promoting more activist ownership strategies, with both labour federations publishing guidelines for pension fund trustees on proxy voting and socially responsible investment since the late 1990s.\(^7\)

Unlike in the United States, DB pension schemes still dominate in the Netherlands. More than 96 per cent of Dutch employees with a workplace pension participate in a DB scheme.\(^8\) Two factors account for this persistence of DB pension schemes. First, the Dutch pension system affords employees some portability of their workplace pension. When employees change employers or industries, they can carry over their pension rights to a new pension fund (although actual carry-over rates are very small).\(^8\) As a result, employee mobility is not a major factor in changes in pension schemes. Secondly, employer liability for DB schemes is circumvented by the inclusion of separate clauses in collective bargaining agreements that absolve employers from making additional payments in case of underfunding. If a pension fund becomes underfunded, current liabilities will be met by either suspending indexation (the adjustment of pensions to rising cost-of-living) or, in extreme cases, a reduction in pension rights. Since the 2008 financial crisis, many funds have been in this situation. As a result of both these mechanisms – conditional indexation and the possibility to reduce pension rights –, many Dutch workers will no longer receive 70 per cent of their average salary at retirement, but rather a pension that comes closer to 50–60 per cent of their average salary.

78 Retirees are also represented on pension fund boards, however their representatives are considered to be part of the «labour» side of the board.  
81 SEO Economisch Onderzoek, De Praktijk van Waardeoverdracht, Amsterdam 2010.
In short, like the United States, the Dutch pension system is characterized by a high degree of financialisation. It has one of the highest pension savings as percentage of GDP in the world, and assets are invested by professional money managers who follow the tenets of modern portfolio theory. Unlike the United States, however, pension financialisation has not been accompanied by individualisation in the Netherlands: Dutch pension funds are managed bipartitely by employers and labour unions, who are jointly responsible for defining the funds’ investment policy. Moreover, whereas the United States has witnessed a broad shift from collective DB pensions to individual DC plans, de jure average-salary DB pensions still account for the overwhelming majority of all pension schemes in the Netherlands (although de facto such schemes do not result in guaranteed pension benefits). The Dutch case thus shows that financialisation is not just an Anglo-American phenomenon, but can also thrive in the institutional context of a corporatist political economy.

The Dutch case also calls into question the extent to which theoretical approaches such as the Varieties of Capitalism (VOC) approach with its distinction between liberal and coordinated market economies is a suitable framework to better understand these «varieties of financialisation». As the process of financialisation increasingly proceeds in areas outside the realm of the stock market (such as the pension system, consumer finance or home mortgages markets) and with the explicit support of non-financial political coalitions including organized labour, the dichotomy central to the VOC approach no longer seems to provide sufficient insights to understand current developments in the pension systems of advanced political economies. Instead, a more historically contingent approach that explains the preferences of actors central to the pension system – employers, labour unions and the state – in light of new funding needs emerging out of nationally specific outcomes in collective bargaining, public finance and financial market development holds more promise to understand the financialisation of pension systems.

4. Conclusion

Financialisation refers to the growing influence of the financial world on the real economy and society at large. One of the consequences of financialisation is citizens’ increased reliance on financial markets for the provision of social goods, such as housing (mortgages) or education (student loans). The growing importance of capital-funded pension schemes in advanced political economies is another driving force behind the financialisation process. Motivated by ageing populations and budgetary strains, policy-makers across the OECD have tried to decrease citizens’
reliance on PAYG pensions, particularly in the first pillar, and instead promoted capital-funded retirement savings in the second and third pillars of the pension system. Other factors contributing to the financialisation of the pension system are the investment of pension assets in riskier asset classes (e.g. corporate equities) in line with the central tenets of modern portfolio theory (MPT) and the shift from defined benefit (DB) to defined contribution (DC) pension schemes with elements of self-direction/self-investment.

Not all political economies have been equally affected by these developments, however. The financialisation of the pension system is most pronounced in the Anglo-American political economies as well as in the continental European political economies with long traditions of capital-funded pension plans. Yet even among this group, institutional diversity remains. The two case studies of the United States and the Netherlands presented here elucidate this point. Both in the United States and in the Netherlands, the financialisation of the pension system has proceeded through growing capitalisation and the adoption of similar investment practices. Yet, while American financial professionals were early adopters of these practices, the Dutch only began to invest in equities in the 1990s. Moreover, whereas the American employers have embraced DC pensions, Dutch employees still rely predominantly on DB pensions. The continued presence of Dutch labour unions in the governance of pension funds could be an explanation for the differences between the two systems.

The enormous concentration of pension capital raises a number of legal and political questions regarding its ownership. Is it owned by the sponsoring employer? By the state, which indirectly subsidizes pensions through tax exemptions? Or by the employee, the beneficiary of these assets? The answer to these questions is not straightforward and depends on one’s understanding of what a pension really is: an employer’s gift to his employees, a worker’s deferred wage, or a tax-deferred social benefit? Complicating matters even further is the fact that pension funds are managed by fiduciaries – oftentimes a board of trustees – who invest the assets on behalf of the beneficiaries. While fiduciaries are bound by their legal duty to invest the assets prudently, it is not always clear what exactly is meant by prudent investment. Should plan assets be invested to realize a maximum return or may other considerations also be taken into account, such as social or environmental concerns? In neither of our cases does the law give a clear-cut answer to these questions.

The state has not been exempt from the political dynamics described above. The state is involved in various aspects of pension provision. First, most governments fund and operate statutory pension schemes for their residents. They are also large employers, who provide workplace pensions for civil servants. Secondly, states set the legislative and regulatory framework regarding public and private pension provisions, such as ERISA in the United States or the Pension Act in the Netherlands. Thirdly, the state is an issuer of government securities, marketed at investors.
such as pension funds. The three roles of the state in public and private pension provision often overlap. The government’s ability to provide public and civil servants’ pensions, for instance, is highly dependent on the state of public finances, which in turn relies in part on the performance of government securities in capital markets. Yet, the state has a great advantage over other market actors, because it sets the regulatory framework for pension fund investment and can thus influence funds’ asset allocation. Such governmental influence is particularly pronounced when pension funds are bound by quantitative investment restrictions rather than a prudent person rule.

In both our cases, the pension system was historically characterized by a close proximity between the state and pension funds. Particularly public pension funds have performed an important role of purchasers of public debt. The close connection between public debt and pension savings has been facilitated by prevailing ideas on prudent investment as well as by restrictive government regulation preventing investment in other asset categories. Today, however, this interdependent relationship between pension funds and governments has fundamentally changed, as pension funds no longer invest the bulk of their assets in government securities. Two factors seem to underlie this process. The first has been the removal of quantitative investment restrictions for (public) pension funds and subsequent changes in these funds’ investment practices – as early as the 1950s in the United States, in the Netherlands from the late 1980s onwards. The second factor is the increased assertiveness of both private and public pension funds as activist investors since the late 1980s and early 1990s. In contrast to earlier periods, pension funds have begun to leverage their ownership stakes in public corporations as major investors and demand changes to corporate policies.

The growing assertiveness of public and private pension funds as global investors has been controversial. Proponents argue that pension funds help to socialize financial markets by including non-financial considerations in their investment decisions. In this view, pension funds’ corporate engagement might offset some of the disciplinary pressures imposed by shareholder value, although others have identified pension funds as important supporters of shareholder value.3 Proponents, on the contrary, warn that the inclusion of social and political criteria in the investment process could result in lower rates of return and thus damage beneficiaries’ retirement income. They also question the political accountability of pension funds putting pressure on democratically elected governments.4 The emergence of what has become known as «pension fund capitalism» has therefore been accompanied by

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growing tensions between pension funds’ fiduciary role in managing citizens’ retirement savings and their economic and political power as global financial institutions. As more political economies are moving towards funded pension systems and are loosening investment regulations, such tensions are likely to increase in years to come.

Financialisation and the Pension System: Lessons from the United States and the Netherlands

The article explores the financialisation of private pensions in the United States and the Netherlands. It proposes two distinct arguments. First, the article shows that both the American and the Dutch pension systems stand out internationally for their high degrees of capitalisation and the absence of substantive investment restrictions for pension funds. The article posits that both pension systems are highly financialised, yet the process of financialisation has proceeded along different historical paths and within different institutional contexts. Secondly, the article maintains that the financialisation of pension systems is accompanied by its own political dynamics. In both political economies, different groups of actors (employers, labour unions, financial professionals) have made claims over the growing concentration of pension assets. Here, particular emphasis is given to the role of the state. It shows how since the mid-1970s, both American and Dutch pension funds have altered their investment strategies, abandoning public debt as the dominant investment category. The article explains this change in terms of the rising popularity of modern portfolio theory and the immense growth of pension capital in need of new investment options. As austerity politics have made governments more dependent on financial markets, pension funds have become more assertive in leveraging their assets and demanding political reform which are in the interest of the financial industries. Financialisation has thus fundamentally altered the balance of power between the state and financial market actors.

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ABSTRACT
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