Dutch legislation on pension accrual by the self-employed needs to be revised

Dr. B. Dieleman

1. Introduction

Although approximately one out of eight of the Dutch workforce qualifies as self-employed, tax favourable pension accrual by the self-employed is hardly possible. According to the Dutch government this is a problem, because not having a reasonable pension generally results in an undesirable decline of income after retirement. Despite the fact that the government and the labour unions recently agreed to revise the Dutch pension system, there is still no draft legislation to tackle this problem.

In this paper, I analyse the tax favourable pension accrual by the self-employed. The structure of this paper is as follows. In paragraph 2, I discuss whether and to what extent the self-employed have built up a pension and why there is a problem. In paragraph 3, I deal with the relevant provisions of the Pension Act and the related legislation. In paragraph 4, I discuss the tax framework for pension accrual by the self-employed. In these paragraphs, I also discuss the pension related consequences of employees who have been wrongly designated as self-employed. In paragraph 5, I make recommendations for improving the pension accrual by the self-employed, while focussing on improving the effectiveness of existing legislation. Paragraph 6 contains the summary and conclusions of this paper. The attachment of this paper contains an overview of the aspects of the Dutch pension system which are relevant for this paper.

2. Why do we have a problem and what is the extent of the problem?

Although the public debate often gives the impression that the self-employed did not accrue pension at all, this is not the case. Research shows that around 77% of the self-employed have built up a pension, while 87% of all employees have accrued a pension. These percentages do not differ that much. This is among others caused by the fact that many of the self-employed have been employed at some point in their career. For employees, there is often a mandatory participation in an industry wide pension fund.

The amount of pension which is accrued by the self-employed, is generally insufficient. Of those who have accrued a pension, just 28% have accrued a pension that results in (lifelong) retirement benefits of more than € 4,000 gross per year. This while 50% of employees who have accrued a pension, will receive retirement benefits of more than € 4,000 gross per year. Research also shows that the gross replacement rate, being the expected retirement benefits divided by the average gross household

1 The original version of this paper will be published in Tijdschrift Recht en Arbeid in July 2019. This paper has been translated to English and modified for international readers with limited knowledge of the Dutch pension system.
2 Dr. Bas Dieleman is a tax and pension advisor for Loyens & Loeff N.V. in the Netherlands. He is also affiliated to the VU University of Amsterdam.
3 Parliamentary documents 2018-2019, 32 043, no. 457, Principeakkoord vernieuwing pensioenstelsel, par 2.4.
4 Central Bureau for Statistics, White spot on pensions, 2016, table no. 3.
5 Central Bureau for Statistics, White spot on pensions, 2016, table no. 11.
income, is 83% for an average employee and 76% for an average self-employed.\(^6\) While reading these figures, it should be noted that gross household income is determined in particular by labour income. As explained elsewhere\(^7\), there are substantial differences in the Netherlands between the salary of an employee and the remuneration of a self-employed.

It falls out of the scope of this paper to determine whether retirement benefits of € 4,000 gross per year result in sufficient income or to determine which replacement percentage is sufficient. However, the aforementioned percentages show us that, compared to employees, the self-employed do accrue pension less often and if they do so, they accrue less pension. I agree with the Dutch government\(^8\), that this is a problem. After all, having an insufficient pension means that upon retirement, one is faced with an undesirable decline in income. In anticipation of paragraph 4.4, I note that having an insufficient pension is especially also problematic because there are no valid alternatives for tax favourable accrual of income after retirement.

3. The Pensions Act, industry wide pension funds and the self-employed

3.1. Participation in an industry wide pension fund

According to the Pensions Act, pension is an agreement between employer and employee. This implies that in order to accrue pension, an individual must qualify as an employee. According to Article 1 of the Pensions Act, this is the person with an employment contract as referred to in Article 7:610 of the Dutch Civil Code or an appointment under public law. Inherent to the self-employed is that they do not have an employment contract (or public law appointment). This means that in principle, the self-employed cannot accrue pension. However, the self-employed can still fall under the scope of the Pensions Act through article 3 of this act. According to the aforementioned article, this is the case if the self-employed are obliged to participate in an industry wide pension fund.\(^9\)

According to article 2 of the Mandatory Participation in an Industry Wide Pension Fund 2000 Act (hereafter Act Bpf 2000), mandatory participation in an industry wide pension fund is possible, if representatives of both employees and employers file a corresponding request at the Ministry of Social Affairs. Representatives of both employees and employers are in principle free to determine to which part of the workforce of an industry the mandatory participation applies, as long as they represent a significant majority of this part of the workforce. According to the Policy Rules of the Act Bpf 2000, there is a significant majority if representatives of both employees and employers represent at least 60% of the workforce who should participate in an industry wide pension fund. This means that from a legal point of view, one can successfully request that the entire workforce of an industry, including the self-employed, are obliged to participate in an industry wide pension fund.

Approximately 90% of all employees accrue pension through a mandatory industry wide pension fund.\(^10\) However, there are just a few industry wide pension funds which are also mandatory to the

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\(^7\) Boot, G.C., Karakteristieken en tarieven zzp’ers – gevolgen voor de kwalificatievraag, Tijdschrift Recht en Arbeid 2019/35

\(^8\) Parliamentary documents 2018-2019, 32 043, no. 457, Principeakkoord vernieuwing pensioenstelsel, par 2.4.

\(^9\) In a limited number of cases, self-employed accrue pension rights based on the Act mandatory professional pension plans. This falls out of the scope of this paper.

\(^10\) Dutch Central Bank, Number of participants industry wide pension funds, statistiek.dnb.nl, update 20 September 2018
self-employed. Well known industry wide pension funds which are also mandatory for the self-employed, are the pension fund for the painting industry and the pension fund for the construction industry. The vast majority of the obligation to participate in an industry wide pension fund, therefore applies to employees only. In my opinion, there are two probable causes for this. The first is the fear of representatives of both employees and employers that when submitting a request for mandatory participation in an industry wide pension fund for the entire workforce of a certain industry, the legally required significant majority is not met. The second cause is that industry pension funds have taken a wait-and-see attitude because of the pending lawsuit regarding mandatory participation in the pension fund for the painting industry by self-employed painters. The Court of The Hague has recently rejected the claims of the self-employed in this case.\textsuperscript{11} Based on this court ruling, there is no longer a need for the aforementioned wait-and-see attitude.

Mandatory participation in an industry wide pension fund by the self-employed can cause various practical issues. The two most relevant issues are determining the pensionable income and enforcement of the mandatory participation. With regard to the pensionable income, it is inherent to the self-employed that they do not have salary and therefore in principle no pensionable income. Representatives of both employees and employers will therefore have to find an alternative for the pensionable income, which alternative is easy to determine and controllable. Such an alternative preferably moves along with the income fluctuations of the self-employed.\textsuperscript{12} For example, the pension fund for the painting industry uses the taxable profit of three calendar years ago as a minimum pensionable income of the self-employed.

Enforcement of a mandatory participation by the self-employed implies, among other things, that the industry wide pension fund knows the workforce of the industry. However, although self-employed are obliged to register with the Chamber of Commerce, this does not automatically mean that the relevant industry wide pension fund will be notified about this registration in a timely and accurate manner. There must also be a willingness by the industry wide pension fund to trace those who do not participate in the industry wide pension fund, while there is an obligation to do so. In case of mandatory participation by employees, an industry wide pension fund can sometimes turn to one employer for tens or hundreds of employees. However, this is not the case with the self-employed. Enforcement among the self-employed therefore has relatively high administration costs. In the context of enforcement, it is also important to note that if the self-employed do not participate in an industry wide pension fund while there is an obligation to do so, the pension fund can in principle claim pension contributions with retroactive effect of five years.\textsuperscript{13}

### 3.2. Voluntary continuation of pension accrual after termination employment contract

Article 54 of the Pensions Act provides for a voluntary continuation of pension accrual for those who gain business profits as referred to in the Personal Income Tax Act 2001, once their employment contract has been terminated (hereinafter the voluntary continuation). The duration of the voluntary continuation is limited to ten years. Article 54 of the Pensions Act is explicitly written for the self-

\textsuperscript{11} Court of The Hague, 30 January 2019, case no. ECLI:NL:RBD:2019:702
\textsuperscript{13} Hoekstra, C., Zuiderman, T., Bedrijfstakpensioenfondsen, zeg maar nee, dan krijg je er twee?, Pensioen Magazine 2018-116.
employed and other entrepreneurs. Voluntary continuation is possible at an industry wide pension fund, but also at company pension funds and other types of pension administrators. If a self-employed prefers voluntary continuation, he or she must notify the pension fund concerning within nine months after termination of the employment contract. Why parliament has chosen a nine-month period is not immediately clear from parliamentary documents. Perhaps unnecessarily, I note that in the case of a voluntary continuation, the self-employed must pay all pension contributions. In case of an average employee, 2/3rd of the pension contributions is borne by the employer.

Research shows that 85% of the industry wide pension funds provide for a voluntary continuation, although the duration is regularly capped at three years. Limiting the duration of the voluntary continuation is probably related to efficiency considerations by pension funds. Furthermore, the aforementioned research also shows that of all self-employed in the Netherlands, the number of self-employed using the voluntary continuation, is limited to just 650. I suspect that this very limited number is partly caused by the legal requirement that one has to opt for voluntary continuation within nine months after termination of the employment. During this period, many self-employed are probably still in the start-up phase of their business, which limits their financial possibilities.

3.3. Employees who are wrongly qualified as self-employed

The past years, there has been a lot of public debate about whether individuals qualify as employees or self-employed. The Court of Amsterdam ruled on this matter in the case against restaurant delivery service Deliveroo earlier this year. It is beyond the scope of this paper to give a substantive opinion on the court ruling itself, but I will discuss the pension related consequences of this ruling.

As indicated in paragraph 3.1, approximately 90% of all employees are obliged to participate in an industry wide pension fund, while there are just a few industry wide pension funds that provide for mandatory participation by the self-employed. This means that once it turns out that employees have been wrongly classified as self-employed, there is a high probability that there will be a mandatory participation in an industry wide pension fund. As a result, the employer who wrongly stated that he did not have any employees but worked with self-employed workers instead, is obliged to pay pension contributions with retroactive effect of five years. On the other hand, employees can in principle claim pension accrual with retroactive effect without a limitation period. If we translate this to companies like Deliveroo and the ruling of the Court of Amsterdam earlier this year, there is probably a mandatory participation in the pension fund for the transport industry. As a result, Deliveroo may be obliged to pay pension contributions with retroactive effect, while the employees who are wrongly qualified are not.

14 Parliamentary documents, 2005-2006, 30 413, no. 3, elaboration of articles.
15 Dutch Central Bank, pension contributions employee and employer, statistiek.dnb.n/dashboards/pensioenen, 2019
19 The question ‘who has to pay these pension contributions, employee or employer?’, falls out of the scope of this paper.
qualified self-employed, may in due course expect retirement benefits from the pension fund for the transport industry.  

4. Tax framework on pension accrual by the self-employed

4.1. Main features of tax favourable pension accrual

Chapter IIB of the Wage Withholding Tax Act 1964 contains the legislation on tax favourable pension accrual. The most important provision of this chapter is article 18a. This article implies that (lifelong) annual retirement benefits may not exceed 75% of the average pensionable income. These annual retirement benefits in principle start as from the age of 68 and can be achieved after forty years of service. The pensionable income is equal to the salary with a legal maximum of € 107,593 (2019) minus an state pension component of € 13,785 (2019). Such definition of the pensionable income means that pension accrual will be accrued only, if an employee has a gross salary of at least € 13,785 per year.

The pensionable income is based on the definition of salary as referred to in article 10 of the Wage Withholding Tax Act 1964 Act. Inherent to the self-employed is that they do not have a salary. As a result, the self-employed in principle do not pay wage withholding tax, which makes it impossible to arrange tax favourable pension accrual through Chapter IIB of Wage Withholding Tax Act 1964. This means that the legislation regarding the tax favourable pension accrual by employees, is unfit for tax favourable pension accrual by the self-employed.

Tax favourable pension accrual by the self-employed is arranged in the Personal Income Tax Act 2001. The starting point of this tax framework is article 1.7 of the aforementioned act. According to this article, a plan in which one has to participate in as a result of the Act Bpf 2000 as well as a plan that is continued after termination of an employment contract, is defined as a qualifying pension plan. By opting for such a definition, the aforementioned article addresses both options for pension accrual by the self-employed as mentioned in paragraph 3, namely the mandatory participation in an industry wide pension fund and the voluntary continuation.

Participation in a pension plan as referred to in article 1.7 Personal Income Tax Act 2001 means that the yearly pension accrual is not included of the taxable profit of the self-employed. This is mentioned in article 3.13 of the Personal Income Tax Act 2001. Based on article 3.8 of the Personal Income Tax Act 2001, pension contributions paid by the self-employed are deductible from the taxable profit. The final component of the tax framework for pension accrual by the self-employed is taxation of the annual retirement benefits. Article 3.100 requires that benefits related to a pension plan as referred to in Article 1.7 of the IB Act 2001, are fully taxable. This means that the progressive tax rates with a minimum of 16% and maximum 52% are applicable.

4.2. Voluntary continuation

21 Alfen, S., van, Pensioenfonds Vervoer kan beter niet dralen met premie-inning bij Deliveroo, Dutch Financial times, Pensioenpro, 4 February 2019.
22 For an indepth analysis, I refer to Dieleman, B., Neutraliseren verhoging pensioenrichtleeftijd naar 68 jaar, Weekblad Fiscaal Recht 2017/908.
There is an additional tax framework for the voluntary continuation. These additional rules are included in the Decree of 11 December 2018.\(^\text{24}\) In accordance with the Pensions Act, the Decree contains a maximum duration of ten years, while the voluntary continuation must have been requested within nine months of the termination of the employment contract.

The Decree of 11 December 2018 contains various conditions regarding the voluntary continuation. The essence of these conditions is that it must concern a continuation of a pension plan which was applicable prior to terminating the employment contract and that one does not accrue another pension. Voluntary continuation is not allowed for obtaining pension accrual related to past years of service or obtaining an earlier retirement date.\(^\text{25}\) In addition, the pensionable income is based on, among other things, the annual taxable profit of the self-employed. The pensionable income may not exceed the legal maximum pensionable income of EUR 107,593 (2019). Altogether, these conditions imply that pension accrual during the voluntary continuation is limited similar to pension accrual by employees.

### 4.3. Missing legislation

Contrary to the voluntary continuation, the Personal Income Tax Act 2001 does not contain a maximum for yearly pension accrual in case of a self-employed who is obliged to participate in an industry-wide the self-employed. This means, among other things, that pension accrual by the self-employed is allowed to result in annual retirement benefits exceeding 75% of the average pensionable income and that the pensionable income of the self-employed is not limited to EUR 107,593. This is striking because the tax framework for pension accrual by employees as mentioned in Chapter II of Wage Withholding Tax Act 1964 Act, is very detailed.

In theory, the absence of any restriction on the tax favourable pension accrual by the self-employed who are obliged to participate in an industry-wide pension fund, could lead to excessive pension accrual. However, as mentioned in paragraph 3, if the self-employed are obliged to participate in an industry-wide pension plan, this plan also applies to employees in that industry. As a result, this plan needs to meet the requirements of the Wage Withholding Tax Act 1964. This means that despite any legal restrictions, the probability that the self-employed will accrue substantially more pension than employees, is limited.

### 4.4. Alternative for pension accrual by the self-employed

If and to the extent that it is not possible for the self-employed to accrue pension, the self-employed are dependent on a third pillar product if they prefer tax favourable accrual of income after retirement. These third pillar products are private pensions as referred to in article 3.124 of Personal Income Tax 2001. Research shows that just 11% of the self-employed participate in such a product.\(^\text{26}\)

The Personal Income Tax Act 2001 provides for tax favourable private pension contributions with a maximum of 13.3% of the contribution basis. This maximum amount of private pension contributions

\(^{24}\) Decree of the state secretary of finance of 11 December 2018, no. 2017-28514, paragraph 2.3.  
\(^{25}\) Decree of the state secretary of finance of 11 December 2018, no. 2017-28514, paragraph 2.3.  
\(^{26}\) Central Bureau for Statistics, White spot on pension accrual, table no. 6, 2016.
is decreased in case of any pension accrual. The contribution basis is basically the same as the pensionable income as discussed in paragraph 4.1. As a result, the maximum amount of private pension contributions is much lower than the maximum amount of pension contributions. To give an indication; two largest pension funds of the Netherlands currently demand pension contributions equal 24.9% and 25.2% of the pensionable income. This means that private pensions are an inadequate alternative for the self-employed who cannot accrue pension.

As mentioned above, tax favourable private pension contributions are allowed only, if and in so far no pension has been accrued. If pension is accrued retroactively, the Personal Income Tax Act 2001 stipulates that the private pension contributions must be added to the taxable income with retroactive effect as well. The regular personal income tax rates with a maximum rate of 52% are applicable, but there is also a fine equal to 20% of the private pension contributions. Altogether, the tax burden of accruing pensions with retroactive effect, can therefore amount to 72% of the private pension contributions paid.

4.5. Employees who are wrongly qualified as self-employed

As indicated in paragraph 3.3, there is a high probability that as soon as it turns out that employees have been wrongly classified as self-employed, these employees are obliged to participate in an industry wide pension fund. From a tax perspective, two things are relevant. These are the pensionable income and how to deal with accrued private pensions.

Regarding the pensionable income, it is important to remind that the legal definition of pensionable income is related to receiving a salary. However, employees who have wrongly been classified as self-employed, did not receive a salary. Industry wide pension funds will therefore have to derive a salary from the remuneration that the employees have received in their capacity as self-employed. Only if this salary is higher than the state pension component as referred to in paragraph 4.1, there will be pension accrual as well as payment of pension contributions. Subsequently, there are two main options for determining the pensionable income. Firstly, the entire remuneration received in the capacity as self-employed person can be considered as a pensionable income. However, this implies a relatively large amount of pension contributions payable, because a part of the remuneration received, relates to costs that had to be made in the capacity of self-employed person. For that reason, I prefer the second option, which is linking the pensionable income to the taxable profit achieved in the capacity of self-employed in a certain year.

For employees who wrongly qualified as self-employed and who subsequently have accrued a tax favourable private pension in the capacity as a self-employed, it is important to remind that tax favourable accrual of private pensions is allowed only, if no pension has been accrued. This means that if employees have been wrongly qualified as self-employed and this results in mandatory participation in an industry wide fund with retroactive effect for five years, employees may be confronted with a tax penalty of 72% of private pension contributions that have been paid during the last five years. Especially in case the workforce of an industry has little influence on the decision to work as an employee or as a self-employed person, I consider the aforementioned tax penalties disproportionate.
5. Recommendations

As discussed in paragraph 2, the average self-employed has accrued less pension than the average employee. In my opinion, this is undesirable because of the expected substantial decline in income after retirement. However, figures regarding the lack of a sufficient pension by the self-employed do not, in my opinion, justify a general legal obligation for the self-employed to accrue pension. We also do not have such a legal obligation for employees. In addition to this and with referral to paragraph 3, there are already various possibilities for pension accrual by the self-employed, although these options are used too little or not at all. This means that the current legislation is not effective.

Before proposing adjustments to the current legislation, I will mention some relevant considerations. These are as follows. In the absence of a legal obligation for the self-employed to accrue pension, I am sceptical on the proposal of the Minister of Social Affairs on a pension fund specifically for the self-employed.27 In addition, I have concluded that in case of self-employed who are obliged to participate in an industry wide pension fund, there is no legal maximum to the tax favourable pension accrual. I also explained in this paper that if employees have been wrongly classified as self-employed, it is necessary to prevent them against disproportionate tax penalties in case of any retroactive participation in an industry wide pension fund. Altogether, I propose the following measures.

Firstly, I am in favour of encouraging the representatives of both employees and employers to change the mandatory participation in an industry wide pension fund in such a way, that this participation applies to the entire workforce of an industry, including the self-employed. For the time being, the most important issue seems to be the requirement that such a change requires a significant majority as referred to in paragraph 3. A specific amendment of the law could be to use a different percentage to the significant majority than the currently applicable percentage of in principle 60%. For a further explanation, I refer to the paper which I have written recently.28

Secondly, I propose to extend the period as mentioned in article 54 of the Pensions Act and the Decree of 11 December 2018, during which period the self-employed can apply for the voluntary continuation. I envisage a period of for example twelve or eighteen months. As a result, I consider it more likely that the self-employed will have passed the start-up phase and that they will have sufficient financial resources for pension accrual.

Thirdly, I think it is important that a clear and simple tax framework for pension accrual for the self-employed is introduced in the Personal Income Tax Act 2001. There are two main reasons for this. On the one hand, I expect that clear and simple rules will stimulate pension accrual by the self-employed. On the other hand, it is in my opinion not necessary that tax favourable pension accrual by the self-employed, is more beneficial that tax favourable pension accrual by employees.

Fourthly, I am in favour of improving the tax framework for private pensions by increasing the maximum premium percentage of tax favourable private pension contributions. This percentage currently amounts to 13.3% of the contribution basis. As indicated in section 4.4, participation in a

private pension based on the current maximum of 13.3%, results in a significantly lower income after retirement than the accrual of pension.

Finally, industry wide pension funds should try to avoid causing tax penalties for employees who have been wrongly qualified as self-employed and have accrued a private pension. For example, industry wide pension funds could only claim pension accrual with retroactive effect if and so far no private pension has been accrued.

6. Summary and conclusions

In this paper, I have concluded that compared to employees, the self-employed have accrued less pension. However, this difference does not justify a general mandatory obligation for the self-employed to accrue pension. I have also concluded that there is legislation which could make it mandatory for the self-employed to participate in an industry wide pension fund and that there is legislation under which self-employed can continue to build up pension after terminating an employment contract, but that this legislation is not used sufficiently. For employees who have been wrongly qualified as self-employed, there is a high probability that retroactive participation in an industry wide pension fund is required.

The tax framework for pension accrual by the self-employed is unclear and incomplete. This leads to the conclusion that in case of a mandatory participation in an industry wide pension fund, there are no limits to tax favourable pension accrual by the self-employed. To the extent that the self-employed cannot accrue a pension, I have noted that they are dependent on insufficient private pensions. If it turns out that employees have been wrongly classified as self-employed and they have paid private pension contributions, this can lead to disproportionate tax penalties.

To prevent self-employed from being confronted with an undesirable decline in income after retirement, I have proposed four measures in this paper. Those measures concern (1) an incentive to extend the mandatory participation in industry wide pension funds to the entire workforce of an industry, (2) to extend the period in which the self-employed can opt for voluntary continuation, (3) a simple tax framework for pension accrual by the self-employed and (4) an increase of the maximum amount of tax favourable private pension contributions. Furthermore, industry wide pension funds should try to avoid causing tax penalties for employees who have been wrongly qualified as self-employed and have accrued a private pension.
Attachment of ‘Dutch legislation on pension accrual by the self-employed needs to be revised’

This document is an attachment of the paper ‘Dutch legislation on pension accrual by the self-employed needs to be revised.’ The goal of this attachment is to give international readers a better understanding of the aspects of the Dutch pension system which are relevant for this paper.

- The past fifteen years, the Dutch workforce has increased with 13% to 8.8 million.
- The past fifteen years, the number of self-employed has increased with 70% to 1.1 million.
- In this paper, the self-employed are defined as entrepreneurs without employees.
- During the aforementioned period, the number of employees with an employment contract for an indefinite period, has decreased with 5% to 5.4 million.
- In this paper, the definition ‘pension’ is used for ‘occupational pensions’. An occupational pension is defined as income in case of retirement, death of disability, while the accrual of this income is related to employment or self-employment.
- In the Netherlands, pensions and the related assets must be administered by a pension administrator. Pension administrators are strictly supervised by the Dutch Central Bank.
- There are three types of pension administrators; pension funds, insurance companies and premium pension institutions.
- All pension funds are independent legal entities.
- Pension funds administer pensions with a value of approximately € 1,400 billion. Insurance companies and premium pension institutions administer the remaining € 100 billion.
- The average cover ratio of all pension funds is approximately 105%.
- Approximately 80% of all pension plans are DB plans. This implies that the remaining 20% of the pension plans is a DC plan. Industry wide pension funds administer DB plans only.
- Approximately 90% of all employees participate in an industry wide pension fund.
- In the Netherlands, lump sum payment of pensions is not allowed at all.
- The tax treatment of pension accrual in the Netherlands is EET. This means that (1) the employer part of pension contributions is exempt for income tax and wage withholding tax purposes, (2) the employee part of pension contributions is deductible for income tax and wage withholding tax purposes, (3) that accrued pensions are exempt for wealth tax and that (4) retirement benefits are taxed as regular income.
- The paper mentions private pensions. Private pensions are defined income in case of retirement, death of disability, while the accrual of this income is not related to being employed or self-employed. Private pensions are third pillar products.
- The relevance of private pensions is very limited in the Netherlands.
- Besides pensions and private pensions, people who work and/or live in the Netherlands are entitled to a state pension.