

<b>Comments Template on EIOPA-CP-11/001</b> <b>Draft response to Call for Advice on the review of Directive 2003/41/EC</b> <b>Scope, cross-border activity, prudential regulation and governance</b>		<b>Deadline</b> <b>15.08.2011</b> <b>18:00 CET</b>
Company name:	...Confederation of British Industry....	
Disclosure of comments:	EIOPA will make all comments available on its website, except where respondents specifically request that their comments remain confidential.  Please indicate if your comments on this CP should be treated as confidential, by deleting the word Public in the column to the left and by inserting the word Confidential.	Public
<p>Please follow the instructions for filling in the template:</p> <ul style="list-style-type: none"> <li>⇒ <b>Do not</b> change the numbering in column "Reference".</li> <li>⇒ Please fill in your comment in the relevant row. If you have <u>no comment</u> on a question, keep the row <u>empty</u>.</li> <li>⇒ Our IT tool does not allow processing of comments which do not refer to the specific question numbers below.               <ul style="list-style-type: none"> <li>○ If your comment refers to multiple questions, please insert your comment at the first relevant question and mention in your comment to which other questions this also applies.</li> <li>○ If your comment refers to parts of a question, please indicate this in the comment itself.</li> </ul> </li> </ul> <p><b>Please send the completed template to <a href="mailto:firstconsultationiorpca@eiopa.europa.eu">firstconsultationiorpca@eiopa.europa.eu</a>, in MSWord Format, (our IT tool does not allow processing of any other formats).</b></p> <p>The question numbers below correspond to Consultation Paper No. 01 (EIOPA-CP-11/01).</p>		
Reference	Comment	
General Comment	<p><b><u>CBI RESPONSE TO EIOPA'S DRAFT RESPONSE TO CALL FOR ADVICE ON THE REIIEW OF DIRECTIVE 2003/41/EC: SCOPE, CROSS-BORDER ACTIVITY, PRUDENTIAL REGULATION AND GOVERNANCE</u></b></p> <p>1. The CBI welcomes this opportunity to provide initial comments on EIOPA's draft response to the European Commission's call for advice on the review of the 2003 IORP Directive. The CBI is the</p>	

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	<p>premier lobbying organisation for UK business on national and international issues. We work with the UK government, international legislators and policymakers to help UK businesses compete effectively.</p> <p>2. In our response last year to the European Commission’s green paper on pensions, we set out that CBI members do not believe that a review of the IORP Directive is necessary. With 84 per cent of Europeans having no experience of working in another member state and three quarters not envisaging doing so, it is clear that the demand and need for cross-border schemes is very limited. Burdening the vast majority of schemes operating at national level with more regulation just to encourage a handful of cross-border schemes is seriously misguided policy-making. Between 2007 and 2010 the number of cross-border schemes rose, from 48 to 78<sup>1</sup>. This shows that where demand exists the current Directive has sufficed. The Commission acknowledged this in its report on implementation of the Directive in April 2009. It also agreed with the conclusions of CEIOPS Occupational Pensions Committee (OPC) that there was no need for a change in the legislation.</p> <p>3. In last year’s green paper and in this call for advice, the barriers to cross-border activity are stated as being the result of regulatory differences and legal uncertainties in many cases, due to the different implementation and interpretation of the Directive by Member States. The CBI disagrees with that position. The Commission’s 2009 report, by contrast, concludes that diversity in implementation has not caused major problems and that the Directive does not need revising on this basis. Member States agreed with this, as do we. The level of flexibility in implementation and interpretation at national level foreseen in the Directive allows Member States to apply the legislation in the most appropriate way according to national circumstances. A revision, leading to more convergent national implementation would therefore be inappropriate. Furthermore, amending the Directive at this stage would be counterproductive, as this would lead to legal uncertainty, which would not further encourage the development of cross-border pension provision.</p> <p>4. In this response we set out that:</p>	

<sup>1</sup> CEIOPS 2010 Report on Market Developments

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	<ul style="list-style-type: none"> <li>• CBI members believe that the scope of the Directive should not be extended</li> <li>• the lack of consensus around the definition of cross-border activity means no changes should be made at this stage</li> <li>• transparency and good governance are key to achieving better and safer pensions</li> <li>• higher solvency requirements are unnecessary and will slow down the recovery and destabilise capital markets.</li> </ul> <p><b><u>CBI members believe that the scope of the Directive should not be extended</u></b></p> <p>5. The European IORP landscape is a very complex one. IORPs are wholesale products that by the nature of their activity are deeply integrated into national social protection systems and therefore regulated by national social and labour laws. This means that the degree of homogeneity found in the financial services industry across Member States is lacking in IORPs due to their adaptation to specific national necessities according to the social nature of their role.</p> <p>6. While the CBI agrees with the need to ensure that all forms of pension provision are properly regulated, we do not believe a one-size-fits-all approach under the IORP Directive can be the right way forward given this diversity. Across the EU, the general objective of all Member States’ regulatory provisions is the safeguarding of pension beneficiaries’ claims at reasonable cost. How this is achieved, however, differs widely across national regimes. Indeed, national social and labour law may determine the content of the pension promise, set minimum governance requirements, determine the level of sponsor commitment and provide insolvency protection. This is the right approach, as Member States should be given sufficient flexibility to put in place appropriate retirement systems that are reactive to the socio-economic circumstances, needs and desires of their citizenry as well as the employers that fund those schemes.</p> <p>7. Under the current regime, different European legislation governs different forms of provision based on the financial characteristics of the product. In those cases where a particular model is not covered – as can be the case in some newer Member States – social security legislation, both at EU and national</p>	

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	<p>level, fills in some of the supervisory gap. Furthermore, as illustrated in section 8 of EIOPA’s draft response – dealing with the interaction between prudential regulation and social and labour law – any attempt to provide legal clarity on the interaction between the Directive and Member States’ social and labour legislation could easily be a straight violation of the subsidiarity principle. In some new Member States the extension of the scope of the Directive would directly limit those Member States’ competences on social and labour legislation. Thus, any attempt at extending the scope of the Directive to try and create a ‘level playing field’ in retirement provision would not only be extremely complex but would also create legal uncertainty through conflicting pieces of European and national legislation increasing costs for governments, employers and scheme members.</p> <p>8. For all these reasons, CBI members strongly believe that the existing scope of the 2003 Directive should not be extended. However, this policy position is based on the limited information provided so far by EIOPA in this first draft response. Once we have seen the full draft response, our position on this question would be subject to change if higher solvency requirements were to be imposed on funded schemes with an employer covenant. A review of the scope of the Directive might then be necessary to ensure a level playing field is restored.</p> <p><b><u>The lack of consensus around the definition of cross-border activity means no changes should be made at this stage</u></b></p> <p>9. In principle, the CBI could support a clear and widely-agreed definition of cross-border activity if drafted proportionately. At present, however, the lack of consensus around the definition of cross-border activity remains the main obstacle to the further development of pension schemes across different Member States. The legal uncertainty surrounding the definition has meant that employers are sometimes reluctant to set up this type of scheme. As the EIOPA draft response rightly points out, currently the use of different definitions had led to a number of cases where two or more Member States are potentially involved in a cross-border activity have come to different conclusions whether or not the proposed activity is cross-border or not.</p>	

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	<p>10. The proposal included in the draft response does not achieve that level of consensus across Member States. The proposal to amend the definition of ‘host’ member state to reflect the position in respect of location of the sponsoring undertaking does not address all of the outstanding issues currently faced by employers looking to set up these schemes. This new definition would not take into account, for example, the location of scheme members and beneficiaries. This means that while the IORP could be subject to the prudential law of the ‘home’ member state, the sponsoring employer would be subject to social and labour law in the ‘host’ member state. This would lead to different regulatory regimes impacting the sponsoring employer, which ultimately funds the scheme, significantly increasing bureaucratic and financial costs.</p> <p>11. Ultimately, the key obstacle to a broad consensus in the definition of cross-border activity is the heterogeneity of IORPs because of their fundamental social role at national level. As the draft response clearly states, there is no possibility of further promoting the single market on pensions without undermining the subsidiarity principle on social and labour law, a move which is unacceptable. This is why the CBI believes little more can be achieved beyond the current text of the IORP Directive. We would encourage EIOPA to abandon its proposal for a review of the definition.</p> <p><b><u>Transparency and good governance are key to achieving better and safer pensions</u></b></p> <p>12. CBI members believe that there is room for improvement on the area of governance in pensions and we would support action in this area. While some Member States have high levels of good governance we support the development of good practice across the EU to ensure that all Member States provide scheme members with clarity on governance standards.</p> <p>13. Having said that, it is important that any review of governance requirements in the IORP Directive is pitched carefully to ensure it fits the requirements of the sector. For example, under the ‘fit and proper’ requirements of the Solvency II Directive the IORP is required to ensure that persons who effectively</p>	

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	<p>run the scheme are fit to do so, including with regards to professional qualifications, knowledge and experience<sup>2</sup>. This would mean that for many IORPs it would be very difficult to appoint member-nominated trustees (MNTs) who often lack relevant qualifications and skills at the time of application. MNTs are a fundamental part of the check and balances model in pension governance, providing members' with an elected representative in the scheme's governance structure. Training and skills development is offered to them by the employer after their appointment, rather than before.</p> <p>14. Crucially, CBI members' support for a revision of governance requirements in the IORP Directive is entirely dependent on ensuring that any changes are proportional. The recent trend away from defined benefit (DB) schemes towards defined contribution (DC) schemes has been due to the significant increase in costs for sponsoring employers over recent decades. This increase has been driven by demographic changes, but also by an increase in the regulatory burden both at EU and national levels. Employers have been badly burnt by misregulation of pensions. A badly thought through review of governance requirements in the IORP Directive could easily lead to a decrease in the provision of pensions across Europe, hurting employees most. In the UK, for example, from October 2012 all employers will be required to automatically enrol their employees into a pension scheme. Pension providers should be able to offer affordable schemes to all employers, including SMEs. Over-prescriptive European rules on how schemes should be designed and run will simply increase costs significantly leading to a levelling down of employer contributions, from higher levels to the statutory minimum, or the inability of employers to afford them altogether.</p> <p>15. It is right that, as part of the review of the governance requirements, EIOPA should look at ensuring that employers and scheme governance structures carry out their duties appropriately. But it is also important that they do not exonerate the individual saver from responsibility in ensuring his or her pension delivers a good income in retirement. CBI members strongly believe that the best way to achieve good member outcomes depends on member engagement with their pension. Empowering savers is the best way to achieve better and safer pensions.</p>	

<sup>2</sup> Article 42, Directive 2009/138/EC

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16. In DB schemes, member engagement benefits from the schemes' decision-making structure which incorporates trustees with a fiduciary duty. Trustees have a fiduciary duty to act in members' interests, protecting their accrued benefit through prudent management of the funds' reserves and meaningful negotiation with the sponsoring employer. DC schemes are, on the other hand, an entirely different proposition. This is because all of the investment risk lies solely with the member.

17. CBI members believe that good DC provision must be built on the principles of transparency, good governance and flexibility. Transparency, allows individual savers to engage and make informed decisions about their pension. Good governance promotes that necessary transparency as well as ensuring internal controls and appropriate decisions are being made in members' interests. And crucially, flexibility ensures that individual scheme design is tailored to the needs of scheme members encouraging engagement. DC at its best is a partnership. Employers provide financial and administrative support, while employees recognise their responsibility to plan for retirement and make their own contributions.

18. CBI members urge EIOPA to bear all of this in mind when putting forward their advice to the Commission on governance. We would be very concerned about any proposal that goes too far down the regulatory approach. By pushing for over-prescription in DC governance, the Commission and EIOPA risk stifling innovation and the ability of employers to adapt their schemes to the needs of their workforce.

**Higher solvency requirements are unnecessary and will slow down the recovery and destabilise capital markets**

19. While this consultation on the first draft of the EIOPA response does not include a specific reference to solvency rules, CBI members feel it is important to stress our serious concerns in this area, particularly following recent financial events in the Eurozone. While it remains unclear what specific proposals the European Commission might put forward, the imposition of a Solvency II-type regime for pensions is

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	<p>unnecessary and would have disastrous economic implications for the EU and the global economy.</p> <p>20. Applying a Solvency II-type regime to UK DB schemes, for example, would increase existing technical provision levels by up to 85%-90%. This represents up to an additional €500bn (over 15% of the market capitalisation of FTSE350 companies)<sup>3</sup>. DB schemes by the nature of their activity have very long-term liabilities and matching investment strategies. This means that, unlike other financial services products, the financial stability is not affected by short-term economic turbulence and therefore this type of capital buffers are unnecessary. Instead, at a time when sources of credit remain scarce and companies' cashflow have not yet recovered from the financial crisis, forcing companies to divert money away from business investment could do serious damage to the pace of economic recovery in Europe.</p> <p>21. Moreover, increasing funding requirements for pensions would have a serious impact on investment flows in financial markets. Currently, European pension funds hold total assets worth €2,500bn. If they were to comply with Solvency II requirements they would have to hold extra assets worth €1,000bn this would mean they would have to sell equities at about the same value. This would further starve the European private sector of sources of financing, preventing them from growing their business and creating jobs. In the specific case of the UK, pension funds own around 20% of assets in the UK equity market and 25% of assets are in overseas equities, including the EU. Therefore, the cost of the sale of these assets would destabilise both the British and international financial markets at a time when the stability of the economy and financial markets remains fragile.</p> <p><b><u>Like many Member States, the UK already has a robust funding regime rooted in employer-trustee dialogue</u></b></p> <p>22. The UK pensions regulatory system already provides sufficient security for member benefits without the need of higher solvency requirements. The long-term nature of pension liabilities means that DB</p>	

<sup>3</sup> 'Solvency funding in pension schemes: the application of solvency regimes to European pensions', Punter Southall Actuaries (2007)



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	<p>schemes' cashflow are also very long-term.</p> <p>23. When a scheme goes into deficit, the Pensions Regulator's funding regime provides trustees with the necessary powers to force the employer to provide additional funding to repair it. Ultimately, the best form of protection for member benefits is a strong, solvent employer. This is why employer covenant monitoring is a crucial part of the UK's regulatory system. Trustees have the duty to monitor the continuously covenant and are empowered to act when the strength of the covenant varies to ensure the solvency of the pension scheme. The Pensions Regulator is also equipped with anti-avoidance powers to go after those employers that fail to support their pension scheme appropriately. Furthermore, the Pension Protection Fund, funded by employers, is a mechanism of last resort to protect most member benefits in the eventuality of the scheme' sponsoring employer going insolvent.</p> <p>24. The European Commission's attempt to impose higher solvency requirements, or more stringent recovery plan rules, would effectively mean replacing the Regulator's regime, rooted on the strength of sponsoring employers, for one in which the sponsoring employer is weakened as a result of the need for higher funding. We do not believe that the Commission's proposal is better than a system that encourages dialogue between trustees and the employer to ensure not only appropriate funding for the scheme, but also that the employer remains financially viable. During the recession, the worst economic crisis since the Great Depression, the UK's funding regime has shown that it can effectively protect member benefits while avoiding mass insolvencies.</p> <p><b>Employment Affairs Directorate</b>  <b>August 2011</b></p>	
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