	Comments Template on EIOPA-CP-11/001 **Draft response to Call for Advice on the review of Directive 2003/41/EC** ***Scope, cross-border activity, prudential regulation and governance***	**Deadline** **15.08.2011** **18:00 CET**
Company name:	Financial Reporting Council Aldwych House, 71-91 Aldwych, London WC2B 4HN Contact Robert Inglis: +44 (0)20 7492 2356 r.inglis@frc.org.uk	
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
	Please follow the instructions for filling in the template: ⇨ Do **not** change the numbering in column "Reference". ⇨ Please fill in your comment in the relevant row. If you have no comment on a question, keep the row empty. ⇨ Our IT tool does not allow processing of comments which do not refer to the specific question numbers below. o 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. o If your comment refers to parts of a question, please indicate this in the comment itself. **Please send the completed template to *firstconsultationiorpcfa@eiopa.europa.eu*, in MSWord Format, (our IT tool does not allow processing of any other formats).** The question numbers below correspond to Consultation Paper No. 01 (EIOPA-CP-11/01).	
Reference	**Comment**	
General Comment	I am writing on behalf of the Financial Reporting Council (FRC) enclosing our response to your Call for Advice on the review of Directive 2003/41/EC. Unfortunately due to the short timescale provided within which to respond we have been unable to consult our Board and its relevant operating bodies; therefore the points made only reflect staff views on the proposals. Nevertheless, we welcome the	

consultation and are pleased to provide a response.

The FRC is the UK's independent regulator responsible for promoting high quality corporate governance and reporting to foster investment. The FRC supports the UK Government's five principles of better regulation which are that regulation should be:

- transparent
- accountable
- proportionate
- consistent
- targeted – only at cases where action is needed.

We consider that these principles should be considered when formulating new regulations for IORPs.

The FRC supports the thrust of the proposals in the paper which are focused on ensuring high quality governance of IORPs. This mirrors our work in developing and maintaining the UK's Corporate Governance Code (Code). The Code sets out standards of good practice in relation to board leadership and effectiveness, remuneration, accountability and relations with shareholders. We consider that there is a parallel between the intent of the Code and the aim of the proposals in the Directive. We understand that the aim is to ensure good practice in relation to the governance of IORPs, in particular with the leadership and effectiveness of the management board of IORPs, their remuneration and accountability and relations with the members and beneficiaries. We recognise that a key role of the governance system is to ensure an appropriate standard of protection for members and beneficiaries.

The Code contains broad principles and more specific provisions. Listed companies are required to report on how they have applied the main principles of the Code, and either to confirm that they have complied with the Code's provisions or - where they have not - to provide an explanation. We consider that a similar approach would be proportionate for most IORPs given their heterogeneity and the differences in social and labour law within the EU.

EIOPA recognises that IORPs are heterogeneous and also have different characteristics to insurance companies. We understand the rationale for considering how the Solvency II governance requirements could be applied to IORPs, but we consider that EIOPA should be careful in trying to fit IORPs into the Solvency II framework. We recommend that EIOPA considers alternative methods to ensure good governance such as codes of good practice coupled with a "comply or explain" approach which can recognise national differences and be implemented in a more proportionate manner. The FRC would be happy to explain to EIOPA how the Code has worked successfully to improve corporate governance in the UK and explore how a similar approach might be developed to apply to IORPs.

An example of a code of good practice, coupled with a "comply and explain" approach applying to the governance of IORPs, is the FRC's Stewardship Code. The UK Stewardship Code was published in July 2010. It aims to enhance the quality of engagement between institutional investors and companies to help improve long-term returns to shareholders and the efficient exercise of governance responsibilities. It does this by setting out good practice on engagement with investee companies to which the FRC believes institutional investors should aspire. While the Stewardship Code was initially aimed at firms who manage assets on behalf of institutional shareholders such as IORPs and insurance companies, the FRC recognises that the management of IORPS and other owners also have a responsibility for monitoring the performance of the firms in which the invest. The FRC therefore encourages all institutional investors, including UK IORPs, to report if and how they have complied with the Stewardship Code. In order to provide accountability we publish on our website the names of those IORPs who have signed up to the Stewardship Code and provide a link to their compliance statements. We consider that a similar approach might be applied proportionately to the wider issue of governance of IORPs.

There are several thousand IORPs in the UK. While there are several very large IORPs with assets over £1bn, the majority of IORPs are small. The median IORP has assets of little more than £10m. Costs of administering most pension schemes are high and it is essential that any new regulations do not impose disproportionate additional costs on smaller IORPs. We are concerned that the current proposals might have a disproportionate impact on many IORPs.

Paragraph 1.2.6 states that EIOPA would have liked, given more time, to have provided a robust assessment of the impact of its draft advice. We believe that the impact on IORPs needs to be understood before any changes are made. There is considerable concern in the UK about the potential impact of changes to UK pension schemes from EU legislation. Given that the Solvency II requirements for insurance companies are likely to be deferred until 1 January 2014, we would

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	encourage EIOPA to take more time considering the approach to IORPs and to carry out a wider review of possible alternatives including a thorough impact assessment to ensure that any recommendations are effective and proportionate.	
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13.	It is proposed that the requirements of Article 41 of Directive 2009/138/EC are introduced for IORPS but with various modifications. The FRC's mission is to promote high quality corporate governance to foster investment. However a good governance regime must be proportionate and should be targeted so it is effective. There is a risk that the proposals will result in significant additional costs with limited benefit to pension scheme members. We consider that Articles 9 and 14 of Directive 2003/41/EC set out guiding conditions of operation which are a good and sufficient foundation for a governance regime when supplemented by principles based codes of practice. We would suggest that any additional prescription should be introduced only if an impact assessment is carried out and if that demonstrates that the consequent additional costs are warranted. We support EIOPA's proposal that an IORP must remain legally separated from the sponsoring undertaking as currently laid down in article 8 of the IORP directive.	

	We also support its proposal that the governance system should not prevent members' and beneficiaries' participation in the governance structure of the IORP. We consider that the proposal for written policies on certain governance areas which must be reviewed regularly is too prescriptive. We accept that for some IORPs written procedures might be appropriate but for others it might lead to disproportionate costs especially for smaller IORPs. We accept that a sound remuneration policy is in general a part of a good governance system. The FRC's UK Corporate Governance Code recognises this by including a section on remuneration. However, given the heterogeneity in the organisation of IORPs we consider that details are best left to a code of good conduct subject to "comply or explain" rather than prescribed within Level 2.	
14.	It is proposed that the requirements of Article 42 of Directive 2009/138/EC are introduced for IORPS but with modifications. Article 9 of Directive 2003/41/EC states that the institution is run by persons of good repute who must have appropriate professional qualifications and experience or employ advisors with appropriate qualifications and experience. The UK Corporate Code also recognises that the composition of a Board is important for its effectiveness and includes a very similar principle to the current directive that says: *"The board and its committees should have the appropriate balance of skills, experience, independence and knowledge of the company to enable them to discharge their respective duties and responsibilities effectively."* This principle is supported by some further principles and provisions. The UK's Pension Regulator has developed a Code of Practice for trustee knowledge and understanding which sets out standards of conduct and practice for pensions schemes which it regulates and a training module which is available on the internet. These resources support trustees in the governance of UK IORPs. IORPs have different characteristics to insurance companies and different governance approaches may be appropriate. It is not clear to us what the benefit to IORPs and their members would be from the proposed change. We recommend that it might be more appropriate to build on the current wording, perhaps within Level 2, along the lines on the FRC's Corporate Governance Code. We would be happy to work with EIOPA in developing this proposal.	
15.	It is proposed that the requirements of Article 46 of Directive 2009/138/EC are introduced for IORPs	

	but with modifications. Article 14(1) of Directive 2003/41/EC states that the competent authorities shall require every institution located in their territories to have sound administrative procedures and adequate control mechanisms. IORPs have different characteristics to insurance companies and different governance approaches might be appropriate. It is not clear to us what the benefit to IORPs and their members would be from the proposed change. The UK's Pension Regulator has developed a Code of Practice for Internal Controls which sets out standards of conduct and practice for pensions schemes which it regulates. It does not prescribe the format of those controls recognising that governing bodies will develop a process that suits their own needs and requirements. To demonstrate accountability, it encourages IORPs to make a positive compliance statement, within for example the trustees' annual report, confirming that they have considered the key risks affecting their scheme together with the effectiveness of controls implemented to mitigate these risks. The FRC has developed and maintains guidance for directors on internal control, the Turnbull guidance. In a survey, conducted when the guidance was last reviewed in 2004, most respondents indicated that substantial improvements in internal control had been achieved without the need for detailed prescription as to how to implement the guidance. The FRC would be happy to explain the Turnbull guidance to EIOPA and work with you to develop a similar Code appropriate for IORPs. If the proposed changes are introduced, we consider that it is essential that the principle of proportionality applies, particularly to the introduction of the compliance function. Otherwise there is a risk that the extra regulation will result in unnecessary extra costs for smaller IORPs.	
16.	It is proposed that IORPs are required to have an internal audit function. While on the face of it the proposals appear to be reasonable, it would appear likely that it will lead to additional costs in the administration of IORPs. It is not clear to us what evidence there is that the introduction of a specific internal audit function on top of other governance requirements would be of benefit to members of IORPS.	
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