SPEECH

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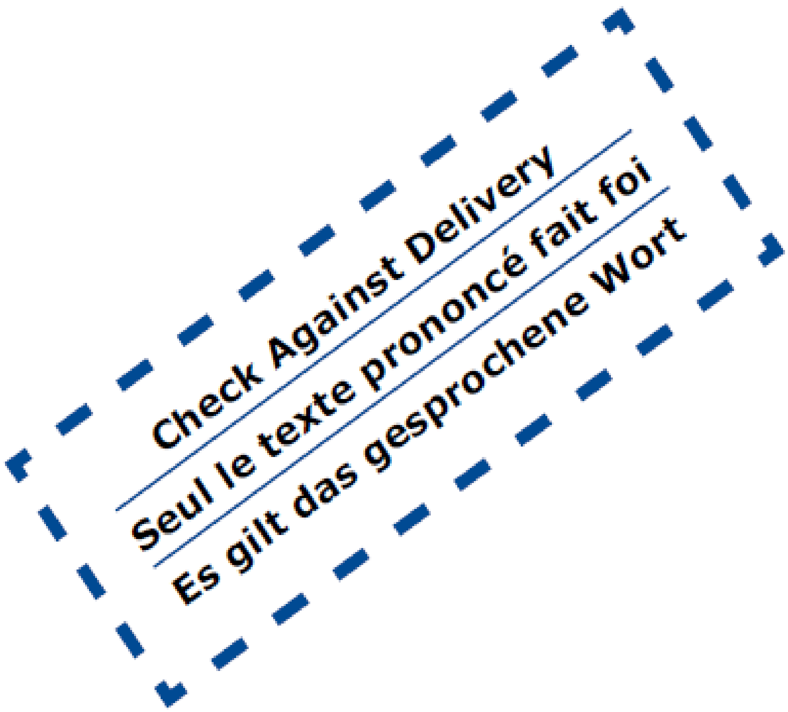
EIOPA's vision on private pensions - Enhanced sustainability, strong governance and full transparency



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Ladies and Gentlemen,

Let me start by thanking the NAPF Chairman Ruston Smith and Chief Executive Joanne Segars for the invitation to speak again at your Conference. As always it is a great pleasure to share my views on pensions with you, representatives of the largest occupational pension market in Europe.

In my intervention today I will talk about EIOPA's vision, strategy and objectives on pensions and how are we delivering and plan to continue to deliver on it.

The pensions' landscape is in constant change, here in the UK and throughout Europe. Pension systems are facing tremendous challenges to deliver on their promises. The longevity growth, the sluggish economic environment, budget deficits and debt burdens, low interest rates and low employment are known factors that contribute to these challenges.

Public pay-as-you-go pension schemes are affected by lower contributions due to higher unemployment and apply further pressure on public finances. Reforms of public pension systems are introduced as part of current initiatives to restore confidence in government finances.

On the other side, private funded schemes are affected by the volatility of asset values and by reduced returns which lower the funding ratios in defined benefit schemes and diminish the ultimate value of pensions paid by defined contribution schemes. These effects are not always transparent to members and beneficiaries contributing to an environment of lack of confidence.

The pensions' landscape in the EU is hugely heterogeneous with a very different role of occupational and personal pension vehicles in the 28 member states.

This reality is a result of different cultures, different traditions, that are understandable, but also a result of different reform timelines and attitudes.

In this context, I want to express my admiration for the unparalleled pace of change in the UK in the last decade. Not only have you acknowledged that we face a real problem, but also you had the courage to act.

And it deserves our appreciation that you understood that reforms in one of the pillars of the pension system should also lead to reforms in the other pillars.

The success of the auto enrolment initiative is just an example of what can and should be done to ensure that citizens will have a chance to maintain appropriate standards of living in their retirement.

But unfortunately, the percentage of the EU population that is covered by private occupational or personal pension systems is still very low.

Faced with this reality we all need to think about what we can do to create conditions to deliver adequate, safe and sustainable pensions to EU citizens?

The priority **goal** for all of us should be to support the further development of private complementary pension savings in the EU, be it 2nd pillar occupational pensions or 3rd pillar personal pensions.

In my opinion, an important **strategy** to achieve this goal is to provide a robust and proportionate EU regulatory framework capable of regaining the trust and confidence of EU citizens in private complementary pension savings.

To achieve this strategy I believe that the regulatory framework needs to deliver on three fundamental **objectives**: **enhanced sustainability**, **strong governance** and **full transparency**.

These are the fundamental building blocks of EIOPA's pensions' vision.

Enhanced sustainability, because the first step to ensure members and beneficiaries protection is to make sure that any pension scheme disposes of sufficient assets to fulfil its liabilities within a realistic valuation scenario.

The QIS that we performed last year showed that pension funds in many member states have vulnerabilities. Local measurements sometimes provide a more optimistic view on pension funds solvency than applying a more realistic measurement.

In these cases, the reliance on future payments by the sponsoring employers is very large. We need to recognise this and assess if this dependence is sustainable in the long run.

Strong governance, because pensions deserve to be governed by fit and proper persons, with the appropriate skills, experience and integrity; because conflicts of interest need to be identified and managed in order to make sure that Board Members act in the sole interest of members and beneficiaries; because strong risk management capabilities and robust internal controls are fundamental to deliver to pensioners the promises made or the expectations created.

Full transparency, because if we want to regain trust of citizens we cannot hide anymore behind "jargon" and difficulties of providing information; we need to provide full disclosure of all costs, be it investment or transaction costs.

In all our work we recognise that pensions are different from other areas.

Pensions are different because of their "embeddedness" in social and labour law; because of their social objectives; because of their particular governance, involving employers and social partners; different because of their unique distribution of risks.

But, in spite of these differences, members and beneficiaries are citizens who deserve adequate protection, who have the right to know the sustainability of the promises that are made to them, who need to understand the risks that they are running, the costs that they are paying, who deserve that pension funds are properly governed and that pension schemes have a high degree of quality.

So pension funds need specific regulation that takes into account these differences and that's what EIOPA has been advocating and practising.

By developing an innovative "Holistic Balance Sheet" approach that takes into consideration all benefit adjustment and security mechanisms, such as sponsor support and pension protection schemes, capturing the specificities of pension funds in the various member states;

By recommending an upgrade in the governance of pension funds, reinforcing the importance of proper risk management and control functions, while applying due proportionality to avoid undue burden and costs to smaller schemes;

By advocating the development of a Key Information Document that should provide standardised information on contributions, costs and charges, investment options and expected benefits.

But also recognising that “too much” information kills information and so that we should adopt a layering approach where members will receive simple and comparable information on the key elements and would have easy access if they wish to access all the other more detailed material.

As a result of all of this work we have now a proposal from the EU Commission to adjust the IORP Directive covering governance and transparency requirements that we very much welcomed.

I am confident that the ongoing and future discussions in the EU Council and the EU Parliament will allow for some further refinements that will contribute to achieve the defined goals, in particular concerning the Pension Benefit Statement.

On the solvency side, we all recognised that further work was needed to develop a robust and tested proposal.

Early this week EIOPA published a consultation paper on further technical work on the holistic balance sheet to gather input from stakeholders. The paper constitutes a further step in EIOPA’s work on a risk-based framework for occupational pension funds. EIOPA is undertaking this work on its own initiative, in its role as independent advisor to the European political institutions.

The consultation paper proposes improved definitions and methodologies to value the holistic balance sheet, covering areas such as the valuation of sponsor support, the benefit reduction mechanisms and discretionary decision-making processes and the definition of contract boundaries.

Most importantly, the paper consults on different possible uses of the holistic balance sheet within a supervisory framework, ranging from an instrument to establish funding requirements to a risk-management and transparency tool to assess the long-term sustainability of IORPs.

The scope of this consultation paper is broader than previous work done by EIOPA in this area. There are indeed various ways to shape a market-consistent and risk-based supervisory framework.

The consultation paper not only considers the holistic balance sheet being used to set solvency capital requirements at the EU level, but also to establish minimum funding requirements and as a risk management tool to assess the sustainability of pension funds.

I would like to emphasise that using the holistic balance sheet as a risk management tool should in my view not be a requirement without consequences.

First of all, the outcomes of assessments should be disclosed to raise awareness about the financial situation of the pension fund and, where necessary, stimulate reforms.

Secondly, if it was concluded that the pension fund is providing unsustainable pension promises, I believe that national supervisory authorities should be empowered to take supervisory action, using a flexible approach.

After all, this is quite similar to the current UK approach.

We are not promoting a EU 'one size fits all' approach. A common prudential regime should have built-in flexibility to deal with a wide range of occupational pension schemes in Member States.

I would like to emphasize that any supervisory framework should in my view be sufficiently flexible to also avoid short-term, pro-cyclical investment behaviour of pension funds during adverse market developments.

It is also essential for me that the holistic balance sheet can be implemented in a proportionate way and without imposing high costs on pension funds. The consultation paper proposes that pension funds with strong sponsors may establish the value of sponsor support as a 'balancing item'. I am convinced that such an approach will considerably simplify the valuation of the holistic balance sheet for a large share of UK pension funds. In addition, it provides the right incentives by requiring pension funds with weak sponsors to do more detailed assessments.

The further work on the holistic balance sheet has to be tested through a quantitative assessment. EIOPA expects to publish draft technical specifications for such an assessment by early 2015.

Our final aim is to deliver robust, tested proposals to the EU political institutions by the end of 2015, beginning of 2016.

I want to thank all stakeholders for the level of engagement and contributions received in our previous consultations, many of them coming from the UK pensions market.

I believe that we showed that we take consultations seriously and that we are ready to listen, discuss and evolve in our proposals, remaining faithful to our vision, but using pragmatic and proportionate solutions.

Please continue to engage with us in this important consultation. Your views, positions and suggestions will be duly considered and will increase the quality of our work and its adherence to reality.

EIOPA is now preparing a pensions stress test. We are taking a two-stage approach: preparatory work in 2014 and running the stress test in 2015.

Our aim is to develop a stress test framework that is appropriate and suitable for pension funds.

An important part of the preparatory work is to gain insight in the role of IOPR’s in financial stability. To analyse transmission channels of IORP’s to financial markets, EIOPA will soon start a data collection exercise covering a sample of defined benefit, hybrid and defined contribution schemes in member states with a significant IORP sector, including, of course, the UK.

This exercise will allow us to assess the pro-cyclicality of pension funds investment behaviour during the past decade, including the financial crisis in 2008.

We would be very grateful for the participation of the UK pension funds in this exercise.

The stress test will assess the resilience and the behaviour of IORP’s in adverse market developments, such as a prolonged low interest environment or a sudden material reassessment of risk premia. It will also incorporate stresses in longevity as one of the major risks in pension funds overall financial condition.

Our intention is that the pension stress test will cover IORP’s that provide defined benefit schemes as well as the ones that finance hybrid or defined contribution plans. We will conduct the stress test in parallel with the quantitative assessment on the solvency side in order to avoid the duplication of calculations. This will limit to the extent possible the burden on pension funds and supervisory authorities.

But our work on delivering on the three objectives mentioned before is also more and more focused on defined contribution plans.

We are looking at costs and charges in the occupational defined contribution world and at different best practices to establish default options.

We will explore how the development of simple, standardised and fully transparent personal pension products could also help to reduce costs and mitigate mis-selling. We will be keen to find a proportionate regulatory treatment for these products to ensure that there are no “excessive burdens” placed on market participants.

We will do all of this by engaging with the experts of all 28 member states, including, of course, The Pensions Regulator, who has been instrumental in our work by bringing to our table the experience of regulating and supervising an important pensions market.

We will continue to involve our Occupational Pension Stakeholder Group that gives an excellent contribution to EIOPA, by providing advice and challenge in a cooperative way.

We will continue to engage with all stakeholders in a clear and transparent manner.

To conclude,

Creating sustainable and adequate pension systems is one of the major challenges for Europe in the coming years. Where Pillar 1 is scaling back, Pillars 2 and 3 need to step in. At the EU level EIOPA will continue contributing to the ultimate goal that every EU citizen has trust and confidence in his private pension scheme.

I have hopefully proved to you that we are committed to achieving this objective, just as the UK pension reforms have proven to Europe that having the courage to act pays off.

Creating a sustainable and adequate pension system is a goal worthy of efforts, yours and ours, for the benefit of society, the economy, citizens and businesses.

I want to finalise by paying tribute to one of the major exports of the UK and in particular the city of Liverpool to the global world. No, it's not pensions, nor the football of the glorious Liverpool team of some decades ago where, as a youngster, I saw Ian Rush and Kenny Dalglish destroying my club (Benfica) in successive European Champions Cup games. No, it's the Beatles!

What is impressive is that when you look at the Beatles songs they have a lot in common with today's subject – pensions.

We need to "Come together" to achieve realistic valuations of IORP's liabilities. But, "With a little help from my friends" it was possible to find a pragmatic way to value sponsor support.

To achieve success on this journey it will probably be "A long and winding road" with a lot of "Twist and shout", but "We can work it out".

One would hope that success for everyone would see our future beneficiaries "When I am 64" looking at their retirement future thinking "Here comes the sun". Please "Don't let me down".

Thank you.