EUROPEAN INSURANCE AND OCCUPATIONAL PENSIONS AUTHORITY

KEYNOTE SPEECH

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European pensions: regulatory achievements and the way forward

Check Against Delivery
Seul le texte prononcé fait foi
Es gilt das gesprochene Wort

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Ladies and Gentlemen,

Let me start by thanking PensionsEurope and particularly Joanne and Matti, for your kind invitation to speak at this conference. I am particularly delighted to see here many people with whom EIOPA has long been engaging and discussing the European pensions system, also in the context of EIOPA's Occupational Pensions Stakeholder Group.

In my remarks today, I will share with you EIOPA's vision of European pensions and will relate it to those regulatory achievements that have been made so far.

I will also focus on the current activities and working plan of EIOPA in the area of occupational and personal pensions. And finally, I will elaborate on some challenges going forward.

EU pensions landscape of today

The European pensions landscape of today reminds of an impassable forest with diverse flora. Pension reforms in the Member States were conducted with various purposes, which in its turn has resulted in very divergent roles of public, occupational and personal pension vehicles in each of the 28 Member States. Furthermore, pensions tend to be embedded in national social and labour law, which makes them different from other products. Some countries have a strong second pillar of occupational pensions, others have built up more third pillar private pensions and a quite a number of countries have yet to develop strong complementary pension systems beyond the public pay-as-you-go social security regimes.

The situation is aggravated by the demographic and economic factors. The ageing of population in the EU might cause intergenerational conflicts, in 30 years or so, when the number of pension beneficiaries will dramatically exceed the number of active workers. And the younger people will no longer be in a position to finance the retirement of their grand-parents' and parents' generation.

The protracted low interest rate environment forces pension funds to increase contributions and, in some cases, to lower the nominal value of pensions. Shifting the risks to employees by switching from defined benefit (DB) to defined contribution (DC) schemes has already become a global trend.

And finally, despite the increasing mobility of the work force within the EU, there are very few cross-border pension funds. Around 6.6 million EU citizens live and work in a country other than their own. A further 1.2 million live in one EU country but work in another one. However, in the whole EU there are only 75 cross-border IORPs that are active. The national prudential regimes are often tailored to the domestic situation and are simply unable to cope with pension arrangements in other EU countries.

EIOPA's vision is to grow this wild forest into a fertile field. Where promises made to members and beneficiaries are fulfilled at any time; where employees can easily transfer their pension rights when changing their country of work; and where EU citizens have a chance to maintain appropriate standards of living during their retirement.

The regulatory activities should be focused on both the second and the third pillar pensions. In this context, the EU should build a robust and proportionate regulatory framework, which delivers on three fundamental objectives:

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.

The second objective is **enhanced sustainability**, because the first step to ensure members and beneficiaries protection is to make sure that any pension scheme holds sufficient assets to fulfil its liabilities within a realistic valuation scenario.

And finally the third regulatory objective **is full transparency**, because if we want to regain trust of citizens we cannot hide anymore behind "jargon"; we need to provide full disclosure of all costs, be it investment or transaction costs; we need to give members and beneficiaries a full picture of the returns that they get on their pension products. And we need to do this in a simple and standardised manner, not flooding members and beneficiaries with hundreds of pages. Too much information kills information.

EIOPA regulatory work

In this context I would like to update you on what has been done by EIOPA in the area of pensions. We delivered to the EU Commission an extensive advice on the review of the IORP Directive, including a sound basis for enhanced governance and better transparency, taking into account due proportionality. EIOPA awaits the political negotiations on the IORP II Directive and stands ready to ensure appropriate consistency in the correspondent supervisory process.

Let me now focus on our current work on pensions:

Quantitative assessment

During the past years we have adopted a consistent approach towards the analysis of solvency issues in occupational pensions. In 2013, in the final report on our first Quantitative Impact Study on pensions, we concluded that further work was needed on methodologies for the valuation of the holistic balance sheet (HBS) and the definition of supervisory responses. This conclusion was in line with the concerns expressed by the stakeholders who did not have a clear understanding on how the HBS could be put in practice. The European Commission decided not to include solvency rules in its IORP II proposal, also concluding that more technical work was needed.

In 2014, on its own initiative, EIOPA conducted further work by consulting on proposals on the use of the holistic balance sheet and possible supervisory responses, with a focus on the valuation of technical provisions and sponsor support. These proposals were issued for public consultation, which I think demonstrated that we are listening very well to the suggestions of the pension fund sector:

- We took a **more principles-based approach** to the valuation of the HBS, instead of a one-size-fits-all approach.
- We proposed **various simplifications** for the HBS valuation, such as the balancing item approach to the valuation of sponsor support;
- We discussed **various possible uses of the HBS** and underlying supervisory frameworks, such as an instrument to set funding requirements and a risk management/transparency tool to assess the sustainability of IORPs.

Already during this public consultation we made it clear that the new valuation methodologies and possible uses of the HBS have to be tested through a quantitative assessment. Consequently, in May 2015, in order to further assess the appropriateness of our proposals and collect the necessary evidence, we launched the quantitative assessment exercise. After its results are analysed, EIOPA will develop an Opinion, which we are going to deliver to the EU institutions in March 2016.

Stress test for occupational pensions

In order to limit the burden on IORPs and supervisors and to avoid the duplication of calculations, we decided to conduct the quantitative assessment in parallel with the pensions stress test. We have the same templates for both exercises so participants need to fill them in only once.

Conducting both exercises together has another strategic objective: the EU law requires EIOPA to "develop common methodologies for assessing the effect of economic scenarios on an institution's financial position". In my view, the holistic balance sheet (HBS) is an appropriate tool to make the impact of the stress test comparable between IORPs in different countries by taking into account their specific security and benefit adjustment mechanisms. I am convinced the EU needs a methodological tool like the HBS to get a transparent view of the financial position of pension funds and to identify the pensions sector's risks and vulnerabilities.
We will continue to refine the methodologies in order to have a robust basis to do stress tests.

EIOPA, in cooperation with the ESRB, designed a stress test that considers the key vulnerabilities of pension funds. The two adverse market scenarios analyse the effects of a prolonged low-interest rate environment (i.e. resulting in a lower risk-free interest rate curve) together with an instantaneous fall in asset prices. Moreover, we have included a stress scenario analysing a further increase in life expectancy.

Here, I would like to express my appreciation to PensionsEurope for their engagement and cooperation. I am convinced that thanks to the discussions EIOPA had with you and other stakeholders, we managed to make our specifications clearer and more streamlined, which perhaps has prevented some unnecessary questions during the running of the exercises.

The objective of the stress test exercise is to test the resilience of DB and hybrid pension schemes to adverse market scenarios and an increase in life expectancy as well as to identify potential vulnerabilities of DC schemes. The stress test will provide insights and raise awareness of the occupational pensions' sector risks and vulnerabilities, while potential transmission mechanisms of IORPs to the rest of the financial sector and the real economy will also be evaluated.

The objective of the stress test is not to review funding or solvency standards. The vulnerabilities identified will be part of supervisory conversations between the pension supervisors and the pension funds and should also be part of risk management considerations. The stress test is a supervisory and risk management tool.

Pension funds that provide defined benefit or hybrid schemes will need to calculate the impact of the stress scenarios on their national balance sheet as well as the holistic balance sheet. Pension funds providing defined contribution plans are asked to evaluate the effect of shocks on future retirement benefits of three representative plan members: one young plan member having 35 years before retirement, one of middle age (20 years before retirement) and one having just 5 years before retirement.

The stress test has been designed for the countries where the IORP sector exceeds 500 million euros in assets. So the majority of the EU member states fall within this scope. In general we expect to achieve coverage of 50% of the pension fund sector in each participating Member State.

The exercise is conducted in close cooperation with the national supervisory authorities (NSAs). NSAs identified and contacted prospective participants in the stress test and are the sole point of contact for pension funds.

EIOPA supports industry participants by carrying out a Questions & Answers (Q&A) process and publishes weekly updates on its website. On 19 May, we also held a workshop for participants in order to provide them with practical information for completing the templates. After summer, EIOPA is going to conduct the centralised quality assurance of all the submissions in order to ensure consistency of the results between and within the Member States.

The report on the pensions stress test will be published by the end of this year.

Let me assure you that EIOPA is aware of the sensitivities among stakeholders with regard to the quantitative assessment and pensions stress test. I am sure that we can count on all your work to have a successful completion of both exercises. It is essential to have reliable information in order to objectively view the vulnerabilities of the pensions sector and to provide the EU institutions with relevant advice on how to improve the supervisory process to ensure the sustainability of pension promises.

Personal pensions

In the area of personal pensions our work is also ongoing. Following the publications of our Discussion paper on a possible EU-single market for personal pension products and Preliminary report "Towards an EU single market for personal pensions", EIOPA received last year a Call for Advice from the Commission with a view to support the development of an EU-wide framework for personal pension products.

In EIOPA we welcomed this call for advice because the personal pensions market across Europe is fragmented mainly due to varying approaches to pension provisions, national taxation differences etc. It is clearly high time to assess the opportunities and the potential of a common EU approach towards personal pensions.

The consideration of the relevant regulatory possibilities has been the focus of our work for already some years.

Currently we are exploring how the development of a **simple, trustworthy, standardised and fully transparent personal pension product** could help to reduce costs and mitigate miss-selling. We are also keen on finding a proportionate regulatory treatment to these products to ensure that there is no “excessive burden” for market participants.

In a few weeks’ time we are going to launch a public consultation about the “Pan-European personal pension product”.

In personal pensions we still have a fragmented market and no common EU approach. So the creation of an effective Pan-European Personal Pension Product will require a constructive approach from Member States and from the different sectors that might offer personal pensions.

The development of such a pan-European product aims at higher levels of retirement income and **pension adequacy** and at the same time has the potential to **contribute to the Capital Markets Union by fostering the supply of long-term capital**. As such, it will present another possible source of long-term investment for the European economy, its growth and creation of jobs.

EU citizens will benefit from more standardized and simple retirement savings products. This relieves consumers from in-depth analysis of investment strategies and different financial instruments.

Developing a Pan-European Personal Pension Product will increase consumer protection, transparency and improve the outcomes for citizens. Pension providers shall be enabled to offer more cost-effective products EU-wide which will allow for successful cross-border selling. Thus, a single market for personal pensions will be advantageous not only for consumers and providers, but for the broader EU economy.

Once EIOPA publishes the consultation paper, I would like to encourage all of you to share with us your views. Every opinion matters if we intend to build up something innovative for the EU and at the same time something beneficial for each EU citizen.

Transparency and disclosure

Another regulatory area I would like to mention is our work on transparency in the pensions area. Already back in 2012, EIOPA took its first step towards standardization by suggesting to the European Commission the introduction of a standard Information Document, which would contain the most essential information for future and current scheme members. I am convinced that such a document providing a clear picture of costs, charges, investment choices and performance will be a huge step towards more transparency and confidence in the area of occupational pensions. And the future scheme members will be put in a position to take informed decisions.

We have already made another step in this direction by carrying out a fact-finding mapping exercise on existing practices and approaches in Member States in respect of costs and charges borne by members and beneficiaries of IORPs. The results of this exercise were published in the beginning of 2015, in our Report on Costs and Charges of IORPs. Costs and charges are a key issue when considering the affordability of saving for one’s retirement. In our view, it is essential that costs and charges within the value chain are disclosed in a transparent and comprehensive way to the parties bearing them. Those parties need to be enabled to assess if the costs and charges they are paying is conducive to good value for money.

EIOPA will take further steps to address this issue taking due note of the national initiatives that have already proven effective in this field, taking into account the specificities of the pensions systems.

Another important element that needs to be further developed is the disclosure issue. It is also crucial for our work to look into the provision of information to members and beneficiaries more in general. High quality information at inception, during the accumulation phase and prior to retirement is paramount for consumer protection. It is necessary to look at information provision from the perspective of an ordinary person and not of an expert who perfectly understands the technical "jargon" of the industry. In our Report on Good Practices relating to the provision of information for Defined Contribution schemes we encourage pension providers (and their regulators) to base their policies on behavioural economics and provide recommendations on how information can be structured and presented to help scheme members make appropriate financial decisions.

The Consumer Protection and Pensions' Experts from EIOPA and NCAs are working to analyse the channels and tools of communication used by occupational pension schemes and employers in order to reach their members. In due course we will make our findings public.

Future role of EIOPA

You have now a detailed overview of what EIOPA is currently doing in the area of pensions. But in order to make a picture more objective, I would like to zoom out and share with you my vision of EIOPA in future.

We have been working on reviewing the EU regulatory framework (Solvency II and IOPR II). But good regulation remains just a first step. The real test will come when this regulation is implemented across the EU. And here I see EIOPA's main responsibility in developing a European supervisory culture and ensuring that the supervisory practices are implemented in a consistent way throughout the EU.

Knowing the current different supervisory cultures in the Member States you would agree with me that this is a huge task. Our vision is to build EIOPA as a credible supervisory authority within the European System of Financial Supervision. We are focused on adding value to the overall supervisory process in the EU, using our unique position to upgrade the quality and consistency of national supervision and strengthen the oversight of cross-border institutions. We believe that it is of the interest of the insurance and pensions market to have a strong European supervisor that fosters consistency of supervision and strengthens consumer confidence.

EIOPA has been instrumental in delivering the desired outcomes for the implementation of the insurance framework Solvency II and the same should be done in due course for pensions. Since 2014, we are reinforcing our oversight work, building trustful relations with national authorities, and providing independent and challenging feedback on supervisory practices.

At the same time I would like to underline: EIOPA does not replace national supervisory authorities. The responsibility of the day-to-day supervision of individual undertakings and groups rests with the NSAs.

As part of our oversight work we also perform "Peer Reviews". Their purpose is to compare and assess the practices of supervisors and contribute to the creation of convergent supervisory standards. EIOPA has developed methods allowing for the objective assessment and comparison between the authorities reviewed. On the basis of the Peer reviews, EIOPA identifies the outcomes achieved; best practices and makes concrete recommendations for improvement.

In my view, this programme fully reflects the purpose for which EIOPA was created: to promote supervisory convergence; to contribute to upgrading of the quality and consistency of national supervision and to strengthen oversight of cross-border institutions.

Let me finally mention two issues that are very relevant going forward:

Firstly, it is important to guarantee that EIOPA will have an appropriate budget framework that will safeguard the overall efficiency of the Authority, reinforce its operational independence and ensure the necessary human and financial resources. A solution could be to have an independent budget line that ensures 100% of EIOPA’s financing from the overall EU budget. Other possible solution that could be explored, in line with the current EIOPA Regulation, would be a partial funding coming from fees from the industry.

Secondly, a deserved reference to the important role that the Occupational Pensions Stakeholder Group (OPSG) has been playing on EIOPA’s work. The level of the discussions, the quality and diversity of the comments and the engagement from the OPSG in EIOPA’s work has been a key source of inspiration. Our deliverables have benefited a lot from this interaction. Going forward, in the process of revision of the EIOPA Regulation, I strongly recommend that the OPSG will be maintained.

In some weeks EIOPA is going to launch the selection process for its Stakeholder Groups and in particular for the OPSG. And I would like to encourage all of you to consult our website and if possible to apply. We can only have good pensions regulation if it captures interests of all the parties involved: beneficiaries, scheme members, IORPs, trade unions, employers, and academics. Only with your input will we be able to analyse the impact of the new regulation from different angles and perspectives. So please do not ignore my call, we need all of you on board!

Ladies and gentlemen,

Our strategic objectives for the next years are quite clear: to have a truly cross-border pensions market, to ensure adequate occupational and private pensions savings and to regain trust and confidence of EU citizens in pensions. We need to have good pensions for the people of Europe. Let’s work on these objectives all together.

Thank you for your attention.