PENSIONS EUROPE

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PensionsEurope Response

OECD Consultation on draft high-level principles of long-term investment financing by institutional investors

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1. Identification

PensionsEurope represents national associations of pension funds and similar institutions for workplace pensions. Some members operate purely individual pension schemes.

PensionsEurope has **23 member associations** in EU Member States and other European countries with significant – in size and relevance – workplace pension systems[1].

PensionsEurope has established a **Central & Eastern European Countries Forum (CEEC Forum)** to discuss issues common to pension systems in that region.

PensionsEurope member organisations cover the workplace pensions of **about 80 million European citizens.** Through its Member Associations PensionsEurope represents approximately **€ 3.5 trillion of assets** managed for future pension payments.

PensionsEurope Members are large institutional investors representing the **buy-side** on the financial markets.

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[1] EU Member States: Austria, Belgium, Finland, France, Germany, Hungary, Ireland, Italy, Luxembourg, Netherlands, Portugal, Romania, Spain, Sweden, UK. Non-EU Member States: Croatia, Guernsey, Iceland, Norway, Switzerland.

2. General Comments

PensionsEurope very much welcomes the OECD's public consultation on its Draft High-Level Principles of Long-Term Investment Financing by Institutional Investors, dated 2 May 2013, as developed by its Task Force on Institutional Investors and Long-Term Financing.

Pension funds are rightfully identified by the OECD as suitable long-term investors. LTI indeed often forms an important part of pension funds' investment activities, due to the match with the long duration and maturities of their liabilities. The debate on LTI touches upon many different areas of expertise and regulation. PensionsEurope deems it to be of utmost importance to monitor the interconnectedness of all of these various areas, across the different jurisdictions.

Pension funds will need a regulatory LTI framework that makes LTI -more- attractive. But not only that, regulation should also not be *dis*couraging LTI. Not only solvency and prudential regulation, but also financial market regulation should not be counter-productive to LTI. There should not be any provisions discouraging LTI in a <u>direct</u> way (for instance by means of imposing Solvency II like rules on pension funds), but also will it be very important to review the <u>indirect</u> influence of the various pieces of regulation. Such legislation can prohibit pension funds, as well as other investors, from making / increasing LTI due to liquidity constraints that are a consequence of such legislation. Examples are the EU Financial Transaction Tax, margin requirements for OTC derivatives, MiFID/MiFIR, and others. Pension funds are not only (increasingly) faced with substantial direct costs of regulatory reform, but also with the indirect effects/costs thereof. Banks will pass on the costs they have to make to the end investors. In sum, the total costs of regulatory reform/change of the market structure will be substantial for the end investors, affecting pension funds' asset allocation policies and restricting the pool of (illiquid) assets they can invest in. LTI regulatory frameworks should also consider the investment horizon of pension funds, while promoting their soundness and solvency as well as broader financial stability and consumer protection.

Please find below our more detailed reaction to the consultation document. Upon your request, at this stage we merely provide you with our major, high-level comments and suggestions only.

3. Draft Principles

Draft Principle 1: Preconditions for long-term investments

In line with our general views as set out above, we strongly feel that in Principle 1.1 it should be mentioned that governments (as defined) should not only put in place framework conditions that are "favourable" to LTI, but also those that would not "discourage" LTI. And this while taking into account both direct and indirect effects, costs and consequences of the various pieces of legislation.

Likewise, in Principle 1.2 it should in our view not only be mentioned that policies to promote LTI need to be "consistent" with prudential objectives, but rather that these prudential objectives should not prohibit or discourage LTI, more specifically in the case of pension funds.

In Principle 1.4 it could be added that institutional investors should not only be "developed", but also that existing (LTI) institutional investors should get proper incentives to enlarge their LTI portfolios. We note that in the last few years, existing regulations such as short-term accounting rules, prudential rules, and asset and liabilities valuation have been detrimental for LTI.

Principle 1.7 points out the fact that at the moment there does not exist appropriate long-term instruments that would match the duration of pension fund liabilities.

Draft Principle 2: Development of institutional investors and long-term savings

In relation to Principle 2.2 we note that savings mobilisation may indeed be a proper financial incentive.

Draft Principle 3: Governance of institutional investors, remuneration and asset management delegation

In relation to Principles 3.1-3.6, we note that the governing body of the institution (which we trust to refer to the long-term investor), does not have to be the entity by which the actual management activities are performed. This goes for instance for collective investment schemes which have hired an external manager. In that case, criteria as having a proper set of skills and capabilities and risk management activities may in practice very well be met by this other entity. We note that in Principle 3.7 (on remuneration) reference has not been made to the governing body of the investor but to the "fund manager". We are not sure whether this distinction has been made on purpose, or not. In our view, all of this requires some clarification in the consultation document.

In relation to Principle 3.7 we further note that in case of a fund manager managing both LTI and non-LTI, "long-term" criteria for performance-based remuneration may have a different meaning than the actual holding period of its long-term (i.e.: illiquid type of) investments. In the EU Alternative Investments Fund Managers Directive (AIFMD), that applies to the management of collective investment schemes, reference is made in the same context to assessment of performance based on "longer term performance", which may be more appropriate wording.

Draft Principle 4: Prudential regulation, valuation and tax treatment

In relation to Principles 4.1 and 4.2 on prudential regulation, we again stress that these measures should not prohibit pension funds from making LTI.

In relation to reliance on credit ratings (Principle 4.1), we note that at least at EU level- this has already been covered by existing regulations.

In relation to Principle 4.3 it is necessary to clarify what has been meant by "standardization" of LTI valuation.

In reliance to Principle 4.4 we would strongly support adding that any possibilities to create (cross-border) LTI tax incentives need to be explored.

Draft Principle 5: Financing vehicles and support for long-term investment and collaboration among institutional investors

In relation to Principle 5.3 we wonder why reference has been made to "regulatory authorities" as opposed to "governments" within the meaning of footnote 4 of the consultation document. It should in any case be clear that local authorities may not be authorized to set more specific standards than the ones applying at EU level, when these are subject to the so-called 'maximum harmonization' principle. The AIFMD may serve as an example.

Draft Principle 6: Investment restrictions

In relation to Principle 6.1 it does not seem quite clear whether reference is made to governmental/supervisory investment restrictions or to 'internal' investment restrictions. In the end it should always be up to the investor to decide whether or not LTI fits its investment strategy, from time to time.

Draft Principle 7: Information sharing and disclosure

In relation to Principle 7.3 it is unclear to whom the information mentioned therein should be disseminated. General information in relation to investment strategies will generally not be made public and reporting requirements to the supervisor will often already be covered by existing requirements.

The same basically goes for the reporting requirements as mentioned in Principle 7.4. Information on specific investments and performances will often not be made public. It is unclear why in this respect the Principle also deals with non-LTI assets.

In our view the information should be available at the level of the individual institution, to all relevant stakeholders, i.e. supervisor, sponsoring undertaking of the pension fund and affiliates and beneficiaries (as it is today). The supervisor -or national statistical agency- could, at a maximum, publish certain information for the general public afterwards and on a consolidated level only, based on the information so received.

And, in relation to Principle 7.5, what should this specific type of monitoring by competent authorities look like?

In general, we are not quite sure how these Principles fit the overall idea of promoting LTI, as in the way these are currently drafted this may even take an opposite effect?

Draft Principle 8: Financial education, awareness and consumer protection

These draft principles are still somewhat vague from the pension fund point of view. We would support financial education and protection forming a part of any (regulatory) reforms that would be processed in order to enhance LTI. Such measures would then have to be tailor-made, taking into account the specific features of, and risks associated with, LTI. These features as well as risks can be often more challenging to educate and communicate than in many other types of investments.