PensionsEurope Position Paper on the Review of the European Supervisory Authorities

12 March 2018
About PensionsEurope

PensionsEurope represents national associations of pension funds and similar institutions for workplace pensions. Some members operate purely individual pension schemes. PensionsEurope Members are large institutional investors representing the buy-side on the financial markets.

PensionsEurope has 23 member associations in 18 EU Member States and 3 other European countries with significant – in size and relevance – workplace pension systems1.

PensionsEurope member organisations cover different types of workplace pensions for over 110 million people. Through its Member Associations PensionsEurope represents more than €4 trillion of assets managed for future pension payments. In addition, many members of PensionsEurope also cover personal pensions, which are connected with an employment relation.

PensionsEurope also has 25 Corporate and Supporter Members which are various service providers and stakeholders that work with IORPs. We have established a Central & Eastern European Countries Forum (CEEC Forum) to discuss issues common to pension systems in that region.

PensionsEurope has established a Multinational Advisory Group (MAG) which delivers advice on pension issues to PensionsEurope. It provides a collective voice and information sharing for the expertise and opinions of multinationals.

What PensionsEurope stands for

- A regulatory environment encouraging workplace pension membership;
- Ensure that more and more Europeans can benefit from an adequate income in retirement;
- Policies which will enable sufficient contributions and good returns;

Workplace pensions offer

- Economies of scale in governance, administration and asset management;
- Risk pooling and often intergenerational risk-sharing;
- Often “not-for-profit” and some/all of the costs are borne by the employer;
- Members of workplace pension schemes often benefit from a contribution paid by the employer;
- Wide-scale coverage due to mandatory participation, sector-wide participation based on collective agreements and soft-compulsion elements such as auto-enrolment;
- Good governance and alignment of interest due to participation of the main stakeholders.

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

Pension institutions are embedded in national social and labour law. Occupational pensions are also built on the foundation of first pillar pensions and therefore closely linked to Member States’ social security systems. PensionsEurope encourages EU policy-makers to take into account these specificities in the Review of the European Supervisory Authorities.

PensionsEurope supports a balanced approach to the convergence of capital market supervision. A vibrant Capital Markets Union, which provides European pension funds with long-term investment opportunities to achieve good returns for members and beneficiaries, requires robust supervision of market participants. At the same time, it is necessary to recognise the important role that national capital market supervisors will continue to play, due to their in-depth knowledge of local markets and providers. Moreover, ESMA’s empowerment means that it will need to increase its engagement with supervised entities and have adequate representation of institutional investors such as pension funds in its Stakeholder Groups.

PensionsEurope questions the need for the enforcement of supervisory convergence in the area of occupational pensions. Under the IORP II Directive, pension funds do not fall under a European framework that aims at full harmonisation, like Solvency II for insurers. As such, there is no European supervisory and prudential framework around which convergence can take place. The proposals would entail new powers for EIOPA to set the policy priorities of national supervisory authorities, to review their supervisory activities and to obtain information directly from pension funds. Pension funds are concerned EIOPA would employ these tools to urge national supervisors to adopt its view of how pension funds should be regulated.

The governance structure of EIOPA should ensure that decision-making is underpinned by sufficient expertise in the area of pensions. Already today, the expertise of its management structures corresponds to the stronger involvement of EIOPA in insurance. EU policy-makers should ensure the Executive Board has the right competences and governance structure to take adequate decisions on all policy areas within its remit.

EIOPA should not disclose individual stress test results and the Board of Supervisors should remain the decision-making body for the stress tests. Due to the differences between national and EIOPA’s valuation methods, EIOPA’s stress test could come to very different conclusions on a fund’s coverage ratio compared to the national supervisor, which can be very confusing for its members. It is not the objective of EIOPA’s stress test to provide information to individual members.

Pension funds are not directly supervised by the ESAs and therefore oppose industry fees, which ultimately would be paid by current and prospective European pensioners. Moreover, there is the concern that the EU institutions and Member States will exercise less oversight over the budget when it is to a lesser degree funded by national and EU contributions.

PensionsEurope welcomes a stronger mandate for the Stakeholder Groups to scrutinise recommendations and guidelines. This should not be a reason to change the composition of the
stakeholder groups. Stakeholders have limited resource, so an absence of a challenge should not be understood as an absence of concern.

The European Systemic Risk Board (ESRB) should avoid having a bank-bias in its approach to other financial sectors. With the ECB President as the permanent ESRB chair, pension funds are concerned that a bank-centric view on financial stability would unduly categorise them as systemic. Due to their long-term investment perspective, pension funds pose a low risk to global financial stability and their investment decisions are not significantly affected by market fluctuations.
1. **Pensions institutions are embedded in national social and labour law**

Institutions for Occupational Retirement Provision (IORPs) across Europe are embedded in historical developments in Member States and in their respective social and labour laws. They are, first and foremost, social institutions active on the financial markets. Therefore, they cannot be compared directly to other financial institutions such as banks and insurers. This is recognised by the European Parliament and Council and codified in the IORP II Directive which clearly states that “IORPs are pension institutions with a social purpose that provide financial services”. Importantly, “such institutions should not be treated as purely financial service providers. Their social function and the triangular relationship between the employee, the employer and the IORP should always be adequately acknowledged and supported as guiding principles”.2

Occupational pensions are also built on the foundation of first pillar pensions (state pension systems), which are different from Member State to Member State. Moreover, in some Member States occupational pensions are closely integrated with first pillar provision. Therefore, occupational pension design, in conjunction with widely-varying first pillar pension provision, aims to achieve adequate pensions overall, where the definition of adequacy is highly dependent on the social policies of a Member State (housing, health care, social welfare).

National prudential legislation and supervision take these national elements into account. A one-size-fits-all approach to the European legislation would be detrimental as it would not take into account the heterogeneity and complexity of the different combined first and second pillar systems. PensionsEurope encourages EU policy-makers to take into account these specificities in the Review of the European Supervisory Authorities3.

2. **PensionsEurope supports a balanced approach to the convergence of capital market supervision**

A vibrant Capital Markets Union provides European pension funds with long-term investment opportunities to achieve good returns for members and beneficiaries. The project should therefore ensure that institutional investors will benefit from a greater choice of investments, accessible at lower costs, with effective investor protection and with equal tax treatment throughout the European Member States. This also entails robust supervision of capital market participants, their infrastructures, governance and conduct.

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2 Recital 32 of DIRECTIVE (EU) 2016/2341 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 14 December 2016 on the activities and supervision of institutions for occupational retirement provision (IORPs)
3 Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL Amending Regulation (EU) No 1093/2010 establishing a European Supervisory Authority (European Banking Authority); Regulation (EU) No 1094/2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority); Regulation (EU) No 1095/2010 establishing a European Supervisory Authority (European Securities and Markets Authority); Regulation (EU) No 345/2013 on European venture capital funds; Regulation (EU) No 346/2013 on European social entrepreneurship funds; Regulation (EU) No 600/2014 on markets in financial instruments; Regulation (EU) 2015/760 on European long-term investment funds; Regulation (EU) 2016/1011 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds; and Regulation (EU) 2017/1129 on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market
The EU has put in place a single rulebook for capital markets through a series of legislative reviews following the financial crisis. ESMA has played an important role in filling in the details of this framework by drafting delegated and implementing acts, recommendations and Q&As. At the same time, capital market supervision is, by and large, still the responsibility of national competent authorities (NCAs).

The proposal of the European Commission now aims to drive further convergence in the supervisory practices and outcomes at the national level and would give some direct supervisory powers to ESMA. PensionsEurope in principle supports this objective in the area of capital market supervision. This is particularly relevant as trust in Member State supervision is a significant factor in facilitating cross-border investing within the EU. ESMA should play a role in ensuring that the harmonised rulebook is applied consistently across the EU. Moreover, it makes sense to boost ESMA’s powers vis-à-vis third country firms, so that European institutional investors can be confident that they too behave prudently.

At the same time, most pension funds make use of external asset managers and pension services providers. This means pension funds are indirectly affected by ESMA’s regulation, as costs stemming from regulation will inevitably be passed on and impact returns. ESMA’s regulatory work should therefore be based on thorough impact assessments and avoid unnecessary costs. Moreover, it is important to recognise that supervisory decisions of NCAs are based on a continuous dialogue and exchange of information with market participants, as well as an in-depth knowledge of their business models. The empowerment of ESMA should not erode this foundation of effective supervision.

Moreover, ESMA’s increased powers should be accompanied by strengthening its engagement with stakeholders. An openness towards dialogue between the regulator and stakeholders is at the core of effective and efficient regulation and supervision. We would be in favour of direct conversations with stakeholders about the impact of its regulatory work on markets and institutions. This is especially important as ESMA’s powers increase. Finally, ESMA should make sure there is adequate representation by pension funds and their dedicated asset managers in its Stakeholder Groups.

3. PensionsEurope questions the need for supervisory convergence in the area of occupational pensions

As set out above, the European occupational pensions landscape is fundamentally different from the capital markets and other financial institutions, such as banks and insurers. It was for these reasons that the European Parliament and Council decided (a) not to harmonise the prudential framework for IORPs and (b) to delete any competences for delegated and implementing acts from the original IORP proposal. This means that there is no harmonised framework around which supervision can converge.

The pensions sector is concerned that in practice EIOPA would use its new tools for supervisory convergence to achieve convergence towards what it believes should be the homogeneous prudential framework for pension funds, thereby undermining the decisions of the co-legislators and (current) national supervision, undercutting national balances between first and second pillar provision. In recent years, EIOPA has undertaken a number of initiatives that aimed to institute its view of prudential supervision outside the scope of the IORP Directive.

First, EIOPA has proposed the mandatory use of the ‘common framework balance sheet’ as a risk management and transparency tool and called for regulatory responses by the national competent
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authorities based on it. PensionsEurope has rejected\textsuperscript{4} EIOPA’s proposal and stressed that, even in the absence of EIOPA’s involvement, risk management is already essential for IORPs. Second, EIOPA has undertaken own-initiative work on a pan-European occupational DC framework, without having any basis in legislation. Third, EIOPA is using its own methodology in its stress tests for occupational pension funds. Its approach is questioned by experts as it does not fit national circumstances, leads to flawed results of the stress testing and is based on the “common framework” that was rejected by the European Parliament and Council. PensionsEurope has emphasised repeatedly that EIOPA should use an appropriate and more principles-based stress testing methodology instead of its current methodology, which does not provide meaningful outcomes\textsuperscript{5}.

The proposals contain several measures to enforce supervisory convergence, thereby upsetting the current balance of power between national competent authorities and EIOPA.

- NCAs would be required to set an annual work plan according to EIOPA’s Strategic Supervisory Plan. We are convinced the NCAs are better placed to determine their policy priorities, as these will be heavily interlinked with domestic developments in social and labour policy.
- The new Executive Board would be empowered to conduct independent reviews of NCAs, replacing the current peer reviews.
- EIOPA would be empowered to circumvent the NCAs and obtain information\textsuperscript{6} directly from IORPs. This request would be backed up by the power to fine pension funds in case of non-compliance.

PensionsEurope feels that these powers could result in EIOPA challenging NCAs’ decisions without a full understanding of the national prudential framework, national social and labour laws and underlying employment terms relevant to the occupational pension provision.

The aforementioned measures that are intended to achieve supervisory convergence should therefore not apply in the area of occupational pensions. NCAs should have the freedom to decide their own supervisory priorities based on the relevant national trends and not adhere to EIOPA’s Strategic Supervisory Plan. And we strongly feel that information requests should continue to run through NCAs (which could transfer these to the relevant ESA), as the NCAs are the supervisors with the relevant understanding of the national pension systems.

\textsuperscript{4} See PensionsEurope Position Paper on EIOPA’s IORP Quantitative Assessment 2015 and EIOPA’s opinion for Risk Assessment and Transparency for IORPs. We stress that IORPs regularly carry out their own stress tests and scenario analyses (e.g. Asset and Liability Management studies) as part of their own risk management processes and on a basis that is relevant to their national pension system. Furthermore, the IORP II Directive contains a thorough framework for pension funds’ future risk management and assessment.

\textsuperscript{5} See PensionsEurope Position Paper on EIOPA’s IORP Stress Test 2015.

\textsuperscript{6} It should be noted that this extends beyond information that IORPs currently hold or obtain (for their own risk-management and governance). Consequently, information requests are likely to impose additional costs on IORPs which will have a negative effect on participants retirement outcomes.
4. **The governance structure of EIOPA should ensure that decision-making is underpinned by sufficient expertise in the area of pensions**

Already today, pension funds are concerned that the decisions affecting them are not always sufficiently based on pensions expertise. Funded pension systems have developed unevenly across Europe and in some Member States pension funds play a much larger role in achieving adequacy of pension provision that in others. Moreover, some Member States have separate supervisory authorities for insurance and occupational pension entities, yet they will have to rely on one single regulatory authority as its voice on the Board of Supervisors. As a result, most individuals in the Board of Supervisors have a background in insurance supervision.

Moreover, EIOPA’s workload on insurance regulation has far outpaced its involvement in occupational pensions. This is not surprising because of the difference in scale, the large amount of delegated law-making under insurance regulation and the fact that cross-border insurance business is common-place whereas only a small number of IORPs operate across borders. EIOPA’s expertise has developed accordingly, and it is likely to continue to do so. The ESA Review proposal makes clear that the majority of the projected additional 35 staff will also work in the area of insurance. Furthermore, EIOPA decided to abolish the Occupational Pensions Committee last summer, which was its internal committee for occupation pensions experts of NCAs. The expert level policy committees on insurance and occupational pensions were merged into a new Policy Steering Committee. Therefore, also individuals at management and expert level have developed more expertise in insurance than in pensions.

Nonetheless, they are also involved in decision-making in relation to IORPs, which differ substantially from insurance companies. This raises the question whether decision-making on pension policy sufficiently takes account of the idiosyncrasies of pension funds. Given that EIOPA’s mandate in the field of pensions would expand under the proposal for the Pan-European Personal Pension Product (PEPP), it is of great importance that EIOPA’s governance structures as a whole are equipped to take adequate decisions on pensions. We therefore suggest that the EIOPA Regulation should require the European Commission to consider the expertise and competences of the Executive Board when shortlisting candidates. The result should be a well-balanced decision-making body that is capable and knowledgeable on all areas of policy within its remit.

5. **Disclosure of individual stress tests results would amount to a first step towards direct European supervision**

As set out above, European pension funds have been critical of EIOPA’s use of stress tests as a means to drive its agenda for the common framework balance sheet. The proposal would provide new tools for EIOPA to pursue this strategy. First off, the decisions on the methodology and communication approach for stress tests are to be taken by the Executive Board. Again, the potential lack of expertise in occupational pensions could lead to problems in this area, with the Board failing to take sufficient account of the specificities of pension funds. The Executive Board also would be unable to take on board national perspectives in deciding on the methodology and communication approach. Therefore, these decisions should remain in the hands of the Board of Supervisors.
Second, even more problematic would be the power to disclose the individual results of IORPs. Due to the differences between national and EIOPA’s valuation methods, the stress test would likely result in significantly different results from those under the national framework. The publication of these results could be used to put pressure on individual funds, as well as NCAs, in particular when communicated inappropriately to the media. This would also have detrimental effects on sponsors of occupational pensions that are identified, as there is the risk that sensitive data relating to the sponsor support is disclosed, which could affect the market valuation of the company. It may lead to those sponsors deciding not to offer retirement provision or move away from defined-benefit pensions, which would be counter to the overarching ambition of ensuring wider and better pension adequacy. For participants, the divergence in solvency ratio between the national balance sheet and EIOPA’s approach would be extremely confusing, which could erode public support for occupational pensions.

PensionsEurope strongly feels that the disclosure of individual results would amount to a first step towards direct European supervision of pension funds. Therefore, EIOPA should not be empowered to disclose the individual results of IORPs in the stress test.

6. Pension funds oppose industry fees and worry that new funding rules provide for inadequate control of EIOPA

As pension funds are not directly supervised by EIOPA, they feel they should not pay industry fees to EIOPA. We understand the need for some degree of flexibility in the ESAs’ funding arrangements to deal with changes to the volume of work which is delegated to them. However, PensionsEurope strongly prefers that the solution for this problem is found within the current funding system based on contributions by NCAs7 and the Union budget. One solution could be to fully fund EIOPA through the Union budget.

However, in case industry fees are introduced nonetheless, we urge the co-legislators to ensure they continue to have sufficient control over the ESAs’ budgets as part of their democratic objective within the European Union. The ESAs have tested and surpassed the limits of their mandates. EIOPA in particular has demonstrated its expansive ambition through its own-initiative work. A larger degree of flexibility should therefore not result in a blank cheque to fund any type of activity of the ESAs.

In the ESA Review proposal, the level of the budget is to be set by the Board of Supervisors at the proposal of the Executive Board. Given that NCA contributions would be scrapped, there would be less of an incentive for NCAs to prevent the ESAs from inflating the share of the budget paid for by industry fees. The European Commission has power over the level of the Union contributions to the budget. It will also hold the pen on the delegated act determining how the share of the budget paid by industry fees is allocated amongst individual financial institutions. However, the European Commission will not have the power to limit the share of industry fees in the budget. PensionsEurope therefore advocates a larger role for the European Commission, Parliament and Council to oversee the budgets of the ESAs.

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7 It should be noted that in some countries pension funds already indirectly contribute to EIOPA’s funding through their contributions to the NCAs.
7. **PensionsEurope welcomes a stronger mandate for the Stakeholder Groups**

The proposal envisages a more prominent role for the Stakeholder Groups of the ESAs, such as the Occupational Pensions Stakeholder Group (OPSG). To date, the Stakeholder Groups have functioned as internal advisory bodies, but now they would be able to refer Guidelines and Recommendations to the European Commission if they believe these measures have gone beyond the legislative text on which they are based.

PensionsEurope is very supportive of greater scrutiny into these non-binding so-called Level 3 measures, which in some cases are enforced as binding legislation by NCAs and which are out of scope of political scrutiny by the European Parliament and Council. We therefore welcome the proposed new powers. However, we believe that the European Commission should not need a referral from the Stakeholder Groups to scrutinise Level 3 measures itself.

It is noteworthy that the Stakeholder Groups currently do not have any own resources for the drafting of thorough legal analysis or legal proposals. We expect stakeholders on the group only to commit their own resources to this new power in the most clear-cut transgressions of the mandate. In these cases, the European Commission should enter into dialogue with the Stakeholder Group to pro-actively explore the reasons for challenging the Guideline or Recommendation. Moreover, given the resource constraints, an absence of a challenge should not be understood as a lack of concerns.

This new power should also not be a reason for the ESAs to change the composition of the Stakeholder Groups. The two-third majority required for the referral and lack of own resources already are significant hurdles, so the ESAs should not build in blocking minorities to avoid the power being used. Therefore, we believe the responsibility for the selection process should be transferred to the European Commission and candidates should be selected based on objective criteria.

With regard to the Stakeholder Group of ESMA, we think that pension funds and their dedicated service providers are not adequately represented and we call for taking into account their role as actors on financial markets. More generally, the expertise of these market participants should be taken into account more, for example by being more open to bilateral conversations with stakeholders. We furthermore observe that the time offered to stakeholders for responding to consultations is often (very) short. More time would enable stakeholders to provide adequate reactions to consultations.

Finally, the mandate of the Stakeholder Groups could further be strengthened by increasing their role in providing recommendations on the work programme of the ESAs. The expertise of the individuals in the Stakeholder Group could help making proposals based on relevant market trends.

8. **Tweaks to the Better Regulation rules are welcome, but thorough cost-benefit analyses should underpin all of the ESA’s work**

The proposal aims to better enshrine the principles of Better Regulation in the ESA Regulations. The ESAs will need to consult stakeholders and conduct cost-benefit analyses as a rule before adopting Guidelines, rather than where thought to be appropriate. PensionsEurope welcomes these amendments.
At the same time, we strongly believe that these principles should apply in all of the ESAs workstreams, not only in the regulatory activities, as is proposed. A good example are new reporting requirements for IORPs proposed by EIOPA. The Authority wants to impose a third reporting template on IORPs, next to NCA and ECB templates. Moreover, it wants large IORPs to report individually, rather than the NCA providing aggregate country-level data. The cost of the onerous new reporting requirements will fall on pension fund members and without there being a clear rationale, given the amount of data that already is collected by the NCAs and ECBs. Furthermore, the individual reporting of large IORPs would be an element of micro-prudential supervision, which is simply not within the mandate of EIOPA. A thorough cost-benefit analysis would have identified the negative net outcome for pension fund members.

9. **The European Systemic Risk Board (ESRB) should avoid having a bank-bias in its approach to other financial sectors**

The ESRB should avoid having a bank-bias in its approach to other financial sectors. The current structure and organisation of the ESRB do not ensure that the ESRB is an independent body.

Currently, the Commission has proposed that the ECB President would chair the ESRB on a permanent basis. We are afraid that this would not ensure that the ESRB is an independent body, and furthermore, the ESRB would continue imposing a bank-biased approach to other financial sectors.

Policy coordination of the ECB and the ESRB with the European Commission, the European Parliament, and Council should be improved to ensure financial stability. However, PensionsEurope urges all parties to refrain from using tools or implementing measures beyond banking without evidence of extant systemic risk.

Due to their long-term investment perspective, pension funds pose a low risk to global financial stability. Pension funds’ main investment choices are not significantly affected by temporary fluctuations of the markets. In addition, the regulatory framework requires that pension funds are transparent, low leveraged and diversified with prudence. Moreover, pension funds have limited short-term liquidity needs, which make them more inclined to buy and hold assets across the entire economic cycle. They have also an ability to behave counter-cyclical.