



EUROPEAN COMMISSION

Internal Market and Services DG

**FINANCIAL INSTITUTIONS
Insurance and Pensions**

PUBLIC HEARING

**Harmonisation of solvency rules applicable to Institutions for
Occupational Retirement Provision (IORPs) covered by article
17 of the IORP Directive and IORPs operating on a cross-border
basis**

- SUMMARY OF PANEL DISCUSSIONS -

27 May 2009

Centre de Conférences Albert Borschette, 36 rue Froissart, 1000 Brussels

The Commission Services held a one-day Public Hearing on the harmonisation of solvency rules applicable to Institutions for Occupational Retirement Provision (IORPs) covered by article 17 of the IORP Directive and IORPs operating on a cross-border basis on 27 May 2009 in Brussels. The Public Hearing attracted more than 200 participants, bringing together senior representatives from Member States, European institutions, supervisory authorities, industry (pension funds, insurance and asset management), independent professionals, users (employers and employees/pensioners) and consumers.

The purpose of the Public Hearing was to draw first lessons from the responses to the consultation launched in September 2008. The Commission Services had received 60 responses and a summary of these responses had been published in the form of a Feedback Statement in March 2009.

The Public Hearing started with opening remarks by Jörgen HOLMQUIST, Director General Internal Market and Services. He outlined the broad context in which the Public Hearing took place and described the key features of today's EU solvency rules for IORPs. This was followed by an introductory statement by the Chair of the Public Hearing, Elemér TERTÁK, Director Financial Institutions. He provided an overview of Feedback Statement and outlined the plan of the day.

The Public Hearing was articulated around four panels. This document provides a summary of the panel discussions.¹ The opening remarks, the introductory statement and the closing remarks are available from the Europa website.

¹ Disclaimer: This summary does not represent the complete discussions but are written with the aim to give a fair and balanced representation of the most relevant issues discussed. Any incorrect or incomplete representation of the discussions is unintentional.

Panel 1: Solvency rules for pension funds

Chair: **David Wright**, Deputy Director General Internal Market and Services.

Panellists: **Maarten Camps**, Director General, Ministry of Social Affairs and Employment, The Netherlands.

Angel Martinez-Aldama, Chairman of the European Federation for Retirement Provision (EFRP).

Carlos Montalvo, Secretary General of the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS).

Ieke Van Den Burg, Member of the European Parliament.

Philip Wynn Owen, Director General of Strategy, Information and Pensions of the Department for Work and Pensions, UK.

The Chairman, **David WRIGHT**, introduced the panellists and explained that the panel discussion would address two core questions:

- How well have the prevailing solvency rules done so far? Have the solvency rules been effective and efficient in dealing with the financial crisis? To what extent have the EU rules contributed to this?
- Do you think that solvency rules for IORPs should be more harmonised in the EU? As part of that question, it needs to be considered what the objectives and principles of prudential supervision for IORPs at the EU level should be.

He explained that the panellists are given the opportunity to provide a five-minute statement and that the floor would then be open to the audience for questions and comments.

Maarten CAMPS (NL) mentioned that the IORP Directive constitutes only a first step towards an internal market for occupational retirement provision. He expressed support for further progress.

He mentioned that the crisis has had a sizeable impact on defined-benefit schemes. The average coverage ratio has dropped to around 90%. The solvency rules in the Netherlands have done well so far, although recovery of the coverage ratio to the required 105% or 130% will not be easy.

Answering to the question whether or not EU solvency rules for IORPs should be further harmonised would require a thorough analysis and a solid business case. The consultation had been one step, but the further examination should be much broader not limited to IORPs subject to Article 17 or cross-border IORPs. He suggested that the further work should consider all IORPs and perhaps even beyond.

Further harmonisation of technical provisions could be desirable, but we should stay clear from applying Solvency II to IORPs as such. In going forward, a careful balance needs to be struck between financial sustainability and guarantees.

Angel MARTINEZ-ALDAMA (EFRP) mentioned that it is difficult to draw conclusions on the need for further harmonisation before knowing the objective. The focus should be on how to ensure an adequate and sustainable retirement income. Considering the challenge of an ageing population for public finances, the aim should be to make private pensions accessible more widely in the population, rather than making private pensions more expensive. Moreover, any legislative proposal for changing the IORP Directive should encourage employers to provide work-place pensions. When considering solvency rules for IORPs, he therefore urges the Commission to take a holistic approach.

He rejected that the existing diversity is a shortcoming that hinders internal market. Given the different national environments, the IORP Directive's current design – principles-based with minimum harmonisation - is suitable. Any new approach should be broad, subject to an impact assessment and start from a clean sheet. He mentioned that the EFRP would be happy to participate in this process.

Carlos MONTALVO (CEIOPS) mentioned that CEIOPS stands ready to continue assisting the European Commission in this project. He reminded that the IORP Directive has already brought clear benefits for the European economy: it enables cross-border business, it regulates the financial aspects of the IORPs while recognising national social and labour law and it introduces the prudent person investment principle. At the same time, the IORP Directive constitutes only a first step towards an internal market for occupational retirement provision. This needs to be followed by more steps. He made reference to the De Larosière Report on financial supervision, which recommended that national discretion should be limited.

He suggested that the IORP Directive has been doing well so far, considering that first steps are never easy and that it is difficult to find the right balance between financial regulation and social policy. But we should also be forward-looking because the future sustainability of occupational and individual pensions are key for meeting today's demographic challenge. In moving forward, the main objectives should be to ensure a high degree of security, provide the right incentives to improve risk management (including asset-liability management) and avoid procyclical effects. In addition, the right level of information should be disclosed in order to support informed savings and investment decisions.

He mentioned that risk-based supervision does not automatically mean applying the Solvency II Directive. Proper account should be taken of the specificities of IORPs, in particular sponsor covenants and pension guarantee schemes.

Ieke VAN DEN BURG (MEP) mentioned that she would have preferred a broader consultation, including a discussion on the scope of the IORP directive. She suggested that we should be much more ambitious, not least because of the important social role of IORPs. She reminded that during the negotiation of the Solvency II Directive she had asked that the debate about solvency rules for IORPs is carried out separately. The main objective for IORPs should be safety of pension promises and avoiding a downward spiral resulting from regulatory arbitrage between Member States. She therefore asked for more harmonisation and suggested that the three pillars of Solvency II could be a good source of inspiration.

She made several practical suggestions on the way forward. First, she called for a review of the IORP Directive using inspiration from the Solvency II Directive. One practical follow-up could be to carry out a Quantitative Impact Study with the close involvement of all stakeholders, as was done for Solvency II. Second, she suggested that the scope of the IORP Directive is revisited. Third, she proposed to launch a broader process with the creation of a Group of Wise Experts to deal with pensions in general, including aspects of social policy and taxation in order to make sure that the EU is ready for population ageing.

Philip WYNN OWEN (UK) welcomed the narrow scope of the consultation. He underlined that stand-alone IORPs are very different from sponsor-backed IORPs. Moreover, the consultation had given little evidence of an unlevel playing field between IORPs and insurance undertakings, which reflects the important differences between the two. In particular, IORPs operate on a not-for-profit basis; they are not commercial enterprises targeting the market of retail consumers, but part of a remuneration package offered in the labour market; they typically have a very long time horizons; and they have more predictable cash flows.

He took the view that the current system of prudential supervision for IORPs in the UK – relying on a proactive supervisor, strong sponsor covenants and a pension protection fund – has proven to be robust, proportionate and flexible. It has worked well for the UK. He mentioned that a Solvency II regime should therefore clearly not be envisaged for IORPs that are backed by a sponsor covenant.

He also suggested that there had not been major shortcoming in current solvency regimes for IORPs subject to Article 17 either. Moreover, the consultation had not brought any concrete evidence of regulatory arbitrage between Member States. The solvency rules for IORPs subject to Article 17 and IORPs operating on a cross-border basis are sufficiently harmonised already. It is important to recognise diversity and it will be difficult to develop one single model. Rather than focusing on solvency rules, there are other barriers to cross-border activity, in particular different interpretations of cross-border activity, lack of transparency about the different national systems and taxation. He also pointed to the work carried out by CEIOPS making progress in supervisory convergence in some areas. Whatever the next step, he invited the European Commission to make a rigorous impact assessment study.

Questions & Answers

Jacqueline LOMMEN (Hewitt Associates) mentioned that the main obstacle for cross-border activity is the lack of transparency about key features of occupational pension schemes in the different Member States. She suggested that more information should be made readily available about funding requirement (what is a sponsor covenant? what is a pension protection scheme?) and that the relevant Social & Labour Law of the different Member States is made available in English throughout the EU. She pleaded for more transparency in order to facilitate more harmonisation at a later stage. Carlos MONTALVO (CEIOPS) informed that CEIOPS is working on making available more information about occupational pensions on its website. Ieke VAN DEN BURG (MEP) took the view that not only more transparency is needed but also a neutral "arbitreur" who rates the value of the different systems.

François VANDERSCHELDE (BBTK/SETCa, Belgian trade union) also argued that more transparency alone is not enough, but that more harmonisation is necessary. Philip WYNN OWEN (UK), however, cautioned that there is a danger of a perverse outcome in that too much harmonisation could jeopardise the existing provision of occupational pensions. Angel MARTINEZ-ALDAMA (EFRP) added that the IORP Directive is still very young in comparison with the insurance Directives, which were adopted for the first time in the 1970s. He argued that therefore more time is needed and prefers, for the time being, convergence within the framework of a principle-based IORP Directive rather than harmonisation.

Withold GALINAT (BASF, DE) also questioned the need for further harmonisation. He pleaded for keeping the status quo. He emphasised that diversity has values and offers natural checks and balances. Ieke VAN DEN BURG (MEP) stressed the importance of avoiding competition from a light touch regime because this is not beneficial for pension security. Withold GALINAT (BASF, DE) also suggested that the usefulness of further harmonisation of prudential rules is limited because cross-border business would still be inhibited by differences in Social & Labour Law. Carlos MONTALVO (CEIOPS) replied that the IORP Directive already today strikes a careful balance between prudential regulation and Social & Labour Law.

Maarten CAMPS (NL) underlined that we do not know enough yet in order to answer questions like "Is more transparency enough?" or " Why more harmonisation?". May be the IORP Directive is too young, may be the scope of the consultation was too narrow, or may be it is necessary to collect more information about the differences. He also reminded that the IORP Directive requires the European Commission to issue a report every 2 years on the calculation of technical provisions from an internal market perspective and that this report is not there yet. He concluded that more examination is necessary before taking a policy decision.

John ASHCROFT (independent consultant) suggested that "if it ain't broke don't fix it". He questioned that there is any evidence that the prevailing solvency rules for IORPs are not functioning correctly. Ieke VAN DEN BURG (MEP) replied that we need to be proactive and Carlos MONTALVO (CEIOPS) added that there is room for improvement.

David WRIGHT (Chair) **concluded** the panel discussion by suggesting that the prevailing solvency rules are probably not "broke". But they are perfectible. While increasing transparency may not be sufficient in itself, we also need to be mindful to manage diversity effectively. He suggested that we need to think carefully about our long-term objective, in particular against the background of the demographic challenge in ageing societies. Moreover, regulatory arbitrage should be avoided and he underlined that the European Commission is committed to move towards a single EU rulebook, including IORPs. A holistic approach for pensions is desirable but will face difficult challenges such as taxation. In going forward, the Commission Services will continue to consult openly, take the necessary time for reflection and examine the evidence and facts very carefully following a "1000 eye" principle.

Panel 2: Is there a level playing field issue between pension funds and insurance undertakings?

Chair: **Karel Van Hulle**, Head of the Insurance and Pensions Unit, Directorate General Internal Market and Services.

Panellists: **Sybille Reichert** (replacing Bruno Gabrielli), Association Européenne des Institutions Paritaires de la protection sociale (AEIP).

Michaela Koller, Director General of the European insurance and reinsurance federation (CEA).

Henri Lourdelle, Advisor, European Trade Union Confederation (ETUC).

Loes Van Embden Andres, Chair of BUSINESSEUROPE's Social Protection Working Group.

Chris Verhaegen, Secretary General of the European Federation for Retirement Provision (EFRP).

The Chairman, **Karel VAN HULLE**, explained that the situation has changed since the adoption of Solvency II. While insurance undertakings will have to apply Solvency II, IORPs continue to be subject to Solvency I. He recalled that one of the most controversial topic that arose during the Solvency II negotiations was the question whether or not there is an unlevel playing field between IORPs and life assurance undertakings. He suggested that the panellists focus on the following questions:

- Do you think that Solvency II introduces an unlevel playing field between IORPs and insurance undertakings? Those who think that this is or is not the case either within a Member State or across Member States, what are your arguments?
- Are IORPs and life assurance undertakings competing in the same market?
- Considering that IORPs are major institutional investors in equity and bond markets, do you think that IORPs should be considered as financial institutions?

Sybille REICHERT (AEIP) stressed that IORPs are not-for-profit organisations and that they are long-term investors. In a document of March 2006, the AEIP explains the differences between insurances, asset managers and IORPs. IORPs are not financial institutions but fall in between: financial markets are used as a tool in order to obtain a social objective.

Solvency II, and the implied harmonisation, should not be applied to IORPs for several reasons. It should be considered that IORPs can benefit from risk mitigation techniques such as changes in indexation and increases in contributions. There is no competition between IORPs and insurances as they are not on the same market. She also thinks that it is not possible to apply one single set of rules to all IORPs, because they differ too much.

The AEIP expressed interest to participate in the follow-up work with the Commission.

Michaela KOLLER (CEA) recalled that a recent OECD report issued in April 2009 found that declines in the funding ratio of IORPs could have been avoided with better risk management and governance rules. If pension funds and insurance undertakings offer the same pension products the principle "same risks, same rules" should apply. The objective of the Single Market is to integrate markets, protect members and promote healthy competition. The risk management system should be modern and consistent with the rules in other sectors.

The challenge for IORPs is the significant diversity. This requires a phased but a clearly focused approach. Insurance undertakings and pension funds should continue to be subject to the same rules. The Solvency II principles should be applied to all financial institutions that carry the same risks. A Quantitative Impact Study (QIS) should be launched as soon as possible to better understand the impact of Solvency II on IORPs. She suggested that the three pillars of Solvency II should be applied to IORPs subject to Article 17, while for non-Article 17 IORPs the second and third pillars would be sufficient. Acknowledging that pension funds are highly complex, she proposes that the application of Solvency II to Article 17 IORPs could be done right now, while non-Article 17 IORPs could be considered later. Moreover, other providers of pension solutions, such as UCITS that offer guaranteed returns, should also be subject to capital requirements.

Henri LOURDELLE (ETUC) mentioned that ETUC represents a user group of around 60 million contributors and beneficiaries. Their main concern is that the right of pensioners are guaranteed. This main objective of a social nature should drive the financial regulation. He advocated the need of a regulation on asset allocation and investment returns, not necessarily on solvency, in order to protect the contribution at the time of retirement. Particular attention should be given to investments in shares.

He took the view that IORPs are financial institutions. Their goal, however, is not to participate in financial markets, but to secure pension engagements over a long-term horizon. In comparison with insurance undertakings, IORPs have a specific purpose which calls for specific rules. Governance and the representation of scheme members is a key concern. It is important to understand what use is made of contributions. Members do not sign a blank cheque to the pension funds, but want to stay informed regularly. This should be more explicit if the IORP Directive is changed.

As regards common rules and convergence, he underlined the fact that "IORP" means different things in different countries, in particular in the new Member States. He suggested that the European Commission carries out a mapping exercise to better understand the existing situation.

He mentioned that for members the two main obstacles for cross-border activity are the non-portability of pension rights and taxation.

Loes VAN EMBDEN ANDRES (Business Europe) noted that supplementary pensions are becoming more important due to the demographics. Benefit security should therefore be achieved at a reasonable cost. Moreover, it is a prerogative of Member States to organise their pension systems.

She stressed that the need for a level playing field is a false perception. Insurers do not compete with IORPs for several reasons. First, IORPs are schemes associated with a

sponsor and there is hence no competition with life assurance to gain clients. IORPs do not aim to maximise return on investment, but aim to provide members with a valuable benefit. Second, IORPs can rely on additional security mechanisms, in particular employer covenants, guarantee funds, very long recovery periods and risk sharing across generations. Third, while, in principle, companies have a choice between an IORP and an insurance undertaking, in many cases, the employer is de facto obliged to participate in an industry-wide pension scheme in consultation with trade unions.

Accordingly, there is no need to have the same rules for insurers and IORPs. Solvency II for IORPs would lead to higher own fund requirements, which is unnecessary given the specificities of IORPs. The cost for companies would increase considerably, exacerbating the trend of employers "walking away" from pension provision.

She is not in favour of further harmonisation at the EU level. But if the European Commission was to come forward with proposals she called for the demonstration of a solid business case with a careful impact assessment.

Chris VERHAEGEN (EFRP) stressed that IORPs and insurance undertakings do not compete in the same market. Rather than being substitutes, insurance undertakings and IORPs operate in related markets and complement each other. IORPs have a specific focus, while insurers offer a much broader range of products and therefore bear a much broader range of risks. Moreover, even if IORPs and insurance undertakings were to compete in the same market, it does not automatically mean that the same rules should apply. Different rules would only become an issue if heterogeneity causes market failure or inefficiencies, and that has not been demonstrated yet. Differences in the regulation of insurance undertakings and IORPs could reflect differences in the governance of the institutions.

Moreover, IORPs do not cater directly to retail consumers, but to employers and employees. Their products are offered at the wholesale level and not at the retail level.

She acknowledged that IORPs are important financial actors in the internal market, but they also have a social purpose. The role of the IORP is to execute a social commitment embedded in an employment relationship.

Questions & Answers

Michel RUQUIER (AGE) mentioned that for users the quality of the security is essential, not the question about competition. The prudential rules for IORPs should ensure pension security. What happens if a sponsor goes bankrupt and the pension fund is underfunded? Which products would be better for a person close to retirement when markets are down? Which products will offer more protection? Henri LOURDELLE (ETUC) added that the EU Insolvency Directive is incomplete and the benchmark set by the Robbin's case is too low. He called for a review of Article 8 of the Insolvency Directive. Sybille REICHERT (AEIP) was supportive. She also mentioned that occupational pensions are complementary to the state pension and that insurance is complementary to occupational pensions.

Burkhart OBER (Allianz GI) explained that security for pensions comes at a price. A recent study has shown that applying Solvency II rules simply imposes higher contributions to beneficiaries. Moreover, investing into fixed-income gives a false

illusion of safety because returns may not be sufficient to outperform inflation. Loes VAN EMBDEN ANDRES (Business Europe) added that security is very important, but that security should not come at any price. There is always a balance to be struck.

Gerard RIEMEN (Association of industry-wide pension funds, NL) questioned the existence of an unlevel playing field. There are many differences between insurance undertakings and IORPs. Are IORPs financial institutions or social institutions? The IORP Directive tries to strike the right balance. Hence the debate about competition should not only focus on financial aspects, but also on social and collective aspects. He advocated that Solvency II should not be applied to IORPs because they are also social institutions.

Given the vast diversity, Ieke VAN DEN BURG (MEP) pleaded for comparable systems rather than for harmonisation. Moreover, she drew attention to the fact that the role of Article 4 of the IORP Directive needs to be considered more carefully. Chris VERHAEGEN (EFRP) mentioned that insurance undertakings should ask for application of Article 4 if they want to offer occupational pensions.

Michaela KOLLER (CEA) explained that there are also not-for-profit insurance undertakings such as mutual companies, but that has not prevented Solvency II to be applied to them. Risk mitigation elements are certainly important but they can easily be inserted and accounted for in Solvency II. Like Ieke VAN DEN BURG (MEP), she called for a Quantitative Impact Study (QIS) to move the public debate into more concrete territory.

Karel VAN HULLE (Chair) **concluded** the panel discussion by saying that the Commission Services had asked CEIOPS to conduct a mapping exercise on the existing landscape for IORPs across Member States. He agreed that an impact assessment is necessary. In the debate about the unlevel playing field, it is important to keep in mind that the objective is security. He acknowledged that proper consideration of risk mitigation elements and safeguards is paramount. IORPs are to some extent also financial institutions and have an important role for financial stability.

Panel 3: Technical provisions and solvency rules in a cross-border context

Chair: **Aerdt Houben**, Chairman of CEIOPS' Solvency Subcommittee, De Nederlandsche Bank.

Panellists: **Wil Beckers**, Director DSM Pension Services, The Netherlands.

Brendan Kennedy, Chief executive of the Pensions Board, Ireland.

Christoph Krischanitz, President of the Actuarial Association of Austria (Aktuarvereinigung Österreichs, AVÖ).

Jacques Maire, Senior Vice President for European and Public Affairs, Axa Group, France.

Bernhard Wiesner, Senior Vice President Corporate Pensions, Bosch Group, Germany.

The Chairman, **Aerdt HOUBEN**, introduced the panellists and explained that the panel discussion would address two core questions:

- What are the drivers for cross-border pensions? What are the obstacles?
- Looking forward, what are the avenues to make progress? What technicalities are involved? Should the EU converge on some of the elements, or do we need a holistic approach? Can we achieve equivalence of security?

Wil BECKERS (DSM Pension Services, NL) underlined that the consultation had not demonstrated evidence of regulatory arbitrage. He is therefore supportive of enhanced supervisory cooperation, rather than regulation of the differences. He did not think that there is case for harmonisation to protect members, and that even if there were one Solvency II would not be the right solution. He noted that the financial crisis had shown that internal models are not good at predicting the future.

As regards technical provisions, he suggested that the boundaries of Social & Labour Law should be carefully reviewed. Moreover, he took the view that the security of members does not depend on the level of technical provisions alone. Account should be taken of the additional security mechanisms.

He made reference to a recent Commission report had observed that despite the crisis, European pension funds have not experienced problems to the same extent as other financial institutions. He argued that legislative stability is very important for the industry and that changes should be introduced only if there is a solid business case.

Brendan KENNEDY (Irish Pensions Board) argued that the benefits of further harmonisation of technical provisions or own fund requirements are not very clear. In any case, harmonisation would probably be difficult or impossible to achieve. The harmonisation of solvency rules would require a harmonisation of the trade-off between security and provision, which is a social and labour law issue.

While suggesting that operating cross-border pension schemes is not a top priority for many employers, he noted that the main obstacle for cross-border activity is uncertainty (e.g. unclear definition of cross-border activity, interaction of Social & Labour Law and taxation). This uncertainty gives rise to a first mover disadvantage which requires the first sponsors wishing to go cross-border to invest more time and resources than subsequent sponsors.

He suggested that the European Commission and CEIOPS should focus on addressing the issues identified in the CEIOPS report "Initial Review of Key Aspects of the Implementation of the IORP Directive" of 2 April 2008.

Christoph KRISCHANITZ (AVÖ, AT) mentioned that in Austria private pension provision (Pensionskassen) is not widespread at present. But the pressure on public finances will lead to changes in social security and more reliance on occupational pensions.

He spoke in favour of further harmonisation, suggesting that this does not necessarily imply a one-size-fits-all approach. Harmonisation implies a multiple sound rather than a monotone. He expects greater harmonisation of technical provisions driven by international accounting standards (IAS 19). If the technical provisions can be higher in pension funds than the defined-benefit obligations on company balance sheets there is a potential for accounting arbitrage.

Moreover, harmonisation could lead to greater consistency with Solvency II and ensure a level playing field for the competition between Pensionskassen and insurance undertakings in Austria. While he suggested that the 99.5% Value at Risk measure in Solvency II could be used, he also underlined that Solvency II is not only about a standard formula. There are three pillars including rules on governance, risk management and disclosure. Solvency II is about quality not quantity. But harmonisation would need to be based on principles rather than on rules.

Jacques MAIRE (Axa, FR) pointed out that pension funds hold vast amounts of assets in management, but that there is very little cross-border activity. This situation is not optimal because in asset management the value is in the scale not in the margin. Further harmonisation is needed to reap the benefits of scale economies.

The issue for insurance undertakings offering retirement products is that it would be difficult to manage both Solvency I and Solvency II on the balance sheets at the same time. He suggested that there could be three reasons to have different capital requirements for IORPs and insurance undertakings. First, it may be decided to target a different level of confidence. This, however, should not be acceptable, in particular when this is not disclosed to the consumers. Second, IORPs have more risk mitigation techniques at their disposal. He pointed out that this could be dealt with by internal models in Solvency II. Third, he suggested that Solvency II is not adapted for long-term business like pensions and this is precisely why he has been arguing in favour of the duration approach in the Solvency II debate.

He also mentioned that cross-border pension funds are not only about transferred employees, but also about schemes for different domestic workforces. He argued that a complete equal treatment of national and cross-border supervision is needed. In

particular, he argued that the requirements regarding funding and ring fencing for cross-border and domestic IORPs should be aligned.

Bernhard WIESNER (Bosch, DE) mentioned that occupational approaches to private pension provision are superior to individual approaches because they are more efficient and involve less administrative costs for the employees. He strongly argued in favour of "not-for-profit" options and that these should not be replaced by "with-profit" options. The IORP Directive should create a framework that encourages employers to provide pensions to their employees, both domestically and across borders.

He mentioned that cross-border IORPs offer companies operating on a European-wide basis significant potential for improved governance, synergies in the areas of controlling, administration and asset management, transparency, as well as easier cross-border transfers of employees. The IORP Directive should not only facilitate cross-border labour mobility, but also provide a common structure to bring together different national pension schemes.

The creation of large cross-border collective pension schemes would be considerably facilitated if there were European-wide standard actuarial parameters (e.g. biometric tables, interest rates, calculation methods, etc.) to calculate technical provisions. At the same time, he stayed clear from suggesting that Solvency II should be applied to IORPs because this would place an unnecessarily high cost on the sponsor. Instead, pension rights would be better protected through a three-pronged system relying on dedicated supervision, strong employer covenants and an effective pension protection scheme in case of insolvency of the employer.

Question & Answers

Joao FERREIRA (Insurance and Pension Funds Supervisory Authority, PT) referred to a recent article in the IPE magazine of 22 May 2009 reporting that some multi-national companies are being advised "to exploit openings in the rules and regimes of other nations if it takes the pressure out of the company's cash flow". Although a number of panellists did not think that this points to a general issue of cross-border regulatory arbitrage, Jacqueline LOMMEN (Hewitt Associates) informed that her experience has also shown that active regulatory arbitrage is a reality, although not necessarily in funding requirements but also for other issues. When arbitrage concerns funding requirements, the question is not about whether these requirements are high or low, but about the degree of flexibility of the funding requirements: the definition of own funds, the use of a pension protection scheme, sponsor covenants and the discount rate. Multinational companies look for countries where they can combine these different elements of the funding regime in an efficient manner. Beyond funding requirements, regularity arbitrage also considers whether the vehicle provides flexibility: e.g. operating both defined-benefit and defined-contribution schemes, optional ring-fencing and supervisory attitude. Aerdts Houben (Chair) noted that the interaction of the different security mechanisms is very important.

Aerdts Houben (Chair) raised the question whether there is any future in trying to value the different security mechanisms with a view to reach a comparable level of security. In other words, is it possible to move beyond the harmonisation of solvency rules to the harmonisation of security levels? Brendan Kennedy (Irish Pensions Board) mentioned

that this would neither be appropriate nor possible. Security is part of social and labour contract. François VANDERSCHELDE (BBTK/SETCa, Belgian trade union) added that security in pensions has different meanings in different countries. In Belgium, the guarantee is a lump-sum at retirement; in the Netherlands, the guarantee is a lifelong income with flexibility in inflation indexation; while in Germany, the guarantee is a life-long pension indexed to inflation.

Aerdt HOUBEN (Chair) asked why we should allow a different level of security for pension funds in different Member States, when this is not the case in banking and insurance. He invited the Commission Services to comment. Karel VAN HULLE (Commission) replied that the main objective of the IORP Directive is to open up borders and facilitate cross-border activity. Obtaining an equivalent level of protection would require taking into account the additional security mechanisms for IORPs. Being difficult is not a good reason for not engaging with the issue. The question is rather what is the objective we want to achieve?

Aerdt HOUBEN (Chair) **concluded** the panel discussion by noting that the harmonisation of technical provisions and solvency rules is a highly complex topic and that more time for further discussions is necessary.

Panel 4: Broader issues raised during the consultation

Chair: **Elemér Terták**, Director Financial Institutions

Panellists: **Pablo Antolín**, Organisation for Economic Co-operation and Development (OECD), Financial Affairs Division.

Peter De Proft, Director General, European Fund and Asset Management Association (EFAMA).

Joao Ferreira, Insurance and Pension Funds Supervisory Authority (Autoridade de Supervisão de Seguros e Fundos de Pensões, ISP), Portugal.

Georg Fischer, Head of Social Protection and Social Services Unit, Directorate General Employment, Social Affairs and Equal Opportunities.

Csaba Varga, Member of CEIOPS' Managing Board, Director General, Hungarian Financial Supervisory Authority (Pénzügyi Szervezetek Állami Felügyelete).

The fourth and last panel of the Public Hearing was dedicated to broader issues that went beyond those directly raised in the consultation document itself. In his introductory remarks, **Elemér TERTAK** introduced the panellists and explained that the discussion would address three core questions:

- On defined-contribution (DC) schemes: Can we continue to have no EU solvency rules for DC schemes? Are the current EU rules for risk management, governance and disclosure for DC schemes sufficient? What about operational risk?
- On pension systems: In the light of population ageing, how do you see the prospects for people in retirement in say five years from now in the EU? Do you see convergence or divergence of national pension systems?
- The international perspective and the OECD policy recommendations for private pensions.

Pablo ANTOLIN (OECD) underlined the continued importance of private pensions and pointed at the following five OECD policy recommendations in this field: i) supervisory oversight should be flexible, risk based and proportionate; ii) funding and solvency rules for defined-benefit (DB) schemes should be counter-cyclical; iii) the design of DC schemes should be improved; e.g. through life-cycling or guarantees; iv) governance and risk management should be strengthened; and v) disclosure, communication and financial education should be stepped up.

He focused in particular on the design of DC schemes and mentioned that the accumulation and pay-out phases must be coherent and that a balance must be struck between investments and risk management in order to ensure adequate pension income. According to him it is important to introduce default options in pension schemes.

Peter DE PROFT (EFAMA) affirmed that pension products offered by IORPs should be matched with an appropriate solvency regime adapted to DB and DC schemes. While DB

schemes require solvency rules, DC schemes need to guarantee a certain performance while relying on governance (including risk management), asset protection rules and disclosure.

He also affirmed that the overall pension system should be modernised. In view of the demographic development in the coming years the pension system has no other possibility than to be adapted to the new challenges. This includes strongly encouraging people to save more for their pensions. According to him, there is now – and will be for the next five to ten years – a window of opportunity to act.

Joao FERREIRA (Insurance and Pension Funds Supervisory Authority, PT) made clear that solvency rules are linked to quantitative requirements which are typical for DB schemes. In order to establish solvency rules for DC schemes particular attention has to be paid to governance issues, financial education and disclosure mechanisms, as enacted in the so-called pillars 2 and 3 of the Solvency II Directive. He mentioned that CEIOPS is in the process of finalising a survey on risk management. The information collected so far already confirms that a broad spectrum of different risk management tools is used across Member States in practice.

He also referred to the 2009 Ageing Report², pointing at the fact that the dependency ratio is expected to drop significantly, from 1:4 today to around 1:2 in 2060. Demographic factors are projected to be the main driver in the future pension expenditure, thus having a considerable impact on public finances.

With regard to the international perspective he affirmed that the OECD recommendations should be taken as best practice and that they should be taken into account by the European Commission.

Georg FISCHER (Commission) identified three trends essential to the broader picture. The first one he deemed to be a rather underestimated point, which is the fact that a lot of state pension systems can be described as modern compared to private schemes (e.g. rules on indexation). A large number of countries have implemented pension reforms such as increasing the age of pensioners or reducing future replacement rates, thus making public pension systems less generous.

Secondly he diagnosed a deep crisis of confidence with regard to the objective of increasing reliance on private pension schemes. Financial education and further information on privately managed pension schemes are vital but must be complemented by more explicit contributions/explanations on the promises made by the industry and supervisors.

Thirdly, he cautioned against procyclical effects. The current rules have enabled to make unrealistic promises in good times that are unsustainable in bad times.

Csaba VARGA (CEIOPS) mentioned the strong trend towards DC schemes. According to him this calls for the examination of appropriate guarantees at European level. He mentioned that the new Member States have shaped their pension systems according to

² See: http://ec.europa.eu/economy_finance/publications/publication14992_en.pdf

the Word Bank model over the last ten years. He spoke in favour of minimum harmonisation at EU level, which could lead to further harmonisation in the future if appropriate.

With regard to the future pensions' landscape he advocated longer working periods for all in order to meet the demographic challenges.

Questions & Answers

Guillaume PRACHE (FIN-USE) supported the views expressed about the need to improve governance and regretted that no representative of small investors and individual savers had been invited on the panel. François VANDERSCHELDE (BBTK/SETCa, Belgian trade union) argued that the main concern of their members focuses on what they eventually get when they retire. Referring back to the question whether insurance companies and pension funds are competitors he argued that they are at least "fishing in the same pond". Xavier COGNAT (FFSA, FR) shared this view and recalled that there is increasing competition on the market. Equivalent solvency rules for all providers would ensure a level playing field and thus set the stage for fair competition. He also took the view that the crisis had underlined the value of guarantees embedded in pension products. Peter DE PROFT (EFAMA) noted that there is a price for the guarantees.

Moreover it was observed that there had been hardly any reference to individual private pensions, which generally offer tax benefits granted under national law. Georg FISCHER (Commission) suggested that the discussion should not focus on pension pillars but rather on how to best ensure rational replacement rates for pensioners. According to him state pensions will continue to be prevalent, however increasingly complemented by different forms of private pensions. Peter DE PROFT (EFAMA) strongly advocated awareness rising campaigns on pension savings, in particular among the younger people, given the fact that state pensions will not be sufficient in the future.

Michel RIQUIER (AGE Platform) raised the question as to the EU's strategy to appropriately meet and manage the current shift from the state to the individual. He asked how to reconcile the principles of sustainability and adequacy in the field of pensions and how to restore confidence in occupational pensions. Pablo ANTOLIN (OECD) replied that the "devil" is in the design of DC plans, such as the introduction of a default option. Disclosure and communication requirements should be stepped up. Joao FERREIRA (Insurance and Pension Funds Supervisory Authority, PT) added that there is indeed room to increase transparency in supervisory measures (e.g. information collected) and to improve communication with members. In addition, Csaba VARGA (CEIOPS) mentioned that financial education is important for two reasons: for fund managers in the context of the prudent person principle, and in the context of MiFID-style "know your customer" rules.

Michael VONK (Logica, NL) referred to the Dutch "Pensionsregister" which could serve as a model for a similar European registers in order to enhance transparency in private occupational and individual pensions. Such a register should be generally accessible and contain all relevant information, including data on solvency. Georg FISCHER (Commission) referred to the MISOC Info-System operated by the ESRC Research Centre on Micro Social Change at the University of Essex.

Elemér TERTAK (Chair) **concluded** the panel discussion by putting forward the most important factors identified. These include a number of high-level principles, in particular flexibility, proportionality, coherence, transparency, governance and sustainability which should be embedded into a holistic approach.