

10 April 2009

EFRP Response

EUROPEAN COMMISSION CONSULTATION ON THE IMPROVEMENT OF SUPERVISION FOR THE FINANCIAL SERVICES SECTOR

Comments on:

- the de Larosière report
- Commission Communication COM(2009)114

EXECUTIVE SUMMARY

1. The EFRP recognises the absolute need to restore trust in financial institutions. It therefore welcomes the serious attention that the European Commission is giving to the issues that the recent crisis has raised with EU systems for the regulation and supervision of financial institutions.
IORPs, as long term investors and providers of security in retirement as a response to the ageing society, should have an important part to play in the recovery.
2. As a representative body for major institutional investors, the EFRP also welcomes the action that is proposed to strengthen the regulation and supervision of the sectors in which the current serious financial problems originated, and to address issues of concern such as pro-cyclicality and mark-to-market accounting rules.
3. The EFRP does, however, have serious concerns about proposed changes to the structure of EU-wide supervision proposed by the de Larosière report and endorsed with an accelerated timetable by the Commission with detailed proposals expected in May 2009. Implementing the proposals without giving due consideration to the supervision of IORPs could prove to be an inappropriate knee-jerk response to the current crisis.
4. The EFRP is also concerned by the absence of any consideration in the de Larosière report or the Commission's proposals of how IORPs fit within the proposed renewed European Financial Supervision System, and the associated initiative to harmonise the implementation of financial services directives. The omission may be understandable given that IORPs, although impacted by the crisis neither contributed to it nor exacerbated it.
5. The omission though creates considerable uncertainty in view of the substantial differences between IORPs and other financial institutions, notably insurers, as IORPs:
 - deliver a key element of employment contracts that contributes to member state pensions and social protection policies that remain within national (not EU single market) competence;
 - are generally not-for profit organisations with employer sponsorship and are run in the interest of members and beneficiaries;
 - their oversight and governance often includes member representation and/or institutionalised social partners involvement;
 - pan-EU IORPs are unlikely for some time to gain the systemic significance that other types of pan-EU financial institutions have;
 - are long term investors, subject to a different risk profile and to limited liquidity risk;
 - can share risks, to varying extents, with sponsoring employers and employee members.

6. In view of the wide diversity in member state pensions systems, the IORP Directive leaves considerable interpretative discretion to member states, by setting minimum standards rather than requiring full harmonisation. Member states can in particular specify the 'social and labour' law which needs to be applied by cross-border IORPs with members in their jurisdiction. This in turn means that cross-border supervisory arrangements differ from other financial services with home/host provisions that render any concept of colleges of supervisors unnecessary and irrelevant.
7. These differences remove the need of, and would make inappropriate, any substantial further harmonisation at this time, as is recommended for other financial services – a conclusion that can also be drawn from two reports issued by CEIOPS Occupational Pensions Committee in March 2008.
8. The proposed replacement of CEIOPS by a 'European Insurance Authority', leaves unclear the continuing status of the work of CEIOPS in the occupational pensions sector, and in particular its Occupational Pensions Committee.
9. A 'European Insurance Authority' including IORPs, but dominated by insurance supervisors and exercising qualified majority voting, cannot be viewed as a strengthening of the supervision of IORPs given the major differences between IORPs and insurers. Furthermore, only a subset of the de Larosière recommendations for strengthened supervisory powers applies substantially to IORPs.
10. The EFRP therefore seeks an arrangement that respects the differences between IORPs and insurers, either through a separate body or a European Insurance and Occupational Pensions Authority that has separate remits and decisions making strands for each of the two sectors. Perhaps even better would be a prudential authority covering all financial services, but with separate strands for each sector yet, that could address the cross-sectoral issues that have been so influential in this crisis. Market conduct might be handled separately applying a 'twin-peaks' model.
11. The EFRP asks the Commission to:
 - confirm that any changes will be in line with Better Regulation Principles and based on clear evidence that change is needed and would achieve its aims;
 - clarify that the proposed initiative to harmonise the implementation of financial services Directives will not cover the IORP Directive;
 - consider and explain how IORPs should fit into the renewed European Financial Supervision System in a way that properly reflects their differences with other financial institutions;
 - work with the EFRP on developing a new supervisory structure that encompasses occupational/workplace pensions.

EFRP RESPONSE TO:

- THE DE LAROSIÈRE REPORT
- EUROPEAN COMMISSION COMMUNICATION “DRIVING EUROPEAN RECOVERY”

I. IDENTIFICATION OF RESPONSE

The **European Federation for Retirement Provision (EFRP)** represents the various national associations of pension funds and similar institutions for supplementary/occupational pension provision. Its membership at large consists of institutions for workplace (2nd pillar) retirement. Some of them are also operating purely individual pension schemes (3rd pillar).

The EFRP has **28 members associations** in most EU-15 Member States and other European countries that have a significant – in size and relevance – workplace pension system¹

Within EFRP the **Central & Eastern European Countries Forum (CEEC Forum)** has been established (26 October 2006) to discuss issues common to pension systems in that region. The CEEC Forum has not expressed its view on this consultation.

83 million EU citizens are covered for their workplace pension plan by EFRP Members. Through its Member Associations the EFRP represents approximately **3,5 trillion of assets (2007²) managed** for future occupational pension payments.

The EFRP is registered in the EU Commission register of interest representation: number 5199259747-21.

Contact:

Ms. Chris VERHAEGEN, Secretary General

Koningsstraat 97 – 1000 Brussels

Tel: +32 2 289 14 14 / Fax: +32 2 289 14 15

efrp@efrp.eu

www.efrp.eu

¹ EU Member States: Austria, Belgium, Finland, France, Germany, Hungary, Ireland, Italy, Netherlands, Portugal, Romania, Spain, Slovakia, Sweden, UK.

Non-EU Member States: Croatia, Guernsey, Iceland, Norway, Switzerland.

² The financial and economic crisis has resulted to a drop of pension fund assets of 15-20% on average. As to date, it is not yet possible to provide aggregate figures for the European pension funds market end 2008.

II. GENERAL REMARKS

1. The EFRP recognises the **absolute need to restore trust** in financial institutions. Pension funds, as major institutional investors, need stable financial markets to invest the contributions of scheme members and to deliver work place pensions, so as to provide greater security in retirement and reduce the burden on State pay-as-you-go pension systems. In this context, the EFRP has consistently called for continued attention to the long term challenges of an ageing population, and notes that a greater role for work place pensions could be particularly timely. Shifting capital into long term investments overseen by institutions with clear fiduciary responsibilities to their members and with social partners' involvement should reduce volatility and increase trust in financial markets.
2. The EFRP therefore **welcomes the serious attention** that the European Commission is giving to the issues that the recent crisis has raised with EU systems for the regulation and supervision of financial institutions.
3. Speaking as a representative body for major institutional investors, the EFRP **finds much to support** in the recommendations made **in the de Larosière report and by the Commission, as they relate to the financial sectors in which the current crisis originated**. The EFRP is especially pleased by the proposals relating to the **pro-cyclicality of capital requirements** and **mark-to-market accounting rules**, as mentioned at the end of this paper. We have commented to the European Commission separately on remuneration³ and hedge funds.⁴
4. The EFRP does, however, have **serious concerns** about proposed changes to the structure of EU-wide 'micro-prudential' supervision proposed by the de Larosière report and endorsed with an accelerated timetable by the Commission with detailed proposals expected in May 2009. Implementing the proposals **without giving some consideration to the supervision of IORPs could prove to be an inappropriate knee-jerk response to the current crisis**.
5. The EFRP notes that **IORPs** and pensions supervision are **not mentioned** in the de Larosière report or the Commission's Communication. This is understandable because IORPs have a **number of features that distinguish them from other financial institutions**. IORPs:
 - have neither been a source of, nor have they exacerbated, the financial crisis; although they have been seriously effected by the fall-out⁵;
 - differ from banks, insurers, asset managers and other financial institutions in that they manage privately funded pension schemes/

³ EFRP preliminary response to questionnaire on CEBS Principles, 9 March 2009

⁴ EFRP Response: EC Consultation on Hedge Funds, 31 January 2009

⁵ European Commission, technical memo 09/99: the economic crisis and pensions in the EU, 6 March 2009

products, the delivery of which is largely defined under national social and labour law;

- do not (yet) generally operate cross-border;
- do not have EU systemic impact; and
- are generally not-for-profit organizations or not market based institutions in that they operate as corporate 'in house' or 'in group' mechanism for occupational pension provision⁶.

6. This omission raises a **potentially serious concern** for the EFRP because it is unclear whether or how the proposed changes are expected to impact on the regulation and supervision of IORPS. **A straight read across from other financial services to pensions would be particularly problematic**, because:

- the IORP Directive is fundamentally different from EU mainstream financial services directives – such as those for banking and insurance - in that it sets minimum standards rather than seeking full harmonisation.⁷ Proposals for harmonising national regulation under the financial services directives to reflect the extensive cross-border activity in those sectors ought therefore not to apply to the IORP Directive.
- the role of CEIOPS in relation to IORPs differs considerably from its role in relation to insurance. In the former sector it encourages and reviews the implementation of the IORP Directive as well as information exchange with host state supervisors. In the latter it works under a harmonisation regulatory framework and coordinates the supervision of cross-border activity.
- at this point in time cross-border IORPs constitute a very small element within the occupational pensions sector, and there have been no problems arising from the allocation of supervisory roles by the IORP Directive to the home and host supervisor. The IORP Directive makes a clear and essential distinction between the home supervisor, responsible for the prudential supervision of an IORP, and the host supervisor responsible for informing the home supervisor of the social and labour law applying to IORP members within its member state. The report's recommendations relating to colleges of supervisors for cross-border financial institutions are therefore irrelevant for occupational pensions.

⁶ Although their aims and fiduciary roles are common, IORPs comprise a wide diversity of institutions delivering a wide range of promises, as acknowledged by the IORP Directive (Dir. 2003/41/EC, 3 June 2003)

⁷ It should be noted that the IORP Directive is not a Lamfalussy Directive, although the decision establishing CEIOPS gives this committee a level 3 and advisory role on IORPs. Having said that, it should be noted that the political compromise of the Solvency II Dir. has taken care of amending the IORP Dir. on this particular point and will insert into article 21b IORP Dir. a comitology clause by its article 305a.

III. RECOGNISING THE DISTINCTIONS BETWEEN PENSIONS AND INSURANCE

7. While the de Larosière report and Commission Communication remain silent on how IORPs might fit within future EU harmonisation of financial services supervision, the proposed transition of CEIOPS into a European Insurance Authority could be read as implying that occupational pensions should be treated similarly to insurance. **The EFRP strongly believes that the treatment of the two sectors needs to be separate and different**, as changes which make sense for insurance may be irrelevant or positively harmful if applied to occupational pensions. The EFRP's position is based on:
- the numerous fundamental differences between IORPs and insurers (box 1);
 - different types of risks to which IORPs are exposed (box 2);

Box 1 – FUNDAMENTAL DIFFERENCES BETWEEN IORPs AND INSURERS

- IORPs operate occupational pension plans which are established as a deferred remuneration element within a long term employment arrangement between employers and their employees, rather than being sold directly by the ultimate provider. Hence, the **employer has a considerable and ongoing stake in their cost-effective delivery and the minimisation of risk**, a role not present for retail products;
- Employers are required to provide through a regulated pension fund/institution fiduciary management of the pension plan which is **in the interests of members and beneficiaries**. This arrangement largely avoids the risk, inherent in commercially provided products, that the provider will seek to take risks or incur costs for commercial gain at the policyholder's expense;
- The **boards running or overseeing occupational pension funds commonly include representatives of the ultimate beneficiaries**, providing a further safeguard unknown in other sectors. In some Member States **institutionalised social partners play a role in the governance** of the IORPs, for instance by sitting on the Board of Directors, or in a Control Committee or Advisory Board. In others, employers and members nominate the trustees who are responsible for running the IORP. These types of oversight mechanism help safeguard the interests of the sponsor and beneficiary, and are absent in commercially led organisations. This needs to be taken into account when considering the supervisory regime of each type of financial institution.
- The EU legislator has recognised the distinction between occupational pensions and other financial products in the cross-border provisions of the IORP Directive, which require the **home regulator to enforce the**

social and labour law of the host nation – diverging significantly from the colleges approach as under insurance supervision.

- Because of the link between occupational pension plans and their sponsoring employers, IORPs can only operate cross-border to the extent that employers find such an arrangement beneficial, a development slowed by the complexity involved in differing sets of social and labour law. Pan-EU IORPs are **unlikely for some time to gain the systemic significance** that other types of pan-EU financial institutions have.

Box 2 – IORPs ARE EXPOSED TO DIFFERENT TYPE OF RISK

- Pension plans are inherently **long term products** designed to take advantage of long term investment opportunities while (in many cases) **spreading risk through inter-generational solidarity**. Regulation against a short-term horizon (such as the one-year horizon in banking and insurance) would be inappropriate and potentially damaging, as is recognized by some national regulatory frameworks in the EU.
- In particular, as retirement products, pension funds are subject to **minimal liquidity risk** compared with other sectors. Pension funds can broadly forecast when benefits will start become payable and hence short and medium term cash flows are reasonably predictable. You cannot have a ‘run’ on a pension fund, as you can on a bank or insurer. This fact has gained in significance given the fundamental issues with the regulation of institutional liquidity identified in the de Larosière report.
- Further, defined benefit pension funds are impacted more heavily than other financial institutions by **longevity risk** and the risks associated with long term movements in **investment returns and interest rates**. Long term capital adequacy is therefore a major issue, but there is usually sufficient time to remedy deficiencies that emerge.
- It can therefore be seen that an insurer or a bank is an institution with limited control over when it will have to pay out, but a good feel for how much will be needed should payment be needed. A defined benefit pension plan knows when it is likely to have to start paying out but cannot easily forecast the duration and hence ultimate size of the payment stream. These are **very different risk environments requiring very different regulatory and supervisory regimes**.
- Many pension funds, however, are **better placed to manage capital adequacy risks** than other financial institutions, because of their unique ability either to call on additional resources from sponsoring employers, or to vary benefit levels (for instance inflation indexation) to reflect their

financial circumstances.

- Risk-sharing makes it possible for pension funds to hold lower reserves than comparable commercial institutions but does expose the fund to **counter-party risk. Different EU countries have taken different approaches**, within their national competence, to regulation for this risk, including insolvency protection funds, powers to sequester associated company assets or requirements to hold additional funds or buffers sufficient to minimise dependence on the sponsoring employer.

8. It can therefore be seen that occupational pension provision differs fundamentally from insurance and other financial services, and can legitimately differ considerably from one Member State to the next. In recognition of national competences over these systems, the **IORP Directive is restricted to the minimum standards needed to permit a single market that protects members**, rather than detailed specification of prudential standards.

IV. HARMONISATION OF THE IMPLEMENTATION OF FINANCIAL SERVICES DIRECTIVES

9. In view of the substantial differences between IORPs and other financial institutions, and of the IORP Directive to other financial services directives, **the EFRP is very concerned** about the potential applicability to IORPs of the proposal for a determined and concerted effort to equip the EU financial sector with a harmonised core set of rules, including the elimination of key differences in national legislation. As explained above, many of the differences in national legislation reflect the national competence over pension provision arrangements. **Comprehensive harmonisation would therefore risk imposing requirements on IORPs that are unsuited** to their role in national pension systems and the social and labour law related to it.
10. **Harmonisation of prudential regulation for occupational pensions is unjustified**, according to the EC Better Regulation principles, as none of the problems identified in the de Larosière report have arisen in the occupational pension sector or can be attributed to differences between pensions regulation. As the EFRP has already explained,⁸ there is no evidence that national pensions regulation falls short of the minimum standards in the IORP Directive, nor that there have been competitive distortions or regulatory arbitrage.

⁸ EFRP: Response to EC Consultative Document Ares(08)14767 on IORPs covered by article 17 of the IORP Directive and IORPs operating on a cross-border basis, 28 November 2008.

11. It would in any case be **inappropriate** for any rush to harmonisation to cut across or **ignore the findings on this subject of CEIOPS** (and its occupational pensions committee (OPC) in particular – see box 3).

Box 3 – CEIOPS FINDINGS ON IORP DIRECTIVE

- The CEIOPS-OPC March 2008 report on the **implementation of the IORP Directive**⁹ concluded that “*its work showed that there is considerable diversity in the way some key aspects of the IORP Directive have been interpreted and implemented, but provides little evidence of major issues arising from these differences*”. The report added that “*there is also some significant scope for further analysis. CEIOPS has identified some issues where action appears to be needed for clarity and for supervisory convergence*”. These issues cover legal definitions of matters that are unlikely to be germane to broader harmonisation.
- The CEIOPS/OPC Solvency sub-committee looked at the implementation of the provisions in the Directive relating to technical provisions and other security mechanisms¹⁰. Its March 2008 report states that “*as a final note, there is an apparent interaction between the different elements that make up the pension frameworks across Member States. For example, emphasis on prudent valuation principles, which results in extra reserves, reduces the need for additional security mechanisms. Overall security or solvency cannot be understood without a full appreciation of all the elements involved. A comprehensive analysis of the overall security level provided to beneficiaries requires a common language to encompass all individual elements*”.

12. A common theme therefore is that the issues that would be involved in further harmonisation are complex and necessitate more analysis and understanding. **No case for hurried harmonisation is evident.** The EFRP assumes that some other harmonisation recommendations in the de Larosière report should also not be intended for occupational pensions. In particular, the recommendation that “*an equal and high level of protection to all depositors, investors and policy-holders should be guaranteed, avoiding competition distortions between institutions and between sectors*” would fall foul of the highly

⁹ CEIOPS-OP-03-08 (final), 31 March 2008: Initial review of key aspects of the implementation of the IORP directive.

¹⁰ CEIOPS-OPSSC-01/08 Final, 31 March 2008: Survey on fully funded, technical provisions and security mechanisms in the European occupational pension sector.

diverse attitude of national governments to pension insolvency protection schemes.

13. **The EFRP asks the Commission to clarify that proposals regarding the harmonisation of the implementation of financial services directives are not intended to apply to IORPs.** Were the harmonisation review nonetheless to cover the occupational pensions sector, it would be essential that it build further on the reviews of the IORP Directive that CEIOPS-OPC already have in hand.
14. Furthermore, **any technical advice** on the potential, if any, for further harmonisation **must come from specialists in the pensions field** who are aware of the constraints and sensitivities, not a body dominated by insurance supervisors and applying qualified majority voting as set forward under the 'European Insurance Authority'. This highlights the importance of an **appropriate structure for EU oversight of IORPs.**

V. DESIGN OF THE EUROPEAN SYSTEM OF FINANCIAL SUPERVISORS

15. The lack of reference to how IORPs might, or might not, fit within the proposed European System of Financial Supervisors could be seen as ignoring the substantial differences between pensions and insurance. In particular, CEIOPS is intended to evolve into a new authority for insurance. The fundamental issue from the EFRP's perspective is whether the new insurance authority should also cover occupational pensions, as CEIOPS does. The title of the proposed new authority excludes occupational pensions, unlike CEIOPS, which suggests that occupational pensions may be excluded, and given the distinctiveness of this sector, there could be good reason for this exclusion. **The EFRP sees serious problems** with any implementation of the Commission's proposals that sought **to apply them to occupational pensions in the same way and structure as insurance, even assuming that the name of the authority includes 'occupational pensions', as of course it must.**
16. Firstly, the new Supervisory Authority is intended to be more pro-active in identifying problems and proposing solutions and use **qualified majority voting**. Consequently, it could easily stray into the national competences relating to pensions which are the cause of many of the divergences that might be seen as problematic by some stakeholders. The EFRP notes, however, that in practice such differences can be acceptable if supervisors – and regulators - accept the mutual recognition of supervisory standards in occupational pension provision instead of relying on harmonisation. The Authority could also inappropriately apply decisions that make sense in the insurance market to pensions **against the better judgment of the relatively few supervisors responsible for substantial occupational pension sectors.**

17. Furthermore, it is clear that **several of the new Authority's functions would not make sense for IORPs** or could potentially harm the sector unless occupational pensions were treated separately from insurance - see box 4¹¹.. This approach would imply separate remits and decision making strands for each of the two sectors.

BOX 4 – NEW AUTHORITY'S FUNCTIONS THAT DO NOT FIT FOR IORPs

- the proposals for **supervisory colleges** for all major cross-border firms, under the wing of the regulatory authority would not in practice apply to IORPs where such entities currently do not exist, even assuming that the fiduciary bodies responsible for pension plans fit within the definition of 'firms'. Hence, a major function of the new Authority would not apply to pensions.
- the proposed **powers over national supervisors in relation to cross-border institutions**, including ensuring a true level playing-field for all cross-border institutions and monitoring of systemic threats, would also be largely irrelevant. To date there are just 70 cross-border IORPs, few (if any) of which operate in more than two member states, representing a very small part of total IORP membership and no systemic risk. National competence over social and labour law puts much of the playing field out of scope. There is no evidence of any disputes to resolve, of any risks from differences in supervisory approach or of any systemic implications.
- the proposed requirement to **ensure consistency of prudential supervision for all actors** to avoid the risk of unfair competition between supervised entities, in particular by receiving complaints about cross-border discrimination, is similarly of little relevance to pensions. Few of the cross-border IORPs established since the IORP Directive came into force are defined benefit and hence subject to significant regulation of funding levels. Furthermore, as the EFRP has already commented, there is no evidence and little likelihood of regulatory or supervisory arbitrage or competitive distortion. There is, however, a risk that this function could be used to justify inappropriate harmonisation that does not respect the differences between national pension systems and between pensions and insurance.
- the proposed **prudential assessment of pan-EU mergers and acquisitions** appears irrelevant to IORPs. It seems unlikely that IORPs sponsored by different employers in different countries would merge in a way

¹¹ All the functions referred in box 4 have been taken from the relevant section of the de Larosière report. The Commission Communication is insufficiently detailed to indicate whether these remarks are supported by the Commission.

that would raise pan-EU prudential issues.

- the proposed power to **give legally binding interpretations of EU Directives** could be relevant to the IORP Directive, where there are a few significant differences in interpretation. It would, however, be essential for such interpretations to be made by pensions experts. There would also need to be safeguards to prevent such interpretations straying beyond the competence of financial market supervision or driving backdoor harmonisation of rules which the Directive deliberately leaves un-harmonised.

18. The EFRP therefore notes that **only a subset of the de Larosière recommendations apply substantially to IORPs** and that some that do apply would need to be approached differently than in insurance. Furthermore, CEIOPS already finds it difficult to balance its role in relation to insurance, where the harmonization of regulation and cross-border supervision are fundamental issues, with its role in relation to occupational pensions where the key issues relate to improving the understanding of how the IORP Directive should be implemented. The committee has struggled to devote sufficient and balanced attention to both sectors, leaving most of the attention to occupational pensions to its Occupational Pensions Committee.

19. The EFRP could therefore **see some merit in placing IORPs under a separate body from insurance** with more limited powers than the 'European Insurance Authority', that are tailored to the particular circumstances of IORPs. We believe that such a body could significantly contribute to the development of common standards for occupational pension supervision without a need to further harmonise the principles-based IORP Directive. The EFRP is open to work with the EU Commission on the structure and mandate of such a specific supervisory structure for IORPs.

20. The EFRP recognises, however, that the majority of supervisors of occupational pensions in the EU also supervise insurance, and hence that functions relating to the supervisors themselves fit readily with a body covering both sectors.¹²

21. It may therefore be that the Commission intends to include occupational pensions within the new authority's remit, in which case, **the EFRP asks that :**

- the title of the 'European Insurance Authority' **should** – as with CEIOPS – **incorporate 'occupational pensions'**;

¹² This is particularly the case for the proposed strengthening of the role of CEIOPS in relation to training and personnel exchange for supervisors, reviewing national supervisors and setting up crisis management groups

- there should also be a requirement for some members of the Authority's governing board and executive to have **recent pensions supervisory experience**;
 - there should be a separate "occupational pensions **consultative panel**".
 - the Authority's **decision making structure should be double-headed** to reflect the two industry/sector lines within its competence and reflecting that a name-change by itself would not sufficiently reflect the substantial differences between pensions and insurance.
22. The separation of functions relating to the regulation of occupational pensions and insurance could be achieved through an **empowered occupational pensions committee** (OPC) with delegated powers over matters relevant only to occupational pensions and the IORP Directive. The Committee, as now, should be restricted to supervisors responsible for financial institutions operating under the IORP Directive. Otherwise, an insurance dominated Authority (with qualified majority voting) would risk imposing decisions paying insufficient attention to the distinctive features of IORPs and hence undermine the appropriate regulatory and supervisory framework for the occupational pension sector.
23. That said, if occupational pensions are to be included in an authority covering other financial services, it is not clear why it should just be insurance. The EFRP notes that the **current problems owe much to the inter-relatedness of financial institutions**. The proposal to retain separate regulatory authorities for different sectors, albeit under the umbrella of the European Systemic of Financial Supervisors (ESFS), appears to be missing an opportunity to respond effectively to the problems that the de Larosière report identifies.
24. The EFRP therefore **supports the Commission's intention to consider seriously the establishment of a single authority** to exercise executive powers in relation to systemic issues and cross-border institutions across all financial sectors. Such an authority should be organised into divisions for each sector, treating occupational pensions separately from insurance, given the much reduced relevance to occupational pensions of pan-EU systemic risk and cross-border activity as yet. This institution with separate strands for each sector could address the cross-sectoral issues that have been so influential in this crisis.
25. If an authority covering all financial sectors were considered too unwieldy, the **EU could consider a 'twin-peaks' model**, with a single authority for prudential supervision and another for market conduct, reflecting the division of responsibilities found in many member states.. This would still retain in one place full responsibility for the prudential supervision of financial institutions operating in multiple markets. There would still need to be an occupational pensions division within the prudential authority but market conduct has limited relevance to occupational pensions, which are mostly not retail products and

any pensions issues arising could be considered alongside issues in other markets.¹³

VI. OTHER RECOMMENDATIONS

26. Turning to some other important issues and recommendations raised in the de Larosière report and the Commission Communication:

- The EFRP **fully supports** the EU Commission initiative to address the **pro-cyclicality of existing capital requirements** in the banking and insurance sector. This issue is especially important for long term investors such as pension funds which are keen to see the returns on their extensive investments in these sectors smoothed rather than made more volatile by regulatory requirements.
- The EFRP **fully supports** the EU Commission intention to have more influence on the **standard setting process of the IASB** in particular in relation to the mark-to-market accounting rules which have exacerbated some of the recent problems of financial institutions. In this context, the EFRP notes that the IASB 'mark-to-market' approach for long-term pension fund liabilities is irrelevant where they will not mature for many years and introduces damaging volatility by seeking to where there is no deep and liquid market.
- The EFRP has made separate submissions on the issues of **remuneration**¹⁴ in the financial services sector and **hedge funds**¹⁵.

VII. CONCLUSIONS

27. It appears evident that little attention has yet been given to how IORPS are to fit in the move to a renewed European System of Financial Supervision

¹³ For instance, in the UK the Pensions Regulator has minimal involvement in market conduct and these issues so far as they affect pensions are covered by the retail division of the Financial Services Authority, the supervisor of other financial services.

¹⁴ EFRP preliminary response to questionnaire on CEBS Principles, 9 March 2009

¹⁵ EFRP Response: EC Consultation on Hedge Funds, 31 January 2009

recommended by the de Larosière report and largely endorsed by the European Commission. The EFRP emphasise that the **differences** between occupational pensions and other financial services **are so great that it would be dangerous simply read-across conclusions applying to other sectors, notably insurance**. In particular:

- there is no evidence to support extending the proposed rapid harmonisation of financial services regulation to occupational pensions;
- many of the proposed new powers for the new supervisory authorities would not fit easily with occupational pensions, or could be harmful if applied in a similar manner to insurance; and
- if a single authority is to be responsible for occupational pensions and insurance it would need a title and double-headed structure reflecting the two sectoral roles.

28. The EFRP also notes that a supervisory authority with similar sectoral scope as CEIOPS may not be the best way forward. The problems caused by the connectedness of financial markets and institutions, and the distinctive position of IORPs (which are not commercial nor multi-nationals), might be better addressed **either by a single authority for all prudential supervision (with sectoral divisions) or a specialist body for occupational pensions**.

29. The EFRP is concerned that any rushed changes that do not fully consider the implications for occupational pensions could prove unworkable, or worse still, cause serious harm to the sector at a time when its potential contribution to the EU's ageing society is increasingly critical for the delivery of good quality pensions. The EFRP therefore calls upon the European Commission to explain how, if at all, its proposals are intended to apply to IORPs, and **seeks assurances that any changes** affecting this sector will:

- be made only where **justified by Better Regulation principles**;
- **reflect the substantial differences** between IORPs and other financial institutions; and
- **leave decisions** on occupational pension supervision **to pensions supervisors**.

30. The EFRP would be very happy to discuss further the most appropriate structure for the renewed European System of Financial Supervision with a view to ensuring that the system takes proper account of the distinctive position of IORPs.
