

Implementation of IORP II:

# **REPORT ON THE PENSION BENEFIT STATEMENT: GUIDANCE AND PRINCIPLES BASED ON CURRENT PRACTICES**

November 2018

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## EXECUTIVE SUMMARY

This report analyses the national practices existing prior to the implementation of the 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 (IORP II), concerning the annual information document (annual statement) sent to institutions for occupational retirement provision (IORP) members and, based on that, draws principles and guidance for the design of a Pension Benefit Statement (PBS) as required under the IORP II.

The report presents the outcomes of national competent authorities' (NCAs) exchanges of views and assessments of current practices for the implementation of the IORP II PBS requirement conducted by EIOPA from Q2 2017 to Q2 2018. NCAs had identified core areas where guidance drawn from existing practices would be beneficial for a significant number of Member States in order to implement the IORP II requirements and promote consistent practices including the development of standardised elements in the PBS templates: content-wise this concerns the information on costs and projections given to members; from a format perspective, the focus is on the presentation of the PBS in line with behavioural economics.

In particular, four areas of work were analysed within the PBS: the goal of the PBS, pension projections, cost disclosure as well as the use of layout and layering tools.

The chapter on the **goal** provides an overview of the behavioural and legal aspects surrounding pension communication, the trend from defined benefit (DB) to defined contribution (DC) and the importance of providing adequate information to help members make informed decision. It also draws general principles on the design of the PBS.

The chapter on **projections** presents the different **possible approaches** and the **assumptions** that are taken currently into account in the projections' methodologies.

On the basis of existing practices as well as considering research on consumer behaviour, the **chapter on costs identifies principles** to be taken into consideration by Member States in the implementation of IORP II in order to serve the behavioural purposes identified in the first chapter.

The chapter on layout and layering presents the practices from existing annual statements at national level and highlights the pros and cons of the different layout and layering tools. Based on that, it identifies several principles to be considered for a PBS design. Finally, two proposals are put forward: a **basic PBS** and an **advanced PBS**, as an attempt to fulfil the PBS goals taking account of the behavioural approach principle and it encourages further consumer testing.

# 1. INTRODUCTION

The 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) provides an updated EU legislative framework for workplace pensions. The Directive will improve the way pension funds are governed, make it easier for pension funds to conduct cross-border business and provide clearer information to pension scheme members and beneficiaries. EU Member States must transpose the new rules into their national law by 13 January 2019.

The IORP II Directive states that every Member State shall require IORPs to draw up a concise document, a so-called pension benefit statement (PBS), which should be made available to each member at least annually.

Second pillar pension communication differs across Member States: some Member States have a long history with providing information on second pillar pensions, require the provision of documents that already closely resemble a PBS and have conducted extensive consumer testing, while other Member States still have to develop second pillar pension communication.

This report provides principles and guidance regarding the design and content of the PBS based on pre-IORP II national experiences with prior documents either required under IORP I or under national legislation.

The principles and guidance relate to the provisions on the PBS in Title IV of IORP II are: “Information to be given to prospective members, members and beneficiaries”. In particular, four articles refer to the PBS: Article 36 (Principles), Article 38 (General provisions), Article 39 (Pension Benefit Statement) and Article 40 (Supplementary information):

- According to the principles envisaged in Article 36, the information in the PBS should, inter alia: be written in a clear manner, use clear, succinct and comprehensible language, not be misleading, have consistency in vocabulary and content, and be presented in a way that is easy to read.
- Article 38 requires the PBS to be concise, to contain key information for each member, to take into consideration the specific nature of the national pension system and relevant social, labour and tax law. The title of the document shall contain the words Pensions Benefit Statement. The exact date to which information in the PBS refers shall be stated prominently. Member States shall require that the information to be accurate, updated and made available to each member free of charge, through electronic means or on paper at least annually. A paper copy of PBS shall be provided to members on request in addition to electronic information.
- Article 39 provides a list of key information to be included (as a minimum) in the PBS, namely: a) personal details and retirement age, b) IORP and scheme identification, c) guarantees, d) pension projection(s), e) accrued entitlements or accumulated capital, f) contributions in the last 12 months, g) breakdown of the costs deducted by the IORP at least over the last 12 months and h) funding level of the scheme).

- Article 40 requires the PBS to indicate where and how to find supplementary information on: member's options, annual accounts, statement of investment policy principles (SIPP), annuities and the level of benefits in case of cessation of employment.

Annex 1 includes a cost and benefit analysis, which covers the rationale and objectives of the policy options that have been considered in the development of this report.

## DEFINITIONS

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List of definitions used in this report:

- **Second pillar:** an occupational pension that can be provided by an IORP, or other pension funds outside of the scope of the IORP II Directive, a financial institution, e.g. a bank, an insurance undertaking or an investment fund, or pension fund management entity. Note that the report addresses only IORPs, and not pension vehicles of the second pillar to which the IORP II Directive does not apply.
- **Pension provider:** either an IORP or other pension fund or financial institution, like an insurance undertaking or a bank, that provides an occupational pension scheme. The report refers solely to pension providers with regard to the IORPs.
- **IORP:** an institution operating on a funded basis for the purpose of providing retirement benefits as defined in Article 6 of IORP II Directive (Directive (EU) 2016/2341)
- **IORP II Directive:** 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).
- **Member:** As defined in Article 6 of IORP II Directive, a 'member' is a person, other than a beneficiary or a prospective member, whose past or current occupational activities entitle or will entitle him/her to retirement benefits in accordance with the provisions of a pension scheme. A further distinction can be made between a current member who is actively saving for their pension and a deferred member who no longer actively saves for their pension with a certain provider but does have accumulated entitlements or a pension pot.
- **Beneficiary:** a person receiving retirement benefits.

## 2. WHAT IS THE GOAL OF THE PBS?

Pension systems around Europe differ remarkably.

Some Member States rely more on first pillar pay as you go (PAYG) systems, while others have a system which is based on funded schemes. Some Member States have a substantial second pillar pension system, mainly based on occupational pension schemes. There are marked differences between the second pillars across Europe. There are some Member States with defined benefit (DB) occupational pension schemes where, for example, the benefits are defined by reference to the member's salary. Other second pillar systems are primarily defined contribution (DC) where the contribution from the employer and employee are defined and the final retirement sum is determined by the contributions and also investment growth minus any costs.

Some European pension systems rely more on the third pillar which is comprised of personal pensions or individual schemes. Many systems have a combination of first, second and third pillars.

In the majority of Member States there is an increasing trend towards DC pension provision. Indeed, the majority of new pension provision is done through DC pensions. DC pensions place more of the risk and responsibility of pension accumulation on the individual in comparison to DB schemes where the risk and cost tend to fall to the employer or the IORP. One of the causes of this trend is that sponsors and employers are increasingly struggling to meet the promises they have made in the past and thus unable to bear the cost of pension risk alone. This risk, which is de facto a funding gap between contributions and promised lifelong payouts, is caused by (1) the increasing volatility of financial markets and the low interest rates which increase the cost of pensions and (2) by demographic changes, including among others increased longevity of the European population. The latter means that pensions have to be paid out for a longer period than originally anticipated.

This leads to an increased need for decision making by pension scheme members themselves, particularly DC members or their representatives - whilst noting that the PBS is of course relevant for informing both DC and DB pension scheme members. The disclosure of information in the PBS is a very important part of keeping members updated with

vital information relating to their savings and their projected benefits.

However, one's future financial situation is typically a sum of various financial sources of which the PBS, or various PBSs, is or are an important component. EIOPA therefore sees the added value of the PBS primarily in a context of more holistic retirement planning. The PBS allows a member to assess a part of their financial situation and consider if there are any actions the member can take. The information in a PBS should prompt the member to address the questions of whether he or she is saving enough during the accumulation period for an adequate and sustainable pension.

### 2.1. GOALS

#### MAIN GOAL

**The main goal of the PBS is to provide an overview of retirement income provided by IORPs in order to improve the adequacy of savings.**

This goal is achieved by four subgoals:

1. outlining the current situation of the member regarding the accrual of his/her pension benefits;
2. projecting future retirement benefits,
3. enabling retirement planning and
4. helping the member to make informed decisions.

#### SUBGOAL 1: OVERVIEW OF CURRENT RETIREMENT SAVINGS

The first key element of the PBS is to inform members about their current IORP savings (be it accumulated capital or accrued entitlements). It is meant to provide an overview of the current retirement savings, i.e. accrued entitlements or accumulated capital, and to answer the main question: **'how much did I save already?'** This question will mainly be answered by showing the accumulated entitlements (for DB schemes) or the currently accumulated pension pot (for



Figure 1 – Overview of four subgoals in the PBS



DC schemes). As a member will receive a PBS annually, he or she will typically see their entitlements or pot accumulate over the years.

Further insight into the current situation might be made transparent by showing the change to the pension entitlements or pension pot from one year to another. For example by showing the contributions made and the costs charged. While not required by IORP II, an IORP can opt to show the return earned in a year or the inflation compensation provided.

The first goal has an important behavioural purpose but at the same time can also serve a legal purpose, as the amount shown on the PBS could have a legal value in the case of a dispute for both the IORP and the member.

Member States can also choose to add other components of the current situation, such as the investment policy that was chosen or the current coverage of the scheme (e.g. survivor's/disability pension).

### **SUBGOAL 2: ESTIMATION OF FUTURE RETIREMENT PROSPECTS**

The second key element of the PBS is to inform members of their projected pension income to answer the key question: **'how much money could I receive at retirement age?'** This will provide the member with an estimate of the income he or she can expect at retirement. IORP II states that in cases that the projections are based on economic scenarios, income should be shown in two scenarios to show the variance in projected pension income.

The projections contained in the PBS should be realistic and include information on the member and the pension scheme, especially if the pension scheme does not offer a (nominal) guarantee. It should be noted that projections are an estimation and any figures should be accompanied by a disclaimer. More information on the calculations underlying the pension projections is included in chapter 2.

Member States can choose to show projections for other products as well, for example projections for survivor's or disability pension or show projections for more than two scenarios.

### **SUBGOAL 3: ENABLE INSIGHT IN RETIREMENT SAVINGS**

The PBS is typically an important component for the planning of a member's retirement savings. In order to make full retirement planning, a member typically could need information from additional sources. The retirement planning should guide and enable a member to answer the key question **'is the projected pension income sufficient?'**

Most members do not have a single employer (or accumulate a pension with one IORP) throughout their career. This means they could receive multiple PBSs. To get an idea of their future retirement savings the information contained in a PBS should be comparable to other PBSs. It should be noted that this report refers to comparability within a Member State.

While not required by the Directive, it is desirable that the PBS should also be comparable in some extent to information on other future retirement incomes, like the state pension (first pillar) and individual retirement products (third pillar). This will make it easier for a member to get insight into his or her full retirement situation and allows him or her to undertake holistic retirement planning.

### **SUBGOAL 4: HELP MAKE INFORMED DECISIONS**

After a member has undertaken retirement planning and is aware of whether the projected income is sufficient, he or she can make an informed decision on possible additional action. Informed decisions are possible within the scheme, for example the level of contributions or the investment profile that a member has chosen, and outside of the scheme, for example whether to take up an additional pension product, to invest in reducing future expenditures or to postpone the retirement date.

The main question that the PBS should help answer is whether the member needs to take action to make sure the financial situation after retirement is adequate. The key question to respond: **'Is my pension adequate?'** and, if not, **'How can I improve my retirement prospects?'**

## 2.2. PRINCIPLES FOR THE DESIGN OF A PBS

EIOPA identified the following principles:

1. **The PBS should be designed with a behavioural purpose and the information respond to the member key questions.**

The purpose of the PBS is to provide understandable information in a structured manner, so that members can make informed decisions about their retirement savings.

While drafting the PBS, it is important to prevent (i) information overload and (ii) the issuance of a document that is very difficult for a member to understand. Thus, a balance between legalistic language and information that is easier for the members to understand should be considered. The latter is better achieved when the information has been developed with a clear behavioural purpose in mind – i.e. what a member should be able to ‘do’ with the information given - and structured so that it responds to the member’s key questions.

The 2013 EIOPA report on good practices on information provision for DC schemes <sup>(1)</sup> proposed that complex, abstract and legal information could be provided in layers which could be accessed and retrieved by scheme members, but kept separate from the first layer of the PBS. This will be discussed in chapter 4 in further detail.

2. **Member States and IORPs should engage with communication experts when designing the PBS**

Engagement with communication experts or behavioural finance experts in the process of the design of the PBS is crucial when national authorities are developing templates or technical guidance, and indeed by IORPs when preparing their own PBS. The presentation of pension projections and costs are key elements of the PBS, for which dedicated sections are examined in chapters 2 and 3. The presentation of formatting aspects in the PBS (layering and layout) are examined in chapter 4, together with the current practices at national level. Altogether several principles and guidance are highlighted throughout the report aimed at

helping Member States in their process of implementing the PBS requirements under IORP II.

Should the Member States decide to develop a template for the PBS, this should be an ongoing process: after developing a template one should test the template on IORP members and improve the template afterwards (consumer testing). Should this not be envisaged, Member States should encourage IORPs to do so.

3. **The PBS design should take into account the characteristics of the pension scheme** (DB vs. DC, investment options).

The design of the PBS should be in line with the characteristics of the pension scheme. The PBS for DC-scheme members will be different from the PBS for DB-scheme members, especially considering DC members often have more choices presented to them.

4. **The PBS design should integrate and complement the communication tools that are in place within the Member States –** such as the availability of an **on-line pension dashboard** or other pension communication channels to **facilitate the insight into the member full retirement situation.**

In some Member States citizens can get an overview of their overall pension entitlements via an online dashboard. These Member States might want to align the design of the PBS with that of the pension dashboard or other pension communication channels. This has the advantage of providing up-to-date addable information on occupational pension entitlements and complementary information on the state pension or other private pension products. When designing the PBS Member States should consider the availability and complementarity as well as the actual use of other pension communication tools by IORP Members.

5. **Information contained in a PBS should be comparable to other PBSs.**

The design of a PBS should take into consideration the comparability within a Member State: IORP members should be in the position of adding up their pension projections or comparing the costs from one PBS to another.

<sup>(1)</sup> EIOPA, “ Good practices on information provision for DC schemes -Enabling occupational DC scheme members to plan for retirement”, 24 January 2013

### 2.3. CHAPTER CONCLUSIONS

The PBS is an important pillar in pension information. The main goal of the PBS is to provide adequate information on the second pillar retirement income to help members to make informed decisions, by:

- outlining the current financial pension savings
- projecting future retirement benefits,
- enabling retirement planning.

In the development of the PBS Member States need to take into account that the PBS should fulfil the legal requirements, but should also be a document that is easy to read and understand for members.

The principles for designing the PBS highlight the importance of having a behavioural approach, involving communication experts and testing the design among members with a view to continue improving the PBS design, the need to consider the characteristics of the pension scheme, the integration of or into the communication tools in place at national level, such as on-line dashboards, to ensure the adequacy and comparability of the information provided through the PBS.

## 3. PROJECTIONS: HOW TO PROVIDE PENSION PROJECTIONS IN THE PBS?

### 3.1. INTRODUCTION

The second sub-goal of the PBS is to provide members with an estimation of future retirement prospects. This is done by providing members with a projection of their benefits or their future income. At the same time pension projections are important for fulfilling the third and fourth sub-goal as well: giving members an insight in their retirement situation and allowing them to make informed decisions. Therefore pension projections are vital to the PBS and should receive considerate attention by Member States and their IORPs when designing a PBS.

The IORP II directive requires pension benefit projections to be included in the PBS.

- › Article 38(5) of the IORP II Directive states that "Member States shall set out rules to determine the assumptions of the projections referred to in point (d) of Article 39(1). Those rules shall be applied by IORPs to determine, where relevant, the annual rate of nominal investment returns, the annual rate of inflation and the trend of future wages."
- › Article 39(1) notes that the PBS should contain "(d) information on pension benefit projections based on the retirement age as specified in point (a), and a disclaimer that those projections may differ from the final value of the benefits received. If the pension benefit projections are based on economic scenarios, that information shall also include a best estimate scenario and an unfavourable scenario, taking into consideration the specific nature of the pension scheme;"

In this report pension projections are defined as the projected values of a member's accumulated future savings and/or future benefits that the IORP will provide at retirement given a chosen set of assumptions.

It is possible to compute pension projections based on one scenario or multiple scenarios. In the latter case, according to the Directive, if the pension benefit projections are based on economic scenarios, the scenarios shall include at least a best estimate and an unfavourable scenario.

How the pension projections are communicated and in what form is largely dependent on what the pay-out phase of the pension scheme or product looks like. In some Member States it is possible to pay-out a lump sum payment, while other Member States prescribe an annuity (i.e. a periodical amount paid by the IORP to members, typically lifelong) or allow for either option. For example, both a lump sum and an annuity are possible in Belgium and the United Kingdom. In other Member States converting the entire pension capital into an annuity may be mandatory, as is the case in the Netherlands.

### 3.2. APPROACHES AND TECHNIQUES ON PROJECTIONS

To compute pension projections there are several aspects to consider. In this report there is a distinction made between guaranteed and non-guaranteed pensions as this affects the way the pension projections are calculated. Attention will also be paid to the difference between deterministic and stochastic approaches to pension projections, and more insight will be given in the usage of various assumptions underlying pension projections. This section will conclude with various examples from Member States.

#### GUARANTEED AND NON-GUARANTEED PENSIONS

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Pension projections which are based on economic scenarios have to be communicated in at least two scenarios: a best estimate scenario and an unfavourable scenario. This can lead to questions where the best estimate scenario and the unfavourable scenario are very similar, as could be in the case of a guaranteed pension.

There are different kinds of guarantees depending on the design of the pension scheme. The pension risks can be borne by the employees, the employer or a mix of both. If the employer bears all the risk, for example in a final pay arrangement where the employer guarantees to pay for a possible deficit it is quite clear what the projected ben-

efit for the member is. There is also the case in which a guarantee is given by the IORP on a certain capital on retirement date or on a certain annual return on the investments, making the projected benefits fairly predictable.

Most pension plans however, whether defined contribution (DC) or defined benefit (DB), do not rely solely on a guarantee and the possible outcome for the member depends on the return earned in the investment policies or other economic scenarios. This leads to members having a degree of uncertainty on the pension benefits to expect. To help members understand this degree of uncertainty it helps to provide them with at least two scenarios. However, the use of multiple scenarios can also make it more difficult for members to understand which of the projections to take into account, though this arguably reflects well the uncertainty in question.

#### **DETERMINISTIC OR STOCHASTIC APPROACH**

Scenarios can be calculated with different approaches, taking into consideration the specific nature of the pension scheme. This report distinguishes between deterministic and stochastic approaches.

A deterministic approach is a calculation in which the assumptions regarding the economic variables, such as the rates of return, are fixed. This means for example that where a return on investments is  $x\%$  in year  $n$  and  $y\%$  in year  $n+1$ , a consistent average return each year can be assumed. This leads to an extrapolated outcome given a certain starting position of the member's savings and the characteristics (and possibly the financing agreement) of the pension plan.

A stochastic approach is typically a more complex and sophisticated calculation. It takes into account hundreds or thousands of scenarios in which the economic variables contain a certain degree of volatility. For pension projection calculations this looks like a personalized asset liability management (ALM) study. The difference with a deterministic approach is that in the stochastic approach multiple scenarios are used to calculate the projected pension benefits, to simulate results according to different probability levels.

After calculating these scenarios, an IORP can pick percentiles of these scenarios to show the best estimate and the unfavourable scenario. One of the examples below shows how this is applied in the Netherlands.

An advantage of the stochastic approach is that it will imitate a large variety of possible future scenarios with varying economic assumptions for each consecutive year.

A stochastic approach is also more adaptable to differences between different IORPs – it can reflect a wider range of variables. An advantage of the deterministic approach is that it is relatively easy to implement in the administration of IORPs. The assumptions for a deterministic approach are typically based on a multi annum average and can therefore be the same for each consecutive year, making it easier to explain to members. However, the deterministic approach is highly dependent on the assumptions set. These would need to be reviewed regularly to state deviations in case the environmental conditions have changed, eg interest rates. This deterministic approach is probably less costly than a stochastic approach. Below are examples of how various Member States have approached calculating pension projections.

### **3.3. EXAMPLES OF APPROACHES**

#### **Example: deterministic pension projections in Italy**

In Italy, pension projections for supplementary pension plans have been mandatory since 2008. IORPs and other pension providers are required to provide members with projections about their expected retirement benefits firstly when members join the scheme and annually during the accumulation phase.

Pension projections are part of the pre-contractual information that pension funds are asked to provide potential members before joining (prior to IORP II). They are standardized and computed using a list of parameters and assumptions set by COVIP (the Italian private pension supervisory authority).

During the accumulation phase, members annually receive personalized pension projections reflecting their personal information (age, investment option, contribution rate, the accumulated capital at the end of the last year). Macroeconomic assumptions to be used for computing these projections are set by COVIP (and refer for example to the expected inflation rate, the mortality tables, the expected rate of returns and the expected growth rate of the salary).

Projections are made following a deterministic approach and are expressed in real terms, gross of taxes and on the basis of a lifetime annuity. A caveat has to be included explaining that projections are only estimates and that the member's account balance can vary during the accumulation phase as a consequence of the variability of returns and other variables.

**FASE DI ACCUMULO: STIMA DELL'EVOLUZIONE DELLA POSIZIONE INDIVIDUALE**

La tabella che segue riporta una stima della evoluzione della tua posizione individuale nel corso della fase di accumulo. La prima riga corrisponde alla posizione individuale effettivamente maturata alla fine dello scorso anno.

Data di riferimento della simulazione	Età anagrafica	Versamenti lordi nell'anno (euro)	Versamenti lordi cumulati (euro)	Posizione individuale a fine periodo (euro)
<b>31/12/2008</b>	....			
31/12/2013	....			
31/12/2018	....			
31/12/2023	....			
31/12/2028	....			
31/12/2033	....			
31/12/2038	....			

The assumptions to be used for expected returns specify a higher return, the higher is the equity allocation. However, the possible higher uncertainty surrounding pension projections is communicated with a written caveat: the higher the equity allocation, the higher the variability of returns.

In addition to paper based projections, pension providers can also offer online simulators on their websites. These simulators allow members to get more personalized estimate of what they can expect at retirement. In this case, pension plans are allowed to incorporate the uncertainty in pension projections by setting symmetric scenarios with respect to the COVIP central scenario (2-4% expected rates of return).

Link to COVIP regulation: <https://www.covip.it/?p=11270>

Link to COVIP standard examples: <https://www.covip.it/?cat=129>

**Example: stochastic pension projections in the Netherlands**

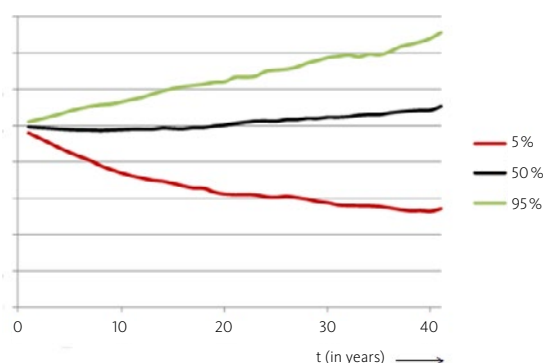
As of the existence of the “Pensioen- en Spaarfondsenwet” from 1952, Dutch law states that members accruing pension benefits should annually receive a pension projection.

As of 2020 the Dutch PBS will show projections in three scenarios: an expected, a favourable and an unfavourable projected benefit at the retirement age. As of 2019 this information will be available on the website [www.mijnpensioenoverzicht.nl](http://www.mijnpensioenoverzicht.nl), which is a pension tracking service where every member can see the projected benefit for first and second pillar pensions.

The method used for calculating the three scenarios is stochastic and based on 2,000 economic scenarios. There are different methods for DB and DC plans.

For DC plans an individual ALM calculation is used. In the 2,000 scenarios economic parameters such as inflation, interest rates and returns on investment are taken into account. On a member level the accrued capital and the future employer and employee contributions are taken into account. At the retirement age the capital is converted into an annuity. The price of the annuity is based, amongst other things, on the interest rate in the scenario. In communicating the height of the retirement income the numbers are corrected for inflation. The outcomes of the projections at retirement age for the 5th percentile (unfavourable scenario), 50th percentile (expected

Graph 1 – Projected benefits in three scenarios (percentile value)



scenario) and 95th percentile (favourable scenario) are being used for communication to the participant. For the example in graph 1 hereunder this is the result at year 40.

For DB plans pension funds have to perform an annual feasibility test (ALM calculation) at a pension plan level that takes into account all characteristics of the pension plan, including the financial set-up. This feasibility test uses the same 2,000 economic scenarios and parameters as for DC plans.

The characteristics of the plan include the contribution being paid, the level of accrual, the level of indexation, the indexation policy and the other tools that pension funds have available (e.g. lowering benefits as a last resort). This ALM feasibility test provides a time set of ratios for the rate of inflation combined with the rate of indexation at every point in time for every scenario. Again the 5th, 50th and 95th percentile of this set of ratios is used for correcting the accrued benefits and the future accrual against inflation. More information (in Dutch) can be found in the ministerial guidelines that were published on 23 April 2018. Link to the official legal UCM rulings: <https://zoek.officielebekendmakingen.nl/stcrt-2018-22286.html>

### 3.4. ASSUMPTIONS USED IN PROJECTIONS

Article 38(5) states that “Member States shall set out rules to determine the assumptions of the projections of article 39(1d). The rules shall be applied by IORPs to determine, where relevant the annual rate of nominal investment returns, the annual rate of inflation and the trend of future wages.”

The projections are very dependent on the assumptions underlying the calculations. This holds for both deterministic and stochastic models. The stochastic models can cover a higher “spread” and thus demonstrate a broader span of possible outcomes, compared to the deterministic scenarios. It is important to decide what assumptions are used. There is a great variety of assumptions that can be taken into account. It is up to Member States to decide which assumptions will hold for the pension plans in their country. Below is a non-exhaustive list of different assumptions a Member State can take into account.

When setting assumptions it is important to ensure economic realism and to use appropriate time horizons. It is equally important to review assumptions in a regular manner. This applies to how returns on assets develop in the long run, how asset classes interact and the impact of short term volatility, especially where there is no life cy-

cling or other technique to reduce this exposure to short term risk towards retirement.

#### ECONOMIC ASSUMPTIONS

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- › Interest (discount) rate: to estimate the price of an annuity.
- › Return on investments: to determine the estimated capital at retirement age or the annuity, either for different asset classes separately or the portfolio as a whole. <sup>(2)</sup>
- › Inflation: if benefits depend on (the increase of) the inflation rate or to correct for the purchasing power effects. This can either be wage or price inflation. <sup>(3)</sup>
- › Volatility of asset classes: to determine the risk surrounding the return of asset classes. <sup>(4)</sup>
- › Correlations between asset classes: to adjust for effects where asset classes move in similar or opposite manner. <sup>(5)</sup>
- › State incentive – tax discount: in some Member States a tax incentive is in place to stimulate pension savings. This is technically not an assumption, but it is an important parameter.

#### DATA RELATED TO THE IORP

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- › Asset allocation: how the IORP actually invests the money on behalf of the members.
- › Costs: to determine the estimated capital at retirement age or the annuity in the pay-out phase.
- › Biometric parameters: to estimate the (price of an) annuity at retirement age. factoring in life expectancy / mortality tables.

#### DATA RELATED TO THE INDIVIDUAL MEMBER

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- › Member contribution: the amount of contributions paid by the member.
- › Employer contribution: the amount of contributions paid by the employer.
- › Salary: is the projected salary increasing or stable and is the possible salary increase collective or individual? <sup>6</sup>
- › Age of the member.

<sup>(2)</sup> Noted in article 38(5)

<sup>(3)</sup> Noted in article 38(5)

<sup>(4)</sup> Mostly used in stochastic models

<sup>(5)</sup> Mostly used in stochastic models

<sup>(6)</sup> Noted in article 38(5)

- Retirement age of the member.
- The number of years the member contributed to the pension plan.

In table 1 below the various assumptions set in a selected number of Member States are shown. Please note that Member States differ when it comes to prescribing the usage of certain assumptions. This table is intended to give an insight in the differences and the choices made in some Member States and should not be seen as a definite list, as some Member States are, as of writing, still in the process of implementing projections or offer IORPs flexibility in choosing assumptions.

### UNIFORMITY OF ASSUMPTIONS

In order to compare and to add projected pension benefits between different IORPs it is important to set uniform (principles for) assumptions throughout a Member State. Projected benefits can only be compared and added in proper mathematical way if the underlying assumptions are the same and appropriate for the IORP (taking into account different IORP features or risks).

This is a key element in making the PBS of IORPs comparable to each other and should receive careful attention of Member States. Moreover, it helps if pension plans from

other pension providers than IORPs also use the same set of assumptions as relevant for the IORP. This will allow members to compare various type of pension products and to allow them to better plan their retirement savings.

The assumptions can be set by various stakeholders, for example the government, supervisors or an independent body.

The subsequent chapters show a selection of different assumptions used.

## 3.5. EXAMPLES OF ASSUMPTIONS

Different countries use different assumptions. The examples hereunder show the different economic assumptions of some EU countries.

### Example: assumptions in the Netherlands

In the Netherlands the assumptions are set by a committee of scientists, representatives of the pensions sector and the supervisor. Every five years they decide upon these assumptions that have to be used in order to calculate projections. In 2014 the following assumptions have been set: (?)

Table 1 – Use of set assumptions for pension projections in various countries

Economic assumptions:	AT	FR	IT	IE	NL	SK
Interest rate (Y/N)	Y	Y	N	Y	Y	N
Return on investments (Y/N)	Y	Y	Y	Y	Y	Y
Inflation (Y/N)	Y	N	Y	Y	Y	Y
Volatility (Y/N)	N	N	N	Y	Y	Y
Correlations (Y/N)	N	N	N	N	Y	Y
State incentives (Y/N)	N	N	N	N	Y	N
Data related to the IORP:						
Asset allocation (Y/N)	Y	Y	Y	Y	Y	N
Costs (Y/N)	Y	Y	Y	Y	Y	Y
Biometric assumptions (Y/N)	Y	Y	Y	Y	Y	N
Data related to the individual member:						
Member contribution (Y/N)	Y	Y	Y	Y	Y	Y
Employer contribution (Y/N)	Y	Y	Y	Y	Y	Y
Individual salary: stable (S) or Increase (I)	Y	S	I	Y	S	Y
Age (Y/N)	Y	Y	Y	Y	Y	Y
Retirement age (Y/N)	Y	Y	Y	Y	Y	Y
Number of years of participation (Y/N)	N	Y	Y	Y	Y	Y

(?) The full report can be found at <https://zoek.officielebekendmakingen.nl/blg-308035.pdf>



Table 2 – Set of assumptions for pension projections in the Netherlands

Category	Gross geometrical parameter	Cost deduction	Standard deviation	Note
Minimum expectation values				
Price inflation	2,00%	N/A	N/A	Growth path of 5 year
Collective wage growth	2,50%	N/A	N/A	Growth path of 5 year
Maximum expectation values				
Government bonds AAA	Approx. 2.5 %	15 bp	8%	Based on forwards
Credits	Approx. 3 %	Approx. 15 bp	Approx. 8 %	Combination of equity and forwards, dependent on the credit risk in the portfolio
Listed equity	7,00%	25 bp	20%	
Other risky assets	7,50%	25 bp	25%	
Non-listed real estate	6,00%	80 bp	15%	
Commodities	5,00%	40 bp	20%	
Diversification effect	Approx. 50 bp	N/A	N/A	Dependent on the portfolio

**Example: assumptions in Italy**

In Italy, COVIP sets rules that have to be followed for the computation of IORP pension projections to be provided to actual and potential members. COVIP sets standardised macroeconomic and demographic assumptions while information related to pension plan characteristics (for instance, IORP costs) and to members' personal data are provided by the IORP.

**Example: assumptions in Austria**

In Austria, the pension projections calculation shall be based on:

1. the respective assumed interest rate for the performance of the premium reserve and
2. earnings performance
  - a) with a zero-interest scenario,
  - b) with an interest scenario based on the assumed interest rate, and

Table 3 – Set of assumptions for pension projections in Italy

	Set by COVIP	Relative to individual IORP	Related to individual MEMBER
Gender			✓
Age			✓
Age of retirement	✓		
Costs		✓	
Contributions			✓
Wage			✓
Wage growth rate	✓ (1%)		
Investment line			✓
Expected real rate of returns	Bond real rate of return: 2 % Equity real rate of return: 4%	Depends on the asset allocation of the investment line	
Inflation rate	✓ (2%)		
Mortality table	✓ (IPS 55 or IPS 55U)	✓	
Technical rate	✓ (0%)	✓	
Annuity charge	✓ (1.25 %)	✓	

- c) with an interest scenario based on the highest permissible percentage rate of assumed interest at the time of the information being provided.

In addition, the Pensionskasse may also make a forecast using an earnings performance based on an interest scenario in the amount of an earnings performance that is assumed by the Pensionskasse, up to a maximum amount that is equal to the respective technical surplus. The forecast is not required if the pension company commitment takes the form of a direct guarantee where the employer has an unlimited obligation to make an additional contribution.

**Example: pension projections in France**

In France, prior to the IORP II implementation for insurance-based pension products, according to the article L.132-22 of the Insurance Code, the insurance company must communicate to the member each year an estimation of the amount of the annuity based on his individual rights already acquired at this time.

The article A.132-7 paragraph IV adds that the amount can be separately disclosed for the guaranteed fund (“euro fund”) and the pure unit-linked funds. The estimations are calculated net of fees and charges. The estimations are calculated according to:

- › The technical provisions at the end of last year,
- › The mortality table applicable to the contract,
- › The technical interest rate applicable to the contract,
- › The retirement age (usually the legal retirement age as well as this age + 5 years).

The estimations must be accompanied with a statement which stresses that the estimation is not contractually binding, based on parameters which can vary or be modified (especially the technical rate and the mortality table). It should also state that fees can be deducted (although it must be clearly described in the contract) and that the real retirement age can differ from the legal one.

### 3.6. PRINCIPLES FOR COMMUNICATING PROJECTIONS

EIOPA identified the following principles:

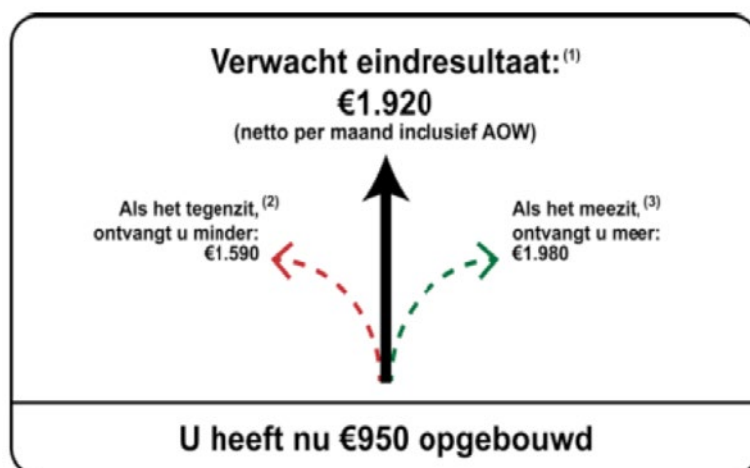
**PRESENTING PROJECTIONS BY MEANS OF A VISUAL**

1. **Communicating pensions scenarios with a visual seems a good way to show the projected benefits.**

After the projections are calculated, they have to be communicated to members on the PBS. This can either be done through graphs, tables or in text. EIOPA’s consumer testing of other disclosure documents showed that the use of graphs can be deceptive – some consumers find graphs useful while other find them difficult to use.

An important decision to make is whether projections are to be communicated to members in real or nominal terms,

Figure 2 – Visual to show pension projection’s scenarios in the Netherlands



how precise the projections should be and whether gross or net amounts are better understood by members. This should be established through consumer testing.

#### **Example: communicating projections with three scenarios in the Netherlands**

In the Netherlands a graph has been developed that needs to be included on every PBS. It shows three projected benefits. It was inspired by how a navigation system for vehicles typically works.

The picture shows the accrued benefits (€950) and the “way forward” to the projected benefits at the retirement age for an expected scenario (€1,920), an unfavourable scenario (€1,590) and a favourable scenario (€1,980).

The pension industry will further develop this graph by consumer testing and adjust where necessary.

#### **NOMINAL OR REAL PROJECTIONS**

2. **Providing pension projections in real terms related to the member’s current income helps members understanding their purchasing power after retirement.**

Many financial products are communicated in nominal terms. Given the long term character of a pension product and the effect on a member’s future purchasing power, an argument can be made to communicate pension projections in real terms. However, research in the Netherlands has shown that showing both nominal and real projections is confusing for members.

Research has also shown that explaining the effect of inflation on purchasing power to members is often too difficult, but that members can relate real projections to their current income and understand what the projections mean.

#### **ROUNDING PENSION PROJECTIONS**

3. **Rounding the outcome of projections to the nearest ten euro can help the member understand that the figure is an estimation.**

Pension projections are estimations of a future income. Those projections typically bear a (large) degree of uncertainty, especially when the member is young. Still in some cases a very precise amount is communicated to members which might suggest a certainty or might even give members the perception of a guarantee.

Article 39(i)d of the Directive states that projections can deviate from the final benefits. <sup>(8)</sup> An option to show members that projections are an estimate is to round the outcome to the nearest ten euro. The perception will probably be that the rounded numbers seem to be an estimation. It is also possible to differentiate for different ages: a 60 year old probably wants a more detailed information than a 30 year old.

#### **GROSS OR NET OF TAXES PROJECTIONS**

4. **Providing the estimation of projections in net terms makes it easier for the member to relate to their current net income.**

Another element to take into consideration is whether projections of pension benefits are net or gross of tax. This will depend on a member’s marginal tax rate which is not always known to the IORP. Therefore taking into account taxation can be difficult to calculate for the IORP without having the knowledge of other retirement income. Member States should make a decision on whether to show net or gross projected retirement income. The advantage of communicating in net terms is that the income is easier to relate to for the member. Projections should be also presented net of costs.

<sup>(8)</sup> Article 39 (1) d states a.o. that a “disclaimer that those projections may differ from the final value of the benefits received” is part of the PBS.

### 3.7. CHAPTER CONCLUSIONS

Pension projections are important to fulfil the second sub-goal of the PBS: to give an estimation of future retirement prospects to members. At the same time, it also plays a vital role in fulfilling the third and fourth sub-goal of the PBS: giving members an insight in their retirement situation and allowing them to make informed decisions.

The IORP II Directive states that Member States shall set out rules to determine the assumptions of the projections.

The technique of calculating pension projections differs across Member States. Some Member States have a system with pension plans that contains some form of guarantee while others rely more on a positive expected value of investment. This can affect how pension projections are calculated.

Another important distinction is whether pension projections are calculated through a deterministic or stochastic approach. A deterministic approach has the benefit of being less complex and less costly to implement, while a stochastic approach can take into account a wider variety of assumptions and thus possible outcomes but it could in principle be more difficult to communicate.

A key element in pension projections are the underlying assumptions used. These can be split up into macroeconomic assumptions, data related to the IORP and data related to the member. Careful attention has to be paid to the uniformity of the assumptions as this will make it possible to compare within a Member State and add various pension projections which is vital in making a retirement planning.

The communication of pension projections also requires careful attention by Member States. A choice has to be made whether projections are displayed in real or nominal terms, in what way the pension projections have to be rounded and whether it has to be displayed in gross or net amounts. In any case, consumer testing has to be conducted in order to find out which form of communication works best.

## 4. COSTS: HOW TO DISCLOSE COSTS IN THE PBS?

### 4.1. INTRODUCTION

In the course of 2014 EIOPA conducted research into costs and charges of IORPs, which led to the adoption of the EIOPA Report on Costs and charges of IORPS <sup>(9)</sup> in early 2015. An important part of the report related to cost disclosure.

One of the main findings was that the methods chosen by Member States to address costs (for example in the field of disclosure) vary widely and that it is difficult to obtain a clear picture of what parties are paying in costs and charges. The report identified the need for greater transparency and clarity, also in the light of the shift towards DC schemes. These findings did not come as a surprise since the IORP I Directive did not contain structural cost disclosure requirements for IORPs. <sup>(10)</sup>

The IORP II Directive introduced such structural cost disclosure requirements for IORPs, both towards prospective and actual scheme members, however solely for schemes where the member bears investment risk or can take investment decisions (DC schemes). <sup>(11)</sup> Scheme members must find in the PBS a breakdown of the costs deducted by the IORP at least over the last 12 months. The directive

<sup>(9)</sup> See *EIOPA report on Costs and charges of IORPs*

<sup>(10)</sup> Most information requirements in art. 11 of Directive 2003/41 were on request.

<sup>(11)</sup> Relevant recitals and articles in the IORP II Directive

- (63) **Taking into account the nature of the pension scheme established and the administrative burden involved**, IORPs should provide clear and adequate information to prospective members, members and beneficiaries **to support their decision-making** about their retirement and **ensure a high level of transparency throughout the various phases of a scheme** comprising pre-enrolment, membership (including pre-retirement) and post-retirement. In particular, information concerning accrued pension entitlements, projected levels of retirement benefits, risks and guarantees, and **costs** should be given. [...]
- (64) Given the specificities of schemes providing a given level of benefits, such benefits are, except under extreme circumstances, not affected by past performance nor by **cost structure**. **Information thereon should therefore be provided only with respect to schemes where members bear investment risk or can take investment decisions.**

#### Article 39

##### Pension Benefit Statement

- The Pension Benefit Statement shall include, at least, the following key information for **members**:
  - [...] (g) a **breakdown of the costs deducted by the IORP** at least over the last 12 months;

does not further specify which costs should be covered, according to which criteria and how detailed the breakdown should be or how the costs should be presented.

This chapter provides guidance to Member States on how to disclose costs in the PBS so that the information helps the member understand the impact of costs on the plan. While from a DC member perspective it is important to understand whether the level of costs is low or high when compared to other schemes or retirement sources in order to take action where appropriate, a proper understanding of information on costs requires that also the risk and return profile of the investment is taken into account. For example, if the investment portfolio has an aggressive and actively managed profile the costs for this strategy may be higher than for a conservative or passive portfolio. However, this need to be set into relation to the achieved returns, this is why “net returns” would be ideally the best indicator.

In a pension environment where the DC model is becoming more and more widespread, the importance of cost disclosure is growing.

### 4.2. DEFINITIONS AND COST TAXONOMY

#### “COSTS DEDUCTED BY THE IORP”

IORPs carry out administration and investment activities to collect and invest pension assets, as well as to pay pension benefits. The costs of these activities are paid for out of contributions and investment gains. Members and employers pay for the costs of the activities through the deductions from contributions, and through costs taken directly or indirectly from the investment portfolio. Therefore, for the purpose of this report, the “costs deducted by the IORP” (IORP II Article 39(g)) include both the costs deducted by the IORP from member and employer contributions and the costs deducted from investment gains.

The PBS is only required to provide information on costs in the case of schemes where members bear the risk or can

take investment decisions. Although Article 39 does not explicitly mention this limitation, this is made clear by recital 64. <sup>(12)</sup> Consequently, defined benefit schemes where members cannot take investment decisions are currently not required to provide information on costs in the PBS and will continue not to be required to do so under IORP II.

### DIFFERENT COST PERSPECTIVES - DIRECT AND INDIRECT COSTS

In occupational pension schemes there are usually three parties involved: the IORP, the employer and the scheme members. One can look at costs from the perspective of each of these parties. The result will not necessarily be the same. Regardless of the perspective from which costs are looked at, a distinction can be made between direct and indirect costs.

#### COSTS BORNE BY THE IORP

From the perspective of the IORP, costs include (i) any outflow from or (ii) any decrease in value of the IORP's assets, except for outflows related to pension benefits payment and decrease in asset value related to price movements/fair value of those assets. <sup>(13)</sup>

The first category are direct costs and include all kinds of payments to managers, staff, service providers, advisors, taxes as well as other costs. Direct costs - taking the form of outflows - are relatively easy to identify. In one way or

another they should be reflected (maybe not in the desired breakdown or degree of detail) in the profit and loss (P&L) statement of the IORP.

The second category are indirect costs. These costs do not take the form of outflows but of a decrease in value of the IORP's assets, because they are immediately reflected in the value of assets. This is for instance the case if the IORP invests through investment funds. Costs on the level of the investment fund will be reflected in the Net Asset Value of this fund, which will have a negative impact on the value of the assets of the IORP. These "hidden" costs in the underlying investment layers will not be visible unless a "look through" approach is applied, i.e. a detail break-down to the level of individual assets, their respective values and related investment (management) costs. Another example of indirect costs are the costs that are "hidden" in the trading, i.e. buying and selling, of some categories of assets. <sup>(14)</sup>

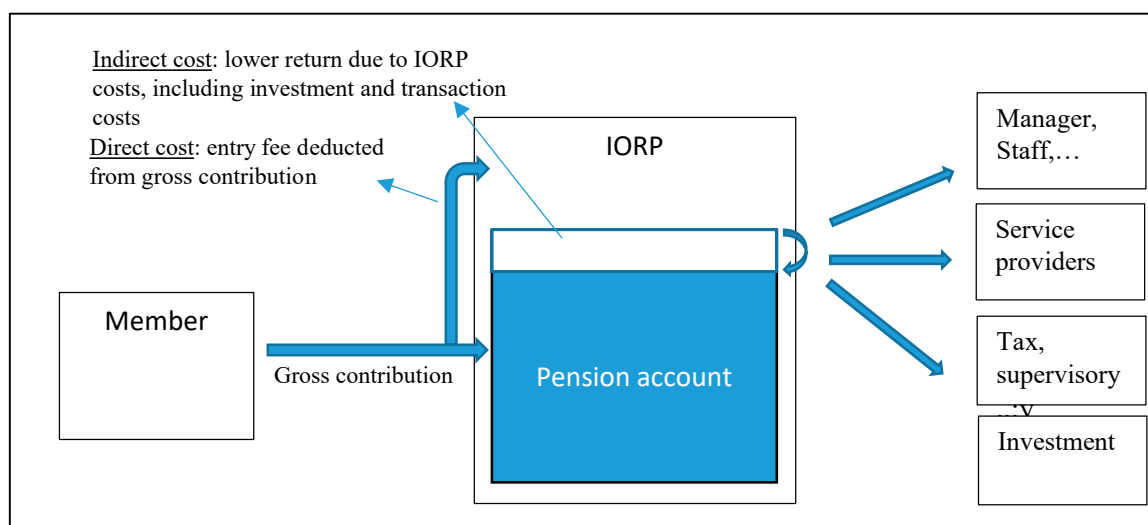
IORP's will pass on all or part of these costs to employers and/or to scheme members, depending on the type of pension scheme and on the terms of the pension scheme.

#### COSTS BORNE BY THE EMPLOYER

Like IORPs, plan sponsors can bear costs either directly or indirectly:

- Directly. In some pension schemes the plan rules provide that some or all of the costs mentioned above are not borne by the IORP, but are directly paid by

Figure 3 – Types of costs from a member perspective



<sup>(12)</sup> idem

<sup>(13)</sup> EIOPA Report on Costs and Charges of IORPs, 4.

<sup>(14)</sup> Especially in fix income instruments, where there are no explicit fees.

the sponsor, for example, when the management agreement between the employer and the IORP provides that costs for legal and actuarial advice are paid directly by the employer to the consultant. In such a case these costs do not affect the IORP's P&L, nor the value of the assets. It is obvious that the question whether or not to take also these costs into account on the PBS, will influence the amount (or the %) of costs that will be shown to the member.

- Another possibility is that costs are initially borne by the IORP, but subsequently fully or partially invoiced to the sponsor.
- Indirectly. Even when there is no direct intervention from the sponsor, the sponsor sometimes bears the costs in an indirect way. This will especially be the case with DB schemes, and is therefore of less importance in the context of this report. Because in many DB schemes the overall financial burden of the pension scheme rests on the shoulders of the plan sponsor, the costs that were in the first place borne by the IORP (costs described under "costs borne by the IORP"), will be in the end borne by the employer; these costs may inherently affect the sponsor's contributions.

#### **COSTS BORNE BY THE SCHEME MEMBER**

From the perspective of the members, costs can be borne either directly or indirectly.

- Direct costs are costs that are charged to the scheme member on the basis of an explicit rule in the schemes' terms and conditions (often called "fees" or "charges"). They mostly take the form of a fixed amount or a fixed percentage that is deducted from the contributions, before their allocation to the members pension account (entry fee). Other variants are fixed amounts/percentages deducted from the members account in case of take up or transfer (exit fee) or fixed amounts/percentages periodically withheld from the members account.

Costs directly charged to the scheme members do not necessarily cover all the costs. In some cases IORPs do not charge any direct cost at all. Of course this does not mean that the cost for the member is zero.

- Indirect costs. In the case that the IORP does not charge any costs directly to the members (or to the extent that direct costs do not cover the entirety of the costs borne by the IORP) DC-scheme members

will bear the costs indirectly, through eventually lower attributed returns.

#### **TAXONOMY OF IORP COSTS**

For the purpose of IORP cost reporting costs are often divided into categories, according to their nature. Often used categories are:

- Administration costs: also called pension management or operating costs, are costs that arise from the IORP's activities when administering accounts, collecting contributions, providing information to members, ensuring pay-outs. For example:
  - Services providers: legal, accounting, actuarial, consultants and advisors
  - Oversight and governance costs
  - Regulatory costs
  - Managers, staff
  - Distribution
- Investment costs: payments to third parties to meet costs necessarily incurred in connection with the acquisition or disposal of assets (excluding portfolio transaction costs). These include costs charged by the investment/asset manager to cover the costs of managing the assets of the fund. Any amount implicitly charged to the IORP by the asset manager/service provider on the amount invested such as the costs incurred for the management of the investments of the IORP. For example:
  - Fund entry and exit costs
  - Custodian/Deposit fees
  - Management fees
  - Performance fees
  - External management fees (in the case of a pension fund invests in turn in other funds)
- Transaction costs: payments by the asset manager to third parties to meet costs necessarily incurred in connection with the acquisition or disposal of any asset in the fund's portfolio not included as investment costs. For example:
  - Brokerage fees
  - Costs of currency exchange
  - Intermediary activities (acquisition or disposal of assets by brokers).

These costs are passed to the member as a reduction of return/assets value or in a fee, that means de facto lowering the amount that contributes to the “pensions savings” (accrued benefits).

EIOPA’s report on costs and charges provides a classification of several subtypes based on these three main categories. <sup>(15)</sup> Another useful example of cost taxonomy can be found in the document Recommendations on Administrative Costs published by the Federation of the Dutch Pension Funds. <sup>(16)</sup>

Not all types of cost will necessarily fit into these categories of costs. Depending on the kind of pension scheme and/or the characteristics of the IORP, other specific categories of costs or a general category “all other costs” might be needed.

### 4.3. PRESENTATION AND BREAKDOWN OF COSTS

Once the relevant costs are identified, the question arises how costs should be presented and according to which criteria and to which degree they should be broken down.

#### BREAKDOWN OF COSTS

When it comes to cost breakdowns, in practice two main approaches can be found: (i) breakdown according to the nature of costs and (ii) breakdown according to the source to cover the cost and linked to that, the periodicity.

- Nature of the cost (= what is it used for by the IORP). Often used classifications are administration costs, investment costs and transaction costs, but other classifications (e.g. distribution costs, insurance costs) or sub-classifications are conceivable;
- As for the source a distinction can be made between costs deducted from the contributions (“entry costs”) and costs withheld from the assets/entitlements on the pensions account. Within this second category a further distinction can be made between recurring costs, that are applied on a periodical basis and costs that are only applied under specific circumstances, such as e.g. performance fees.

IORP II does not provide any details regarding the breakdown of cost. Therefore none of these approaches should be ruled out a priori. The choice of the approach should be made taking into account which presentation best suits the interests of the member and allows to present an understandable and clear picture of the impact on the “retirement savings” / the accrued benefits = entitlements.

Both approaches have advantages and disadvantages. It is clear that an approach based on the nature of costs gives the best insight in the “cost drivers” of the IORP:

- which part of the total costs emerges from transactions?
- which part goes to investment managers?
- which part is due to administration cost?

However, the question is whether members are capable of understanding this kind of information. For non-experts the distinction between administration, investment and transaction cost might seem quite abstract – as well as what they can do with this information. The added value of this kind of information for scheme members might be higher in cases where members have to make investment choices.

An advantage of a breakdown in terms of the source (contribution, assets/entitlements), is that there is a clear link with the fee structure as defined in the schemes rules. Members can link information on costs in the PBS to the scheme terms and conditions. When a pension scheme for example applies both costs on contributions and costs on assets/entitlements, it seems logical and transparent to structure the costs in the PBS in the same way.

Of course both approaches could also be combined, for example by a further breakdown of costs on assets/entitlements according to their nature (administrative, investment, transaction). Again, while there is no doubt that such an approach would provide a more detailed insight in the cost structure of an IORP, the question to be answered by NCAs (and national legislators) is whether the PBS is the right place to provide such degree of detail, given the characteristics of the PBS (concise, key information, easy to understand).

#### PRESENTATION OF COSTS: EUR OR %?

When it comes to cost presentation, in practice two main approaches can be found: in monetary terms (EUR) or as a percentage. Member States or IORPs might also opt to present costs in both monetary terms and percentages.

<sup>(15)</sup> EIOPA Report on Costs and Charges of IORPS.

<sup>(16)</sup> <https://www.pensioenfederatie.nl/website/engelse-website/publications-in-english/recommendations-on-administrative-costs>.



Consumer testing research in the context of the legislative process of the PRIIPS directive, has shown that retail investors can understand monetary figures (e.g. in EUR) more readily than percentages.

Small differences in costs expressed in percentages may correlate with large differences in the costs borne by the retail investor when expressed in monetary terms. <sup>(17)</sup>

On the condition that amounts in Euro all refer to the same date, different amounts can simply be added up in order to obtain an overall picture.

This is not necessarily the case with percentages, for example if some costs (like entry costs) are expressed as a percentage of the contribution and others as a percentage of assets/entitlements. Only percentages on the same basis can be added up. Using percentages on different bases risks blurring the overall picture for the scheme member.

On the other hand, percentages are easy to compare because – in principle – they are the same for all scheme members. This is not the case for amounts in monetary terms which will be different for every scheme member.

In some Member States costs are capped. Cost caps are mostly expressed as maximum percentages. In order to allow members to compare the effective cost levels with the maximum cost levels, costs should be presented in the same way as the cost caps.

#### REDUCTION IN YIELD (RIY)

RIY is a technique to show the impact of the costs on a yield in a way that enables comparing the effect of different basis of costs as well as to present a total cost figure – putting all costs together into a single figure. This approach is used in the PRIIPS key information document (KID), where the reduction in the yield (%) is obtained by calculating a yield of a product with and without costs. The difference between the two represents the loss in terms of yield due to costs.

The RIY approach has the advantage that it can summarize costs on different bases – both one-off and ongoing costs - in one figure, which makes it easy for investors to under-

stand the overall impact of cost on the investment outcome and thus to compare products in terms of costs. <sup>(18)</sup>

RIY could also be used to look at costs in pension products. However the PRIIPS KID methodology for calculating RIY may then need to be adapted to a PBS context. The PRIIPs methodology uses the RIY in projections, which is different from the retrospective approach of the PBS, which aims to give insight in the costs over the past 12 months. The RIY in PRIIPs also requires – for the sake of projections - a fixed time horizon (the “recommended holding period”), which is less evident in a PBS context because the time horizons will be different for every member.

## 4.4. EXAMPLES OF COST DISCLOSURE

This section looks closer at a number of existing examples of cost disclosure in a few Member States, and which might serve as inspiration for Member States, NCA or IORPs. It should however be noted that these examples were used in a pre-IORP-II context.

### ITALY

The current Italian PBS provides information on costs at two levels. At the beginning of the PBS – in a general section together with the total amount of assets and the return - total costs are shown as a percentage of assets.

Further in the PBS there is a specific section which repeats the total cost percentage and provides a breakdown in administration costs and investment costs, also presented as a percentage of plan assets.

The costs are calculated according to the “Total Expense ratio (TER)” approach. The TER concept required for IORPs in Italy takes into account all operational costs of the IORP, but does not take into account transaction costs and tax. It doesn't show how these costs are borne by the Member, which are paid out of the contributions and which from assets.

Breakdown	Administration	Investment
Presentation	% of assets	% of assets

<sup>(17)</sup> Commission delegated Regulation (EU) 2017/653, of 8 March 2017, supplementing Regulation (EU) No 1286/2014 of the European Parliament and of the Council on key information documents for packaged retail and insurance-based investment products (PRIIPs) by laying down regulatory technical standards with regard to the presentation, content, review and revision of key information documents and the conditions for fulfilling the requirement to provide such documents, recital 12.

<sup>(18)</sup> If the aim of cost disclosure is to show the impact of costs on the pension benefit an even more telling approach might be the “charge ratio”, developed by IOPS. It does not compare the yield with and without costs but instead the final balance of the pension account in a scenario with and without cost. The ratio thus represents the loss in pension income due to costs. IOPS (2014) Update of IOPS Work on fees and charges, IOPS Working Papers on Effective Pensions Supervision, No. 20.

SEZIONE 2 – Dati riepilogativi al 31/12/2016	
<b>Valore della posizione individuale (euro):</b>	***
<b>Rendimento del comparto Garanzia (*):</b>	*** %
<b>Costi del comparto Garanzia (TER)<sup>(1)</sup>:</b>	*** %
(*) Il dato indica il rendimento netto (della tassazione e degli oneri sostenuti) realizzato dal comparto nel 2016. Questo rendimento differisce da quello della posizione individuale, che risente anche del momento in cui le entrate e le uscite si sono realizzate (vedi nota alla Tabella Entrate e Uscite – Sezione 3). (**) Il dato esprime l'incidenza dei costi effettivamente sostenuti nell'anno per la gestione finanziaria e amministrativa (a eccezione degli oneri connessi alla negoziazione dei titoli e di quelli fiscali) sul patrimonio del comparto alla fine del 2016.	
Costi (TER) <sup>(1)</sup> - 2016	
<b>Comparto Bilanciato</b>	
- Oneri di gestione finanziaria	***%
- Oneri di gestione amministrativa	***%
Totale	***%
(1) Il Total Expenses Ratio (TER) esprime l'incidenza dei costi effettivamente sostenuti nell'anno per la gestione finanziaria e amministrativa (a eccezione degli oneri connessi alla negoziazione dei titoli e di quelli fiscali) sul patrimonio del comparto alla fine del 2016.	

### NETHERLANDS (DB SCHEMES)

The Netherlands have a broad experience in cost disclosure for IORPs. In 2011, after a report from the Dutch Authority of Financial Markets on administrative costs for IORPs, the Pension fund industry published for the first time a set of “Recommendations on Administrative Costs”.<sup>(19)</sup> This self-regulation initiative was later on embedded in legal and regulatory measures. This is not used however for the PBS, but for example in the annual report of the IORP. It has to be noted that the use of the recommendations for the purpose of the PBS would require further work in averaging per member or completely individualising the cost information.

The main characteristics can be summarized as follows:

- Detailed taxonomy of costs
- Comprehensive cost-approach
- Look-through principle
- Methodology to address implicit transaction costs
- Pension costs are broken down according to their nature: administration costs, investment costs and transaction costs
- Presented in €/member or % according to the type of cost.

Breakdown	Administration	Investment	Transaction
Presentation	€ per member <sup>(20)</sup>	% of assets	% of assets

<sup>(19)</sup> <https://www.pensioenfederatie.nl/website/engelse-website/publications-in-english/recommendations-on-administrative-costs>. The notion “administrative costs” covers all types of costs: pension management costs, asset management costs and transaction costs. In this paper – and also in earlier EOPAs reports - the notion “administration cost” has a narrower meaning, covering only the first type of costs, the pension management costs.

<sup>(20)</sup> Only active scheme members and beneficiaries are taken into account.

Many aspects might very well serve as inspiration for cost disclosure in the PBS. However, there are a few differences that should be taken into account:

- The requirements apply to DB schemes, not to DC schemes;
- The requirements apply to cost disclosure for annual reports that are meant to inform professionals and not for a PBS that is meant to inform members, i.e. consumers (“retail customers”)
- All costs are taken into account (including costs paid by the employer). The central question is: “what does the pension scheme cost”?
- A presentation of costs in € per member might be less suitable for PBS-use and is only provided for administrative costs. This figure represents an average that is the same for all members, independently of the size of their contributions or savings. This way of presenting costs works very well if the goal is to allow employers/social partners to assess and compare the cost of a pension scheme. In a PBS context this way of presenting seems tricky and might even be misleading because the cost that is effectively borne by a specific member will be different from the average.

### UK NEST-SCHEME

The Annual Statement of the Nest Pension scheme contains a specific cost section. This section gives an overview of the “charges” (direct costs) on contributions and on savings and presents them as a percentage of contributions and entitlements respectively.

Breakdown	Charge on contribution	Charge on entitlements
Presentation	% of contribution + Pence per £10	% of account balance + EUR

- › Costs are broken down in costs on contributions and costs on entitlements, giving no insight in the nature of costs;
- › The impact of costs (charges) is well explained in a very simple and comprehensible manner, thanks to the “pence per £”-wording. Where percentages may seem abstract to scheme members, this wording might help to understand the effect of costs on contributions and entitlements.

**“CURRENT ACCOUNT” APPROACH (BELGIUM – UK – NL (DC))**

Based on the findings of an investigation regarding transparency on costs and returns in DC schemes, the Belgian authority FSMA published in 2016 a communication containing expectations and recommendations. The communication contains examples of the PBS that are based on different best practices found in the market.

**NEST's charges**

There are two different charges you pay. We take a small percentage of the money going into your pot. This amount is 1.8 per cent. So, for each £10 being paid into your account we take a contribution charge of 18p.

We also take a very small percentage off the value of your retirement pot over the year. This amount is 0.3 per cent. So, for each £100 in your retirement pot we take 30p off the total value of your retirement pot over the year.

		Total
<b>Votre réserve de pension au 1/1/2016</b>		<b>10.000 EUR</b>
<b>Contributions versées au cours de l'année 2016</b>		
Contributions prévues par le règlement <sup>16</sup>		1.000 EUR
Taxe (4,4 %)	(-)	44 EUR
<b>Total des contributions</b>	<b>(+)</b>	<b>956 EUR</b>
<b>Rendement attribué pour 2016</b> (vous trouverez un calcul détaillé plus loin)		
Rendement du placement (3,2 %)	(+)	335 EUR
Frais prélevés sur la réserve (0,9 %)	(-)	94,2 EUR
<b>Rendement total (2,3 %)</b>	<b>(+)</b>	<b>240,8 EUR</b>
<b>Votre réserve de pension au 1/1/2017</b>		<b>11.196,8 EUR</b>

Saldo per <begin periode>	€ <bedrag>
Hoeveel premie heeft u in <periode> voor uw beleggingsverzekering betaald?	€ <bedrag>
Subtotaal 1: saldo per <beginperiode> plus inleg <periode>	€ <bedrag>
<i>Hiervan trekken we het volgende af:</i>	
premies overlijdensrisicodekking	€ <bedrag>
premies arbeidsongeschiktheidsrisicodekking	€ <bedrag>
premie verzekerd garantiebedrag	€ <bedrag>
kosten verzekeringsmaatschappij (eerste kosten en doorlopende kosten)	€ <bedrag>
kosten bemiddelaar of verzekeringsadviseur	€ <bedrag>
aan- en verkoopkosten	€ <bedrag>
Totaal	-/- € <bedrag>
Subtotaal 2: na aftrek kosten en premies	€ <bedrag>
Hoeveel heeft u in <periode> verdiend op de beleggingen (resultaat)?	€ <bedrag>
Saldo per <einde periode>	€ <bedrag>

In these models costs are not a separate topic, but are part of a “current account” in which all in- and outflows in terms of contributions, costs and returns are integrated. The current account explains the evolution of the account of the member between the beginning and the end of the year. In addition pension institutions are also asked to present **costs as a percentage of contributions or entitlements** respectively.

Breakdown	Charge on contribution	Charge on entitlements
Presentation	% of contribution + EUR	% of account balance + EUR

A comparable approach is followed in the Netherlands. For DC schemes an annual statement is sent to members. In this statement there is a distinction between:

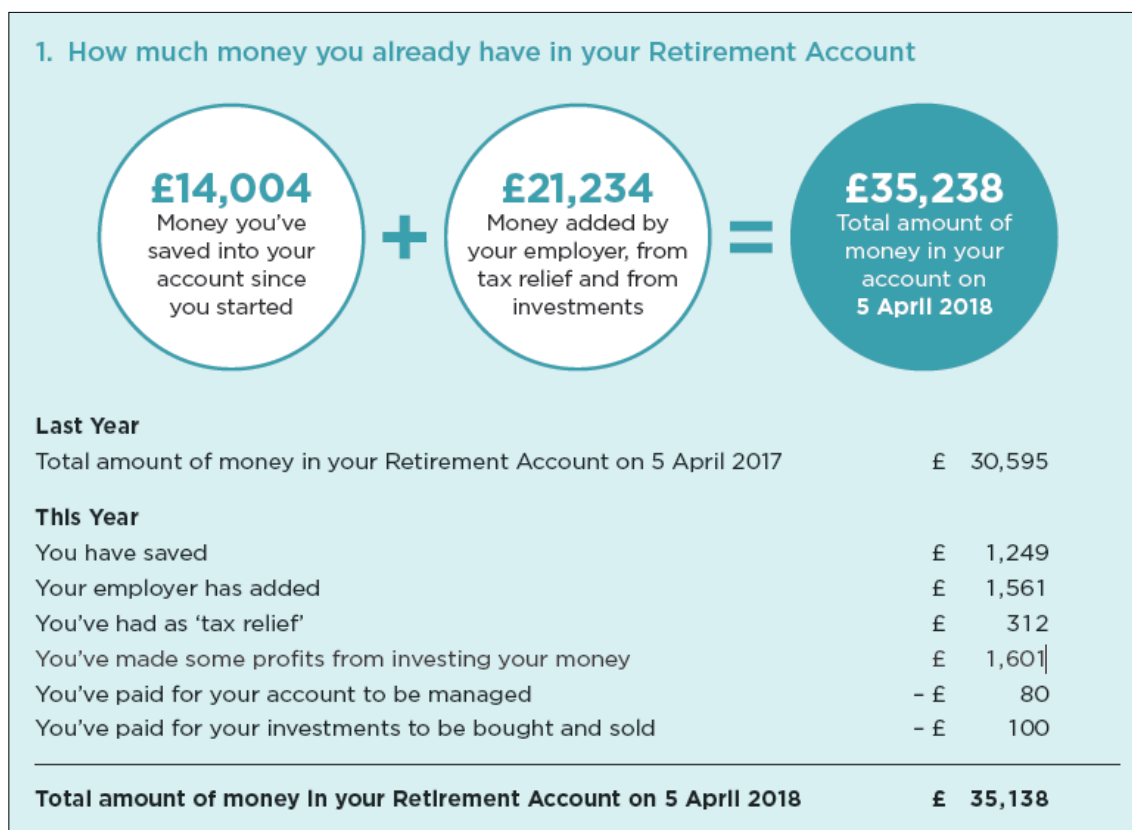
- First costs and ongoing costs
- Costs for the advisor or intermediate
- Buy and sell costs

Another example of this approach was found in the PBS of a UK DC workplace pension. <sup>(21)</sup>

- Costs are broken down into costs on contributions (if any) and costs on savings, which means that the PBS does not say anything on the nature of the costs;
- The current account gives members insight in the evolution of their accounts from one year to another, by showing in and outflows. In order to this all major flows have to be taken into account: contributions, costs and returns. However, IORP II does not explicitly require returns to be mentioned on the PBS.

### SPAIN

On a semi-annual basis, the management entities in Spain have to forward to the members and beneficiaries of occupational pension schemes information on the evolution and status of their entitlements in the plan, as well as on the events that may affect them, especially changes in the plan rules or in the investment policy and changes in the management and deposit costs. The semi-annual



<sup>(21)</sup> [https://quietroom.co.uk/wp-content/uploads/2018\\_04\\_5\\_Annual-Statement\\_QRdesign.pdf](https://quietroom.co.uk/wp-content/uploads/2018_04_5_Annual-Statement_QRdesign.pdf)

**Management fees: % Position Account**

Maximum limits set by law (legal cap):	Real fees (Average)
- For fixed-income funds: cap of 0.85%	To be determined
- For mixed funds: a cap of 1.30%	To be determined
- For equity funds: a cap of 1.50%	To be determined

**Custody fees: % Position Account**

Maximum limits set by law (legal cap):	Real fees (Average)
0.20%	0.03%

information also contains a summary of asset values, the costs and the return. <sup>(22)</sup>

The costs in the PBS are broken down according to their nature. The PBS mentions two types of costs: management fees and custody fees. Both are presented as a % of assets.

In Spain costs are capped. <sup>(23)</sup> The PBS both mentions the effective costs and the cost cap, so that members can assess the costs of their pension scheme in the light of the legal limits.

## 4.5. PRINCIPLES FOR COSTS DISCLOSURE

On the basis of existing practices as well as considering research on consumer behaviour, EIOPA members have identified the following principles to be taken into consideration by Member States in the implementation of IORP II in order to serve the behavioural purposes identified in chapter 1.

EIOPA identified the following principles:

- 1. Cost disclosure in the PBS should aim at giving members the ability to understand the impact of costs on their pension entitlements and to compare cost levels**

Within the context of national pension policies and taking into account the specificities of the pension schemes concerned, cost disclosure in the PBS should aim to:

- help scheme members understand the impact of costs on (the evolution) of their pension entitlements: how will costs affect my future pension income? How much was deducted from the (employee and/or employer) contributions (before going into the fund)? How much was taken from my account / from investment gains?
- help scheme members compare the cost of different schemes, especially when the member can opt out or transfer his or her savings or when the member has different investment options (with different cost structures);
- contribute to one of the PBS main goals (chapter 1), allowing scheme members to make informed choices. From a broader perspective, cost disclosure may also contribute to reducing costs (and thus increase value for money), because it might lead to greater cost awareness among scheme members and help them to apply competitive pressure to pension providers; <sup>(24)</sup>
- increase accountability of pension providers.

<sup>(22)</sup> Furthermore, entities are compelled to give further information on the name of the Management entity, Custody entity, the auditor, and where necessary, the delegated entity for the management of the Fund's financial assets.

<sup>(23)</sup> Until 2018 year there was a single cost cap of 1.50% but the average real management fees were of 0.18 %. The cap for custody fees was of 0.25%, and the real fees of 0.03%.

<sup>(24)</sup> Idem, p. 19. Cf. OECD, *Pension costs in the accumulation phase: policy options to improve outcomes in funded private pensions*, 2018, 13-17.

It is clear that none of these goals can be achieved through the PBS alone, especially taking into account its concise and simple character. Thorough understanding and full comparability of costs require more information than can be presented on a PBS. However, in such a case, the PBS can serve as a starting point for scheme members to look for further information, which has to be indicated.

**2. Cost disclosure should be accurate and consistent with the pension plan design and with the cost-structure of the plan**

The way costs are disclosed should be consistent with the pension plan design and with the cost structure of the plan. Plan design and cost structure vary greatly across (and within) Member States. For example: in some Member States entry fees (taken from contributions) are not common. It is obvious that a breakdown model that is exclusively based on the distinction between costs of contributions versus costs on assets might not offer the best solution in such a context.

**3. Information should be member-oriented**

To help members understand the impact of costs, the communication should be customized to the perspective of the member and the member's individual amounts. The PBS is intended to inform the member about his or her pension entitlements, and not just to provide general information about the pension scheme. Also when cost disclosure is at stake, the focus should be on the members' information needs. This implies that information on costs should be relevant and useful for the member.

As a consequence the primary focus of the PBS should be on the costs that are directly and indirectly borne by members. It is important to note that this does not exclude costs paid by employers. In some cases employers cover all or part of the IORP's costs, based on arrangements between the IORP and the employer. To the extent that these arrangements have an impact on the accrued benefits for the member, they can be taken into account in the cost disclosure on the PBS.

IORP II does not seem to prevent Member States from requiring IORPs to mention all types of employer costs on the PBS, for example when the employer does not pay the cost into the IORP but directly to a service provider. This is a larger cost concept, giving an answer to the question:

what is the total cost of the pension scheme (whether costs are borne by the IORP or by the employer)? Member States might opt for such an approach in order to assure consistency with information on costs that is accessible to scheme members through other documents. However, the information on the total cost of the pension scheme must not conceal or provide confusion about the affect of costs on an individual member's accrued benefits (see below 4.).

The member orientated approach also implies that information should be presented in a way that is easily understandable by members.

Therefore coherence in the cost presentation is also crucial. The member should be able to understand the impact of the costs. This understanding might, for example, be hampered if different ways of presenting costs (% for one type of costs, EUR for another) are used alongside each other, making it difficult for members to comprehend the overall impact of costs. Information on costs must also be consistent with other information on the PBS, such as accrued entitlements or contributions.

**4. Information should be individualized**

The way costs are presented to the member should reflect the costs that were effectively borne (directly and indirectly) by the member. The PBS provides individualized information. It is not enough to provide the amount(s) of total cost for the whole of the IORP (even when broken down). PBS should give the member the ability to get insight in the costs deducted from the contributions or from his account/assets value (i.e. the impact on the member's accrued benefits).

**5. Comprehensive cost approach: look-through**

In order to assure comparability of information on costs between IORPs, the costs included in the PBS should include all the costs in the value chain that are reducing gross return or the asset value of the member.

As a consequence:

- the PBS should take into account all costs, both direct costs ("charges", "fees"), and indirect costs, this means costs on the level of the IORP which lead to lower returns;

- IORPs are encouraged to follow a “look-through approach”, in order to make all the (investment) costs transparent, not only the costs they pay for directly, but also the costs of the underlying investment layers. This means that where an IORP invests through investment funds, the cost of these funds must be incorporated. Indeed, whether a cost is borne directly by the IORP, or indirectly via a lower asset value in the investment fund, the impact for the member is the same. This approach is also followed in packaged retail and insurance-based investment products (PRIIPs).

#### 6. Cost information should cover at least the last 12 months

The PBS gives an overview of the costs deducted by the IORP over at least the past 12 months. Cost disclosure in the PBS should therefore follow a retrospective approach: it serves to explain evolutions over the past year and is not intended in the first place to provide projections on future costs. Future costs will be reflected in the pension projections.

#### 7. Cost information should be disclosed at the appropriate level of granularity and complexity

A member oriented approach sets constraints to the level of granularity (= breakdown) and complexity. Unlike fund trustees and social partners, who need to be able to monitor and control cost, scheme members are not necessarily interested in the full detail of cost, and the general principle of ‘less is more’ should be borne in mind. Scheme members need to understand the overall impact of the costs on contributions/assets/pension entitlements, not necessarily the details. Although some kind of breakdown is necessary to be IORP II compliant, this means that costs only need to be broken down to the extent that it represents an added value for the member. This is also in line with the concise nature of the PBS and the fact that it should contain key information (art. 38.1).

Scheme members are consumers, i.e. retail customers not professionals. Therefore cost should be presented in a way that is easy to understand for consumers. The breakdown of costs should be as simple and as comprehensive as possible.

The aggregate, simple and concise nature of cost disclosure in the PBS does not mean that members should not be given access to further available information on costs via other documents. Indeed, as for costs, more detailed information can be found in the annual accounts and annual report. The PBS should indicate where and how members can obtain this information (IORP II art. 40.1.b). Yet, unlike the information on the PBS this information is not individualized.

## 4.6. CHAPTER CONCLUSIONS

In a pension environment where the DC model is becoming more and more widespread, the importance of costs is growing.

The IORP II Directive introduced structural cost disclosure requirements in the PBS for IORPs where members bear the investment risk or can take investment decisions. The costs included in the PBS should include all the costs – whether direct or indirect – in the value chain that reduce the accrued benefits/pension entitlements of the member.

Cost disclosure in the PBS should aim at giving members the ability to understand the impact of costs on the evolution of their pension entitlements and to compare cost levels. Cost disclosure should therefore be member oriented. This means that the primary focus of the PBS should be on the costs that are directly and indirectly borne by scheme members, although Member States may opt to include also costs borne by the employer. It also means that costs should be individualized and that the level of granularity and complexity should be appropriate for scheme members.

IORP II does not provide detailed rules on breakdown and presentation of costs. In most cases costs are broken down according to their nature (administrative, investment, etc.) or according to the source to cover the cost (costs on contributions, costs on assets). Costs can be presented in monetary terms or as a percentage. All of these approaches – which can also be combined – have their advantages and disadvantages. The choice of the approach should be made taking into account which presentation suits best the interests of the member and should be consistent with the pension plan design and with the cost-structure of the plan.

## 5. LAYOUT AND LAYERING: HOW TO DESIGN A PBS?

### 5.1. INTRODUCTION

The landscape in the design of pension statements differs across Member States and only in some Member States it is standardised with detailed methodologies and a specific layout.

The majority have defined a set of information requirements to be observed by the IORPs, without requirements set on the form/presentation. A few have developed PBS templates, ranging from voluntary to compulsory application by the IORPs. In view of the IORP II implementation, many Member States are taking steps towards the practical transposition of the PBS, including considerations to develop a template at national level.

EIOPA has developed previous work in the area of pension information and communication. In this regard, the EIOPA Report on Good Practices on information Provision for DC Schemes, better known as “Max Report” is a good starting point for the design of pension information and reflects the principles of behavioural economics.

Max, an average European DC pension scheme member, has limited time and motivation to be involved in retirement planning. Moreover, ‘Max is discouraged when he is overloaded with information, and is facilitated if layers of information are readily available. On the other hand, if Max has some more time and motivation, but cannot easily find further information, this might put him off.’<sup>(25)</sup>

In addition, the EIOPA “Report on Good Practices on Communication Tools and Channels for Communicating to Occupational Pension Scheme Members”<sup>(26)</sup> refers to the multi-channel communication strategies as a good practice.

So that the PBS can have a clearly defined behavioural purpose, the presentation of the information should aim to aid the member in understanding his/her current entitlements or accumulated retirement pot (for DC schemes), retirement prospect, if possible the overview of his/her re-

tirement situation (pillar 2 and more), for the purpose of making informed retirement planning decisions.

The format and design of the PBS should be aligned to the goal and subgoals of the PBS, in a way that the information presented responds to the key questions of the member/beneficiary.

Layering and layout are among the tools available to shape the form and design of the PBS and EIOPA has found several current practices from templates used at national level prior to the implementation of IORP II Directive. The present chapter aims at analysing those examples and extracting some key principles that can help members develop the PBS at national level.

Since the IORP II Directive is subject to implementation at national level, it needs to be noticed that any choices made in layering and layout should be taken on that level.

### 5.2. DEFINITIONS

The EIOPA Max Report states that policymakers and experts should anticipate the financial decisions members need to make. Therefore, they have to 1) think through the behavioural purposes; 2) provide layers of information, where, in the first layer, members’ key questions are answered, and 3) in further layers legal or more complex information is retrievable; 4) information is comprehensible; and finally, 5) support members as much as possible towards financial decisions.

As such and in order to enhance the role and effectiveness of information provision, policymakers should have a clear idea about what a member should be able to ‘do’ with the information given.

Often policymakers require the provision of too much information that they believe is relevant for members and what members ‘should know’ about a pension scheme. Moreover, much less attention is paid to the format, the way to structure and provide the information so that it is clear to members how they should ‘use’ this information. The assumption is that members will nevertheless read, and use this information to make informed decisions, but

<sup>(25)</sup> idem, page 32

<sup>(26)</sup> EIOPA, “Report on Good Practices on Communication Tools and Channels for communicating to occupational pension scheme members”, 31 August 2016



experience shows this is not the case. Furthermore, pension providers have rather the compliance with legislation or legal requirements in view than the members' needs.

From a behavioural point of view, people are prone to turn away from information if they do not quickly understand how it is relevant to them and how they should translate the information into financial decisions. This behaviour is even more acute when there is an information overload. The aim of layering and layout of information is to help members retrieve the answers to key and further questions easily, and substantially improve the effectiveness of information.

In this context, EIOPA underlines the importance of layering - structuring information on layers by level of relevance to members - and layout - presentation or display of information is such a way that is easily understood and transmitted to members, also in alignment with the sub-goals of the PBS.

#### **LAYERING ACCORDING TO THE ELEMENTS REQUIRED BY ARTICLE 39**

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From a behavioural point of view, the PBS may be composed of separate layers where in the first layer of information members should be able to find answers to their key questions. Given the need for the implementation of the IORP II Directive, the first layer of information in a PBS may very well contain sections covering already many of the mandatory elements of information required mainly in Article 39.1. This approach, however, does not prevent the provision of full information in the first layer, but proposes to ensure retrievability of further, more detailed information in subsequent layers (e.g. second and third layer). These layers may contain information for the more inquisitive or financially and legally literate, or additional information with no direct connection to the most relevant key questions of the members. Nevertheless, it is not possible to determine in general the final approach that IORPs should adopt during the creation of layers of the PBS, taking into account specificities of the pension systems in the respective Member States. However, in the future, examples of layout design examples could be worked upon for indicative and illustrative purposes.

#### **TYPES OF LAYOUT**

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From a layout point of view, the PBS could be structured and presented in such a way that promotes the most relevant information - questions in headings, text characteristics, graphic structuring of information in sections, boxes or tables – or better realise a connection with members

in order to improve understanding and awareness – visual aids, symbols, colours, diagrams, or animations (the latter achievable only in an electronic environment).

#### **TYPES OF LAYERING**

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Layering of information can be done within the PBS as a tool that helps structure information by separating it in clusters or sections to be more comprehensible. Depending on the approach chosen, such sections can be independent or linked to each other, typically offering general/key information at a glance, which is then expanded in more detail in a subsequent section/layer. It can also be applied to a set of information documents that are located either inside of the PBS – by redirecting the reader to another section – or, outside the PBS, by redirecting the reader towards different mediums of information such as electronic mediums – direct web links - or different ways of asking for more information directly from the IORP, sponsor or NCA, such as phone numbers, mail or e-mail addresses, websites, instant messaging services, video chats, etc.

#### **PAPER AND ELECTRONIC PBS**

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Layering can be done in paper-printed documents, as well as through the use of electronic means, most likely in an easier and more successful manner. Websites are a very effective medium to provide layered information and an appealing layout, thus prompting action, as it brings the possibility of interaction directly to the reader. As such, the electronic environment might easier enable members to retrieve further information in a subsequent layer and better promote engagement. This is especially useful for members who wish to know more of legal terms or who are more financially literate and desire to continue to inform themselves of more complex aspects. Within an electronic environment the information should be as accessible as possible, ideally being one click away.

Moreover, in the Report on “Good Practices on Communication Tools and Channels for Communicating to Occupational Pension Scheme Members”, EIOPA considers as a good practice if IORPs, employers and/or any other relevant entities make use of a multi-channel strategy to communicate to their members.

In this regard, However, regardless whether members have access to electronic means or not, the information provided and the PBS layering and layout should be the same. So the core information transmitted to members in PBS should be the same irrespective of the means of communication, either paper or electronic.

### 5.3. EXAMPLES

The examples depicted below are examples taken from existing PBS templates at national level and prior to the IORP II implementation.<sup>27</sup> Parts of the PBS have been extracted

and classified according to the type of layout and layering tool being analysed. Based on these practices a number of principles have been highlighted in the next section.

#### 1. LAYOUT: QUESTIONS AS HEADING

Source: NL “Uniform Pension Overview (UPO)”: question headings being used

- “What pension can you expect to receive?”
- “What will you receive when you retire?”

Source: BE “Résumé & Dossier” (see below)

PROs (Behavioural purpose)	CONs
<ul style="list-style-type: none"> <li>• Members quickly relate to one of their key questions;</li> <li>• Members better understand what the underlying information is about,</li> <li>• Impetus (nudge) to possible member's curiosity.</li> </ul>	<ul style="list-style-type: none"> <li>• Key question may not be equally relevant for all members.</li> </ul>

#### 2. LAYOUT: USE OF FONT AND COLOUR

Source: BE “Résumé & Dossier”: combination of font sizes, types, styles and coloured boxes to present a section of information.

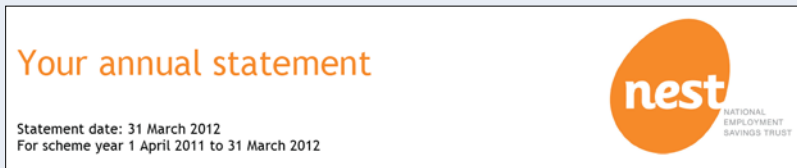


PROs	CONs
<ul style="list-style-type: none"> <li>• Text attracts members' attention to relevant information;</li> <li>• Members can easily read and navigate through the information;</li> <li>• Information is structured in a concise manner;</li> <li>• Such presentation of information is not discouraging or tiresome for members when reading.</li> </ul>	<ul style="list-style-type: none"> <li>• Members may ignore information that is not specifically highlighted or that does not stick out;</li> <li>• An overload of such tools could diminish the comprehensibility of the PBS. For example the PRIIPs Regulation states: 'Where colours are used in the key information document, they shall not diminish comprehensibility of the information if the key information document is printed in black and white'.</li> </ul>

(27) From BE, IE, IT, NL, SK and UK.

### 3. LAYOUT: USE OF SYMBOLS AND SIGNS


**Source: UK NEST Annual Statement:** the logo of the pension scheme is prominently displayed at the top of the first page. Title and date of the PBS also clearly stated.




**Source: NL Uniform Pension Overview:** use of symbols previously tested.

**Source: BE “Résumé & Dossier”:** visual display of second pillar pension entitlements of a person who has worked as an employee as well as a self-employed worker with an equation metaphor.

**Which pension amount can you expect to receive?**

 **What you will receive when you retire**  
When you retire, you will use your investment value to



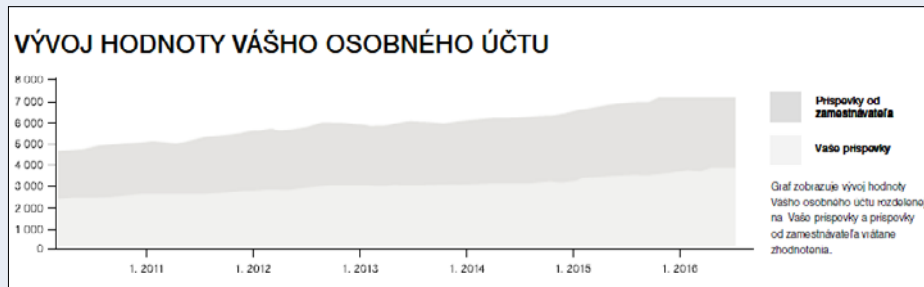
 **If you have a partner and/or children, what will they receive in the event of your death?**  
Suppose that you die before your retirement date and that you are a member of this plan at the time of your death.



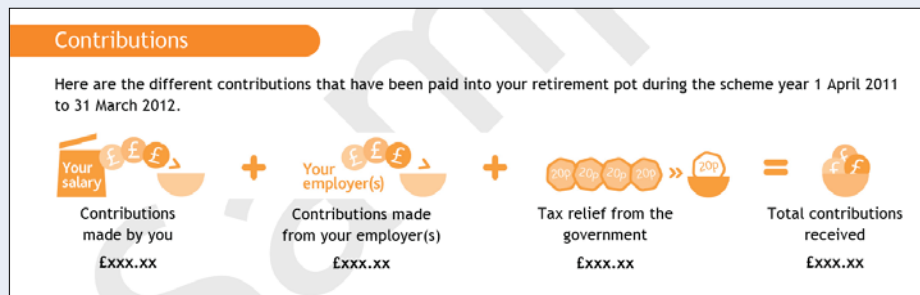
PROs	CONs
<ul style="list-style-type: none"> <li>• Symbols and signs attract members' attention to relevant information;</li> <li>• Members can easily navigate through the information;</li> <li>• Information is structured in a concise manner;</li> <li>• Symbols are a way to reduce text and thus save space.</li> </ul>	<ul style="list-style-type: none"> <li>• Symbols may give rise to different interpretations.</li> </ul>

#### 4. LAYOUT: USE OF CHARTS & DIAGRAMS

**Source: SK “Account statement complementary pension”:** presenting the pension pot broken down by employer and employee contribution over the last 5 years in a chart



**Source: UK NEST Annual Statement:** use of a diagram with visuals of coins, pots and mathematical symbols to explain the source and sum of contribution received.



**Source: The Economic and Social Research Institute working paper, together with Pensions Authority in Ireland:** “Supporting decision-making in retirement planning: Do diagrams on pension benefit statements help?”: explanatory diagram with projections placed inside a cartoon pot of money.



PROs	CONs
<ul style="list-style-type: none"> <li>Charts and diagrams attract members' attention to relevant information;</li> <li>May foster easy associations with day to day life;</li> </ul>	<ul style="list-style-type: none"> <li>Not all members may easily understand the graph or diagram and so the message of the PBS is lost on these members.</li> </ul>
<ul style="list-style-type: none"> <li>Information is structured in a concise manner, and it is better understandable;</li> </ul>	
<ul style="list-style-type: none"> <li>Charts and diagrams save space.</li> </ul>	

## 5. LAYOUT: BOXES, TABLES

**Source: IT “Schema di Comunicazione periodica”:** Under the last section ‘Useful information’, there is a table with information on 1) Legal requirements and fiscal information, 2) Personalised projection, 3) Hotline and contact e-mail of the IORP, 4) Official address of the IORP.

<b>Recapiti utili</b>
<b>Sito web</b>
Sul sito web <a href="http://www.fondopensioneexemplum.it">www.fondopensioneexemplum.it</a> , nella sezione “Documentazione” sono disponibili, oltre alla Nota Informativa, il regolamento, i documenti sul regime fiscale, sulle rendite, sulle anticipazioni e il rendiconto. Su richiesta, i predetti documenti possono essere inviati agli interessati.
<b>Consultazione della posizione individuale on line</b>
Nella sezione “La tua posizione individuale” del sito web è possibile verificare la posizione individuale e l’evolversi della stessa, utilizzando il codice utente e la password personale (modificabile). Nella medesima sezione è possibile accedere al motore di calcolo che consente la realizzazione di proiezioni personalizzate dell’evoluzione tempo per tempo della propria posizione individuale e dell’importo della prestazione complementare attesa (La mia pensione complementare).
<b>Assistenza tecnica</b>
Il personale del servizio clienti della società è a disposizione degli aderenti dal lunedì al venerdì, dalle ore 9 alle ore 18 al numero: 06/243.280.31. È inoltre attivo il servizio e-mail: <a href="mailto:info@fondopensione.exemplum.it">info@fondopensione.exemplum.it</a>
<b>Comunicazioni e richieste</b>
Sede legale: Via della Gioconda, 1 – 00122 Roma - Tel.: 06/243.280.32 - Fax: 06/243.280.35

PROs	CONs
<ul style="list-style-type: none"> <li>Information is structured in a concise manner, and it is better understandable (segmentation of information can be considered in order to make the information fit to the needs of the reader as much as possible).</li> </ul>	<ul style="list-style-type: none"> <li>Structuring information as such might occupy more space in detriment of other information.</li> </ul>

## 6. LAYERING: DIVISION IN SECTIONS/PARTS FROM GENERAL TO SPECIFIC/DETAILED

**Source: BE “Fiche de Pension”:** Two clear sections to layer information: Part 1 General accrued rights and pension estimation, Part 2: Details and explanations on pension entitlements.

<p><b>PARTIE 1 Aperçu général de vos droits de pension</b></p> <p>Vous trouverez ci-dessous un aperçu succinct de vos droits de pension. Le calcul de ces droits a été opéré en tenant compte de votre situation personnelle au &lt;date de recalcul&gt;. La Partie 2 fournit davantage de précisions ainsi que des informations complémentaires sur ces droits. Vous y trouverez notamment un relevé détaillé de l’évolution de votre réserve de pension en 2016.</p> <p><b>Droits de pension au 1/1/2017</b></p>
<p><b>PARTIE 2 Détails de vos droits de pension</b></p> <p><b>Votre plan de pension</b></p> <p>Cette fiche de pension vous donne un aperçu des droits que vous avez constitués à la date du 1<sup>er</sup> janvier 2017 dans le cadre du plan de pension de votre employeur. Elle ne tient pas compte d’éventuels événements ultérieurs. Il est possible que les montants aient entre-temps évolué.</p>

PROs	CONs
<ul style="list-style-type: none"> <li>Information divided in sections provides structure to the PBS in main areas/questions for the reader, from the more general (key aspects at a glance) to the more detailed information;</li> <li>A layered PBS (with sections) can help the reader classify the type of information that will appear and give expectations on the content;</li> <li>Limited number of sections to prevent overload of information.</li> </ul>	<ul style="list-style-type: none"> <li>Labelling of sections may not coincide with the preferences of the reader.</li> </ul>

**7. LAYERING: DIVISION BY TOPICS/STRIPES/BOXES INDEPENDENT FROM EACH OTHER (BUT AT SIMILAR LEVEL REGARDING DETAILNESS OF INFORMATION, COMPARED TO 6.)**

**Source: UK NEST Annual Statement:** clear sections with orange stripes; highlighted information presented within a colour box.

**About you**

<b>Name:</b> John Smith	<b>You joined NEST on:</b> 18 July 2011
<b>Date of birth:</b> 25 March 1984	<b>Your NEST retirement date:</b> 25 March 2054
<b>Your NEST ID:</b> 123456	

**Your retirement pot**

This section shows the value of your retirement pot. This means the total of all the contributions made as well as the investment performance after charges have been taken into account.

It also shows where your retirement pot was invested as at the date of this statement.

<b>Value of your retirement pot on 1 April 2011:</b>	£x,xxx.xx
<b>Value of your retirement pot on 31 March 2012:</b>	£x,xxx.xx
<b>As at this date your retirement pot was invested in:</b>	NEST 2054 Retirement Date Fund

You can log in to [www.nestpensions.org.uk](http://www.nestpensions.org.uk) to view your retirement pot and see how your money is invested.

PROs	CONs
<ul style="list-style-type: none"> <li>Information in small "digestable" parts/sections, with intuitive titles/topics provides a concise and clear structure to the PBS;</li> <li>Coloured boxes favour catching the attention of the reader;</li> <li>The order of the sections is logical for the reader;</li> <li>Limited number of sections to prevent overload of information.</li> </ul>	<ul style="list-style-type: none"> <li>Titles may not always be understandable for the reader.</li> </ul>

**8. LAYERING: REDIRECTION WITHIN THE PBS**

**Source: IE Standard template:** redirection to Section at the end of the PBS

**2. Your projected benefits**

Your scheme contributions are invested on your behalf and your retirement benefit depends on how much money has been built up in your fund at retirement. We use assumptions to show you what your retirement fund might be, and the income that it might provide for you, at your normal retirement age.

If your contributions continue...	At normal retirement age	Value in today's money
Your projected fund will be:	€350,000 <sup>2</sup>	€280,000
This provides a projected income of:	€17,000 a year	€14,000 a year

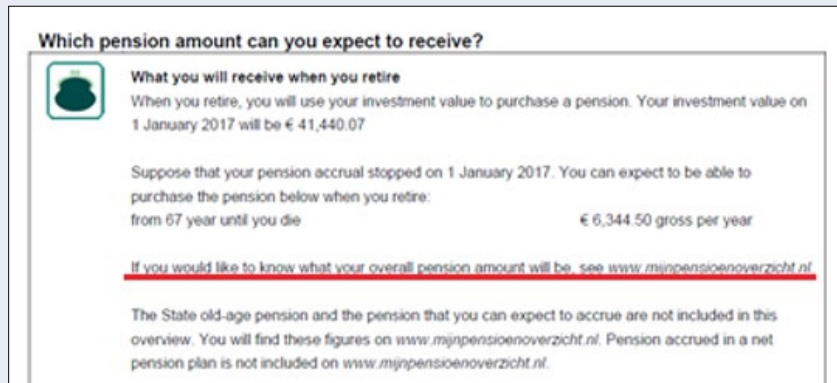
These projections assume that your regular contribution of €200 per month, additional voluntary contributions (AVCs) of €500 per year and your employer's regular contribution of €200 per month will continue until your retirement age.

Please see section 8 for notes on these projections.

PROs	CONs
<ul style="list-style-type: none"> <li>The reader can easily retrieve the information at the end of the document.</li> </ul>	<ul style="list-style-type: none"> <li>See next CONs (under 9.).</li> </ul>

## 9. LAYERING: REDIRECTION TO ANOTHER SOURCE OUTSIDE THE PBS

Source: NL Uniform Pension Overview: redirection to the pensions' dashboard.



PROs	CONs
<ul style="list-style-type: none"> <li>Redirection to a pension calculator or dashboard with information on the state pension and other pension products, can help the reader understand his/her overall retirement entitlements.</li> </ul>	<ul style="list-style-type: none"> <li>If the reader is not directed to a specific page or section within a website where the information is available (or if a link is not easy to find for the reader) the information could get lost or the reader is demotivated to deal with his/her retirement planning;</li> <li>The reader should be able to retrieve the information through small efforts (e.g. through single sign-on where multiple dashboards can be entered after logging in just once).</li> </ul>

## 5.4. PRINCIPLES FOR PRESENTING A PBS

EIOPA identified the following principles:

### BEHAVIOURAL ASPECTS

- Any design of the PBS should be tested among users, to ensure that the combination of design features and tools fit both the information needs of the member and the legal requirements.**

Behavioural economics could provide fundamental guidance for any design decision about a PBS. Therefore, Member States drafting a PBS format should take basic behavioural mechanisms into account so as to enable members

a conscious perception of information. Those mechanisms are affected by how the information is presented: can the member easily relate to the information? What should he do with the information received? Members are also affected by positioning of information. For example it has an effect whether information is provided above or underneath a line, presented in a table or as a running text.

Considering the variety of design features for structuring and presenting a PBS it is difficult to promote any as the best one. It might be more appropriate to say that all practices presented above are specific layout and layering tools, which could be considered when developing a PBS. In any case, there are undoubtedly further layout and layering tools worth consideration. It is key in this context therefore to test concrete designs with consumers to the extent possible.

## LAYOUT

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2. **The use of layout stylistic and visual tools can make the PBS attractive and easy to read for the member. A combination of these tools can drive the reader's attention to the most important information and enable him/her to navigate easily through given information.**

In regard to the layout of a PBS, the use of stylistic and visual tools such as questions as headings, font and colour as well as signs and symbols can be effective: they render the information more attractive, easier to understand and navigate, and have a behavioural effect of capturing the member's attention at a glance and right at the beginning.

Non-text tools, such as boxes and tables, structure information in a concise manner, which makes information better understandable: they have the behavioural effect of not discouraging the member from reading. The use of charts & diagrams also help the member visually capture and process information faster.

On the other hand, excessive use of those stylistic tools might drive members to ignore other important information or simply put some off from reading. Different members may well have different capabilities, e.g. in using graphs. A balanced and considered approach is therefore important.

Members States should take behavioural economics into account when designing a PBS, in particular stylistic and visual tools to facilitate understanding and keep the scheme member motivated to engage in retirement planning.

## LAYERING

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3. **All basic PBS elements should be included in the PBS and the layering structure should respond to the member's key questions, guiding him/her as much as possible towards key financial decisions.**

The Max Report states: 'The discussion should concern how the information should be put in the appropriate layers (for example: must know, should know, nice to know). And how the information can be organised in such a way that members can easily find the information they search.'

This can be done in at least two ways: either implicitly, by presenting the facts in an understandable manner and letting the member draw its own conclusions or, explicitly by presenting the facts in an understandable manner and showing the member, what his/her range of possibilities are and which concrete steps he/she can take.

In this regard, two types of PBS could be envisaged:

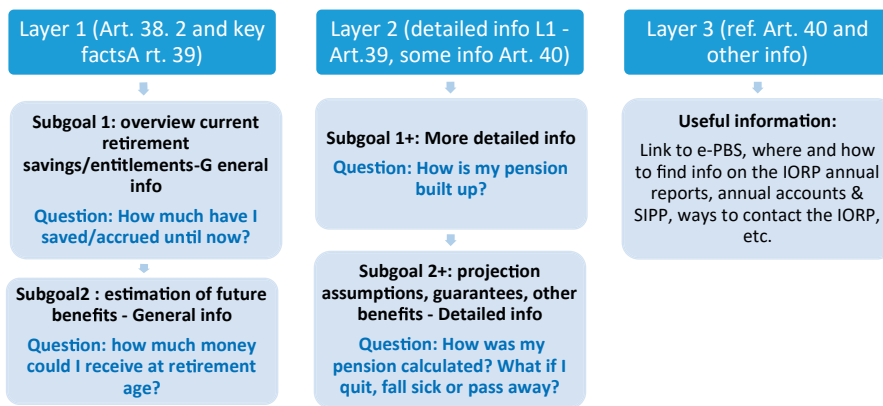
- A **basic PBS**, that is a very concise document covering the mandatory elements of IORP II, and that uses a layered approach, from general/key information to more detailed information;
- An **advanced PBS**, a concise document that aims to provide the member – in addition to the basic PBS – with a more complete overview for his or her retirement planning regarding future pension/retirement sources and suggests possibilities to improve the retirement prospect. The layering approach is a combination from key/general to detailed information and sections. Digital distribution is likely most fitted for the advanced PBS.



## 5.5. PBS PROPOSALS

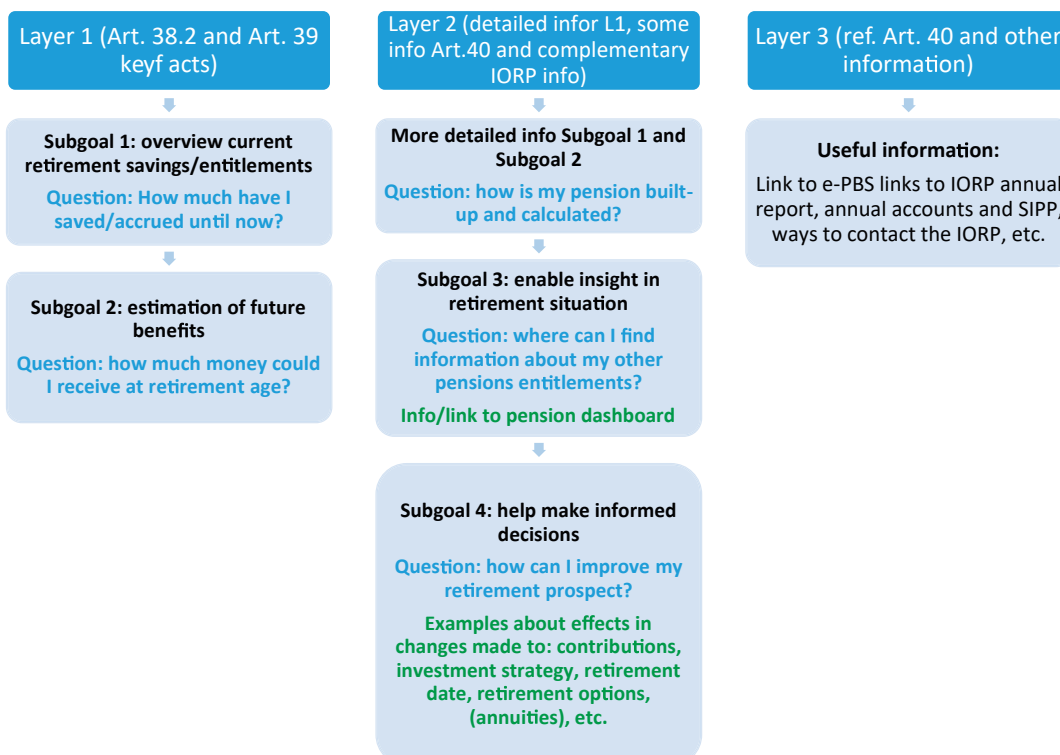
### PROPOSAL 1) BASIC PBS

In the “basic PBS” sub-goals 3 and 4 are implicit in the conclusions drawn by the member. Based on the information received, the member can make its own conclusions on changes needed to his retirement scheme (increase of contribution, change of scheme or investment option, if permitted/offered in the Members State), but he or she is not guided step by step to do so.



### PROPOSAL 2) EXTENDED/ADVANCED PBS

The advanced PBS proposes to go beyond the minimal PBS requirements in order to provide the member comprehensive information on his or her pension/retirement situation and help him or her in taking action to improve his retirement outcome, if relevant.



As the advanced PBS contains more information, a layered presentation of the PBS becomes more relevant. In a digital setting, there are more possibilities to layer information. This means that layer 2 information can be provided via redirecting the reader to a webpage that contains a pension calculator or a pension dashboard. Depending on the type of tool, subgoals 3 and 4 could be merged in one section.

The PBS proposals are mere examples on how to achieve the PBS subgoals and at the same time consider the new IORP II requirements. The policymakers should design the PBS bearing in mind the behavioural approach principle. Further testing of those and other possible combinations would be desirable in order to assess the effectiveness of the communication and the degree to which members understand it.

## 5.6. CHAPTER CONCLUSIONS

The PBS should address the key questions of the member and establish what (s)he should do with this information.

Layering and layout should be taken into account in developing PBS.

Information is layered according to the relevance to the member: the use of layers provides a comfortable framework to members that helps to easily navigate through the document (from one layer/part of information to the other) and find answers to his/her key questions.

The use of layout tools and devices should be geared towards making a PBS design effective, attractive and easy to read for the member: a meaningful combination of these tools help the member identify key information at a glance and prompt his interest on the other aspects of the PBS.

Irrespective of whether the PBS is electronic or paper, the core information transmitted to members should be the same.

Member States should consider the different forms of layering available. A first step is to allocate different information to different layers. Layers can also be used to easily contact pension administrators via diverse channels and/or find information in the other documents outside the PBS.

The next step could be to consider different communication channels. EIOPA encourages a multi-channel strategy to reach a wide array of members.

Independent of the applied strategies, Member States have to match and meet the legal requirements according to IORP II. Having regard to the PBS goals and the layering and layout possibilities, two possible ways to design the PBS are proposed:

- › A basic PBS that covers the mandatory elements of IORP II, implicitly helping the member towards a retirement decision, and
- › An advanced PBS, which goes beyond the mandatory PBS requirements and provides additional information to the member (e.g. using a pension calculator or dashboard) and explicitly shows the various options at hand to improve the member's retirement prospect.

The PBS proposals are just two examples of how the new IORP II requirements could be embedded in a PBS that takes the behavioural purpose approach. Further work and testing of possible combinations of layering and layout tools would be desirable in order to assess the effectiveness of the communication and the degree to which members understand it.

## 5. CONCLUSIONS

In an environment in which more risk is placed on the member, the importance of receiving adequate information on the second pillar retirement income is growing. A way to ensure that information is understood and has the desired impact, is to facilitate it with a clear view on its behavioural purpose. The purpose of the PBS is to help members make informed decisions about their savings. To fulfil this aim, a shift of approach needs to be made in the design of a PBS: from a rather legalistic and compliance to a behavioural approach. The PBS goal should therefore address the key questions of the member and establish what (s)he should do with this information.

Four subgoals have been identified in the PBS: 1) provide an overview of current retirement savings (accrued entitlements or accumulated capital), 2) provide an estimation of future retirement prospects 3) enable insight into the individual retirement situation and 4) help the member make informed decisions.

The principles for designing the PBS envisage the involvement of communication experts and the testing of the design, the need to consider the characteristics both of the pension scheme and the member profile and the integration of the communication tools in place at national level to ensure the adequacy and effectiveness of the information provided through the PBS.

EIOPA is the view that information contained in a PBS should be comparable in relation to other PBSs within a Member State. For the disclosure of pensions projections, two techniques used prior to the implementation of IORP II have been analysed: a deterministic and a stochastic approach. Regardless of the approach chosen, it is important to decide on the assumptions used to ensure the comparability between PBSs and the possibility for the member to add various pension projections for his/her retirement planning.

Similarly, in order to understand the impact of costs on the evolution of the pension entitlements, the cost disclosure should be member oriented and include at least all costs that are directly and indirectly borne by scheme members. This should possibly be calculated in an individualised manner and its presentation understandable

for the member, whilst consistent with the pension plan design and its inherent cost structure.

From a format perspective, layout and layering should reflect the goals of the PBS. The layering of information should provide a comfortable framework for members to navigate from one layer of information to the other and find answers to his/her key questions. The use of layout tools should be geared towards making a PBS design attractive, effective, understandable and easy to read for the member. A meaningful combination of these formatting techniques should help the member identify key information at a glance.

In a digital environment, layering can be done easily through electronic or web-based means. However, EIOPA is the view that core information transmitted to members in the PBS should be the same irrespective of the communication channel used.

Bearing in mind the new legal requirements and the behavioural approach of the PBS, EIOPA proposes two ways of designing the PBS: a basic PBS and an advanced PBS. The basic covers all mandatory elements of the PBS and implicitly helps member towards a retirement decision. The advanced PBS relies on additional information that goes beyond the mandatory requirements and which is usually available by means of a pension dashboard, and explicitly guides the member towards possible options to improve his/her retirement prospect.

EIOPA is of the view that further testing of the PBS proposals and other possible combinations of layering and layout tools is needed to understand, from an empirical perspective, if the PBS fulfils its purpose.

# ANNEX I:

## COST AND BENEFIT ANALYSIS FOR THE PBS

### WHY HAS EIOPA DONE THIS ANALYSIS?

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The project aims at identifying current practices as a first step towards an identification of best practices as foreseen under Article 39 (2) of the IORPII Directive which requires that “(...) Member States shall exchange best practices with regard to the format and the content of the Pension Benefit Statement”.

In the development of the current practices report, EIOPA has duly considered the possible options for the different areas of this work and the potential cost and benefits for relevant stakeholders (including IORPs, members and national competent authorities).

The present Report on the Pension Benefit Statement (PBS) has been consulted with the EIOPA Occupational Pensions Stakeholder Group in the course of August 2018 and their feedback has provided valuable input to the work.

### RATIONALE

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The IORP II Directive introduces new requirements on disclosure, in particular in relation to the annual statement to be sent to members, known as the PBS. Article 39 foresees a list of mandatory elements to be included in the PBS, among which:

A few Member States have acquired experience with pension communication with scheme members, in particular those that have already a template for benefit statements prior to the implementation of IORP II Directive. However, most Member States have no such requirement in place and would need to start the work from nil.

As a minimum harmonisation Directive with no Delegated Acts, regulatory and supervisory practices implemented under IORP II are more likely to vary significantly from one NCA to another. However, NCAs are faced with similar challenges regarding the implementation of the PBS:

#### 1. Trend from DB to DC pension schemes

PBS approaches should take into account key trends in the pensions landscape, notably the shift from DB to DC types of scheme, which place more responsibility (and risk) on the individual in comparison to DB schemes where the risk and cost tended to fall to the employer. There are several causes connected with this shift, such as the increased longevity of the EU population and the increasing volatility of the financial markets and interest rates, altogether making it more difficult for sponsors to assume the costs and risks of occupational pensions.

#### 2. Behavioural component of pension communication

Behavioural economics helps explain why people under-save for retirement. There are several psychological and social factors that impact on economic decisions. Among the cognitive barriers we find inertia (a tendency to avoid decisions for fear of regret), present bias (preference of consuming today over saving for tomorrow) and anchoring (keep the minimum pension contribution believing that it will provide an adequate sum in retirement). We also know from the EIOPA prior work in the area of information provision for DC schemes that members are discouraged if overloaded with information. Therefore, special attention ought to be paid to pension communication. Consumers and members of occupational pension scheme should be able to receive information in an understandable and simple manner, and in a way that it responds to a behavioural purpose: what should they do with this information?

#### 3. Interpretation of Art. 39 on the PBS:

There are new requirements on the annual pension benefit statement, which vary from how the information should be transmitted (principles, means) to which elements (mandatory components) should the PBS contain.

The principles <sup>(28)</sup> envisage that the PBS should be written in a clear manner, use clear, succinct and comprehensible language, not be misleading, have consistency between vocabulary and content, and be presented in a way that is easy to read. Also <sup>(29)</sup> that the PBS should be a concise document containing key information for each member. The PBS should be accurate, updated and made available to each member free of charge, through electronic means or on paper at least annually.

The IORP II Directive requires Member States to ensure that the PBS entails at least information on: a) personal details and retirement age, b) IORP and scheme identification, c) guarantees, d) pension projection/s, e) accrued entitlements or accumulated capital, f) contributions in the last 12 months, g) breakdown of the costs deducted by the IORP at least over the last 12 months and h) funding level of the scheme). Among them, the most challenging for the Member States are pension projections and cost break down, according to the stocktaking exercise conducted by EIOPA in June 2017. <sup>(30)</sup>

Moreover, the outcome of this exercise was helpful to understand the current practices (prior to the implementation of IORP II Directive) by NCAs in a number of relevant areas:

- **Standardisation:** only few Member States use a standardised PBS template [BE, BG, IT, IE (voluntary model), NL and SK]. The remaining 18 MS have general disclosure requirements embedded in their law.
- **Projections:** some Member States require a projection of future entitlements (compulsory annually only in 8), however only one requires the provision of different scenarios on the PBS (AT).
- **Costs:** while in many jurisdictions general information on costs is required in the documents for members, it is rarely required to present the information broken down per types of costs.
- **Pension communication:** only two MSs have so far developed guidelines on how information should be communicated (BE, NL).
- **Legal gap:** internal analysis showed that there is a gap between the current national legislation

and the upcoming IORP II Directive concerning the PBS. In this regard, a majority of Member States will need to catch-up with the new requirements concerning costs and projections.

EIOPA staff analysis has highlighted the current, pre-IORP II divergence of approaches as regards to the use of a standardised template, with examples found from existing templates at national level. In view of IORP II implementation, a significant number of Member States are taking steps towards the practical transposition of the PBS, including considerations to develop a template.

For the purpose of this work, it seems logical to undertake an exchange of current practices with regard to the format and the content of the PBS and to analyse which solutions are used at national level for approaching the main challenges. The outcome should help draw conclusions from the existing practices and propose principle-based guidance to tackle key aspects in the areas of pension communication, pension projection and cost breakdown.

## OBJECTIVE

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The main objectives are to:

- Facilitate the implementation of the new information requirements under IORP II with the objective to promote consistent practices.
- Promote the exchange of practices under IORP I, drawing conclusions from the members' insights and knowledge, including their experience with national consumer testing.
- Building on the "Max" Report, to consider the latest research on behavioural economics applied to pension information, both on paper and with digital means.
- Develop principle-based guidance to national authorities for the design of the PBS, with a focus on pension communication, pension projection and cost breakdown.
- Building on the PBS work, develop principle-based guidance to national authorities for the design of other (non-regular) information documents, with focus on pension communication, ESG factors and past performance disclosures.

In addition, and in view of the mobility of workers within Member States and at EU level, consumers should be able to compare PBS information gathered from several employers.

<sup>(28)</sup> Article 36 (2)

<sup>(29)</sup> Article 38

<sup>(30)</sup> Together with the Occupational Pension Committee (OPC) and the Committee on Consumer Protection and Financial Innovation (CCPFI)

These objectives are consistent with the following objectives of the IORP II Directive: <sup>(3)</sup>

- ensuring a high level of protection and security for members and beneficiaries of occupational pension schemes;
- ensuring a higher level of transparency of retirement provisioning and informed personal financial and retirement planning; and
- facilitating further the mobility of workers between Member States.

In particular, they are consistent with Recital (66) of the IORP II Directive, which provides the following: “For members, IORPs should draw up a Pension Benefit Statement containing key personal and generic information about the pension scheme. The Pension Benefit Statement should be clear and comprehensive and should contain relevant and appropriate information to facilitate the understanding of pension entitlements over time and across schemes and serve labour mobility.”

These objectives are also connected with EIOPA tasks to contribute to the consistent, efficient and effective application of the EU legal framework for IORPs and to foster the protection of pension scheme members and beneficiaries.

### POLICY OPTIONS

From a regulatory perspective, the following options have been considered with respect to the implementation of IORP II Directive regarding the PBS:

- Option 1: Exchange of practices regarding PBS at Members States' initiative,
- Option 2: Developing guidelines/recommendations,
- Option 3: Identification of current practices and extraction of key principles

These three options with the related pros and cons for each of the affected parties (IORPs, IORP members and NCAs) are analysed below.

#### Option 1: Exchange of practices regarding PBS at Members States' initiative

Under this option, Member States would exchange - at own initiative - those national practices with regard to the format and the content of the PBS that they deemed “best practices”. If EIOPA were not to organise a coordi-

nated exchange of views prior to the implementation of IORP II and assessment of content and form of the PBS among NCAs with publication of results:

	Benefits	Costs
IORPs	No relevant benefits are identified	Limited possibility that requirements implemented are based on identified current good/best practices from other Member States.
IORP members	No relevant benefits are identified	Limited possibility that requirements implemented are based on current good practices from other Member States, which are consumer-friendly and take a behavioural approach.
NCAs	No relevant benefits are identified	Limited exchange and identification of good/best practices of NCAs.

<sup>(3)</sup> See Recitals 2, 4 and 11 of the IORP II Directive.

**Option 2: Developing guidelines/recommendations**

Under this option, EIOPA would use the regulatory powers in Article 16 of the Authority’s Regulation issuing guidance (guidelines/recommendations addressed to national com-

petent authorities or IORPs) on the form and content of the PBS in order to ensure the common, uniform and consistent application of the requirements in IORP II Directive.

	Benefits	Costs
IORPs	<p>More certainty on PBS content and form</p> <p>Favourable for the cross-border IORPs and possibility to use the PBSs for the track and trace your pension in Europe (TTYPE) project in the future.</p>	<p>Compliance costs</p> <p>Careful attention would need to be given for considering the national specificities</p>
IORP members	<p>More consistent and comparable PBSs across Member States, which favours labour mobility and facilitates understanding of aggregated IORP retirement income from different member states.</p>	<p>Careful attention would need to be given for considering the national specificities</p>
NCA	<p>Stronger supervisory convergence</p>	<p>Compliance costs</p> <p>Careful attention would need to be given for considering the national specificities</p>

**Option 3: Identification of practices and extraction of key principles**

Under this option, EIOPA coordinates the exchange of views and assessment of content and form of the PBS among NCAs, with a publication of results in the form of

a report, which analyses and identifies the current practices and extracts key principles and high-level guidance to inspire the content and form of the PBS:

	Benefits	Costs
IORPs	<p>Increased possibility that requirements implemented are based on current practices from other Member States.</p>	<p>No relevant costs are identified</p>
IORP members	<p>Increased possibility that requirements implemented are based on current practices from other Member States, which are consumer-friendly and take a behavioural approach.</p>	<p>No relevant costs are identified</p>
NCA	<p>Proportionality of the tool, as it provides help and facilitates in a cost-efficient way the exchange of views that Member States are required to conduct.</p> <p>EIOPA to facilitate the joint analysis and identification of key principles.</p> <p>Use of existing know how from other Member States for an optimal implementation of the IORP II requirements, with lower budget and resources implications than if research conducted by each NCA individually.</p>	<p>No relevant costs are identified</p> <p>The necessity of sharing practices arise from the Level 1 provisions in IORP II.</p>

The option that has more advantages and represents a proportionate approach is Nr. 3, namely to identify current practices and to extract principles and guidance for the content and form of the PBS.

One of the conclusions of this Report is that consumer testing of the PBS proposals and other possible combinations of layering and layout tools are recommended to understand, from an empirical perspective, if the PBS fulfils its purpose.

As a follow-up to the Report, EIOPA envisages to develop indicative PBS designs in collaboration with communication experts and professional designers to explore the effectiveness of both, the behavioural approach and the combination of different layering and layout tools in the PBS. A number of such indicative PBS designs could be tested among industry participants and IORP members. A cost efficient way of triggering relevant and valuable feedback on the designs would be through a public consultation/survey.



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