OPSG

OCCUPATIONAL PENSIONS STAKEHOLDER GROUP

Draft Opinion on the supervisory reporting of costs and charges of Institutions for Occupational Retirement Provision (IORPs)

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EIOPA Consultation Paper, new deadline: 27 July 2021
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OPSG Opinion

INTRODUCTION

(cf. CP, p. 4):

This consultation paper sets out the draft Opinion on the supervisory reporting of costs and charges of Institutions for Occupational Retirement Provision (IORPs).

Considering that a transparent and comprehensive view of all costs and charges is essential for IORPs, social partners and supervisors to assess the efficiency, value for money and affordability of occupational pension schemes, the Opinion sets out expectations on the supervisory reporting of costs and charges of IORPs, using a proportional and risk-based approach.

The Opinion provides a generic classification of all costs to be reported to national supervisors, including templates, both for supervisors to collect cost information from IORPs and to assist IORPs to collect cost information from investment managers. Moreover, principles are provided for the compilation of the cost information. Most notably the look-through principle, meaning that not only direct investment costs have to be included but also indirect costs at the level of investment managers – they should practicably be assessable for the IORP without any undue additional costs.

The Opinion also provides guidance on the supervisory use of the cost data. National supervisors are expected to assess the efficiency of IORPs, affordability for sponsors and the value for money offered to members and beneficiaries, not considering the costs in isolation, but in conjunction with risk and return characteristics and other individual partially qualitative criteria (e.g. possible alignment of interests, if performance dependant fee schedules are successful). The results of such exercises should feed into the supervisory review process and the regular dialogue with the IORPs' management boards.

EIOPA QUESTIONS TO STAKEHOLDERS:

Q1: Do you agree with the objective of implementing a transparent and comprehensive cost reporting for supervisory purposes? Please explain.

OPSG comment:

We agree. At the European level the IORPs II Directive introduced structural cost disclosure requirements for IORPs, both towards prospective and actual scheme members. Nonetheless, the directive 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.

Therefore this data collection of costs and charges is strongly necessary, as – in EIOPA's Questionnaire of 2020 (cf. Annex 4 of CP) and in the 2015 report on costs and charges of IORPs - EIOPA found that there is a lack of detailed information and practical experience to obtain details on costs and charges in a number of Member States. In consequence, it proved not to be possible at that time to fulfil the original goal of the project to develop common definitions and breakdowns of costs and charges. But this original goal has to be achieved, because EIOPA has to include IORPs in its annual report on "Costs and Past Performances" requested by the Commission.
Some OPSG members additionally stress that IORPs in different member states are investing into different asset classes leading to the fact that a certain breakdown of costs will not work for all asset classes. This should usually be no problem regarding fund investments but with regard to (non-fund-based) direct investments e.g. into real estate or German registered bonds this will simply not work for technical reasons.

The objective of implementing a transparent and comprehensive cost reporting for supervisory purposes is based on the Decision of the Board of Supervisors on EIOPA's regular information requests toward NCAs regarding provision of occupational pensions information of 2 June 2020 (EIOPA BoS 20-362), which again is based on the former Decision of EIOPA's BoS 18-114. The template "Expenses" (PF.05.03.24) outlines the following items: administrative, investment, tax, other and total expenses.

Additionally the European Securities and Markets Authority (ESMA), the EU's securities markets regulator, has identified costs and performance for retail investment products and market data quality as the Union Strategic Supervisory Priorities for national competent authorities (cf. ESMA PR of 13 November 2020). Some OPSG members add that occupational pensions in many cases cannot be equated with retail products, especially when there are compulsory memberships, no choice options for beneficiaries etc.

Q2: Do you agree that Annex 1 provides a balanced view of the costs and benefits of the draft Opinion? Please explain and provide any suggestions.

OPSG comment:

Some OPSG members agree. EIOPA correctly stresses that "as institutional clients, IORPs should be able to request to service providers the itemised cost disclosure under MiFID II to collect detailed data on investment and transaction costs and report it accordingly to the NCA." Therefore, option 3 as pointed out by EIOPA, seems to be adequate: "Development of reporting templates for IORPs to report data to the CAs, according to principles, as well as templates for IORPs to collect data from service providers." There is no contradiction between granularity and flexibility, if the principle of proportionality for SMEs will be applied appropriately.

Other members do not agree stressing that MiFID II is a reporting standard, which is quite suitable for fund-based investment products. However, in some European countries not only funds are used for investments covering occupational pensions. For certain other forms of investments the MiFID II standard definitely does and will not work. So, if this standard will be used for occupational pensions cost reporting, we would have to limit this to fund-based investment, where this standard works.

Q3: Do you agree with the generic cost classification distinguishing investment, transaction and administration costs as well as costs borne by the sponsor? Please explain and provide any alternative classification that should be considered.

OPSG comment:

Some OPSG members agree that the section 3.2 in the consultation paper provides very detailed and logical classification of costs. They believe that the suggested cost-classification and the presented reporting templates for the industry would be a good starting point. They agree that there should be also a distinction between direct investment charges and "bundled" investment / administration charges, i.e. insured schemes. What is important is to be able to have a clear view of all the costs paid by the sponsor and paid by the IORP, as long as producing this information does not generate disproportionate additional costs.

But this generic classification should be complemented by giving distribution costs a separate disclosure (cf. our comment on Q4). There are many IORPs which offer their services on the free market of occupational and private retirement provision (and not only to a clearly fixed number of sponsors), and in consequence they have to calculate distribution costs. That is why for classification and definitions we refer to EIOPA's 2021 Report on Costs and Past Performances (administration / distribution costs: box 5, p. 36/37, and definitions of one-off and ongoing costs, p. 57/58) as well as to EIOPA's 2020 Report on Costs and Past Performances on "Cost Mapping" (Annex II, p. 37).

There must not be any hidden costs. Transparency on the fees could be a lever in order to be able to put pressure to reduce them, and therefore lower costs could possibly lead to an increase in accumulation of contributions in a CD context or increased benefits in a DB context. As it is clearly stated in the paper, annual charges of 1% of assets during 40 years of service will reduce, as a rule of thumb, pension benefits with some 20%. Therefore, the cost transparency is vital for well-being of society in long term perspective. Considering the latest Ageing and Poverty reports we believe that all mechanisms should be used to ensure reasonable pension benefits after retirement.

Other OPSG members disagree to the proposal that costs borne by sponsors should be included, because – under certain conditions (cf. explanations below) - they do not have any influence the future pension result of the beneficiaries. Including such costs would also often not contribute to a higher degree of comparability and would often tell us nothing about the IORP´s efficiency and/or the affordability of the IORP for sponsors.

First, if an IORP has a sponsor company, to which a big part of its pension products can be assigned, and beside that only few sponsor companies having a relatively small share on the IORP´s pension products, it is sometimes the case, that this "majority" sponsor companies pays certain costs. So, in such a case, strictly speaking, the cost level for different sponsor companies might be different. Often sponsor companies have also certain information requirements with regard to an IORP – and are willing to pay for that. In such a situation the cost level is influenced by these sponsor companies themselves and it would be misleading to compare the cost structure (including such costs paid by the sponsors) of that IORP with the cost structure of another IORP having sponsors with much less information requirements resulting in lower administrative costs. Also the argument, that reporting of these cost blocks may give additional insight with regard to the question, if – especially in the situation of a crisis – a sponsor company can still afford the pensions provided by this IORP, has to be questioned, because experience tells, that the size of such administrative costs is usually quite irrelevant for the respective employer. This aspect has already been treated in the OPSG position paper regarding DC risk assessment earlier this year.

Q4: In your view, do the definitions in Annex 2 cover the most important items of investment, transaction and administrative costs? Please explain and provide any suggestions for the inclusion of other cost elements not explicitly mentioned in the definition.

OPSG comment:

We only partially agree to the cost categories mentioned in this annex, but following to our comment on Q3 the category of administration costs should be renamed as "administration and distribution costs". Furthermore, transaction costs are not always possible to quantify (as there may be hidden elements) for all asset classes – especially if it comes to bid-offer-spreads.

Q5: Do you agree that all costs should be reported as nominal amounts in the reporting currency and as a percentage of average assets under management? Please explain.

OPSG comment:

Some OPSG members only agree upon the nominal amounts, but not upon the percentage of average assets under management. No matter if a saver uses a private or an occupational pension product, from beneficiary's perspective the contributions having been paid are always the most important parameter of reference. All costs are deducted from these "gross premiums" or "gross contributions".

That is why there should be consistency with the PEPP regulation as much as possible. The PEPP level 2 regulation (EU/2021/473) of 18 December 2020 stipulated the "Methodology for the calculation of costs, including the specification of summary indicators" (Annex III., Part III., No. 30): "In the PEPP Benefit Statement, the PEPP provider shall present the estimated impact of costs on the final PEPP benefits by using the 'Reduction in Wealth' approach. The 'Reduction in Wealth' shall be calculated as the difference between the projected accumulated savings at the end of the accumulation and the projected accumulated savings at the end of the accumulation period in a cost free scenario. The difference shall be disclosed in monetary and percentage terms relative to the projected accumulated savings." For reasons of understandability and comparability providers of occupational and private pension products should use the same methodology with regard to the calculation of costs.

While agreeing on the use of the same methodology to calculate costs for comparability, other members disagree on the point of consistency with PEPP regulation as much as possible. PEPPs are personal pension products regulated by an own framework, which is different from the IORP2 directive, it has relevant implications on the methodologies for costs computations which, for IORPs, are defined at national level. Furthermore, the PEPP regulation states that the product is an individual non occupational pension product and that it should not affect occupational pension schemes and products. It may be worthwhile to highlight that even if an IORPs may apply for registration of a PEPP, it is only possible if they are authorised and supervised to provide also personal pension products at national level and all assets and liabilities corresponding to PEPP provision business shall be ring-fenced, without any possibility to transfer them to the other retirement provision business of the institution. The ring-fencing is deemed necessary given the differences between IORPs and PEPPs, both in terms of purpose and management. The methodologies defined for PEPP costs does not fit for IORPs.

Other OPSG members stress that in certain cases it is right to report costs as percentage of AUM. The reporting of the costs as a percentage of average assets under management (basically costs related to the investment of the assets) should be assessed considering the landscape of IORPs at national level. If, for supervisory purpose, it is wise to assess costs with this metric it has to be done, otherwise it may not be relevant.

Additionally OPSG members stress that costs are to cover expenses, so it is good the administrative costs to be reported as nominal amounts per member / beneficiary. That will enable a comparison with the nominal costs. For investment related costs, we would suggest to report them both as a nominal amount and as a percentage of Assets under management. Therefore, we consider Table 2 from Annex 2 as a good starting point for reporting. It could be the case that for some of the costs only one of the values is reasonable (nominal amount or relative as a percentage). There will be issues with non-unitised funds (such as legacy with-profit funds or segregated funds) as fees are not expressed as a percentage of assets under management.

Q6: Do you agree that the cost reporting should also be at the level of the schemes/investment options where IORPs provide multiple schemes / investment options with different investment policies? Please explain and provide any benefits of or obstacles to report costs at the level of pension schemes or investment options.

OPSG comment:

Yes, we fully agree (cf. CP, no. 3.8, p. 9).

Q7: Do you agree with the principles for the compilation of information on costs and charges:

- look-through and no netting;

- costs paid directly by the sponsor;

- matching;

- taxation;

- reporting currency;

- estimations;

- proportionality?

Please explain and provide any suggestions to improve the principles.

OPSG comment:

Yes, we agree (cf. CP, no. 3.9, p. 10-11). Except for costs directly paid by the sponsors they should be excluded as argued before under question Q3. Nevertheless with regard to the application of the principle of proportionality EIOPA should clearly specify from which quantitative thresholds (mainly asset allocation, number of members and beneficiaries) NCAs may allow smaller IORPs to “soften” these principles for compiling cost information.

Q8: Do you agree that the possibility under MiFID II to request investment and transaction cost data from portfolio managers and transaction counterparts will facilitate the supervisory cost reporting by IORPs? Please explain and describe any limitations observed with MiFID II disclosure requirements in practice.

OPSG comment:

Yes, we agree since MiFID II is a reasonable reporting standard mainly for fund-based investments (cf. CP, no. 3.11 and 3.13, pages 11-12).

Q9: Are you aware of other cost classifications used by IORPs to collect information on costs and charges from portfolio managers and transaction counterparts? If yes, please describe and explain these other cost classifications.

OPSG comment:

No, not at a European level. Of course German and Italian IORPs e.g. have to provide a certain break-down of costs according to national laws within their annual financial statement – of course on the level of the IORP.

We urge EIOPA to take into consideration its own definition of "Investment Management Costs" outlined in its 2021 Report on Costs and Past Performances (Box 5: "Drivers of costs in the IBIPs markets", p. 38): "Costs item that can be categorized as investment management are: transaction related costs, payment of investment service. For unit-linked and hybrid products there can also be: costs due to the unit valuation and fund accounting services, fund related governance, regulation and compliance costs, fund related property management and headcount costs, performance fees, carried interest."

Q10: Does in your view the investment cost template in Annex 3 facilitate the collection of costs by IORPs from portfolio managers? Do you agree that the more detailed breakdown of costs enhances the understanding of IORPs in the underlying investment cost structure? Please explain and provide any suggestions to enhance the practicality and insightfulness of the template.

OPSG comment:

We only partially agree (cf. no. 3.13 of CP). However, the extra costs which IORPs would have to pay in order to receive such a breakdown from their investment providers should be limited to a reasonable extent, because such extra costs would have to be paid in the end by beneficiaries and/or sponsor companies (which both would not strengthen occupational pensions in Europe). So, we propose, that EIOPA enters into a dialogue with the investment industry (their respective European associations) and assesses if this can be done without charging additional costs to the IORPs or – if not – to what extent such additional costs might be.

Q11: Do you agree that supervisors should have discretion to determine the level of cost reporting requirements for DB IORPs under paragraph 3.14 to ensure an approach that is proportionate to the objectives? If yes, in what way:
- reduced scope of costs reporting (e.g. only investment, transaction, administrative costs),
- lower frequency of reporting,
- full exemption for certain DB IORPs,
- other.
Please explain.
OPSG comment:
No, we do not agree upon any full exemption for certain DB IORPs. Only in a very particular general market situation like in spring 2020 due to the pandemic there may be allowed a lower frequency of reporting. The crucial risk of beneficiaries' detriment by overly calculated costs is too high ("value for money" from consumer protection perspective, cf. CP no. 4.1c, p. 14). EIOPA itself has stated: "The impact of costs can be very significant. Pension pots can end up much smaller than expected because investments carried higher costs than expected." (CP, p. 17)
However, we definitely urge EIOPA in the context of proportionality to think about simplifications for non-for-profit IORPs (i.e. IORPs not having any third party equity holders or something comparable) when there is compulsory membership and beneficiaries do not have any investment options. In these cases there will be no detriment for beneficiaries resulting out of simplifications. As said before, that does not mean, that such IORPs should not report on costs at all, but the scope indeed should be reduced in the manner proposed in this question and no further granularity should be provided since this would not deliver any additional value.

Q12: Do you agree that supervisors should conduct comparative analysis of IORPs' cost levels to assess efficiency, affordability and value for money offered to members and beneficiaries? Please explain and provide any suggestions for such analysis.
OPSG comment:
Yes, we agree (cf. no. 4.2 and 4.3 of CP).
One example on the national level: on 26 February 2021 the *German Actuarial Association (DAV)* published a study justifying the forthcoming reduction of the guaranteed minimum interest rate for life-insurers and IORPs by the legislator. It argued that - under the ongoing conditions of low or zero interest rates - strongly reduced or even no guarantees could increase the return of long-term pension plans. Only by reducing or completely abolishing the capital guarantees the returns will be high enough to cover the costs.

These conclusions were criticized by the *German Association of Insured (BdV)* by stressing that first the costs of distribution, of administration and of investment have substantially to be reduced by the product providers (public position paper of 31 March 2021 on website). Nevertheless the legislator followed the proposals of the actuaries: now the highest level of interest rates guaranteed for the entire contract duration by life-insurers and IORPs (under the Solvency II-regime) is at 0,25%.

This controversy between actuaries (DAV) and consumerists (BdV) clearly emphasizes how important is the issue of "value for money" particularly with regard to long-term savings under the general extremely challenging economic conditions of ongoing low-interest rates, increasing inflation, volatile stock markets, pension plans with defined benefits / minimum guarantees and the additional impact of costs on the real returns for the beneficiaries.

In Italy, the national supervisor Covip, displays, on a yearly basis, the costs of the supplementary pension schemes, both IORPs and Personal Pension Products (Comparatore dei costi delle forme pensionistiche complementari – Comparator of the costs of supplementary pension schemes - https://www.covip.it/isc_dinamico/).
The comparison is a useful tool for members in a market where IORPs and Personal Pension Products share almost the same legislative and regulatory framework). The tables report the values of the "Indicatore sintetico dei costi" (Synthetic cost index, based on assumptions determined by Covip), for each investment option offered to members. There is also a graphical representation of the average costs, for type of pension scheme (closed, open, insurance contracts) and for category of investment option.
The assessment of the cost is associated with a similar tool for net returns (Elenco dei rendimenti dei Fondi pensione – List of the return of supplementary pension schemes https://www.covip.it/per-gli-operatori/fondi-pensione/costi-e-rendimenti-dei-fondi-pensione/elenco-dei-rendimenti), to show both sides of the coin: costs and returns.

It is agreed that costs are by far not the only dimension used for comparison between IORPs. There may be an IORP having higher costs but providing in the long run a better quality for the beneficiaries (better long-term investment returns, better service level, better guaranteed benefits etc.). So just "cheering the cheapest" is an approach, supervisory authorities should definitely not follow.

Q13: Do you agree that supervisors should be encouraged to publish aggregated cost levels and the results of the comparative cost analyses and that they should encourage IORPs to publicly disclose their cost levels? Please explain.
OPSG comment:
Yes, we fully agree.
In an EU member state like Germany IORPs represent only a rather small market share of occupational and private pension plans. Following to the 2019 figures of the Association of German Insurers (GDV) and the Federal Ministry of

Labour and Social Affairs (BMAS) the two types of IORPs (“Pensionskassen / Pensionsfonds”) represent only about a quarter of all five existing occupational pension vehicles (about 4,2 million contracts out of 16,25 million contracts). Besides these occupational pension plans there are about 18 million contracts of state subsidized private pension plans (about 16 million “Riester” contracts and 2 million “Rürup” contracts) and more than 20 million private annuities. These figures show that IORPs are in a very strong competition with all providers of pension products or long-term savings, and in consequence from consumers perspective comparability of costs constitutes a fundamental and crucial element for any “informed decision making” by retail customers.
Source:
https://www.gdv.de/de/themen/news/betriebliche-altersversorgung-weiter-auf-wachstumskurs-60730

For Italy, please refer to the previous answer.

However, some OPSG members explicitly feel differently. They of course support the idea, that all IORPs should publish their total cost level in a way that beneficiaries can easily see, what value they are getting for their money. However, this can comprise only costs being carried by the beneficiaries – and not such being carried by the employers. A granular breakdown should also not be published in cases, where there are compulsory memberships and no investment options to be chosen by the beneficiaries, since this offers no advantage for the beneficiaries in these cases.

Other OPSG members think that information of the costs, also when they are carried by the employers, is important to have. Other employers will pay higher contributions if the costs are paid in full by the IORP. Also for the members /beneficiaries it is important to be aware that the employer is still paying a substantial part of the costs, so they can value this commitment as it keeps the contributions to the IORP lower than otherwise would be the case. When there is no choice for members/beneficiaries they need to get at least transparency regarding all aspects of the scheme including costs.

Q14: Do you have any other comments on the draft Opinion? If yes, please provide these other comments.
OPSG comment:
We support EIOPA’s approach of introducing the new concept of “Value for Money” for the supervision of cost reporting:

> *“EIOPA considers that products offer value for money where the costs and charges are proportionate to the benefits (i.e., investment performance, guarantees, coverage and services) to the identified target market and reasonable taking into account the expenses born by providers and in comparison to other comparable retail solutions on the market*.” (cf.

EIOPA consultation paper on the framework to address value for money risk in the European unit-linked market, 13 April 2021, no. 1.7, p. 18).

Therefore the concept of “Value for Money” is ready to be applied to all categories of life-insurances / insurance-based investment products and pension plans (occupational and private ones). The EU-wide harmonized and reliable cost reporting of IORPs constitutes the crucial basis of transparent comparability and understandability of pension data not only for supervisors but for retail investors, policyholders, long-term pension savers and beneficiaries.

Nevertheless, some OPSG members stress that any additional reporting requirement for IORPs must be doable for the IORPs without triggering inadequate additional costs and must have a proven advantage for supervisory authorities and/or beneficiaries. So, the OPSG recommends before introducing new requirements, that a thorough cost-benefit-analysis and a feasibility study is done by EIOPA. It also should be taken into account, that some IORPs use certain individually negotiated fee schedules for external managers, which are not based on fixed annual fees. One example is a fee schedule, which pays fees which depend on the performance achieved. This aligns the interests of the beneficiaries, the IORP and the respective external manager. Simply comparing fees paid in a given year, where very good performance could be achieved and hence relatively high amounts of performance-based fees have been paid would lead to totally wrong conclusions. So, any cost analysis must allow for such individual fee schedules and take them into account appropriately.