

<b>Comments Template on EIOPA-CP-11/001</b> <b>Draft response to Call for Advice on the review of Directive 2003/41/EC</b> <i>Scope, cross-border activity, prudential regulation and governance</i>		<b>Deadline</b> <b>15.08.2011</b> <b>18:00 CET</b>
Company name:	<b>NATIONAL ASSOCIATION OF PENSION FUNDS</b>  Cheapside House 138 Cheapside London UNITED KINGDOM  <i>Contact:</i> James Walsh Senior Policy Adviser, workplace pensions <a href="mailto:james.walsh@napf.co.uk">james.walsh@napf.co.uk</a> <a href="http://www.napf.co.uk">www.napf.co.uk</a>	
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Please follow the instructions for filling in the template: <ul style="list-style-type: none"> <li>⇒ <b>Do not change the numbering</b> in column "Reference".</li> <li>⇒ Please fill in your comment in the relevant row. If you have <u>no comment</u> on a question, keep the row <u>empty</u>.</li> <li>⇒ Our IT tool does not allow processing of comments which do not refer to the specific question numbers below.               <ul style="list-style-type: none"> <li>○ If your comment refers to multiple questions, please insert your comment at the first relevant question and mention in your comment to which other questions this also</li> </ul> </li> </ul>		

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- applies.
- o If your comment refers to parts of a question, please indicate this in the comment itself.

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The question numbers below correspond to Consultation Paper No. 01 (EIOPA-CP-11/01).

Reference	Comment
General Comment	<p><b>About the NAPF</b></p> <p>The National Association of Pension Funds is the UK’s leading voice for workplace pensions. Our members operate 1,200 pension schemes. They provide retirement income for nearly 15 million people and have almost €950 billion of assets under management. Our membership also includes over 400 providers of essential advice and services to the pensions sector. This includes accounting firms, solicitors, fund managers, consultants and actuaries.</p> <p>The NAPF is also a founder member of the European Federation for Retirement Provision (EFRP).</p> <p><b>Scrutiny of the case for a new Directive</b></p> <p>The NAPF urges EIOPA to start its response with a rigorous examination of the Commission’s assumption that a new version of the IORP Directive is needed.</p> <p>The Commission’s case for reform is based on what it sees as the slow growth of cross-border pension schemes. Yet EIOPA’s own research, published on 14<sup>th</sup> July, shows that the total number of cross-border pension schemes increased from 78 to 84 in the past year – an 8 per cent increase.<sup>1</sup></p>

<sup>1</sup> 2011 Report on Market Developments, EIOPA, 14<sup>th</sup> July 2011, para 2.1

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Although the overall number of cross-border schemes is still modest, an 8 per cent growth rate is good progress at a time of sluggish economic activity. EIOPA's response should draw attention to these figures and point out that, if such progress is being achieved, there really is no case for a new IORP Directive.

EIOPA's response should also challenge the EC's assumption that the current form of the IORP Directive is one of the reasons for the low number of cross-border schemes. Far more rigorous analysis and evidence is required if this point is to be used as justification for new legislation. EIOPA should point out that there are far more significant barriers to cross-border pension provision, such as differences between Member States' tax regimes.

**No default acceptance of Solvency II**

The NAPF recognises that EIOPA is obliged to answer the questions put to it by the European Commission's *Call for Advice*. On most points, those questions seek EIOPA's advice on how sections of the Solvency II Directive could be adapted for pensions.

The NAPF urges EIOPA to ensure that its response subjects this Solvency II-based approach to rigorous scrutiny.

Although the NAPF shares many of the Commission's objectives – particularly greater security for members' pension benefits, we do not accept that Solvency II provides the right starting point for this work, and EIOPA's response should reflect this. We recommend that EIOPA puts the following points to the Commission.

- Pensions are fundamentally different from insurance. Unlike insurance products, pensions are paid over the long term in a relatively predictable manner. So it is be wrong to assume that a

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	<p>regulatory framework designed for insurance should apply to pensions.</p> <ul style="list-style-type: none"> <li>• There are very diverse systems and traditions of pension provision across EU Member States. Designing a more harmonised regulatory system would not only be almost impossible, it would also be undesirable and costly. These extra costs would be passed to members.</li> <li>• Policy-makers should recognise that workplace pension funds have weathered the financial storm well and have proved to be resilient. Security should not be seen as being synonymous only with solvency; governance also has a crucial role to play.</li> <li>• It would be inappropriate to apply a Solvency II-style regime to pension funds in the UK, where members' benefits are already strongly protected by the employer covenant, by the work of the Pension Regulator and by the Pension Protection Fund.</li> <li>• It is important to recognise that introducing an extra solvency buffer for pension schemes – in addition to existing funding requirements – would inevitably force more employers to reduce or cease providing pension benefits to their employees, resulting in less generous benefits for scheme members and creating a pensions system in which members have a greater exposure to risks. So although a Solvency II-style regime might – in theory at least – strengthen <i>security</i>, it would undermine <i>adequacy</i> – contrary to the Commission's objectives as set out in the July 2010 Green Paper <i>Towards Adequate, Sustainable and Safe European Pensions Systems</i>.</li> </ul>	
1.	<p><b>SCOPE</b></p> <p><b>Do stakeholders agree with the analysis of the options (including the positive and negative</b></p>	

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	<p><b>impacts) as laid out in this advice? Are there any other impacts that should be considered?</b></p> <p>EIOPA has identified the full range of options for the future scope of the IORP Directive..</p> <p>We recognise that the pensions landscape has changed in at least two important respects – the growth of DC pensions and the advent of funded occupational pension provision in the Central and Eastern European member States.</p> <p>However, these changes do not automatically mean that a new Directive is required, so Option 1 (leave the Directive unchanged) must remain on the table.</p> <p>EIOPA should also advise the Commssion to ensure that its policy-making is correctly sequenced. The first task – and one that should be completed before any changes to the scope of the IORP Directive – is for DG Employment to finish its review of Regulation 883/2004, which has a major impact on which schemes are defined as social security schemes.</p>	
2.	<p><b>Are there any other options that should be considered? Please provide details including where possible in respect of impact.</b></p> <p>No – NAPF sees no further options that should be considered.</p>	
3.	<p><b>Which option is preferable?</b></p> <p>The NAPF supports Option 1 – leave the IORP Directive unchanged.</p> <p>However, we recognise that there are issues – particularly the position of the pension schemes in the Eastern European countries – that need to be addressed. We would propose two steps:</p>	

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	<p>First, EIOPA or the EC should draw up a clear classification of the different types of pension scheme across the EU. This would provide a stronger foundation for future policy-making.</p> <p>Second, in order to address one of the key challenges for the Eastern European schemes, their national regulators should adopt and apply a high-level framework of governance standards. This would strengthen the independence of these schemes and would improve operation and oversight.</p>	
4.	<p><b>How should it be determined whether a compulsory employment-related pension scheme is to be considered as a social-security scheme covered by Regulations (EEC) No 883/2004 and (EEC) No 987/2009 (see Art. 3)?</b></p>	
5.	<p><b>DEFINITION OF CROSS-BORDER ACTIVITY</b></p> <p><b>Do stakeholders agree with the analysis of the options (including the positive and negative impacts) as laid out in this advice?</b></p> <p>EIOPA's response should start by urging the EC to identify clear evidence of where the definition has obstructed cross-border pension provision.</p> <p>The response should also point out that the real barriers to cross-border pensions lie in tax and social security systems, not in pensions legislation. Furthermore, the low number of cross-border schemes does not reflect inadequate legislation; it reflects a lack of demand. Most occupational pension</p>	

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	<p>schemes have no ambition to provide pensions in other Member States.</p> <p>The EC should first conduct research to establish the <i>potential</i> number of cross-border schemes, based on the number of truly multi-national companies operating across the Internal Market. This work should recognise that many multi-nationals also operate beyond the borders of the EU.</p>	
6.	<p><b>Are there any other options that should be considered?</b></p> <p>The proposed new definition of cross-border pension schemes might not encompass DC schemes entirely, as in DC schemes the relation between the sponsor and the IORP may be mediated by the trust. Therefore, we suggest amending Article 6 (c) and (j) as follows:</p> <ul style="list-style-type: none"> <li>• 6 (c) “sponsoring undertaking” means any undertaking or body, regardless of whether it includes or consists of one or more legal or natural persons, which acts as employer or in a self-employed capacity or any combination thereof and which <u>has a direct agreement with either the institution or the members and pays contributions into or supports an institution for occupational retirement provision.</u></li> <li>• 6 (j) “host member state” means the Member <u>State where the sponsoring undertaking is located.</u></li> </ul>	
7.	<p><b>Do you agree with EIOPA that option 2 is preferable?</b></p> <p>Yes</p>	
8.	<p><b>Even with defining the sponsoring undertaking, problems of overlapping or contradicting</b></p>	

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	<p><b>regulation between member states could emerge. Should the revised Directive include procedures to settle such problems between the Home and the Host member states and/or also between the Home member state and the member state of the applicable social and labour law?</b></p> <p>It is impossible for the Directive to anticipate all the circumstances that could give rise to uncertainty over the regulation of cross-border schemes, so the system needs to be flexible. EIOPA should recommend that the maximum use is made of liaison between Member States' supervisory authorities in order to resolve such issues.</p> <p>EIOPA should advise that incomplete definition should not be a reason to stop cross-border activity, as this would be against the spirit and the main purpose of the Directive 2003/41/EC. Therefore, we suggest that setting clear and practicable legal conditions for cross-border operation of IORPs, in cases which are not entirely ruled out by the IORP Directive, should be the main objective of co-operation between national supervisors, within the institutional framework of the European System of Financial Supervision.</p>	
9.	<p><b>PRUDENTIAL REGULATION AND SOCIAL AND LABOUR LAW</b></p> <p><b>Do stakeholders agree with the analysis of the options (including the positive and negative impacts) as laid out in this advice?</b></p> <p>The NAPF acknowledges that there may be a case for a clearer distinction between prudential regulation and social / labour law, in order to clarify the boundaries of each regulator's activities. But this should not be allowed to generate extra regulatory burdens.</p>	



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	<p>In the interests of evidence-based policy-making, EIOPA should ask the EC to demonstrate that there is a demand or need for a change in the law in this area. EIOPA should also press the EC to show how a change in the law would strengthen cross-border pension provision.</p>	
10.	<p><b>Are there any other options that should be considered?</b></p>	
11.	<p><b>Do you agree with EIOPA that option 2 is preferable?</b></p> <p>Yes.</p>	
12.	<p><b>Even with defining the scope of prudential regulation, problems of overlapping or contradicting regulation between member states could emerge. Should the revised Directive include procedure to settle such problems between the Home and the Host member states and/or also between the Home member state and the member state of the applicable social and labour law?</b></p> <p>The NAPF would support settlement procedures between Home State supervisors and any "third" Member State if and when problematic situations arise.</p> <p>It is important that these procedures should keep fully intact the principle of Home State control. We would not support colleges of supervisors as used in insurance supervision.</p>	

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13.	<p><b>GOVERNANCE</b></p> <p><b>What is the view of stakeholders on the proposed principles of the revised IORP Directive? How do stakeholders evaluate the positive and negative impacts of the introduction of proposed governance requirements?</b></p> <p>The NAPF agrees that the governance elements of Solvency II could reasonably be used as a basis for a new section of the IORP Directive.</p> <p>However, it will be essential for EIOPA to stress that this does not mean the same applies to the quantitative elements of Solvency II (Pillar I).</p> <p>Any new governance clause must allow for flexibility; the diversity of pension and governance systems at national level should be seen as a strength for the EU, not as a weakness.</p> <p>EIOPA should also point out that governance requirements must not impose burdensome requirements on IORPs. As EIOPA states at section 10.3.4, "A new supervisory system for IORPs shall not undermine the supply or the cost efficiency of occupational retirement provision in the EU"<sup>2</sup>.</p>	
14.	<p><b>FIT AND PROPER</b></p> <p><b>What is the view of the stakeholders on the proposed principles of the revised IORP Directive? How do stakeholders evaluate the positive and negative impacts of the introduction of proposed fit and proper requirements?</b></p>	

<sup>2</sup> EIOPA, Draft response to the Call for Advice on the Review of the Directive 2003/41/EC, EIOPA-CP-11/001, p. 43

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The NAPF disagrees with EIOPA's draft recommendation that the 'fit and proper' definition in Article 42 of Solvency II should be copied across into the IORP Directive.

Article 42's requirement for 'professional qualifications' fails to take account of the approach to governance in the UK, where lay trustees play a major – and very effective – role in ensuring that members' interests are well protected. The UK's Pensions Act 2004 requires trustees to have knowledge and understanding of the law relating to pensions and trusts and the principles of funding and investment. They are also expected to be familiar with the scheme's deed, rules and other documents.

Article 42 would also fail to recognise the effective contribution to good pension scheme governance made by the Myners Principles for Occupational Pension Schemes, first published in the UK in 2001, which set a widely respected benchmark for good governance. The first principle, on 'Effective decision-making', is as follows:

'Decisions should be taken only by persons or organisations with the skills, information and resources necessary to take them effectively. Where trustees elect to take investment decisions, they must have sufficient expertise and appropriate training to be able to evaluate critically any advice they take.

'Trustees should ensure that they have sufficient in-house staff to support them in their investment responsibilities. Trustees should also be paid, unless there are specific reasons to the contrary.

'It is good practice for trustee boards to have an investment sub-committee to provide the

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	<p>appropriate focus.</p> <p>'Trustees should assess whether they have the right set of skills, both individually and collectively, and the right structures and processes to carry out their role effectively. They should draw up a forward-looking business plan.</p> <p>'We recognise that it is important to ensure all trustees have the necessary skills and knowledge, and this is why the NAPF runs training courses for trustees and strongly supports the Pensions Regulator's requirements on Trustee Knowledge and Understanding (TKU).'</p>	
15.	<p><b>INTERNAL CONTROLS</b></p> <p><b>What is the view of the stakeholders on the proposed principles of the revised IORP Directive? How do stakeholders evaluate the positive and negative impacts of the introduction of a compliance function?</b></p> <p>The NAPF notes – and supports – EIOPA's comments (at 12.3.3 and 12.3.5) that Article 46 of Solvency II is not appropriate for IORPs. However, we are concerned that EIOPA does not carry this line of argument through into its formal advice to the EC (at section 12.4). It should do so.</p> <p>EIOPA should also note that the a new compliance requirement – in addition to existing requirements for internal controls - would weaken the cost-effectiveness of IORPs.</p> <p>Furthermore, in many IORPs, scheme members are represented in the governance structure of the IORP, which is a compliance check in itself. Scheme members and their representatives will always</p>	

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	<p>press the IORP's management to ensure that the IORP is compliant with the laws, regulations and administrative provisions as well as with the relevant social and labour law.</p> <p>If there must be a new compliance function, then it will be essential to exempt small schemes, as they do not have the resource or personnel to comply with Solvency II-style internal control requirements.</p>	
16.	<p><b>INTERNAL AUDIT</b></p> <p><b>What is the view of the stakeholders on the proposed principles of the revised IORP Directive? How do stakeholders evaluate the positive and negative impacts of the introduction of an internal audit function?</b></p> <p>The NAPF disagrees with EIOPA that the introduction of an internal audit function in the revised IORP Directive would be beneficial and would advise against transposing Art. 43 of Directive 2009/138 into IORP II.</p> <p>The requirement to set up and run an internal audit function would significantly increase costs without a corresponding increase in the security for scheme members.</p> <p>IORPs are already subject (article 10 of the IORP Directive) to the requirement to have their annual accounts and annual reports approved by authorised persons (ie, an external auditor).</p> <p>An external auditor performs his/her task impartially and objectively and he/she is also not involved in the management of the IORP. An external auditor has the right to express his/her findings and</p>	

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	<p>recommendations freely. External audit reports can be accessed by the supervisory authorities who can check how the recommendations of the external auditor are addressed by the IORP.</p>	
17.	<p><b>SUPERVISION OF OUTSOURCED FUNCTIONS AND ACTIVITIES</b></p> <p>EIOPA's cautionary note about the pros and cons of new regulations on outsourcing is welcome.</p> <p>Most outsourcing is to organisations that are already regulated in one way or another. EIOPA should beware duplication.</p> <p>Futhermore, EIOPA should be clearer about its justification for a written statement on outsourcing. Although this may not sound like a major imposition, it adds an extra item to the administrative burdens on IORPs. The UK has a 'one in, one out' rule for regulations. Will EIOPA support a similar approach?</p>	
18.	<p><b>OUTSOURCING</b></p> <p>See answer to q.17.</p>	