European Insurance and Occupational Pensions Authority

EIOPA-BoS-21/426
07 October 2021

POLICY DEPARTMENT

Opinion on the supervisory reporting of costs and charges of IORPs

1. LEGAL BASIS

1.1. The European Insurance and Occupational Pensions Authority (EIOPA) provides this Opinion on the basis of Article 29(1)(a) of Regulation (EU) No 1094/2010[1]. This article mandates EIOPA to play an active role in building a common Union supervisory culture and consistent supervisory practices, as well as in ensuring uniform procedures and consistent approaches throughout the Union.

1.2. EIOPA delivers this Opinion on the basis of Directive (EU) 2016/2341[2] (the IORP II Directive), in particular in relation to Article 19(1)(a), Article 45(1), Article 46, Article 48(8)(a), Article 49 and Article 50 thereof.

1.3. This Opinion is provided to the competent authorities (CAs), as defined in Article 4(2) of Regulation (EU) No 1094/2010.

1.4. The Board of Supervisors has adopted this Opinion in accordance with Article 2(7) of its Rules of Procedure[3].

2. CONTEXT AND OBJECTIVE

2.1. A transparent and comprehensive view of all costs and charges is essential for IORPs, social partners and supervisors to assess the value for money – considering costs in conjunction with risk and returns – and affordability of occupational pension schemes. According to the OECD[4], annual costs and charges of 1% of assets reduce final pension

[1] Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC, OJ L 331, 15.12.2010, p. 48.
[2] 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), OJ L 354, 23.12.2016, p. 37.
[3] Decision adopting the Rules of Procedure of EIOPA's Board of Supervisors, available at: https://www.eiopa.europa.eu/sites/default/files/publications/administrative/bos-rules_of_procedure.pdf.
[4] OECD, Pension costs in the accumulation phase: Policy options to improve outcomes in funded private pensions, OECD Pensions Outlook 2018: https://doi.org/10.1787/pens_outlook-2018-en

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income by more than 20% after 40 years of pension saving – or equivalently raise contributions by more than 20% to achieve a given level of retirement income.

2.2. The IORP II Directive establishes that the main objective of prudential supervision is to protect the rights of members and beneficiaries, as set out in Article 45 thereof. Article 46 of the IORP II Directive mandates Member States to ensure that IORPs are subject to prudential supervision including investment management. Furthermore, IORPs have to adequately protect the interests of scheme members and beneficiaries, as set out in Article 48 of the IORP II Directive, and in particular invest the assets in the best long-term interest of members and beneficiaries, as set out in Article 19 thereof. In addition, the IORP II Directive affords CAs the necessary powers to review the strategies, processes and reporting procedures established by IORPs to comply with the relevant regulations adopted pursuant to that Directive, as set out in Article 49 thereof, and the necessary powers and means to supply at any time information about all business matters, as set out in Article 50 thereof.

2.3. Directive 2014/65/EU[5] (MiFID II) has imposed requirements on investment firms (brokers, portfolio managers) to disclose information on all costs and charges to clients, including IORPs. Pan-European Personal Pension products (PEPPs) are not occupational pension schemes, but they may be provided by IORPs. Regulation (EU) 2019/1238[6] (the PEPP Regulation) requires providers to disclose a breakdown of all costs, incurred directly at the level of the provider or at the level of an outsourced activity or investment fund, in the PEPP key information document. The costs related to the PEPP are broken down by administrative, investment and distribution costs. Further, any additional charges for a financial guarantee must be disclosed separately.[7]

2.4. In the 2015 report on costs and charges of IORPs[8], 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 possible at that time to accomplish the original goal of the project to develop common definitions and

[5] Article 24(4)(c) of Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (recast), OJ L 173, 12.6.2014, p. 349: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32014L0065 .

[6] Regulation (EU) 2019/1238 of the European Parliament and of the Council of 20 June 2019 on a pan-European Personal Pension Product (PEPP), OJ L 198, 25.7.2019, p. 1.

[7] Article 5 of Commission Delegated Regulation (EU) 2021/473 of 18 December 2020 supplementing Regulation (EU) 2019/1238 of the European Parliament and of the Council with regard to regulatory technical standards specifying the requirements on information documents, on the costs and fees included in the cost cap and on risk-mitigation techniques for the pan-European Personal Pension Product; OJ L 99, 22.3.2021, p. 1; http://data.europa.eu/eli/reg_del/2021/473/oj .

[8] EIOPA Report on Costs and charges of IORPs, EIOPA-BoS-14/266, 7 January 2015: https://eiopa.europa.eu/Publications/Reports/EIOPA-BoS-14-266-Final_report_on_costs_and_charges_of_IORPs.pdf .

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breakdowns of costs and charges. Since then, the pension sectors in a number of European countries have taken initiatives to enhance the transparency of costs.[9,10]

2.5. EIOPA surveyed existing national practices and gaps with regard to supervisory cost reporting among CAs in twenty Member States.[11] The answers to the questionnaire make clear that only a few CAs have a transparent view of IORPs' cost levels under their supervision. Most CAs receive costs information based on the IORPs' annual accounts, which follow national accounting rules and are commonly not subject to a look-through approach, i.e. including fees and charges of external investment funds/managers as well as transaction costs.

2.6. In addition, several CAs have also responded that IORPs are required to report data on costs to the CA directly through supervisory reporting, and others indirectly through disclosure documents envisaged by the IORP II Directive. Five out of twenty-five surveyed CAs collect transparent cost data from IORPs, explicitly disclosing all of the costs charged, in particular with respect to investment costs.

2.7. The main objective of the Opinion is to foster an effective cost supervision across the EU in order to enhance the value for money offered to members and beneficiaries, the cost efficiency of IORPs and the affordability for sponsors.

2.8. The supervisory reporting of transparent cost data will allow CAs to assess the cost efficiency of IORPs, the affordability for sponsors and the value for money offered to members and beneficiaries and consider the outcomes within the supervisory review process, including in the dialogues with the IORP's management board.

2.9. The cost reporting to CAs obliges IORPs to assess and manage their cost structure in a more comprehensive and transparent way, in particular where IORPs are now only considering direct and not indirect investment costs.

2.10. This Opinion further aims to facilitate risk-based and proportionate supervision of IORPs. In this context, CAs may take into account national specificities of the IORP sector to determine the requirements necessary for implementing this Opinion considering a risk-based and proportionate approach. In particular, EIOPA recognises that changing national reporting requirements to implement this Opinion may require substantial time.

[9] See the (revised) set of recommendations for classifying and reporting costs in Federation of the Dutch Pension Funds, Recommendations on Administrative Costs, February 2016, The Hague: https://www.pensioenfederatie.nl/website/engelse-website/publications-in-english/recommendations-on-administrative-costs

[10] The Cost Transparency Initiative (CTI) in the UK developed a set of templates to assist pension schemes in receiving standardised cost and charges information from asset managers: https://www.plsa.co.uk/Policy-and-Research-Investment-Cost-Transparency-Initiative

[11] See Annex of the cost-benefit analysis in EIOPA, Impact assessment - Opinion on the supervisory reporting of costs and charges of IORPs, EIOPA-BoS-21-427, 7 October 2021.

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3. SUPERVISORY REPORTING OF COSTS AND CHARGES OF IORPS

Annual reporting of cost information

3.1. CAs should require IORPs to report on an annual basis information on all costs and charges.

Classification and definitions of IORP costs and charges

3.2. In the collection of information on costs and charges, CAs should distinguish the cost categories specified in the following high-level generic cost classification:

Cost category	Description
Investment costs	All on-going and one-off investment costs incurred in connection with the management of assets (excluding portfolio transaction costs): - Fiduciary fees - Remuneration to the external asset manager for management of (discretionary) portfolios and for the management of the investment funds. - Internal management costs incurred for the management of assets - Investment administration - Costs of safekeeping of assets - Other asset management costs - Management costs for direct investments in property
Transaction costs	All costs incurred as a result of the acquisition and disposal of investments, including indirect transaction costs for when part of the portfolio is invested in one or more investment funds: - Broker commissions and transaction taxes (explicit costs) - Amounts charged to investors at the entry into or withdrawal from an investment fund, in favour of the fund, the manager, and/or the already existing investors. - Subscription and redemption fees charged by underlying investment funds (indirect costs) - Acquisition costs (including investments in property and private equity) - Implicit transaction costs
Administrative costs	All administrative costs of the IORP: - Collection of contributions/premiums, pension payments, accrued pension rights, value transfers - General administrative costs such as staff and premises - Communication to participants and employer - Oversight (certifying actuary, auditor) and advice (except for asset management related advice) - Costs of adapting to changes to the pension system
of which:	Costs of distribution, including distribution to sponsoring undertakings, where applicable
Costs paid by sponsors	Additional costs borne by the sponsor[12], not charged to the IORP

[12] For example transaction costs (broken deal costs), administrative costs (staff, IT equipment and office).

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3.3. Annex 1 contains further definition of investment, transaction and administrative costs (Table 1) and a reporting template to assist CAs to collect the information on costs and charges of IORPs (Table 2).

3.4. CAs are encouraged to collect cost data at a higher level of granularity than the generic cost classification. The granularity of the classification can be increased by including more detailed cost categories or by distinguishing investment and transaction costs by asset class. A higher level of granularity will contribute to validating the cost data as well as explaining the differences in cost levels when comparing cost data of IORPs.

3.5. All costs should be reported in the reporting currency and as a percentage of average investment assets (including that related to third party investments). In addition, administrative, distribution costs and sponsor costs should be reported in the reporting currency per participant. The CAs should define whether the number of participants is the combined number of active members and pension beneficiaries or is only composed of active members. Where the IORP collects the investment and transaction costs data based on MiFID II disclosures by the service providers, this should be indicated in the reporting template submitted. The use of estimates should also be clearly communicated.

3.6. The 'administrative costs' category includes 'distribution costs'. To ensure consistency with the PEPP Regulation, IORPs providing PEPPs should also report this cost component separately. CAs may choose to apply this more detailed breakdown to other IORPs.

3.7. Where the sponsor is paying directly any cost related to the IORP, either in cash or in kind, and that cost is not charged to the IORP, and when reporting of such cost is deemed proportionate as referred to in paragraph 3.16, those costs should be reported as a separate cost category.

Cost reporting at scheme level, if IORPs provide multiple schemes

3.8. CAs should expect IORPs, where possible, to report at the level of the scheme or of the investment option where IORPs provide different schemes or investment options that differ in term of features, such as the investment strategy. Reporting at the level of schemes/ investment options will provide better insight in the costs for sponsors and plan members of a specific scheme and in the costs for plan members of a specific investment option. If there are no material differences in the cost structure, e.g. because the different schemes have the same investment policy, IORPs are not expected to differentiate cost reporting at the scheme level.

Principles for compiling the cost information

3.9. CAs should expect IORPs to apply the following principles in compiling the information on costs and charges:

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Look-through and no-netting

3.10. In order for all costs and charges to be reflected in the reported costs, CAs should expect IORPs to apply a look-through approach, i.e. include all costs and charges incurred at the level of investment funds, managers, and transactions. Moreover, the no-netting principle should be applied, meaning that cost items should not be subtracted from income items and vice versa. The cost data that can be requested by IORPs from their portfolio managers and brokers in accordance with MiFID II rules is assumed to fulfil the look-through and no-netting principles.

Costs paid directly by sponsors

3.11. CAs should expect IORPs to report the costs paid directly by sponsoring undertakings, including pension administration activities that IORPs outsource to the sponsoring undertaking. The latter would require sponsoring companies to provide an estimate of the staff and resource allocated to the administration of the IORP. Including costs directly paid by the sponsor ensures that CAs receive cost data that will allow for greater comparability between IORPs which bear the administrative costs themselves and IORPs for which the sponsor bears (a substantial part of) these costs.

Matching principle of accounting

3.12. Reported costs are attributed to the accounting period to which they relate, and costs are stated in the accounts for the same period as the related revenues. For example, performance fees are stated in the accounts for the period in which the associated performance occurred, and not the period when the fee is paid.

Taxation

3.13. Indirect taxes are implicit in the price of a product or service and are thus payable by the IORP or by the investment fund. Examples are value-added tax (VAT) and transfer tax. Taxes that add to cost price should be stated as costs in the category under the relevant cost category where the tax in question applies. For example the VAT on asset management costs is attributed to and stated under investment management costs and transfer tax on direct transactions in property is attributed to transaction costs.
Taxes that are levied on the investment return of IORPs or investment funds should not be stated as costs. Such taxes include, for example, withholding tax on dividends and interest (levies on direct return) and capital gains levies on book profits.

Reporting currency

3.14. Costs should be reported in the national reporting currency.

Estimations

3.15. If costs cannot be directly identified from IORP records or data provided by third parties, CAs should expect IORPs to estimate the costs, ensuring that the estimates are plausible and underlying assumptions can be verified. Therefore, IORPs are expected to indicate which costs are estimates, and which are not.

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Proportionality

3.16. In applying the above principles, CAs should allow IORPs to apply a proportionate approach in terms of costs and benefits. The benefits of a more complete view of indirect costs and charges incurred at the level of investment funds, managers, and transactions in terms of accuracy may not outweigh the costs of obtaining this information. In some cases, a full look-through of costs and charges may also not be feasible. Similarly, the benefits of including costs paid directly by the sponsor in terms of comparability may be small relative to the costs for the sponsor to estimate/provide these data. In addition, even though an IORP provides different schemes with distinct investment strategies, distinguishing the costs and charges at scheme level may be relatively costly.

Guidance for IORPs to collect costs from asset managers

3.17. To assist IORPs in collecting costs and charges, CAs should provide IORPs with the templates included in Annex 2 and 3, to facilitate the collection of investment and transaction costs from their asset managers.

3.18. Under MiFID II, investment firms providing brokerage and portfolio management services have to provide, at the request of their clients, including IORPs, an itemised breakdown of all cost and charges related to investment and ancillary services as well as to financial instruments. Annex 3.1 provides this itemised breakdown of cost and charges and explains how the breakdown can be mapped to the cost categories 'Investment costs' and 'Transaction costs' of the generic classification above.

3.19. With regard to a higher level of granularity than the generic classification of cost reporting per asset class, investment firms are currently not required to disclose an asset-by-asset (ISIN-by-ISIN) breakdown of investment and transaction costs to their clients. However, as this is necessary to distinguish these costs by asset class, IORPs, being important institutional investors, could request investment firms to provide such a breakdown.

3.20. Not all investment and transaction costs items are included in the scope of MiFID II, most notably costs and charges related to direct investments in property and private equity. The Institutional Limited Partners Association provides guidance and a reporting template for fees, expenses, and carried interest of investments in private equity.[13] For real estate investments, the European Association for Investors in Non-Listed Real Estate Vehicles provides a global standard for fees and costs.[14]

3.21. The template in Annex 3 can be used by IORPs to receive standardised granular cost

[13] See https://ilpa.org/wp-content/uploads/2016/10/ILPA-Reporting-Template-Guidance-Version-1.1.pdf; and https://ilpa.org/reporting-template/get-template/ (page visited on 11 February 2021)

[14] Total Global Expense Ratio, see: https://www.inrev.org/news/inrev-news/new-global-standard-fees-and-costs (page visited on 11 July 2021)

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and charges information from asset managers, and report the aggregated costs and charges information, which is a summary of key information across all investments, to the CA. The more granular information included in this template will provide IORPs with better insight in the main drivers of investment costs.

Proportionality

3.22. IORPs' cost reporting should be proportionate to the transparency and supervisory objectives of this Opinion and take a risk-based approach. In particular, CAs should have discretion to determine the level of cost reporting for DB IORPs, e.g. a lower frequency of reporting, reduced scope of cost reporting or full exemption for certain DB IORPs, where certain DB IORPs should be considered non-commercial small or non-commercial closed DB IORPs. As a first step to exercise this discretion and to determine the level of cost reporting, CAs may conduct a one-off fact-finding exercise to assess the national situation regarding the costs and benefits of cost reporting.

4. USE OF COST DATA FOR SUPERVISORY REVIEW AND OTHER SUPERVISORY ACTIONS

Comparative analysis of cost levels

4.1. Within their supervisory activities, CAs are expected to use the data to conduct comparative analysis of the cost levels reported by IORPs to assess:

Cost efficiency

4.2. Benchmarking costs across IORPs may improve peer pressure in the market. Cost information allows to identify inefficiencies in the investment supply chain, for example if the fiduciary manager does not choose the most cost efficient external asset managers, or if asset managers charge high fees.

4.3. Thematic reviews, for example, can identify whether conflicts of interest occur between IORPs and fiduciary managers as well as other asset managers (or as well whether costs add too much to employers' costs). Differences in cost levels of similar-sized pension funds (for instance for the same asset class) is an indicator of uncompetitive market or conflicts of interest that permit identifying outliers in the best interests of members.

Affordability to sponsors

4.4. The cost efficiency of IORPs has direct implications for the affordability to sponsors, in particular with regards defined benefit (DB) schemes. Costs are one of the relevant factors when assessing the affordability of DB schemes, and as such may play an important role in DB closures.

Value for money

4.5. From a consumer protection perspective, CAs should have a holistic view of IORPs costs and charges to ensure they provide value for money to members and do not use up savers' pension pots.

4.6. IORPs provide value to members, when their needs for retirement and investment

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preferences, when these are expressed, are addressed[15]. The consideration of costs is part of the suitability of the investment policy to the IORP membership structure.

4.7. For "value for money" assessments, CAs are expected to take into account return and risk data, as well as the type and quality of the service provided, jointly with cost data, as absolute levels of costs do not give enough information to make this assessment.

4.8. Assessments should also compare against what other, similar pension schemes are paying (benchmarking). Although typically low costs are a good indication of better outcomes (they usually correlate with higher returns), the assessment of the efficiency, affordability and value for money requires to take into account the risk levels of the investment strategy and the net return (after costs) delivered.

Comparability of results

4.9. Costs should be reported in supervisory templates according to a comparable approach. CAs should compare "equals to equals", taking into account differences between schemes (investment strategy) or IORPs (DB and DC, hybrids), decumulation options and the role of the sponsor, if relevant. In particular, costs need to be assessed taking into account the investment strategy, the risk profile of the IORP and the financial return achieved.

4.10. The comparability and usefulness of the cost reporting will generally increase with the comprehensiveness and granularity of the costs data. For example, including costs paid directly by sponsors increases comparability between IORPs where sponsors do and where sponsors do not bear such costs. As a second example, the collection of costs at the scheme level, where IORPs provide multiple schemes, will increase the usefulness of comparisons.

Supervisory review

4.11. In order to enhance efficiency, affordability and value for money, CAs should address the results of the comparative cost analyses in the supervisory review of IORPs, according to Article 49 of the IORP II Directive, including during the regular dialogue with the IORP's management board.

4.12. CAs are expected to evaluate costs over time, assess whether IORPs act to improve the cost-efficiency of the schemes, and assess the consistency of cost reporting.

[15] The importance of the membership structure is laid down in recital 45 of the IORP II Directive. The Opinion on the supervision of long-term risk assessment of DC schemes sets out EIOPA's expectations on IORPs' consideration of risk-return preferences in the conduct of long-term risk assessment from the perspective of members and beneficiaries and the design of the investment strategy. See EIOPA, Opinion on the supervision of long-term risk assessment by IORPs providing DC schemes, EIOPA-BoS-21/429, 7 October 2021.

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Disclosure of costs

4.13. Taking into account confidentiality, CAs are encouraged to publish the outcomes of the analysis as well as aggregated cost figures. The publication of the results of benchmarking assessments can bring benefits to the market in the form of "peer pressure" for IORPs to select cost-efficient asset managers and improve further competition between service providers. In addition, cost data may be also used internally for official statistics and research activities.

4.14. CAs should encourage IORPs to disclose the reported costs and charges to the sponsor and to the public.

5. MONITORING BY EIOPA

5.1. Two years following the publication of this Opinion, EIOPA will look into the supervisory practices of the CAs with a view to evaluate supervisory convergence.

5.2. This Opinion will be published on EIOPA's website.

Done at Frankfurt am Main, on 30 September 2021.

[signed]

For the Board of Supervisors
Petra Hielkema
Chairperson

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ANNEX 1: SUPERVISORY COST REPORTING TEMPLATES

CAs are expected to require IORPs to submit cost reporting data to the CA using the template presented in Table 2 of this Annex. For the purposes of this Annex, the definitions in Table 1 of this Annex should apply.

Further breakdown of cost types and associated definitions in the table s below aims at securing uniformity of the reported data. IORPs should verify whether they have identified the full range of costs.

Table 1: Definitions	
Cost category	**Definition**
Investment costs	All on-going and one-off investment costs incurred in connection with the management of assets (excluding portfolio transaction costs), which should include: ▸ Fiduciary fees (risk management fee, remuneration strategic and fiduciary advice, including VAT); ▸ Remuneration to the external asset manager for management of (discretionary) portfolios (strategic and investment advice, research, the management of assets and liabilities), including any fees and charges paid through Net Asset Value (less management fee rebate); ▸ Remuneration paid to the external asset manager for the management of the investment funds. Services covered by the fund management fee include the day-to-day management of investment funds and portfolios, the administration thereof, reporting and communication with investors, including any fees and charges paid through Net Asset Value (less management fee rebate); ▸ Investment administration: remuneration paid to an administrator for the administration of assets and liabilities in the fund, and for other bookkeeping and reporting activities. Execution of administration of the investments may be outsourced to specialist companies by the pension fund and/or asset manager; ▸ Internal management costs: all expenses (operational costs) incurred for the internal management of assets, such as personnel costs allocated to the asset management, facility costs or advice costs borne by the IORP; ▸ Custody or safekeeping of securities in a fund, payable by the fund & depositary fees (AIFs), if not reported jointly with investment administration costs; ▸ Other asset management costs: fees incurred for the establishment of funds or partnerships, auditing costs of the investments, consultancy fees, and fees including financing fees, technology costs, performance fees including paid through NAV, tax advice; ▸ Stock lending and borrowing fees; ▸ For investments in property: management property expenses.
Transaction costs	All transaction costs, which should include costs incurred as a result of the acquisition and disposal of investments, including indirect transaction

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	costs for when part of the portfolio is invested in one or more investment funds: - Explicit costs such as broker commissions (exchange fees, settlement fees, clearing fees) and transaction taxes (financial transaction tax); - Amounts charged to investors at the entry into or withdrawal from an investment fund, in favour of the fund, the manager, and/or the already existing investors; - Indirect transaction costs: subscription and redemption fees charged by underlying investment funds; - Acquisition costs (within investment funds or, in fund-of-funds structures) such as broken deal expenses, appraisal and auditing fees, fiscal and legal consultancy fees related to transactions, bank fees; - Costs of direct investments in private equity; - Implicit transaction costs, which represent the loss of value implied by the difference between the buying or selling price and the mid-market price of the asset (embedded in the bid-offer spread).
Administrative costs	All administrative costs of the IORP: - Collection of contributions/premiums, pension payments, accrued pension rights, value transfers; - General administrative costs such as staff and premises; - Communication to participants and employer; - Oversight (certifying actuary, auditor) and advice (except for asset management related advice); - Where applicable, any cost for the distribution of the IORP, including to sponsors.
Costs paid by sponsors	Additional costs borne by the sponsor[16], not charged to the IORP

[16] For example transaction costs (broken deal costs), administrative costs (staff, IT equipment and office)

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Table 2: IORP cost reporting template to CAs					
Cost category	**Definition**	**In reporting currency**	**In % of average assets under management**	**In reporting currency per participant for administrative, distribution and sponsor costs**	**[Optional: add columns per asset class]**
Investment costs	All on-going and one-off investment costs incurred in connection with the management of assets including safekeeping of assets (excluding portfolio transaction costs)	[figure should be inserted]	[figure should be inserted]	Not applicable	[figure should be inserted]
Transaction costs	All transaction costs, which should include costs incurred as a result of the acquisition and disposal of investments, including indirect transaction costs for when part of the portfolio is invested in one or more investment funds.	[figure should be inserted]	[figure should be inserted]	Not applicable	[figure should be inserted]
Administrative costs	All administrative costs of the IORP	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]	Not applicable
Of which	Cost for the distribution of the IORP to sponsors	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]	Not applicable
Costs paid by sponsors	Additional costs borne by the sponsor[17], not charged to the IORP	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]	Not applicable

[17] For example transaction costs (broken deal costs), administrative costs (staff, IT equipment and office).

ANNEX 2: ITEMISED MIFID II CLASSIFICATION OF COSTS AND CHARGES TO BE DISCLOSED BY INVESTMENT FIRMS TO CLIENTS

For the reporting to the CA on investment and transaction costs in Table 2 of Annex 1, aggregated costs items as presented in Table 2 of this Annex can be used.

For that purpose, the MiFID II itemised tables included in Table 1 here below have to be collected, or aggregated where diverse service providers are providing services to the IORP, including where the IORP manages investments internally, in order to collect investment and transaction costs. IORPs can use the itemised MiFID II breakdown of costs relating to investment/ancillary services and financial instruments to calculate a generic classification of investment/transaction costs.

The following items will not be included in the MiFID II breakdown and would have to be added by the IORP itself:

- Direct investment costs of the IORP (i.e. staff and equipment);
- All charges and incidental costs related to direct investments in property and private equity;
- All costs related to transactions related to direct investments in property and private equity.

According to Article 24(4) of MiFID II and Article 50(2) of the Commission Delegated Regulation (EU) 2017/565[18], firms should aggregate costs and charges in connection with the investment service and costs and charges associated with the financial instruments. Third party payments received by investment firms in connection with the investment service provided to a client should be itemised separately. The aggregated costs and charges should be totalled and expressed both as a cash amount and as a percentage.

This does not only apply to investment firms providing "portfolio management" services but also investment firms providing brokerage services relating to the "reception and transmission of orders in relation to one or more financial instruments" and the "execution of orders on behalf of clients".

According to Article 24(4) of MiFID II, where the client so requests, an itemised breakdown should be provided. Where applicable, such information should be provided to the client on a regular basis, at least annually, during the life of the investment.

Annex 2 of the Commission Delegated Regulation (EU) 2017/565 specifies the itemised breakdown to be provided:

[18] Commission Delegated Regulation (EU) 2017/565 of 25 April 2016 supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive, OJ L 87, 31.3.2017, p. 1.

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Table 1 - itemised breakdown of investment and transaction costs according to Annex 2 of the Commission Delegated Regulation (EU) 2017/565			
MiFID II Annex 2 - Table 1 - All costs and associated charges charged for the investment service(s) and/or ancillary services provided to the client that should form part of the amount to be disclosed			
	Cost items to be disclosed:		**Examples:**
1.1	One-off charges related to the provision of an investment service	All costs and charges paid to the investment firm at the beginning or at the end of the provided investment service(s).	Deposit fees, termination fees and switching costs.
1.2	On-going charges related to the provision of an investment service	All on-going costs and charges paid to investment firms for their services provided to the client.	Management fees, advisory fees, custodian fees.
1.3	All costs related to transactions initiated in the course of the provision of an investment service	All costs and charges that are related to transactions performed by the investment firm or other parties.	Broker commissions, entry- and exit charges paid to the fund manager, platform fees, mark ups (embedded in the transaction price), stamp duty, transactions tax and foreign exchange costs.
1.4	Any charges that are related to ancillary services	Any costs and charges that are related to ancillary services that are not included in the costs mentioned above.	Research costs. Custody costs.
1.5	Incidental costs		Performance fees
MiFID II Annex 2 - Table 2 - All costs and associated charges related to the financial instrument that should form part of the amount to be disclosed			
	Cost items to be disclosed:		Examples:
2.1	One-off charges	All costs and charges (included in the price or in addition to the price of the financial instrument) paid to product suppliers at the beginning or at the end of the investment in the financial instrument.	Front-loaded management fee, structuring fee, distribution fee.
2.2	On-going charges	All on-going costs and charges related to the management of the financial product that are deducted from the value of the financial	Management fees, service costs, swap fees, securities lending costs and taxes, financing costs.

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		instrument during the investment in the financial instrument.	
2.3	All costs related to the transactions	All costs and charges that incurred as a result of the acquisition and disposal of investments.	Broker commissions, entry- and exit charges paid by the fund, mark ups embedded in the transaction price, stamp duty, transactions tax and foreign exchange costs.
2.4	Incidental costs		Performance fees

Currently, MiFID II does not include a requirement that investment firms should provide an ISIN-by-ISIN breakdown of costs and charges. ESMA's Technical Advice to the Commission on the impact of the inducements and costs and charges disclosure requirements under MiFID II (31 March 2020, ESMA35-43-2126) recommends that investment firms should also be required to provide an ISIN-by-ISIN cost breakdown at the request of clients.

The industry[19] has developed templates for asset managers to collect and disclose MiFID II cost data to clients, European MiFID II Template - Version 3.0. This template can be used as a starting point for the collection of data.

Where the IORP is relying on MiFID II itemised cost disclosures for the reporting of investment and transaction costs to the CA, the following cost items from Table 2 should be included in "investment costs" and "transaction costs" of Table 1 of Annex 2.

Table 2	
INVESTMENT COSTS	
1.1	One-off charges related to the provision of an investment service
1.2	On-going charges related to the provision of an investment service
1.4	Any charges that are related to ancillary services
1.5	Incidental costs related to the provision of an investment service
2.1	One-off charges related to the financial instruments
2.2	On-going charges related to the financial instruments
2.4	Incidental costs related to the financial instruments
*****	Direct investment costs IORP (i.e. staff and equipment)
******	All charges and incidental costs related to direct investments in property and private equity

[19] The MiFID II template has been developed by FinDatEx (Financial Data Exchange Templates), a joint structure established by representatives of the European financial services sector with the view to coordinate, organise and carry out standardisation work to facilitate the exchange of data between stakeholders in application of European Financial markets legislation, FinDatEx.eu

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TRANSACTION COSTS	
1.3	All costs related to transactions initiated in the course of the provision of an investment service
2.3	All costs related to the transactions related to the financial instrument
*****	All costs related to transactions related to direct investments in property and private equity

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ANNEX 3: TEMPLATE FOR IORP'S COLLECTION OF COSTS DATA FROM ASSET MANAGERS AND OTHER SERVICE PROVIDERS

In order to report investment and transaction costs, following the -look through approach, IORPs can use the following template to request detailed cost data from fiduciary managers, external asset managers and other service providers.

Preferably the costs collected from the asset manager include the itemised list provided in Table 1 below, in order to enable the IORP to request a detailed report from fiduciary/external asset manager(s), and conduct a due diligence on the quality of the data provided by the fiduciary/asset manager(s) with regards investment and transaction costs.

When the CAs deem necessary to collect more granular data, CAs should request IORPs to provide more granular cost information than those included in the template in Annex 1. This can be done, for instance, by requesting the filled out template in Table 1 of this Annex in order to assess the reporting consistency.

Table 1: Template for IORP's collection of investment and transaction costs data from asset managers and other service providers

Cost category	Definition	In reporting currency	In % assets	[Optional: add columns per asset class]
Investment costs	Total on-going and one-off investment costs incurred in connection with the acquisition or disposal of assets (excluding portfolio transaction costs):	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
	Detailed costs broken down per item:			
	‣ Fiduciary fees (risk management fee, remuneration strategic and fiduciary advice, including VAT)	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
	‣ Remuneration to the external asset manager for management of (discretionary) portfolios (strategic and investment advice, research, the management of assets and liabilities), including any fees and charges paid through Net Asset Value (less management fee rebate)	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
	‣ Remuneration paid to the external asset manager for the management of the investment funds. Services covered by the fund management fee include the day-to-day management of investment funds and portfolios, the administration thereof, reporting and communication with investors, including any fees and charges	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]

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	paid through Net Asset Value (less management fee rebate)			
	▸ Investment administration: remuneration paid to an administrator for the administration of assets and liabilities in the fund, and for other bookkeeping and reporting activities. Execution of administration of the investments may be outsourced to specialist companies by the pension fund and/or asset manager	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
	▸ Internal management costs: all expenses (operational costs) incurred for the internal management of assets, such as personnel costs allocated to the asset management, facility costs or advice costs borne by the IORP.	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
	▸ Custody or safekeeping of securities in a fund, payable by the fund & depositary fees (AIFs), if not reported jointly with investment administration costs	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
	▸ Other asset management costs (Fees incurred for the establishment of funds or partnerships, auditing costs of the investments, consultancy fees, and fees including financing fees, technology costs, performance fees including paid through NAV, tax advice)	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
	▸ Stock lending and borrowing fee	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
	▸ For investments in property: property expenses	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
	▸ Costs of direct investments in private equity	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
Transaction costs	Total costs incurred as a result of the acquisition and disposal of investments, including indirect transaction costs for when part of the portfolio is invested in one or more investment funds:	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
	Broken down cost per item:			
	▸ Explicit costs such as broker commissions (exchange fees, settlement fees, clearing fees) and transaction taxes (financial transaction tax)	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
	▸ Buy and sell costs for direct holdings in investment funds: amounts charged to investors at the entry into or withdrawal from a fund (allocation or withdrawal of	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]

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	monies to an investment fund), in favour of the fund, the manager, and/or the already existing investors.			
	▸ Indirect transaction costs: subscription and redemption fees charged by underlying investment funds.	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
	▸ Acquisition costs (within investment funds or, in fund-of-funds structures) such as broken deal expenses, appraisal and auditing fees, fiscal and legal consultancy fees related to transactions, bank fees	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]
	▸ Implicit transaction costs, which represent the loss of value implied by the difference between the buying or selling price and the mid-market price of the asset (embedded in the bid-offer spread)	[figure should be inserted]	[figure should be inserted]	[figure should be inserted]

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Impact assessment

Opinion on the supervisory reporting of costs and charges of IORPs

Policy Department
EIOPA-BoS-21/427
07 October 2021

European Insurance and Occupational Pensions Authority

EIOPA-BoS-21/427

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EIOPA-BoS-21/427

1. ANALYSIS OF COSTS AND BENEFITS

1.1. Procedure and consultation of stakeholders

According to Article 29 of Regulation (EU) No 1094/2010, EIOPA should, where appropriate, analyse the potential costs and benefits relating to opinions provided to CAs, proportionate to their scope, nature and impact.

In developing the opinion, EIOPA analysed current supervisory practices at national level through a survey completed by CAs and engaged with stakeholders including the Occupational Pensions Stakeholder Group, most notably through a workshop held on 15 January 2021.

A draft opinion and its draft costs and benefit analysis have been subject to a public consultation, in line with Article 29 of Regulation (EU) No 1094/2010.

The analysis of costs and benefits is undertaken according to EIOPA's Impact Assessment methodology.

1.2. Problem definition

When analysing the impact from proposed policies, the impact assessment methodology foresees that a baseline scenario is applied as the basis for comparing policy options. This helps to identify the incremental impact of each policy option considered. The aim of the baseline scenario is to explain how the current situation would evolve without additional supervisory intervention.

For the analysis of the potential related costs and benefits of the proposed Opinion, EIOPA has applied as a baseline scenario the current state of play, where most CAs collect cost data based on IORP expenses disclosed in annual accounts, and only in a few Member States, CAs collect in addition comprehensive IORP cost data based on a look-through approach.

Unlike the investment fund sector, where international market standards on the calculation of costs have been developed, IORPs have faced lower market incentives[1] to develop national and international standards on costs that follow a look-through approach.

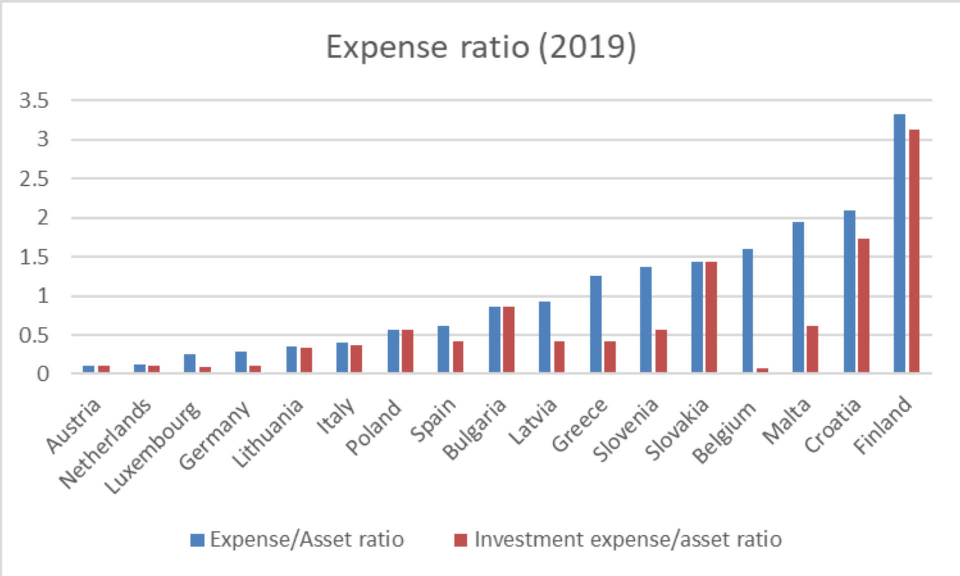
The impact of costs can be very significant. Pension pots can end up much smaller than expected because investments carried higher costs than anticipated. The findings of the AFM report on 'Cost

[1] Unlike pension schemes, mutual funds are targeted to both institutional and retail investors.

of pension funds needs more attention', published in April 2011, show that costs overly influence retirement pensions.

Based on EIOPA 2019 occupational pensions statistics[2], which differentiate expenses by categories of "investment" or "other", the expense ratio of occupational pension sectors, which is calculated as the ratio of investment and other expenses over assets, shows that the total expense ratio is very diverse across Member States (see Chart 1 below).

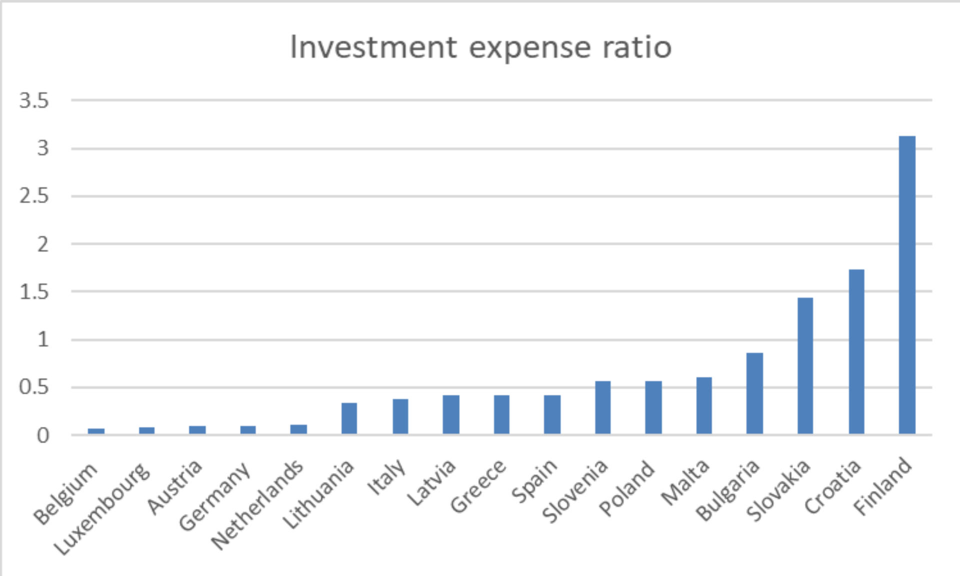
Chart 1: Expense and investment expense ratios, % assets



In particular when looking at the investment expenses ratio (see Chart 2 below), significantly more investment expenses are incurred to manage assets in FI, HR, SK, BG, MT, PL and SI. In contrast, the occupational pension sector in DE, BE, LU, AT and NL seem more efficient. The differences across countries might reflect different asset allocations and types of schemes, but it might also reflect different levels of efficiency of IORPs. However, it is not clear whether the reported data include both direct and indirect expenses, and therefore the assessment of cost levels based on the statistical data is limited.

[2] Data available at: https://www.eiopa.europa.eu/tools-and-data/occupational-pensions-statistics_en#AboutOccupationalPensionsStatistics

Chart 2: Investment expense ratio, % assets



Without transparent cost data, it is not possible to assess how well different IORPs are performing in practice. In order to ensure comparability of IORPs, cost information should be consistent, and include all costs in the value chain that are reducing a gross return or the asset value, as any fees or charges deducted from investment portfolios ultimately come out of members' contracts.

However, currently most CAs do not collect granular cost data. In 2020, EIOPA carried out a survey to map the instruments used by CAs to collect information related to IORPs costs. The results (see Annex) show that cost disclosure is not effective and comparable across the EEA. Most CAs receive IORP costs information as part of the annual accounts, which follow national accounting rules. It is assumed that only IORPs' direct expenses need to be identified as expenses in the annual accounts. Costs charged directly to an investment fund by asset managers (thus not charged to the pension fund) and transaction costs fall under indirect investment revenues. Such costs are not paid directly by the IORP but have always been charged to an invested fund, and effectively reduce the returns achieved by that fund. As a result a look-through approach is commonly not possible. In addition, according to the CA survey, in most Member States expenses can be set off against revenues. This means that the expenses listed in the annual accounts are not explicitly disclosing all of the costs, most notably those related to the investments.

The IORP II Directive introduced structural cost disclosure requirements for IORPs, both towards prospective and actual scheme members. However, the IORP II Directive does not specify which costs should be covered, according to which criteria and how detailed the breakdown should be or how the costs should be presented.

On the other hand, MiFID II requires investment firms to disclose to clients all costs and charges in connection with the investment service and costs and charges associated with the financial instruments. Third party payments received by investment firms in connection with the investment service provided to a client should be itemised separately. ESMA Q&As[3] provide more specific details on how to report specific costs. As institutional clients, IORPs are able to request from asset managers and other investment firms the itemised cost disclosure under MiFID II to collect detailed data on investment and transaction costs and report them accordingly to the CA.

In addition, in the 2015 report on costs and charges of IORPs[4], 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. The urgency of the uniform reporting of cost data has increased since the European Commission has already in 2017 requested EIOPA to include occupational DC schemes in its costs and past performance reports.[5]

1.3. Objective

A transparent and comprehensive view of all costs and charges is essential for IORPs, social partners and supervisors to assess the efficiency the value for money and affordability of occupational pension schemes. Jointly with comparable risk and return information, comparable cost information across IORPs can contribute to putting national IORPs sector on sound foundations.

The main objective of the Opinion is to foster an effective cost supervision across the EU in order to enhance the value for money offered to members and beneficiaries, the cost efficiency of IORPs and the affordability for sponsors.

Without a comprehensive overview of costs, it is not possible to assess whether IORPs are delivering "value for money" and whether there are conflicts of interest or other inefficiency problems in the IORP sector.

In addition, the experience of CAs shows that requiring cost transparency (reporting or disclosure) based on a look-through approach has a positive impact on the cost levels of IORPs as it drives costs down. For instance, in the Netherlands costs have decreased up to 10 times compared to the costs levels before a transparent cost reporting was introduced.

[3] ESMA, Questions and Answers on MiFID II and MiFIR investor protection and intermediaries topics ESMA35-43-349, 22 December 2020.

[4] EIOPA Report on Costs and charges of IORPs, EIOPA-BoS-14/266, 7 January 2015: https://eiopa.europa.eu/Publications/Reports/EIOPA-BoS-14-266-Final_report_on_costs_and_charges_of_IORPs.pdf

[5] https://eiopa.europa.eu/Pages/News/EIOPA-receives-request-on-costs-and-past-performance-of-IBIPs,-personal-pension-products-and-Defined-Contribution-pension-s.aspx

1.4. Policy issue and options

EIOPA has identified as policy issue the incomplete and inconsistent cost information reported to CAs. As a result, CAs may not be able to assess the cost efficiency of IORPs, the affordability of occupational pension schemes and whether IORPs offer value for money, jeopardising the protection of members and beneficiaries. To address this risk, EIOPA considered different options with regards the level of standardisation and granularity of the cost reporting to CAs.

The following options have been considered, with the preferred option for the cost reporting marked in bold:

1. High-level principles for reporting
2. **Common minimum standards on reporting, according to principles, with definitions and templates to assist the data reporting**
3. Fully standardised reporting

The options reflect the most relevant policy issue which concerns the level of standardisation of supervisory cost reporting. Under all options, CAs perform comparative analysis of the cost efficiency of IORPs, the affordability for sponsors and the value for money offered to members and beneficiaries and consider the outcomes within the supervisory review process, including in the dialogues with the IORP's management board.

POLICY OPTION 1: HIGH-LEVEL PRINCIPLES FOR REPORTING

The first policy option consist of limiting the guidance for CAs to defining high-level principles for reporting of costs. Such a principles-based approach would give flexibility to CAs to collect the cost data, while also giving flexibility to IORPs to report costs on the basis of a specific classification.

Policy option 1: High-level principles for reporting		
Stakeholder groups	**Benefits**	**Costs**
Competent authorities	Easier to implement across a range of different IORPs.	No comparability across IORPs if the reporting is not standardised in a granular way. Not possible to assess the consistency or completeness of the reported data, unless the CA

		introduces a granular classification of costs. Without a mandatory granular break-down of costs, it is more difficult to identify conflicts of interest or other inefficiency problems in the IORP sector. More resource intensive to implement. Less supervisory convergence across the EU.
IORPs	More flexibility possible, for example to tailor the requirements to specific types of IORPs.	If the reporting is not standardised, less certainty on reporting content and form and higher compliance risk. Higher costs of collecting and analysing the data.
Members and beneficiaries	Improved transparency of costs, in particular with regards hidden costs, can lead to improved cost efficiency of IORPs and hence better value for money.	Limited trust and confidence in the industry, due to possibly different interpretation of the principles-based costs reporting requirements by IORPs, and as a result inconsistent or inaccurate data.
Sponsoring undertakings	Improved ability to assess the affordability of the IORP.	

POLCIY OPTION 2: COMMON MINIMUM STANDARDS ON REPORTING

The second policy option is to define principles for reporting as well as minimum standards to be reported, composed of a mandatory template which includes a generic cost classification, without requiring to report to the CA costs broken down in a very granular way.

This option foresees a standardised reporting of costs which includes mandatory reporting templates from IORPs to CAs exhibiting a cost classification with clear definitions of each category of costs, to be reported to CAs according to principles. For investments managed by asset managers, the approach foresees the possibility to report on costs for investment funds based on MiFID disclosures, however does not impose it. It includes voluntary templates for the collection of costs from asset managers to IORPs.

With regards to the cost breakdown, EIOPA has considered different options. The proposed tailored approach consists of collecting data, following a look-through approach, on all IORP costs related to the investments, including expenses incurred by the IORP as well as expenses incurred by third parties related to the IORP investments, such as transaction costs and investment costs. The cost break-down proposed is the following:

- Investment costs
- Transaction costs
- Administrative costs, including distribution costs
- Costs paid directly by the sponsor

The breakdown aims at ensuring a high comparability of data in particular due to inclusion of sponsor costs and for multi-employer IORPs the inclusion of distribution costs. Costs paid by the sponsor may not be currently collected by IORPs.

The proposal deviates from the PEPP supervisory reporting breakdown[6] with regards to the separation of transaction costs from investment costs, which under the PEPP approach are presented jointly, and with regard to the presentation of distribution costs, which in the PEPP approach are presented separately from administrative costs, and the split of costs related to the provision of a guarantee from other costs. The reasons for deviating are the following:

- Collecting transaction costs jointly with investment costs without a further split would make it difficult to supervise whether transaction costs of IORPs are being reported. In particular given that in some Member States, IORPs commonly collect Total Expense Ratio as investment costs (without transaction costs). In addition, transaction costs levels depend on investment management styles (active or passive).
- Distribution costs are more relevant for savers of personal pension products while they might not be present in an IORP context.

[6] See Commission Implementing Regulation (EU) 2021/897 of 4 March 2021 laying down implementing technical standards for the application of Regulation (EU) 2019/1238 of the European Parliament and of the Council with regard to the format of supervisory reporting to the competent authorities and the cooperation and exchange of information between competent authorities and with the European Insurance and Occupational Pensions Authority.

The look-through approach presented in this Opinion is overall consistent with the PEPP approach, as set out in Commission Delegated Regulation (EU) 2021/473[7], allowing for an important degree of comparability of IORPs with PEPPs. According to the Commission Delegated Regulation, costs disclosed refers to actual incurred costs, incurred directly at the level of the provider or at the level of an outsourced activity or investment fund, including all related overhead costs.

The cost break-down deviates from the current reporting to EIOPA to ensure that CAs are able to supervise all costs following a look-through approach. Since 2020, EIOPA receives detailed data on IORPs[8] which includes data on IORPs' investment expenses, administrative expenses, other expenses and taxation expenses (template 'expenses' PF.05.03.24), but costs paid directly by sponsors are not reported.

Policy option 2: Common minimum standards on reporting with templates to assist the data reporting		
Stakeholder groups	**Benefits**	**Costs**
Competent authorities	Allows for comparability between IORPs Proposed level of granularity would facilitate conducting comparative assessments to enhance value for money for members and beneficiaries and affordability for sponsors and would ensure a higher quality of the supervision. High possible level of comparability and consistency of reported data.	Limited flexibility to make adjustments to the cost classification. More resource intensive to implement. Could risk some principles not to be implemented or considered due to minimum approach.

[7] Commission Delegated Regulation (EU) 2021/473 of 18 December 2020 supplementing Regulation (EU) 2019/1238 of the European Parliament and of the Council with regard to regulatory technical standards specifying the requirements on information documents, on the costs and fees included in the cost cap and on risk-mitigation techniques for the pan-European Personal Pension Product.

[8] EIOPA's Decision of the Board of Supervisors on EIOPA's regular information requests towards NCAs regarding provision of occupational pensions information (EIOPA BoS/18 114 of April 10, 2018).

	Enables higher supervisory convergence than policy option 1. Less costly to supervise the quality of the costs reported.	
IORPs	Potentially improved quality of data provided to IORPs. Full transparency could lead to lower level of IORP costs due to competition among asset managers. Reduction of costs of collecting and analysing these data by IORPs, in particular since for investment funds the reporting of investment and transaction costs can be collected from service providers based on MiFID II disclosures. More certainty on reporting content and form. Clearer and more detailed understanding of the charges of their investments.	Less certainty on reporting content and form compared to fully standardised reporting. Some compliance risk. Costs of collecting and analysing the data, particularly for smaller entities. Some specific costs such as sponsor related internal costs and transaction costs might be difficult to calculate, leading to increased costs to schemes.
Members and beneficiaries	Full transparency of costs, in particular with regards hidden costs, can lead to improved cost efficiency of IORPs and hence better value for money.	Costs related to the cost reporting exercise may lead to an increase of charges to members, which may nonetheless not lead to lower returns as the cost efficiency of the IORP may improve.
Sponsoring undertakings	Improved ability to assess the affordability of the IORP.	

POLICY OPTION 3: FULLY STANDARDISED REPORTING

This option foresees a fully standardised reporting of costs, which includes mandatory reporting templates from IORPs to CAs with a detailed breakdown of costs per type of cost, based on a cost classification with clear definitions of each category of costs. For investments managed by asset managers, the approach requires to report on costs based on MiFID II disclosures.

Policy option 3: Fully standardised reporting		
Stakeholder groups	**Benefits**	**Costs**
Competent authorities	The level of granularity would facilitate conducting comparative assessments to enhance value for money for members and beneficiaries and affordability for sponsors and would ensure a higher quality of the supervision. Highest possible level of comparability and consistency of reported data. Stronger supervisory convergence than policy option 1 or 2.	Lack of flexibility to adjust the templates for specific features of types of IORPs.
IORPs	Improved quality of the data provided to IORPs. Full transparency could lead to lower level of IORP costs due to competition. Reduction of costs of collecting and analysing these data by IORPs, in particular since for investment funds the reporting of investment and transaction costs should be collected from service providers based on MiFID II disclosures.	The most resource intensive and expensive for IORPs, particularly for smaller entities. Some specific costs such as sponsor related internal costs and transaction costs might be difficult to calculate, lead to increased costs to schemes,

	More certainty on reporting content and form. Clearer and more detailed understanding of the charges of their investments.	
Members and beneficiaries	Improved transparency of costs, in particular with regards hidden costs, can lead to improved cost efficiency of IORPs and hence better value for money Publication of consistent and accurate cost data reported to the CA allows to accurately compare costs charged by IOPRs and determine whether IORPs are providing good outcomes to members. From a consumer protection perspective, indirect benefits of a fully standardised reporting would result from supervision, where it should be easier for supervisors to supervise that IORPs provide value for money to members and do not use up savers' pension pots, and identify potential market failures and outliers	Costs related to the cost reporting exercise might lead to higher charges to members.
Sponsoring undertakings	Improved ability to assess the affordability of the IORP.	Costs related to the cost reporting exercise might lead to higher costs for sponsoring undertakings.

1.5. Conclusion

EIOPA has considered three policy options to address the policy issue of this Opinion.

Setting only high level principles (Policy Option 1) was discarded as it would be difficult for CAs to assess whether the data provided is complete and consistent. Similarly, for a fully standardised reporting (Policy Option 3) the costs are expected to outweigh the benefits.

The most advantageous in terms of costs and benefits is Policy Option 2, i.e. common minimum standards on reporting with templates to assist the data reporting. The proportionate and risk-based approach envisaged by the opinion will contribute to ensuring that the benefits surpass the costs at the level of individual IORPs. In particular for DB IORPs, CAs have the discretion to adjust the intensity of the cost reporting in line with the expected costs and benefits.

This policy option is expected to ensure comparability and higher quality and comprehensiveness of data, which result in informed supervisory actions, and provide clear guidance to IORPs on the data to be reported. The benefits of cost reporting could significantly exceed the costs where IORPs do not have a transparent view of their cost levels, given that seemingly small reductions in costs and charges may have a substantial impact on final retirement income or on the affordability for sponsors. The cost and benefits of cost reporting will be relatively modest where IORPs already receive transparent information on costs and charges relating to investment management.

ANNEX: SUMMARY OUTCOMES OF SURVEY OF NATIONAL PRACTICES AND GAPS

RESPONSE

In 2020, EIOPA conducted a questionnaire among CAs with the aim of mapping the existing national practices regarding the collection by CAs of cost information related to IORPs and to identify any possible 'gaps' within the costs collected.

The questionnaire covered the following national practices of IORP data collection in order to identify what is the data available for cost supervision by CAs:

- IORP reporting of costs to the supervisor, of which
  - costs disclosed in the IORPs' annual accounts;
  - costs disclosed to members and prospective members;
  - costs, other than costs disclosed in annual accounts, PBSs and pre-enrolment documents.

EIOPA received responses from 25 CAs, whereas five CAs did not complete the cost section of the survey because IORPs are largely absent (BG, CZ, EE, IS, LT).

TYPES OF SUPERVISORY COST REPORTING

Among the questions on national practices regarding IORP reporting of costs to the CA, nearly all reported that IORPs are required to report data on costs to the CA. Most CAs receive IORP costs information based on the annual accounts, which follow national accounting rules and others with respect to costs disclosed to members and prospective members envisaged by IORP II. Some CAs collected more granular broken down costs for supervisory reporting of costs and charges other than annual account or disclosure documents to members and prospective members.

Table 1: Current reporting of cost data to CA		
Type of cost source data/document	Number of CAs	Member States
Costs included in the IORPs' annual accounts	23	AT, BE, DE, DK ES, FI, FR, GR, HR, HU, IT, LI, LU, LV, MT, NL, NO, PL, PT, RO,SE, SI , SK
Breakdown of costs included in the IORPs' Pension Benefit Statements (PBSs)	7	DK, ES, GR, LI, LU, RO, IT
Costs in pre-enrolment documents for prospective members	6	DK, ES, IT, LI, RO, SI
Granular broken down costs for supervisory reporting of costs and charges, other than covered in the three rows above	8	AT, DE, FR, GR, HU, IT, NL, PT
None	2	CY, IE

CAs mentioned a number of reasons for collecting the data, among others for reporting and accounting purposes, statistics, comparative studies, benchmarking and taking supervisory measures.

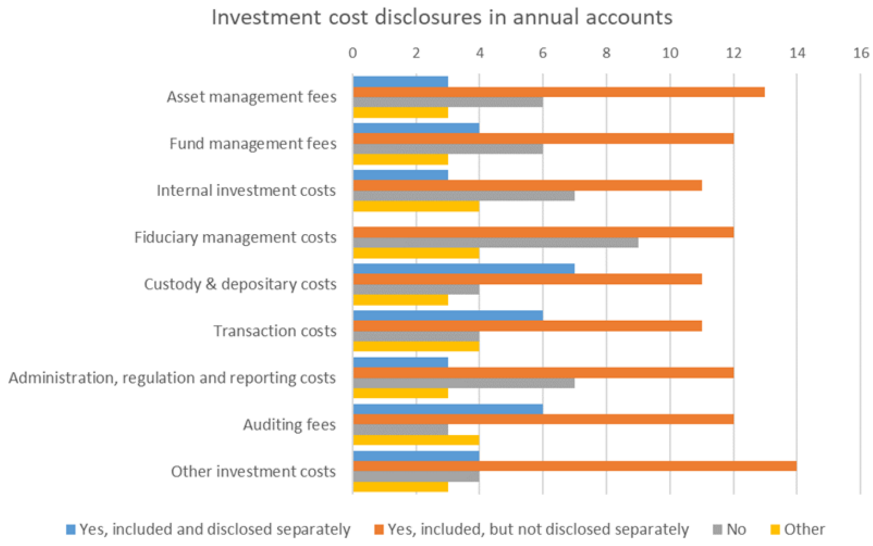
GRANULARITY OF COSTS IN ANNUAL ACCOUNTS AND OTHER DISCLOSURES REPORTING

IORPs' annual accounts are most often subject to national accounting rules, sometimes also established by the CA, which may prescribe detailed uniform rules or a set of minimum requirements.

The level of granularity of the cost data disclosed in the annual accounts differs between (and sometimes within) countries. Some CAs reported that it is aggregated at the level of administrative and investment expenses (BE, DK, ES, FI, LV, MT, NO, SI). Other CAs reported that it is broken down in more detail (AT, DE, FR, GR, HR, HU, IT, LI, NL, PL, PT, SE, SK), while the remaining CAs indicated that another answer is applicable.

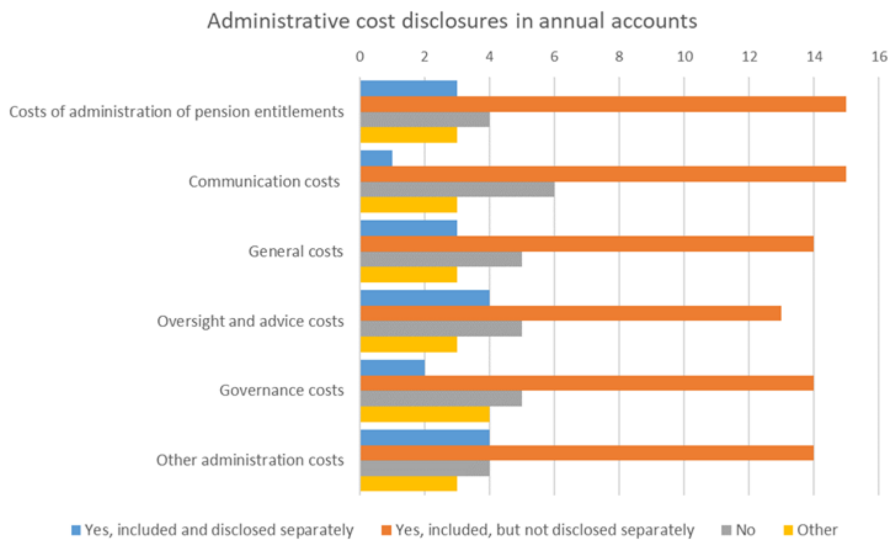
The survey put forward a number of sub-categories of investment costs. CAs were asked whether these are included in the IORPs' annual accounts and whether the sub-categories are disclosed separately. A majority of CAs indicated that these investment cost sub-categories are included, but often these items are not disclosed separately. Many CAs mentioned that investment costs are reported using different definitions and granularity in their annual accounts.

Chart 1: Investment cost disclosures in annual accounts, number of CAs



Most CAs also indicated that the administrative cost sub-categories they were presented with in the questionnaire are included in the annual account, but usually not reported separately or using the same definitions and granularity.

Chart 2: Administrative cost disclosures in annual accounts, number of CAs



Whereas expenses in the annual accounts often distinguish between administrative and investment costs, and often provide more detail, the costs communicated through the pension benefit statement (PBS) often do not make that distinction. In contrast, the reporting to CAs of costs, other than those relating to the annual accounts and information provision to (prospective) members, often distinguishes investment costs (GR, HU, IT, NL, PT) and administrative costs (DE, GR, HU, IT, NL, PT). In NL, investment costs are also reported by asset class.

LOOK-THROUGH AND NO-NETTING APPROACH

Where IORPs invest through collective investment funds or have other indirect exposures, a look-through approach ensures that all costs at the level of these collective investment funds and other indirect exposures are included. The no-netting approach ensures that such costs (e.g. management fees) recognised within cost items and not deducted from income items.

In most Members States, costs reported in the annual accounts and communicated through the PBS are not subject to the look-through and no-netting approach is not applied in the annual accounts. CAs in only five Member States receive cost information from IORPs using a look-through and no-netting approach: ES (PBS data), LV (annual accounts) and HU, IT and NL (other supervisory cost reporting). In FR and LV, cost disclosures in the PBS also follow the look-through and no netting approach, but this cost information is not reported to the CA.

COSTS PAID DIRECTLY BY SPONSORS

In many Member States sponsoring undertakings may directly bear some of the costs of administering the IORP. In a minority of Member States, these costs are recognised in the IORPs' annual accounts, information to plan members or other cost reporting. In eight Member States costs paid directly by the sponsor are included in the reported cost data: NL, NO and MT (annual accounts), LI (annual accounts & PBS data), GR (annual accounts & other supervisory cost reporting), DK and ES (PBS data) and IT (other supervisory cost reporting).

LEVEL OF COST REPORTING: IORP VERSUS SCHEMES

Most CAs answered that the annual accounts disclose cost information at the level of the IORP or, where IORPs provide multiple pension schemes, at the level of the scheme. CAs in DK, GR, HR and SK explained that IORPs do not provide multiple schemes. In AT costs have to be reported at the level of investment- and risk-sharing groups, in IT at the level of investment lines. In BE, FR and LU, expenses have to be disclosed separately for ring-fenced compartments.

Table 2: Level of cost reporting in annual accounts		
Level of cost reporting	Number of CAs	Member States
Always at the level of the IORP, even where IORPs provide multiple schemes	13	BE, CY, DE, DK, ES, HR, LI, LU, NL, NO, PL, PT, SE
At the level of the scheme, where IORPs provide multiple schemes	6	FI, HU, LV, MT, RO, SK
Other	6	AT, FR, GR, IE, IT, SI

Where the annual accounts in the majority of Member States do not disclose expenses at scheme level, cost information in the PBS is most often personalised, where relevant taking into account the member's specific pension scheme.

CONCLUSIONS

Most CAs receive IORP costs information as part of the annual accounts, which follow national accounting rules.

While annual accounts usually include administrative and investment expenses, these details are limited to the direct expenses of the IORP and do not cover indirect costs such as investment and transaction costs that are reflected in the Net Asset Value and therefore hidden. Costs charged directly to an investment fund by asset managers (thus not charged to the IORP) will often lower investment revenues. The same holds true for transaction costs relating to the buying and selling of investment assets. Only five CAs have a transparent view of IORPs' cost level by requiring the supervisory reporting of cost information based on a look-through and no-netting approach.

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European Insurance and
Occupational Pensions Authority

EIOPA-BoS-21/429
07 October 2021

POLICY DEPARTMENT

Opinion on the supervision of long-term risk assessment by IORPs providing defined contribution schemes

1. LEGAL BASIS

1.1. The European Insurance and Occupational Pensions Authority (EIOPA) provides this Opinion on the basis of Article 29(1)(a) of Regulation (EU) No 1094/2010[1]. This article mandates EIOPA to play an active role in building a common Union supervisory culture and consistent supervisory practices, as well as in ensuring uniform procedures and consistent approaches throughout the Union.

1.2. EIOPA delivers this Opinion on the basis of Directive (EU) 2016/2341[2] (the IORP II Directive), in particular in relation to Article 25, Article 28 and Article 49 thereof.

1.3. This Opinion is provided to the competent authorities (CAs), as defined in Article 4(2) of Regulation (EU) No 1094/2010.

1.4. The Board of Supervisors has adopted this Opinion in accordance with Article 2(7) of its Rules of Procedure[3].

2. CONTEXT AND OBJECTIVE

2.1. Due to the ongoing shift from defined benefit (DB) to defined contribution (DC) pension schemes, financial market and longevity risks are increasingly borne by members and beneficiaries. Moreover, operational risk tends to be more immediate for members and beneficiaries of DC schemes compared to DB schemes.[4] This means

[1] Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC, OJ L 331, 15.12.2010, p. 48.
[2] 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), OJ L 354, 23.12.2016, p. 37.
[3] Decision adopting the Rules of Procedure of EIOPA's Board of Supervisors, available at: https://www.eiopa.europa.eu/sites/default/files/publications/administrative/bos-rules_of_procedure.pdf.
[4] See paragraph 3.15-3.20 of EIOPA, Opinion on the supervision of the management of operational risks faced by IORPs, EIOPA-BoS-19-247: https://www.eiopa.europa.eu/sites/default/files/publications/opinions/opinion_on_the_supervision_of_the_management_of_operational_risks_faced_by_iorps.pdf

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a risk-sensitive supervisory approach to DC risk management is necessary to ensure that risks borne by DC IORPs – most notably operational risks – and by members and beneficiaries in terms of future retirement income are appropriately managed and supervised.

2.2. In past occupational pension stress tests applied to IORPs providing 'pure' DC schemes, where all risks are borne by members and beneficiaries, EIOPA assessed the risks of adverse market scenarios on the assets of the IORPs and on the future retirement income of three groups of plan members with varying remaining duration to retirement.[5]

2.3. The IORP II Directive introduced new requirements for IORPs[6] to have in place an effective and well-integrated risk-management system, in accordance with Article 25 thereof. Furthermore, IORPs are required to carry out and conduct their own-risk assessment (ORA), in accordance with Article 28 of that Directive. In particular, where members and beneficiaries bear risks, in accordance with the conditions of the pension scheme, the risk-management system should also consider those risks from the perspective of the members and beneficiaries. The ORA should include an assessment of the risks to members and beneficiaries relating to the paying out of their retirement benefits. Within the supervisory review process, as set out in Article 49 of the IORP II Directive, CAs are required to assess the risks IORPs face and the IORPs' ability to assess and manage those risks.

2.4. The objective of this Opinion is to enhance supervisory convergence in the supervision of risk management by IORPs providing DC schemes, in particular with respect to operational risk assessment and long-term risk assessment from the perspective of members and beneficiaries, in order to foster the protection of members and beneficiaries and improve the functioning of the internal market.

2.5. The aim is to promote efficient and innovative occupational DC schemes with sound investment strategies and risk management that result in optimal long-term risk-return characteristics aligned with the membership structure of the IORP, also in view of the persistent low interest rate environment.

2.6. This Opinion recognises the heterogeneity in occupational DC schemes across Europe. DC schemes feature different risk-mitigation techniques in the accumulation phase and designs of the pay-out phase. DC schemes also differ in respect of the choice they offer. Some DC schemes offer plan members a range of investment options to choose from in accordance with certain retirement needs and risk preferences. Others take a

[5] See for the most recent occupational pensions stress test section 5 of EIOPA, 2019 IORP Stress Test Specifications, EIOPA-BoS-19/157, 29 March 2019: https://www.eiopa.europa.eu/sites/default/files/publications/other_documents/stress_test_specifications.pdf

[6] Including the occupational retirement provision business of life insurance undertakings subject to Article 4 of the IORP II Directive.

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more collective approach, often with an important role for social partners in the design of the scheme and its investment policy.

2.7. The expectations contained in this Opinion should not be interpreted to be comprehensive, covering all aspects of DC risk management. Proper risk management depends on a broad range of factors, starting with the integration of risk management considerations in the IORPs' wider system of governance. In this sense, this Opinion restricts itself to two aspects that are relevant for DC IORPs:

- The use of quantitative elements in operational risk management, supplementing the guidance provided in EIOPA's Opinion on operational risk management[7], which takes a more qualitative approach;
- The use of projections of future retirement income, as part of the long-term risk assessment from the perspective of members and beneficiaries, also in interaction with the determination of their risk tolerance and the establishment of investment strategies.

The long-term risk assessment using pension projections complements the ongoing risk management of DC IORPs to effectively manage risks from the perspective of members and beneficiaries.

2.8. Furthermore, the expectations set out in this Opinion, including those on long-term pension projections, are made in the context of DC IORPs' risk assessment and not in relation to the provision of information to members. Still, the information contained in risk management documents, the statement of investment policy principles (SIPP) and information disclosure documents for members should be consistent.[8]

2.9. EIOPA surveyed existing national practices and gaps among CAs in twenty Member States.[9] In three Member States, national regulation and/or supervisory guidance lays down specific quantitative risk measures for operational risk.[10] In other three Member States, national regulation and/or supervisory guidance specifies how IORPs should conduct DC risk assessment from the perspective of members and beneficiaries

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[7] EIOPA, Opinion on the supervision of the management of operational risks faced by IORPs, EIOPA-BoS-19-247: https://www.eiopa.europa.eu/sites/default/files/publications/opinions/opinion_on_the_supervision_of_the_management_of_operational_risks_faced_by_iorps.pdf

[8] EIOPA, Opinion on the use of governance and risk assessment documents in the supervision of IORPs, EIOPA-BoS-19-245, 10 July 2019, p. 10-11: https://www.eiopa.europa.eu/sites/default/files/publications/opinions/opinion_on_the_use_of_governance_and_risk_assessment_documents_in_supervision_of_iorps_0.pdf

[9] See Annex of the cost-benefit analysis in EIOPA, Impact assessment - Opinion on the supervision of long-term risk assessment by IORPs providing DC schemes, EIOPA-BoS-21-430, 7 October 2021.

[10] In ten Member States, operational risks are borne by DC IORPs through capital requirements, rather than by sponsoring undertakings and/or members and beneficiaries. Often these DC IORPs are subject to the regulatory own funds requirement of the IORP II Directive, which can be interpreted to contain an implicit allowance for operational risk.

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relating to their future retirement income. The Opinion therefore aims to fill gaps in national regulations supplementing the IORP II Directive.

2.10. This Opinion further aims to facilitate risk-based and proportionate supervision of IORPs. In this context, CAs may take into account national specificities of the IORP sector to determine the requirements necessary for implementing this Opinion, applying a risk-based and proportionate approach.[11]

3. SUPERVISION OF DC RISK MANAGEMENT

Definition of DC schemes and scope of application

3.1. CAs should understand DC schemes as occupational pension plans under which the plan sponsor pays fixed contributions and has no legal or constructive obligation to pay further contributions to an ongoing plan in the event of unfavourable plan experience.[12]

3.2. In addition to DC schemes, CAs should also apply this Opinion to other pension schemes where members and beneficiaries bear material risks, taking an approach proportional to the risks. For instance, this could be the case, for pension schemes where the share of assets for which members and beneficiaries bear investment risk is, based on analysis of the CA, material in relation to the guarantees provided.

Forward-looking supervision of DC long-term risk assessment

3.3. To ensure that supervision is based on a forward-looking and risk-based approach, in accordance with Article 47(2) of the IORP II Directive, CAs should assess the risks to which DC IORPs and their members and beneficiaries are exposed to and the ability of DC IORPs to assess and manage those risks. This can be achieved through various supervisory means, such as reviewing the IORPs governance documents and challenging the IORP's management board on the results of their risk assessments and the management of those risks.

3.4. The objective of this Opinion is not to provide comprehensive guidance on all aspects of DC risk management. It supplements and should be read in conjunction with the following opinions EIOPA already issued in the area of governance and risk management, which are also relevant for DC risk management:

- Opinion on the use of governance and risk assessment documents in the supervision of

[11] For further guidance on risk-based and proportionate supervision: EIOPA (2017) A common supervisory culture, https://eiopa.europa.eu/Publications/Speeches%20and%20presentations/A%20Common%20Supervisory%20Culture.pdf

[12] This is in line with the definition used by EIOPA; see Decision on EIOPA's regular information requests towards NCAs regarding provision of occupational pensions information, EIOPA-BoS/18-114, 10 April 2018, which refers to the corresponding OECD definition; https://stats.oecd.org/glossary/index.htm

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IORPs[13], providing an overview of the governance documents required by the IORP II Directive and setting its supervisory expectations with regarding their content, in particular in relation to the IORP's SIPP and the ORA;

- Opinion on the practical implementation of the common framework for risk assessment and transparency for IORPs[14], in so far as IORPs provide DC schemes in which part of the risks is borne by the IORP and/or the sponsor;
- Opinion on the supervision of the management of environmental, social and governance risks faced by IORPs[15], containing supervisory guidance on the integration of ESG risks in the IORPs' risk management;
- Opinion on the supervision of the management of operational risks faced by IORPs, offering supervisory guidance on reviewing the resilience of DC IORPs to operational risks, including outsourcing and cyber risk.

3.5. The latter Opinion emphasises that operational risk events have an immediate impact on members and beneficiaries of DC schemes in terms of accumulated capital and projected future retirement income. Moreover, it draws attention to the emergence of new multi-sponsor IORP providers, increasing the need to clarify operational obligations and to assess operational viability.

Assessment of possible quantitative impact of operational risks

3.6. The Opinion on operational risk management recognises that the frequency and severity of operational risks may be hard to quantify. IORPs perform a multitude of activities – either internally or outsourced to third parties– which may be subject to several types of operational risks. Consequently, good qualitative operational risk management, as substantiated further in that Opinion, is of primary importance and best suited to the different national specificities.

3.7. Given this diversity of operational risks, there is no single algebraic formula or model which could capture overall operational risk. Nevertheless, to gain a better understanding of the possible quantitative impacts, CAs should encourage DC IORPs to estimate the possible impact of operational risk, taking into account risk mitigating

[13] EIOPA, Opinion on the use of governance and risk assessment documents in the supervision of IORPs, EIOPA-BoS-19-245, 10 July 2019.

[14] EIOPA, Opinion on the practical implementation of the common framework for risk assessment and transparency for IORPs, EIOPA-BoS-19-246, 10 July 2019: https://www.eiopa.europa.eu/sites/default/files/publications/opinions/opinion_on_the_practical_implementation_of_the_common_framework_for_risk_assessment_and_transparency_of_iorps.pdf

[15] EIOPA, Opinion on the supervision of the management of environmental, social and governance risks faced by IORPs, EIOPA-BoS-248, 10 July 2019: https://www.eiopa.europa.eu/sites/default/files/publications/opinions/opinion-on-the-supervision.pdf

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mechanisms,.[16] This can be done by means of own custom-made operational risk estimates or by using the standard formulas included in EIOPA's common framework for risk assessment and transparency[17] (see Annex 1).

3.8. A quantification of operational risk exposures allows DC IORPs to gain insight in the adequacy of means to cover the impact of (severe) operational risks. Where members and beneficiaries bear operational risks, as opposed to the IORP itself, IORPs could consider the impact of operational risks on the account values of DC members in the short term and projections of future retirement income in the long term.

Long-term risk assessment in relation to future retirement income

3.9. As part of considering the risks from the perspective of members and beneficiaries in the risk management system, CAs should expect DC IORPs to conduct long-term risk assessments by using projections of members' future retirement income. This involves:

- assessing the risks for members and beneficiaries using projections of future retirement income;
- comparing the results of the risk assessment with the established risk tolerance of the members and beneficiaries;
- mitigating the risks, where risk tolerance limits are exceeded, most notably through adjusting the investment strategy or strategies in case of multiple options.

The above risk assessment framework is also relevant where IORPs provide DC members with a choice of investment options, in particular in situations where there is a default investment option in which DC members are enrolled if they fail to make an active choice. It ensures that the default investment option matches the needs of the membership. The other investment options may be considered to already reflect the risk-return preferences of the DC members because they would have to make an active choice to enrol. Nonetheless, the risk assessment framework will help DC IORPs to design and review a range of investment options that are suitable for the membership, taking into account the members' risk tolerance, also considering that not all DC members may make a well-informed choice.

3.10. The long-term risk assessments using projections of retirement income complement the on-going risk management of DC IORPs, monitoring and assessing the risk limits

[16] For example, external providers for outsourced activities may be subject to capital requirements and/or dispose of insurance cover for operational risk.

[17] See section 4.6 of EIOPA, Principles and Technical Specifications for the Common Framework – Annex 1 to Opinion on the practical implementation of the common framework for risk assessment and transparency for IORPs, EIOPA-BoS-19-246, 10 July 2019: https://www.eiopa.europa.eu/sites/default/files/publications/opinions/annex_to_opinion_eiopa-bos-19-246_technical_specifications_1.pdf

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imposed on investment managers, e.g. bandwidth around strategic asset allocation, tracking error with respect to benchmark and value at risk limits.

3.11. Compared to such short-term risk management, the long-term risk assessment using projections of future retirement income should be conducted less frequently, for example, at the time of conducting the ORA or reviewing the SIPP, or when there is a significant change in the investment policy or risk profile.

Principles for long-term risk assessment using projections of future retirement income

3.12. Taking into account the specificities of DC schemes, CAs should expect DC IORPs to base the projections of future retirement income on the following main principles:

Stochastic and deterministic scenarios of asset returns

3.13. The projections of future retirement income of members and beneficiaries should be based on deterministic or stochastic scenarios of asset returns. The deterministic scenarios may be constructed on a standalone basis, i.e. based on deterministic assumptions about future returns, or based on a number of return paths taken from a stochastic scenario set.

3.14. The use of a stochastic modelling approach[18] has distinct advantages compared to the use of deterministic scenarios[19]. Analysing a large range of scenarios contributes to preventing that certain scenarios are overlooked. Another advantage of stochastic modelling is that it allows IORPs to calculate a wide range of risk (and performance) indicators and to attach probabilities to scenarios, like the 50th or 5th percentile. This helps to interpret and present the results of the risk assessment.

3.15. However, stochastic scenario analysis is more demanding than a deterministic one, both in terms of complexity and resources. IORPs would need to have in-house expertise on stochastic modelling of asset returns and/or acquire stochastic scenario sets from external service providers. Therefore, CAs may also allow the use of deterministic scenarios for pension projections.

3.16. The risk assessment from the perspective of members and beneficiaries should not be restricted to financial market risks, but consider all risks to which DC members are exposed, like – where relevant – longevity risk, inflation risk, counterparty default risk, expense risk operational risk (see paragraph 3.8) as well as ESG risks. However, adding

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[18] See for examples of stochastic modelling approaches EIOPA, Pan-European Personal Pension Product (PEPP): EIOPA's stochastic model for a holistic assessment of the risk profile and potential performance, EIOPA-20-505, 14 August 2020: https://www.eiopa.europa.eu/sites/default/files/publications/eiopa-20-505_pepp_stochastic_model.pdf and OECD, OECD Pensions Outlook 2020 - Selecting default investment strategies, Chapter 4, 7 December 2020: https://www.oecd-ilibrary.org/finance-and-investment/oecd-pensions-outlook-2020_1c7381db-en

[19] See for example of deterministic scenario analysis section 5 of EIOPA, 2019 IORP Stress Test Specifications, EIOPA-BoS-19/157, 29 March 2019.

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non-asset return variables to a stochastic model may increase its complexity. To avoid that, a practical solution would be to combine the stochastic return scenarios with deterministic scenarios for other material risks.

Market-sensitive and realistic assumptions

3.17. To ensure a market-sensitive and risk-based approach to the management of risks from the perspective of members and beneficiaries, the risk assessment should incorporate latest financial market data. This implies that the initial values of DC members' accounts should reflect market prices of assets and that the assumptions underlying future returns should be consistent with market interest rates.[20,21] This ensures a realistic assessment of future returns and risk, by - for example - properly taking into consideration the consequences of a low-interest rate environment.

3.18. Other assumptions determining future returns, not observed in financial markets, should be realistic. Most notably, this applies to the expected risk premiums (over risk-free interest rates) as well as the correlations between the returns on the asset classes considered. The risk premiums and correlations can be based on long-term historical observations of market data. When there is no up-to-date and reliable historical market information available, the risk premiums assumed for the most recent IORP stress test can be a point of reference (see Annex 2). It also means that the projections of future returns should avoid assuming mean reversion in equity returns, i.e. that a fall in equity prices results in higher future risk premiums.[22,23] Current market information on interest rates for long maturities may not be available in deep, liquid and transparent markets. Also in that case, realistic assumptions have to be made by extrapolating current interest rates for shorter maturities or by determining economic long-term equilibrium risk free yields taking into account historical observations.

Characteristics of members and beneficiaries

3.19. The risk assessment should take into account the characteristics of DC members. For

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[20] In term of stochastic modelling, this means that the asset return model should be calibrated to fit the initial term structure of market interest rates.

[21] The application of market-sensitivity principle requires good judgement to avoid that pension projections are based on asset prices and interest rates which are observed during exceptional or stressed market circumstances.

[22] This is in line with EIOPA, PEPP: EIOPA's stochastic model for a holistic assessment of the risk profile and potential performance, EIOPA-20-505, 14 August 2020, p. 4 and EIOPA, 2019 IORP Stress Test Specifications, EIOPA-BoS-19/157, 29 March 2019, p. 36.

[23] The existence of mean reversion is disputed in the academic literature. An issue is that time series for stock market returns cover limited timeframes compared to the horizons in which mean reversion is assumed to materialise. Due to limited number of independent long-term observations, findings of mean reversion tend to be surrounded with considerable parameter uncertainty. Luboš Pástor and Robert F. Stambaugh, Are stocks really less volatile in the long run?, The Journal of Finance, Vol. LXVII, No. 2, April 2012: https://onlinelibrary.wiley.com/doi/pdf/10.1111/j.1540-6261.2012.01722.x show that stock returns are mean diverting when the parameter uncertainty is taken into account, as this uncertainty will compound over time.

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example, the expected retirement age and life expectancy at retirement, which determine the level of future retirement income. DC members' salary and expected salary growth will be needed where contributions into the DC scheme are linked to wages.

3.20. It is not the intention of the risk assessment to make projections for individual members and beneficiaries. Instead, the plan members should be grouped in a way that results in a fair reflection of the risks posed to individuals within the group. At least a number of different age groups should be distinguished in order to take into account the aim of having an equitable spread of risks and benefits between generations in occupational retirement provision, in accordance with recital 57 of the IORP II Directive.

Pension scheme characteristics

3.21. The assessment should take into account the characteristics of the pension scheme, most notably the investment strategy, risk-mitigation techniques, contributions rates over the life-cycle, costs and charges and the characteristics of the pay-out phase.

3.22. Expected future retirement income and surrounding risk will depend to an important extent on the investment strategy and the accompanying risk-mitigation techniques. Broadly three types of risk-mitigation techniques can be distinguished:

- Life-cycling approaches, where the allocation to risk assets is reduced in favour of fixed income assets with DC members getting closer to retirement;
- Buffers to smooth unfavourable and favourable returns over time;
- (Minimum) return guarantees, provided by the IORP or the sponsor.

3.23. The objective of the risk-mitigation techniques is to limit the risk exposure of members and beneficiaries. Conversely, the aim of the risk assessment is to ascertain that the design of the risk-mitigation techniques meets the objective of risks not exceeding the risk tolerance of DC members and beneficiaries.

3.24. Besides investment returns, projected retirement income will be determined by the contributions that are paid into DC members' accounts and the costs and charges that are deducted from investment returns and contributions.[24]

3.25. The design of the pay-out phase also influences the risks in terms of future retirement income. For example, DC members will be subject to interest rate risk before retirement, if accumulated capital will be converted in a life annuity and assets are not fully invested in long-term bonds. As another example, where DC members are entitled to receive lump sum payments, an assessment will have to be made to what

[24] The Opinion on the supervisory reporting of costs and charges of IORPs sets EIOPA's expectations on the transparent compilation and supervisory reporting of administrative and investment costs. See EIOPA, Opinion on the supervisory reporting of costs and charges of IORPs, EIOPA-BoS-21/426, 7 October 2021.

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extent DC members will convert the lump sum in a regular income stream, like a life annuity, variable annuity or programmed withdrawal.

Target variables and risk & performance indicators

3.26. The pay-out phase should inform the choice of target variable for future retirement income, e.g. annuities, scheduled withdrawal or lump sum. The choice should be made with a view to facilitate the interpretation of the risk and performance indicators. The target variable could be future retirement income in euros. It can also be considered to express this as a percentage of the DC members' projected final earnings, especially when setting up a new scheme.

3.27. Appropriate indicators have to be selected to evaluate risk and performance, i.e. considering the trade-off between risk and return. A range of possible indicators exist[25], measuring:

- Performance, e.g. projected retirement income in a median (50th percentile) or favourable scenario (75th / 95th percentile) and the probability to reach a given ambition;
- Risk, e.g. projected retirement income in an unfavourable scenario (25th / 5th percentile), dispersion of income, expected loss and the probability of not reaching some lower level of retirement income.

3.28. Where deterministic scenarios are used without any underlying stochastic return modelling, it will be difficult to define objective risk indicators based on a probability distribution. Still, it would be possible to establish a best estimate scenario (as a measure of expected performance) and one or more adverse scenarios with low interest rates/returns (to measure risk).

3.29. The weights attached to the indicators will depend on the IORPs' objectives and, ultimately, the preferences of the members. In the end, the aim is to relate the risk and performance indicators to the established risk tolerance of members and beneficiaries.

Risk tolerance of members and beneficiaries

3.30. CAs should expect IORPs to establish the risk tolerance of their members by using appropriate methodologies, recognising the specificities of IORPs and the different approaches. The methodologies should distinguish between different generations/cohorts, given possible differences in risk tolerance.

3.31. The risk tolerance of members and beneficiaries can be understood as consisting of at least two components:

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[25] See for a discussion of risk and performance indicators section 3 and 4 of EIOPA, Pan-European Personal Pension Product (PEPP): EIOPA's stochastic model for a holistic assessment of the risk profile and potential performance, EIOPA-20-505, 14 August 2020 and section 4.1 of OECD, OECD Pensions Outlook 2020 - Selecting default investment strategies, Chapter 4, 7 December 2020.

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- The extent to which DC members want to avoid taking risk, which depends on their risk-return preferences;
- The extent to which DC members are able to bear risk, which depends on other sources of retirement income, including human capital (i.e. future earnings capacity) housing wealth and private savings.

3.32. There are broadly speaking two methods to establish the risk tolerance of DC members from an ex ante perspective[26]:

- Analysing internal and external data sources, such as internal data on members' profiles (age, income, education level etc.) and relevant scientific literature (e.g. on financial versus human capital)
- Approaching DC members directly, e.g. surveys, including self-assessment questionnaires to assist prospective members choosing an investment option, or panels, or indirectly through representatives of DC members.

3.33. The first method would be particularly suitable to assess DC members' capacity to bear risk, while the second method would be more suitable to gauge members' preferences on taking risks.

3.34. From an ex post perspective, offering a range of investment options can reveal risk-return preferences of plan members who make an active choice, especially in combination with self-assessment questionnaires to support them in their decisions.

Design and review of investment strategy

3.35. CAs should expect IORPs to consider the long-term risk assessment from the perspective of members and beneficiaries in the design and review of the investment strategy, or strategies in the event of multiple investment options, taking into account their risk tolerance.

3.36. To ensure that the investment policy is geared to the membership structure of the IORP, in line with recital 45 of the IORP II Directive, the design and review process should at least consider whether the investment strategy in terms of its risk-return characteristics is aligned with the risk tolerance of a number of different age groups.

3.37. The review of the investment strategy can take place during the periodical review of the SIPP and the conduct of the ORA.[27,28]

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[26] See also section 6 ("Membership structure in the investment policy") in Annex 1 of EIOPA, Opinion on the use of governance and risk assessment documents in the supervision of IORPs, EIOPA-BoS-19-245, 10 July 2019.

[27] The SIPP and the ORA have to be carried out at least every three years or whenever there is a significant change in the investment policy or the risk profile, in accordance with Article 28 and Article 30 of the IORP II Directive, in this case from the perspective of members and beneficiaries.

[28] It may not always be possible to adjust the investment strategy, e.g. if the investment strategy is contractually agreed with members and beneficiaries.

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Reporting and disclosure

3.38. CAs should expect DC IORPs to report on the long-term risk assessment from the perspective of members and beneficiaries in their:

- ORA results report, explaining the assumptions, methodology and results of the risk assessment from the perspective of members and beneficiaries, how the results compare to the established risk tolerance and any mitigating measures taken;
- SIPP, explaining how the investment policy takes into account the results of the risk assessment from the perspective of members and beneficiaries and their risk tolerance.

3.39. Where the social partners bear (part of the) responsibility for the design of the DC scheme and its investment policy, the outcomes of the risk assessment should also be shared and discussed with them.

Proportionality

3.40. CAs should determine the frequency and depth of their supervision of DC IORPs' risk management, taking into account their supervisory priorities and prudential objective of protecting the rights of members and beneficiaries and ensuring the stability and soundness of IORPs, as well as a proportionate application of the rules relating to the risk management of DC IORPs.

4. MONITORING BY EIOPA

4.1. Two years following the publication of this Opinion, EIOPA will look into the supervisory practices of the CAs with a view to evaluate supervisory convergence.

4.2. This Opinion will be published on EIOPA's website.

Done at Frankfurt am Main, on 30 September 2021.

[signed]

For the Board of Supervisors
Petra Hielkema
Chairperson

ANNEX 1: VALUE AT RISK MEASURE FOR OPERATIONAL RISK

The below value at risk measures for operational risk are based on EIOPA's common framework for risk assessment and transparency. The measures relate to the IORP's gross risk, i.e. without taking into account to what extent the value at risk is borne by sponsors (security mechanism) and members and beneficiaries (benefit adjustment mechanisms) as well as other risk-mitigating mechanisms. To obtain the IORP's net exposure to operational risk, the extent to which the losses can be absorbed by the sponsor, members and beneficiaries and other risk-mitigating mechanisms will have to be estimated.

Value at risk for pure DC schemes

The value at risk for operational risk of pure DC schemes calibrated to a 0.5% probability of occurrence within a one-year horizon equals:

$$VaR_{Op} = 25\% \cdot Exp_{DC}$$

where:

Exp_{DC} denotes the amount of expenses incurred during the previous 12 months in respect of pension obligations of DC schemes where the investment risk is fully borne by members and beneficiaries.

Value at risk for other schemes (where members and beneficiaries bear material risk)

The value at risk for operational risk of other schemes calibrated to a 0.5% probability of occurrence within a one-year horizon equals:

$$VaR_{Op} = \min(1.2\% \cdot TP; Op)$$ [29]

where:

TP denotes technical provisions for pension obligations in other schemes;

Op denotes basic value at risk for operational risk.

The basic value at risk for operational risk should be calculated as follows:

$$Op = \max(Op_{contributions}; Op_{provisions})$$

where:

$Op_{contributions}$ denotes the value at risk for operational risks based on contributions received;

$Op_{provisions}$ denotes the value at risk for operational risk based on technical provisions.

The value at risk for operational risks based on contributions received should be calculated as follows:

$$Op_{contributions} = 4\% \cdot Contr_t + \max\left(0; 4\% \cdot \left(\frac{(Contr_t - Contr_{t-1})}{Contr_{t-1}} - 20\%\right) \cdot Contr_{t-1}\right)$$

where:

[29] In EIOPA's common framework for risk assessment and transparency the first term between parentheses is equal to 30% of the basic standardised value at risk (BVaR), which comprises the aggregate VaR of all risks, except operational risk. To ease the calculation, the BVaR has been replaced by 4% of technical provisions, line with the regulatory own funds requirement in the IORP II Directive.

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$Contr_t$ denotes the contributions received during the last 12 months for pension obligations in other schemes;

$Contr_{t-1}$ denotes the contributions received during the 12 months prior to the last 12 months for pension obligations in other schemes.

The value at risk for operational risk based on technical provisions should be calculated as follows:

$Op_{provisions} = 0.45\% \cdot TP$

where:

TP denotes the technical provisions for pension obligations in other schemes.

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ANNEX 2: RISK PREMIUMS SPECIFIED IN EIOPA'S 2019 IORP STRESS TEST

The table below displays the risk premiums prescribed in the 2019 IORP stress test specifications. The risk premiums on government and corporate bonds are based on EIOPA estimates for long-term average spreads minus the costs of default/downgrade. This so-called fundamental spread is the part of the credit spread that does not constitute a compensation for risk. The risk premium on non-fixed income assets is assumed to be equal to 3%, the risk premium on cash and deposits is assumed to be equal to zero.[30]

Risk premiums	
Fixed incomes risk premiums over risk-free interest rate	
Government bonds	28 basis points
Corporate bonds (and other fixed income excl. cash and deposits)	86 basis points
- non-financial	56 basis points
- financial	101 basis points
Non-fixed income risk premium over risk-free rate	
Equities, property, alternatives and other non-fixed income	300 basis points
Cash and deposits risk premium over risk-free rate	
Cash and deposits	0 basis points

[30] See for further information section 5 of EIOPA, 2019 IORP Stress Test Specifications, EIOPA-BoS-19/157, 29 March 2019.

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Impact assessment

Opinion on the supervision of long-term risk assessment by IORPs providing defined contribution schemes

Policy Department
EIOPA-BoS-21/430
07 October 2021

European Insurance and Occupational Pensions Authority

CONTENTS

1. ANALYSIS OF COSTS AND BENEFITS

1.1. Procedure and consultation of stakeholders

According to Article 29 of the Regulation (EU) 1094/2010, EIOPA should, where appropriate, analyse the potential costs and benefits relating to opinions provided to CAs, proportionate to their scope, nature and impact.

In developing the opinion, EIOPA analysed current practices at national level through a survey completed by CAs and engaged with stakeholders including the Occupational Pensions Stakeholder Group, most notably through a workshop held on 22 January 2021.

A draft Opinion and its costs and benefit analysis have been subject to a public consultation, in line with Article 29 of the Regulation (EU) 1094/2010.

The analysis of costs and benefits is undertaken according to EIOPA's impact assessment methodology.

1.2. Problem definition

When analysing the impact from proposed policies, the impact assessment methodology foresees that a baseline scenario is applied as the basis for comparing policy options. This helps to identify the incremental impact of each policy option considered. The aim of the baseline scenario is to explain how the current situation would evolve without additional supervisory intervention

The IORP II Directive introduced new risk-management requirements. In particular, where members and beneficiaries bear risks, the risk-management system as set out in Article 25 thereof should also consider the risks from the perspective of members and beneficiaries. The ORA, set out in Article 28 of the IORP II Directive, should include an assessment of the risks to members and beneficiaries relating to the paying out of their retirement benefits. Recital 57 of the IORP II Directive explains that it is essential that IORPs improve their risk management while taking into account the aim of having an equitable spread of risks and benefits between generations in occupational retirement provision.

The IORPs' assets should be invested in accordance with the 'prudent person' rule and in particular in the best long-term interest of members and beneficiaries as a whole, in accordance with Article 19 of the IORP II Directive. Compliance with the prudent person therefore requires an investment policy geared to the membership structure of the individual IORP, as set out in recital 45 of the IORP II Directive.

The ORA should also include a qualitative assessment of operational risks. EIOPA issued an Opinion on the supervision of the management of operational risks faced by IORPs, offering supervisory guidance on reviewing the resilience of DC IORPs to operational risks, including outsourcing and cyber risk.

Member States may supplement the IORP II Directive through national regulation or supervisory guidance. The survey conducted by EIOPA demonstrated that only a handful of Member States' national measures specify how IORPs should conduct DC risk assessments from the perspective of members and beneficiaries relating to their future retirement income, also in relation to establishing their risk tolerance and designing and reviewing the investment strategy (see Annex 1). Even though a number of Member States had not yet decided to put in place supplementary measures, this implies that the provisions of the IORP II Directive may potentially not have been implemented consistently. In particular, DC IORPs' investment strategies may not be aligned with the risk tolerance of their membership, considering a long-term risk assessment using projections of future retirement income, jeopardising the protection of members and beneficiaries.

Similarly, the survey results showed that, in a few Member States, national regulation and/or supervisory guidance lay down specific quantitative measures for operational risk. Good qualitative management of the wide range of potential operational risks, in line with EIOPA's Opinion on operational risk management by IORPs, is essential. The quantification of operational risk exposures would allow DC IORPs to gain insight in the adequacy of means to cover for the impact of (severe) operational risk. Operational risk events may have an immediate impact on members and beneficiaries of DC schemes, as opposed to DB schemes, in terms of accumulated capital and projected future retirement income. Moreover, new for-profit, multi-sponsor IORP providers are emerging, increasing the need to clarify operational obligations and to assess operational viability.

1.3. Objective

The objective of this Opinion is to enhance supervisory convergence in the supervision of risk management by IORPs providing DC schemes, in particular with respect to operational risk assessment and long-term risk assessment from the perspective of members and beneficiaries, in order to foster the protection of members and beneficiaries and improve the functioning of the internal market.

The aim is to promote efficient and innovative occupational DC schemes with sound investment strategies and risk management that result in optimal long-term risk-return characteristics aligned with the membership structure of the IORP, taking into account the heterogeneity in occupational DC schemes across Europe.

1.4. Policy issue and options

EIOPA has identified as policy issue the inconsistent supervisory approaches to DC IORPs' use of quantitative elements in operational risk management and long-term risk assessment from the perspective of members and beneficiaries, also in relation to the establishment of their risk tolerance and the design and review of investment strategies.

A more consistent supervisory approach will not only enhance the protection of members and beneficiaries, but also contribute to improving international supervisory coordination, encouraging cross-border activity, as well as reducing regulatory arbitrage.

To meet the objectives set out in the previous section, EIOPA has analysed two policy options to address the identified policy issue, with the preferred option highlighted in bold:

1. **Principle-based approach to the use of quantitative measures for operational risk and the risk assessment from the perspective of members and beneficiaries using pension projections, also in interaction with the determination of their risk tolerance and the establishment of investment strategies;**
2. Uniform approach to the use of quantitative measures for operational risk and the risk assessment from the perspective of members and beneficiaries using pension projections, also in interaction with the determination of their risk tolerance and the establishment of investment strategies.

In both options, the expectations towards CAs would not only relate to IORPs providing DC schemes, but to all IORPs where members and beneficiaries bear material risks, where materiality is determined based on an analysis by the CA.

POLICY OPTION 1: PRINCIPLE-BASED APPROACH

Under the principle-based approach, CAs are expected to encourage DC IORPs to quantify operational risk exposures in terms of asset value losses, using their own risk estimates or the standard formulas based on EIOPA's common framework on risk assessment and transparency.

In addition, CAs should expect DC IORPs to use projections of future retirement income to assess the risks from the perspective of members and beneficiaries. The pension projections may be based on deterministic or stochastic scenario of asset returns. In the EEA's four largest IORP sectors (DE, IE, IT, NL) representing 90% of the total IORP sector in terms of assets, IORPs already conduct deterministic or stochastic projections for the purpose of risk assessment and/or information provision to plan members through the annual Pension Benefit Statement.

This option sets forth a number of high-level principles for conducting the pension projections, including on the consideration of the characteristics of the membership and the pension scheme. The assumptions underlying pension projections should be market-consistent and realistic to ensure that projected investment returns are not overstated nor understated. Moreover, appropriate risk and performance indicators have to be selected for the risk assessment, so that the indicators fit the national specificities.

CAs should expect DC IORPs to establish the risk tolerance of their membership to assess the outcomes of the risk assessment. This option prescribes that appropriate methodologies are used, at least distinguishing between different generations/cohorts, taking into account different national approaches and methods.

Lastly, CAs should expect DC IORPs to integrate the risk assessment from the perspective of members and beneficiaries - in conjunction with the established risk tolerance - in the design and review of DC IORPs' investment strategies.

Policy option 1: Principle-based approach		
Stakeholder groups	**Benefits**	**Costs**
IORPs	IORPs will benefit from more consistent approaches across the EEA, where relevant, fostering equal conditions of competition.	The investment and risk management functions, and potentially other functions, will require additional resources and/or more services will have to be sourced from external providers. In particular, this will be the case for IORPs not already doing similar risk assessments to inform the design and review of investment strategies. The fact that most IORPs already have experience with

		deterministic or stochastic projections limits these costs.
Members and beneficiaries	Enhanced protection of members and beneficiaries by ensuring a design of investment strategies that is aligned with the risk-return preferences of the membership, considering a risk assessment of future retirement income based on realistic assumptions. In particular, this will be the case for the membership in IORPs not already doing such an assessment.	The additional costs on IORPs may be shifted to members and beneficiaries (and also sponsoring undertakings).
Competent authorities	Convergence of supervisory approaches across the EEA will reduce regulatory arbitrage. It will also facilitate international supervisory coordination, thereby promoting cross-border activity.	CAs will have to bear the costs of implementing and supervising the expectations in national supervision.

POLICY OPTION 2: UNIFORM APPROACH

Under the uniform approach, CAs should expect DC IORPs to quantify operational risk exposures in terms of asset value losses using the standard formulas based on EIOPA's common framework on risk assessment and transparency.

In addition, CAs should expect DC IORPs to use projections of future retirement income to assess the risks from the perspective of members and beneficiaries, where he pension projections should be based on stochastic scenarios of asset returns.

This option puts forward principles for conducting the stochastic pension projections, such as the consideration of the characteristics of the membership and the pension scheme, but also specifies the term structure of risk-free interest rates and the maximum risk premiums to be assumed. Moreover, specific risk and performance indicators would be prescribed for the risk assessment, for example, similar to the requirements for the PEPP (Article 14 of the Commission Delegated Regulation (EU) 2021/473[1]):

- The risk defined as the shortfall between the projected sum of contributions and the accumulated assets at retirement in a 5th percentile adverse scenario;
- The return defined as the probability of outperforming the projected inflation rate during the accumulation phase.

The expectation of using stochastic scenarios, prescribing interest rate term structures and maximum risk premiums as well as specifying specific risk and performance indicators would admittedly result in strong supervisory convergence, as well as cross-sectoral consistency with PEPP. However, it will also imply that many IORPs would have to modify existing practices. For example, IORPs already tend to make scenario-based projections of future retirement, but often using deterministic scenarios and not stochastic scenarios. Moreover, the specific risk and performance indicators are likely to conflict with currently used indicators at the national level.

Under this option, CAs should also expect DC IORPs to establish the risk tolerance of their membership using surveys be completed by members and beneficiaries, in order to assess the outcomes of the risk assessment and to support the design and review of investment strategies. Such a uniform approach would results in higher supervisory consistency, but also increase the likelihood of clashing with existing national practices.

Policy option 2: Uniform approach		
Stakeholder groups	**Benefits**	**Costs**
IORPs	IORPs will benefit from uniform approaches across the EEA, where relevant, fostering equal conditions of competition. IORPs providing PEPPs will benefit from consistency with	The investment and risk management functions, and potentially other functions, will require additional resources and/or more services will have to be sourced from external providers. In particular, this

[1] Commission Delegated Regulation (EU) 2021/473 supplementing Regulation (EU) 2019/1238 of the European Parliament and of the Council with regard to regulatory technical standards specifying the requirements on information documents, on the costs and fees included in the cost cap and on risk-mitigation techniques for the pan-European Personal Pension Product, OJ L 99, 22.3.2021, p. 1.

	Commission Delegated Regulation (EU) 2021/473.	will be the case for IORPs not already doing similar risk assessments to inform the design and review of investment strategies. A considerable group of IORPs will have to make stochastic projections, instead of the current practice of deterministic projections. Moreover, a substantial group of IORPs will have to adjust their approach to establishing the membership's risk tolerance.
Members and beneficiaries	Enhanced protection of members and beneficiaries by ensuring that IORPs are expected to quantify operational risk exposures and perform long-term risk assessment using stochastic pension based on realistic and uniform assumptions. In conjunction with the establishment of their risk tolerance, this ensures investment strategies are aligned with the risk-return preferences of the membership, especially where IORPs are not already considering such risk assessments in the design and review of investment strategies.	The additional costs on IORPs may be shifted to members and beneficiaries (and also sponsoring undertakings).

Competent authorities	Uniform supervisory approaches across the EEA will significantly reduce regulatory arbitrage. It will also facilitate international supervisory coordination, thereby promoting cross-border activity.	CAs will have to bear the costs of implementing and supervising the expectations in national supervision.

1.5. Conclusion

EIOPA considered two policy options to reach supervisory convergence with regard to the use of quantitative elements in operational risk management and long-term risk assessment from the perspective of members and beneficiaries: a principle-based (option 1) and a uniform approach (option 2). Policy option 1 is EIOPA's preferred option in terms of cost and benefits.

The principle-based approach strikes the best balance between enhancing protection of members and beneficiaries and limiting the costs for IORPs. This is in line with the aim to promote the provision of efficient occupational DC schemes with sound investment strategies and risk management that result in optimal long-term risk-return characteristics aligned with the membership structure of IORPs.

The uniform approach may deter the provision of occupational DC schemes by imposing risk assessment methods which result in considerable adjustment costs for IORPs and may even not fit national specificities. Even though some of the uniform methods, e.g. stochastic projections, may be technically superior, the potential discouragement of occupational pension provision would not be in the best interest of members and beneficiaries. These costs likely outweigh the potential benefits of a uniform approach in terms of the functioning of the internal market, e.g. preventing regulatory arbitrage and stimulating cross-border provision.

ANNEX: SUMMARY OUTCOMES OF SURVEY OF NATIONAL PRACTICES AND GAPS

RESPONSE

EIOPA conducted a survey among CAs in the third quarter of 2020 to map existing practices and gaps at national level relating to DC risk assessment.

All CAs responded to the survey. Twenty CAs responded to the specific questions on DC risk management, while ten CAs did not complete these questions because DC IORPs are largely absent (BE, DK, FI, LI, MT) or IORPs are largely non-existent (BG, CZ, EE, IS, LT).

Most CAs indicated that no further level 2 measures, e.g. regulations, (14 CAs) or level 3 measures, e.g. supervisory guidance, (12 CAs) supplementing the IORP II Directive were foreseen in the area of DC risk management. At the time, over one-third of CAs responded that further level 2 (CY, FR, HR, IE, LV, NO, PL, PT, SK) and/or level 3 measures (CY, FR, HR, IE, LU, NO, PL, PT, SK) have not yet been decided. In a few Member States further national regulations (GR, IT) and supervisory measures (DE, GR, IT, SK) in the area of DC risk assessment were still expected.

QUANTITATIVE MEASURES FOR OPERATIONAL RISK

In half of the Member States where the CA completed the survey (DE, FR, HR, HU, LU, NO, PT, RO, SE, SK) operational risks are borne by DC IORPs or their management companies through capital requirements (see Chart 1). Often these DC IORPs are subject to the regulatory own funds requirement of the IORP II Directive, which can be interpreted to contain an implicit allowance for operational risk. In other Member States, operational risks in DC schemes are borne by members and beneficiaries (AT CY, IT), the sponsoring undertaking (ES, LU) or by a combination of the IORP and members and beneficiaries (NL, SI) or the sponsor and members and beneficiaries (GR, PL). In IE, the party responsible for the operational failure would ultimately typically cover any loss e.g. investment manager, advisor, administrator, sponsor (on behalf of themselves or the trustees).

In three Member States (AT, NO, SE), national rules lay down specific quantitative risk measures for operational risk (see Chart 2), of which in two Member States derived from the operational risk module of the standard formula in Solvency II (NO, SE). In most Member States this is not the case or was not decided yet.

Chart 1: Operational risk bearers in IORPs providing DC schemes, number of CAs

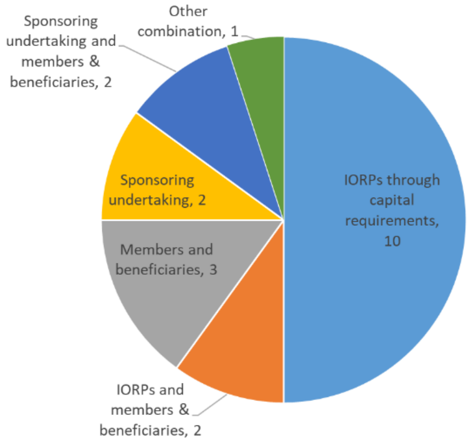
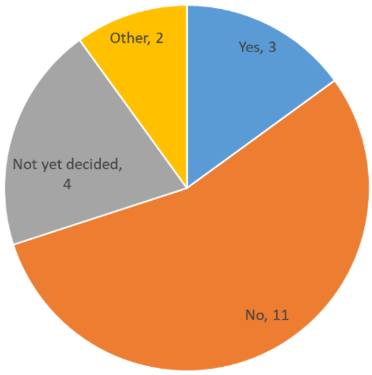


Chart 2: Quantitative measures for operational risk in national regulation and/or supervisory guidance, number of CAs



RISK ASSESSMENT FROM THE PERSPECTIVE OF MEMBERS AND BENEFICIARIES

Three out of 20 CAs (AT, DE, NL) indicated that national regulation and guidance specify how IORPs should implement DC risk assessment from the perspective of members and beneficiaries relating to their future retirement income (see Chart 3), as prescribed by Article 25 (Risk management) and Article 28 (Own-risk assessment) of the IORP II Directive. Still, in four Member States (AT, GR, LV, NL), CAs expect DC IORPs to assess – as part of their risk management - the risk from the perspective of members and beneficiaries using pension projections (see Chart 4).

Of the Member States where DC IORPs are expected to use pension projections as part of their DC risk management, only in NL, national regulation and supervisory guidance impose restrictions on the assumptions underlying the projections, like the type of scenarios and the return assumptions. The CA in NL provides IORPs with a pre-defined set of 10,000 stochastic scenarios containing trajectories for interest and inflation rates as well as asset returns.

Chart 3: National regulation and guidance supplementing the IORP II Directive with regard to risk assessment from the perspective of members and beneficiaries, number of CAs

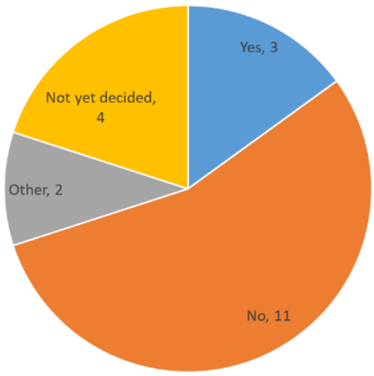
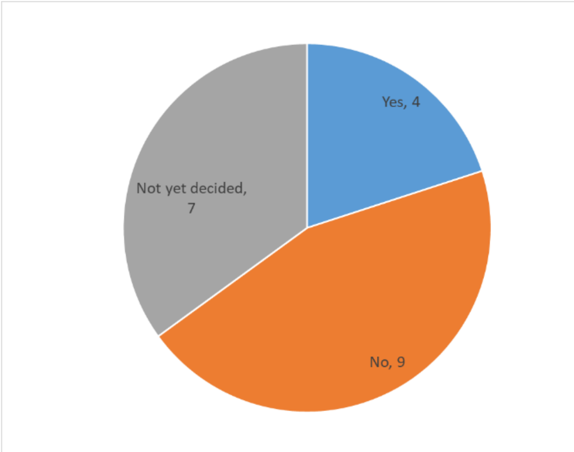


Chart 4: Expectation towards DC IORPs to assess within their risk management the risk from the perspective of members and beneficiaries using pension projections, number of CAs



In four Member States (AT, CY, IT, NL), national regulations and supervisory guidance contain provisions for DC IORPs to consider and/or establish the risk tolerance of members and beneficiaries (see Chart 5). In most other Member States, this is not the case or has not been decided yet. This does not necessarily mean that DC IORPs do not consider the risk tolerance. CAs were asked how DC IORPs established the risk tolerance of members and beneficiaries. While most CAs did not have experience in this regard, some provided examples. CAs explained that the DC IORP's investment portfolio considered the overall risk tolerance of the membership that life-cycling strategies reflected differences in risk aversion between younger and older plan members and/or that a choice of investment option aligns the risk-return characteristics with members' preferences. Methods to establish the (ex-ante) risk tolerance included member panels and surveys, including self-assessment questionnaires to assist prospective members in choosing an investment option, the use of member administration / socio-demographic data and the implicit or explicit establishment of the risk tolerance through social partners.

In five Member States (AT, CY, IT, LU, NL) national regulation or guidance contain provisions stipulating that the investment policy or strategy has to consider the interaction between the risk assessment from the perspective of members and beneficiaries and their risk tolerance (see Chart 6). In most other Member States, this is not the case or has not been decided yet. Still, nearly half of CAs (AT, CY, GR, HU, IT, LV, NL, NO, SE) indicate that DC IORPs typically determine the investment strategy taking into account the risk assessment from the perspective of members and beneficiaries and their risk tolerance, while the other half of CAs responded that this is usually not the case.

Chart 5: National regulation and guidance containing provisions to consider/establish the risk tolerance of DC members and beneficiaries, number of CAs

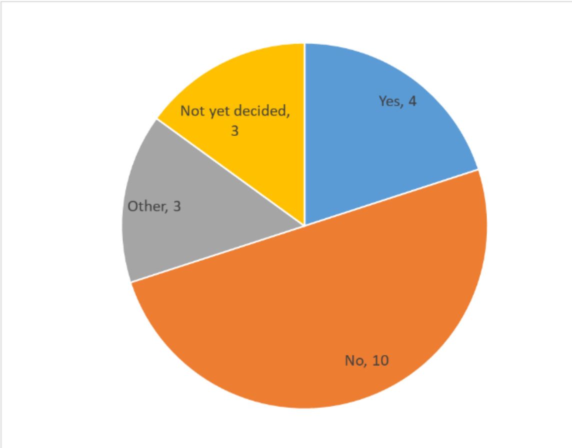
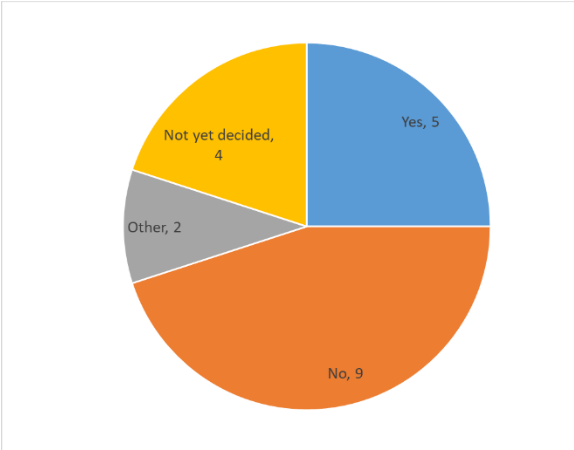


Chart 6: National regulation and guidance specifying the interaction between the risk assessment from the perspective of DC members and beneficiaries, their risk tolerance and investment strategy, number of CAs



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