

EIOPA PPP consultation – FSUG response

General comments from FSUG

While FSUG welcomes EIOPA's consultation on PPPs, we wish to make clear that this is only a second best option compared to the much more preferable and effective Pan-European Personal Pension product approach (PEPP). We doubt that any meaningful harmonisation of the myriads of PPP regulatory regimes within the EU could happen any time soon. But the pension issue is a ticking time bomb of tremendous magnitude, so time is of essence, and no further delay should be allowed for the completion of a common market for personal pensions in the EU. Only a PEPP approach can achieve this.

As the successful experience of the UCITS funds (the only Pan European retail investment product so far – almost 60 years after the Treaty of Rome which was supposed to provide for a common market in products, services and capital) shows, the only realistic and effective approach is a Pan-European PP Regulation.

Q1: Would PPPs benefit from harmonisation of provider governance standards? What should be the basis for provider governance standards for PPPs? Do you agree with EIOPA's proposals?

FSUG fully support the EIOPA's proposals on the harmonization of providers' governance standards as pointed out in CP, pages 15 to 25 and following Annexes VI and VII. PPPs are often sold on individual basis as a product to a client, who in reality does not understand the governance processes behind the product. Governance processes should be therefore materialized in a way, that a NCAs have full understanding of provider operations and client is able to see the results of high-quality management through transparency and disclosure requirements. This approach should be harmonized fully to bring the necessary trust into long-term savings products like PPPs.

Looking closer on particular governance aspects, it should be noted, that the product should be in the centre of interest, both for provider as well as for NCA. It is the product, which is bought by consumer and the consumer-product centric governance standards should be preferred. When considering various governance processes (especially risk management, safeguarding, actuary services, asset management services, internal as well as external audit, depositary services, distribution services), there should be a person delegated on the side of a provider, who is deemed responsible for each particular aspect. The names of persons responsible for particular governance areas should be disclosed to the public and tied to the product. This is the way, how the product is not anonymous on the side of a provider and this approach could lead to a closer relationship between the client and provider, notwithstanding the ability of such approach to increase the trust in such products.

On the side of outsourcing services, it is obvious from the experience of many countries, that outsourcing is not only the way how to decrease the costs of PPPs, but on the other side, it is the way how to shift responsibility for the outcomes to a third party. Therefore, any outsourcing services should not lead to the diminishing of the responsibility of a main provider for the outcome of outsourced services and a PPP as such.

International standards for governance of pension products as presented in annex VII could

be a good starting point for further clarification of rules. However, FSUG thinks, that their application should not create uneven conditions for different providers as the clients consider and buy the product and not the providers.

PPPs should be viewed as an ongoing contract and not one-off sale. Governance standards should acknowledge this long-term relationship between client and provider in the area of strong disclosure and information requirements based on EIOPA's layering approach. Inclusion of PBS requirements as suggested by international standards and many research studies should positively contribute to the wider development of high-standard trustworthy products and providers as well. Therefore, FSUG thinks that in order to develop a truly "good governance" standards, sanctions regime, as well as unified (or at least understandable) reporting requirements and obligations with regard to product information before, during and after the contractual relationship between consumer and PPP provider allowing for comparison of products should be implemented.

Additionally, it should be mentioned that one of the new governance standards that accept the role of a client in the whole process is the recognition of the switching. As the PPP is long-term contract, client should have the right to switch to another PPP if the performance or the governance level is weak. This would allow not only NCAs but directly clients to put indirect pressure on non-complying or poorly performing providers to improve their operations.

Q2: Would PPPs benefit from harmonisation of product governance rules? What should be the basis for product governance rules for PPPs? Do you agree with EIOPA's proposals?

EIOPA's proposal is well balanced and provides a solid ground that encompasses existing and more importantly functional rules. FSUG welcomes proposed strong Consumer-Centric Approach pointed out in EIOPA's CP on page 48. Accompanying consumer-centric approach with strong product oversight and governance rules could lead to an overall higher standard for PPPs. It constitutes a useful and necessary clarification of EIOPA's preparatory POG Guidelines on product oversight and governance arrangements by insurance undertakings and insurance distributors in October 2015 and POG requirement outlined in annex VIII of the CP (page 108).

FSUG emphasises a strong pre-sale testing of the product oriented on increasing the consumer protection. Having in mind the long-term commitment of a client, only PPPs that have a clear positive value-for-money should be recommended by NCAs. At the same time, the rules for pre-sale testing could serve as a benchmarking procedure not only for providers, but for consumer organizations as well. This could strengthen the self-managing processes on the market with clear support from NCAs and EIOPA as well.

Recognition of existence of behavioural biases within financial products decision-making process on the side of consumers is a positive step forward. FSUG thanks EIOPA for including this highly relevant area into the consideration described in the CP on pages 28 and following. Creating rules that accept layering of information designed specifically for each of all three phases the client undergoes during the contract duration could really contribute to the "good product design" process. In this respect, EIOPA has identified many important information rules for each phase (pre-contractual, on-going, pre-retirement) we fully support. In general, using KID PRIIPs for PPPs could become a good starting point, if few additional rules on PBS are added.

Specific rules oriented on the saving process that increase the awareness and understanding of the product materialized in the PBS will be also positively viewed by consumers. FSUG thinks that having a rule requiring providers to regularly provide information on the status of client's savings with a looking-forward feature could increase the trust in PPPs and might bring the necessary recognition of long-term and pension savings.

Taking into account that consumers have many short and long-term savings and insurance products, it would be worth paying more attention to the additional on-line services tied to the product that increase the information and understanding of the product. Having an on-line access to the individual pension account could rapidly decrease the costs of disclosure and information requirements. On-line accounts should have at least passive access where the client is able to see and download layered information including the PBS. Several countries (including Netherlands, Slovakia, Romania, Bulgaria, Croatia, Sweden) have adopted provisions to support digitalized and on-line features of PPPs (notwithstanding the 1bis pillar pension products of individualized retirement accounts that fall under the SLL).

Q3: Would PPPs benefit from harmonisation of distribution rules? What should be the basis for distribution rules for PPPs? Do you agree with EIOPA's proposals?

Harmonisation of distribution rules for PPPs should be based on a recognition of consumer-centric approach and acknowledgment of cognitive biases. Negative experience in many central and eastern European countries with unit-linked insurance products provides explicit examples of wrong approach towards regulation of distribution processes. Mis-selling of such products where no consumer appropriateness tests have been performed give a warning sign for NCAs and EIOPA and put a lot of expectations on implementing a high-standard harmonized approach for distribution rules.

EIOPA's POG requirements presented in Annex VIII of this CP (pages 108 – 110) present a very valid introduction into the debate and technical details on distribution rules. Combining the ideas with provision set in MiFID II and IDD could serve also for harmonized rules for distribution processes of PPPs. It is necessary to set the obligation of PPP providers to monitor on an on-going basis that the product continues to be aligned with the interests, objectives and characteristics of the target market. Responsibility of a PPP provider should be assured by the requirement to present appropriateness test of a target consumers as well as distribution channel and intermediaries when selecting distributors. It should be the PPP provider who sets the target market for PPPs. At the same time, the PPP designer (provider) should explicitly set the group of consumers for whom the product is considered unlikely to meet their interests, objectives and characteristics and thus is not suitable. This would give the NCAs the ability to easily identify the potential mis-selling attempts from distributors.

Distribution rules should implement the "cooling-off" period, where the client has the possibility to return the product and cancel the contract free of charge. Additionally, the distribution rules should recognize the right to switch, even for insurance based contracts. The distribution rules should limit the "frequent-flyer" incentive that often arises on the side of financial intermediaries, who try to switch the consumer from one product to another only to get sales commission. Distribution rules should establish the provisions requiring to compare features of existing and newly offered PPP. Additionally, distributors should be obliged to use NCA's or EIOPA's approved comparison procedure of product features, where not only key features are compared, but comparable products that have the same objective are presented and compared.

Key consumer-centric approach for distribution rules should be based on pre-contractual transparency and comparability of PPPs. Both aspects, transparency and comparability, are closely linked to the ability of consumers to make an informed decision on financial products. However, comparability is determined by the ability to obtain necessary information on financial products and particular features. New trend in the area of comparison web-sites that collect, sort, evaluate and disclose information on product features should be recognized in the distribution process. Each PPP that is to be distributed should have a dedicated web-site. The web-page should be maintained during the PPP life-cycle and should contain publically available information on key features of the product including valuation of units (in case of saving PPPs or unit-linked insurance based PPPs). A consumer has to have access to layered information that are easily accessible through the web-page dedicated to the product. Such an approach should be also envisaged by a regulator overseeing the provider. In many cases, detailed information on product features is available only to official (exclusive) distributor and consumers do not have access to such information. This creates an information asymmetry and thus potential mis-selling incentives. Information on distributed (sold) PPP's feature should not be available only to the distributor selected by a provider, but should be publically available in order to maintain higher transparency and comparability of products.

Q4: Would PPP benefit from harmonisation in disclosure rules? What should be the basis of these rules? Do you agree with EIOPA's proposals?

1. FSUG believes that PPP would benefit from harmonisation of disclosure rules. Actually, this is the most important area of EU savings and it is the least harmonised despite the identification of pension savings as a critical area already in 2007 by the European Commission in its first "Green Paper on retail financial services". Since then, personal pensions have however been excluded as such from all the post 2008 crisis reforms on investor protection. However, some "individual pension products" (PRIIPS Regulation terminology) are covered by recent investor disclosure rules. For example:
 - life cycle UCITS funds (which are investment funds solely designed for retirement purposes) are covered by the UCITS IV Directive and the Regulation on "KIID" (Key Investor Information Document) that standardize and simplify pre-contractual disclosures for UCITS investment funds;
 - insurance-regulated PPPs that include a surrender value are covered by the recent PRIIPs Regulation and will have to produce a standardized (i.e. comparable) "KID" (key information document) from 1st January 2017.
 - More generally, following article 2(2g) of the PRIIPs Regulation¹ - all "*individual pension products*" that do not require by law a mandatory contribution from the

¹ The PRIIPs Regulation defines its scope as every retail investment product that is not expressly excluded in article 2. Article 2g excludes «*individual pension products for which a financial contribution from the employer is required by national law and where the employer or the employee has no choice as to the pension product or provider.* »

employer and where the employee has a choice on the product or the provider fall under the PRIIPs scope.

Therefore, it is not correct to pretend that PPPs are not retail investment products, as quite a few “individual pension products” are already included in the scope of the PRIIPs Regulation. But, there is still no harmonisation for all PPPs, making it almost impossible for EU pension savers to compare one PPP offering to another, except if it is two life cycle funds (then the current KIID is a good tool for that purpose).

2. FSUG believes the basis for these PPP rules should be inspired (but not copied) from the UCITS funds KIID and from the PRIIPS KID, but should also take into account the diversity of PPPs and therefore not try to be too specific and normative. The OPSG agrees with the common basic structure for PPP pre-contractual disclosures as a starting point, except for performance and risks (see below paras. 3 and 4), and as listed on pages 32-33 of the EIOPA consultation. In particular EIOPA’s approach on cost disclosure would bring a very important improvement to pension savers’ protection: *“Include all costs – in a manner that is consistent with the approach used for the PRIIPs KID – covering both PPP costs and those at the level of the underlying investments (‘look through’). It should include both monetary and % figures, and include ‘cumulative’ figures to the retirement date used for the projection information. »*
3. FSUG is concerned about the approach taken by EIOPA regarding performance disclosure: *“include projections to retirement under different scenarios, and information on the possible income in retirement »*. EIOPA mentions that this is inspired from the ESAs approach to performance disclosure in the PRIIPs « KID ». EIOPA does not make any reference to past performance disclosure. A number of consultative bodies² have however already formally alerted the ESAs and the Level I EU Authorities about the disastrous consequences of eliminating all disclosure of past performance in key information documents and its replacement by “future performance scenarios”.

In a nutshell, eliminating past performance disclosure (together with that of the benchmarks chosen by the asset manager as currently applicable for UCITS funds) will prevent savers from:

- knowing whether any PPP has made money or not in the past;
- knowing if any PPP has met its investment objectives or not;
- knowing if any PPP has performed below or above its benchmark;
- comparing the performance of similar PPPs (for example two different life cycle funds).

² The ESMA Securities and Markets Stakeholder Group http://ec.europa.eu/finance/finservices-retail/docs/fsug/opinions/160119-fsug-letter-priips-annex_en.pdf and the European Commission’s Financial Services User Group (FSUG) http://ec.europa.eu/finance/finservices-retail/docs/fsug/opinions/160119-fsug-letter-priips_en.pdf
at least

It will also make it very difficult for the ESAs and any other regulator to perform their legal duty to collect analyse and report on the performance of long term and pension savings products as they were reminded by the EU Commission in its 30/09/2015 Capital Markets union Action Plan³.

Worse, the replacement of past performance disclosure by “future performance scenarios” will be even more misleading. One reason is that the three scenarios considered by the ESAs: “*an unfavourable one, a neutral one and a favourable one*” (page 35) – which are not at all probability- weighted will most likely make individual pension savers believe the “neutral” scenario is the most probable which it is certainly not.

Another reason is that these scenarios will always prove wrong contrary to past performance, which is an historical fact. Of course past performance is usually not a good predictor of future performance, especially when formatted for marketing purposes. But, if its disclosure is standardised and supervised and accompanied by that of its benchmark (as it is currently the case for the UCIRTS funds’ KIID), it helps understanding the benefits of the product for pension savers. In particular, it tells if the pension product has ever made money or not for the pension saver, something “future performance scenarios” alone will never tell you.

This would constitute a major step back in EU pension saver protection.

4. FSUG is concerned about EIOPA’s approach to risk disclosure: “*a risk indicator similar to that with the PRIIPs KID could be designed to indicate risk in the short term, while performance scenarios could be more useful for communicating risk in the long term* ». This approach seems too complex for savers and does not reflect a key specificity of pension savings and PPPs : the long term nature of these savings, and the fact that the risk and volatility of asset classes is different over the long term then over the short term. For instance a portfolio of diversified equity is less volatile over 20 years or more than a bond portfolio. This is very critical for the performance and the protection of the real value of pension savings over the long term. It is also critical for the financing of the EU economy, for growth and jobs as outlined in the Capital Markets Action Plan.

FSUG therefore favours more a specific approach to pension savings and PPP risks that takes into account not only the underlying asset classes in which the PPP intends to invest but also the different time horizons involved. The risk indicator could therefore take the format of a table crossing time horizons and asset classes, contrary to the ESAs approach for PRIIPs where the risk indicator table is for one time horizon only (the recommended holding period for the PRIIPs product).

³ “*To further promote transparency in retail products, the Commission will ask the European Supervisory Authorities (ESAs) to work on the transparency of long term retail and pension products and an analysis of the actual net performance and fees, as set out in Article 9 of the ESA Regulations.* » (page 18)

Q5: Are you aware of any differences in prudential regimes that would lead to an unlevel playing field amongst PPP providers? Do you agree with EIOPA's view not to add specific capital requirements for PPPs?

Q6: Are further supervisory powers - tailored to PEPP - necessary? Do you agree with EIOPA's proposals?

The proposals from EIOPA should be beneficial. But further measures needed.

If the PEPP is to be successful from the perspective of consumers then two conditions must be met:

- PEPPs must comply with meaningful standards relating to terms and costs (both level and structure of charges); and
- Consumers must be able to access to these better value products.

Competition and choice is not effective at driving up standards in markets such as pensions – especially on a EU wide basis. Product intervention is a much more effective form of regulation and has been shown to introduce real competitive pressures into markets – if the product standards and conditions for distribution are right. The standards relating to product governance and product regulation must be meaningful and robust if they are to represent an improvement on existing products. We set out elsewhere in this response the key elements of product governance and regulation,

This may be stating the obvious but the benefits of having a good product is undermined if consumers cannot get access to the product – in other words, if the product ‘sits on the shelf’. We cannot rely on demand pressures from consumers to pull these products off the shelf. Moreover, as we explained in our submissions to retail market integration and regulatory call for evidence initiatives, one of the main barriers to effective market integration are the behaviours of dominant intermediaries and distribution practices in local markets. Even if a good value PEPP is created, these dominant intermediaries are unlikely to distribute PEPPs unless compelled to do so by some form of regulatory intervention.

There are two forms of effective intervention which could be deployed here.

The first relates to the behaviours of intermediaries when advising on and recommending a pension product. One of the most successful interventions in the UK was the combination of stakeholder pensions (SHPs) and the RU64⁴ rule. Stakeholder pensions were a huge improvement on existing personal pensions. But it was recognised that the pensions industry and intermediaries would not recommend SHPs as they would not receive as much commission. Therefore, additional measures were needed. RU64 required advisers to justify in writing why they were recommending a high charging personal pension when a similar SHP was available. This transformed the pensions market almost overnight as charges on personal pensions fell to the level of SHP. A similar intervention will be needed to make PEPP

⁴ Regulatory Update (RU) 64

market work. Indeed, this would have two benefits. Not only would it ensure consumers who needed a pan EU pension could get one, it would also have a positive impact on the quality of personal pension products in local markets.

The second relates to comparative information tables. Providers of comparative information tables in local markets should be compelled to include information on PEPPs to ensure that consumers in the local market are aware of the availability of PEPPs. This would allow those consumers who are confident enough to buy PEPPs direct from a provider to do so. But consumers who still want the protection that comes with regulated advice would have the opportunity to seek advice.

Q7: Do you agree with EIOPA's assessment of the policy options' impacts?

We agree with EIOPA's proposals for an appropriate legal and regulatory framework aiming at developing safe, cost-effective and transparent PPPs and PEPP (cf. product features, information provision and conduct of business rules: CP, pages 72/73). Therefore we agree, too, with EIOPA's fundamental choice of a standardized PEPP with flexible elements implemented under a second regime (although we believe EIOPA should eliminate any reference to a «2d Regime ». This wording is not intelligible for EU citizens, as it is not clear if a « 1st regime » already exists in all 28 Member States.

But we consider these fundamental policy options only as minimum standards that have to be clarified and complemented in order to prevent any consumer detriment. In order to achieve a simple, transparent and trustworthy PEPP, additional product features should necessarily be integrated.

PEPPs should include these four basic principles:

- The higher the accumulated capital by payments/contributions is, the higher the payouts have to be.
- Any PEPPs must guarantee a life-long annuity as one of the decumulation / pay out options (cf. EIOPA's Fact Finding Report on decumulation Phase Practices, October 2014).
- At the end of the payment / contribution phase there has to be an open market decision for the consumer for choosing a provider for the payout phase (possibly free of charge).
- There has to be a mandatory and fair participation to risk benefits (related to longevity / death risk).

Only by adopting these four basic principles, consumers will develop the necessary trust that PEPP is not just another investment saving plan, but it will definitively offer a safe income at retirement. That is the reason why we believe that the EU Authorities should also establish EU-wide transparent, competitive and standardised retail annuities markets; and grant more freedom to pension savers to choose between annuities and withdrawals (but after enforcing a threshold for guaranteed life time retirement income).

A PEPP contract should be a contract with transparent contract clauses related to cooling-off period, early withdrawal, exemption from payment of premiums; participation to benefits;

and with several pay-out options (annuities or lump sum). A simple and cost effective Default option' must be included. In addition some key features should be included in particular cap on charges and advice free delivery, at least for the default option.

In order to ensure a high minimum standard of consumer protection, the terms and conditions of the calculation of the annuity ought to be disclosed and fixed in a mandatory way at the time of the contract subscription (mortality table, participation at risk benefits, fees for any changes of the contract etc.). Regulation of PEPP must include these parameters.