	Comments Template on Consultation Paper on the creation of a standardised Pan-European Personal Pension product	Deadline 05 October 2015 23:59 CET
Name of Company:	**The Investment Association**	
Disclosure of comments:	Please indicate if your comments should be treated as confidential:	Public
	Please follow the following instructions for filling in the template: ⇨ Do **not** change the numbering in the column "reference"; if you change numbering, your comment cannot be processed by our IT tool ⇨ Leave the last column empty. ⇨ Please fill in your comment in the relevant row. If you have no comment on a paragraph or a cell, keep the row empty. ⇨ Our IT tool does not allow processing of comments which do not refer to the specific numbers below. **Please send the completed template, in Word Format, to CP-15-006@eiopa.europa.eu. Our IT tool does not allow processing of any other formats.** The numbering refers to the Consultation Paper on the the creation of a standardised Pan-European Personal Pension product (see Annex 3 of consultation paper)	
Reference	**Comment**	
General comment	The Investment Association represents the asset management industry operating in the UK. Our members include independent fund managers, the investment arms of retail banks, life insurers and investment banks, and the in-house managers of occupational pension schemes. They are responsible for the management of around £5.5 trillion of assets in the UK on behalf of domestic and overseas investors. The UK asset management industry strongly believes in promoting the need for long term savings across Europe in pension and investment products. The Pan European Personal Pension (PEPP) is an opportunity to do so and we welcome the opportunity to respond to EIOPA's consultation on the PEPP.	

	The Investment Association supports attempts to increase pension saving around Europe. While we believe that there are some domestic markets that are already well catered for by existing pension provision (notably the UK, Ireland and the Netherlands) there are other countries with nascent Defined Contribution (DC) markets or a tradition of state provision that is becoming unsustainable in the context of challenging public finances whose citizens and economies would benefit from the opportunity to increase long term savings via a PEPP. The PEPP has the potential to improve outcomes for individual savers through the provision of an attractive vehicle that allows them to invest in assets that have a much better chance of delivering them good outcomes over the longer term than cash. It can also help European economies grow by contributing to the Capital Markets Union (CMU) agenda through the provision of new long term savings flows that will help to deepen European capital markets. By aiding the flow of capital to productive uses in European economies, it can help strengthen the link between individual outcomes and broader economic growth. We explore some of the key issues that EIOPA raises in our response to the questions below, but in the first instance we wish to comment briefly on three specific areas. <u>The role of asset managers in providing PEPPs</u> The Invesment Association supports the creation of a single market for personal pensions in the EU. While economies of scale already exist – and should continue to be encouraged – in investment products such as UCITS, the current fragmentation of the pensions market makes economies of scale harder to achieve and limits the choice of products and providers. Given its central role as an investment vehicle for the accumulation of long term savings, the PEPP is an ideal product for asset managers to provide. With its expertise in developing investment options and managing DC retirement savings products, the asset management industry can play an important role in developing the market for PEPPs. The industry's experience in large scale cross-border business may also help it	

take a leading role in the promotion of its PEPPs on a cross-border basis as far as is possible.

EIOPA recognises in its consultation the need for a plurality of PEPP providers, which we strongly support. However, we note that EIOPA signals a possible preference for guarantees to be provided within PEPPs. Quite aside from the implications of this for individual PEPP savers (discussed further in our answers below) any preference for guarantees embedded within PEPPs will immediately bias provision away from asset managers, who act as agents on behalf of their clients, to banks and insurance companies that can use their balance sheets to underwrite guarantees. Plurality amongst PEPP providers, can only be achieved through proportionate regulation of product design.

Defining the target market for PEPPs

We would note the importance of defining the target market for the PEPP. Without understanding who will buy the product and through which distribution channels, we do not see how it is possible for providers to design appropriate products. There is a danger that without an analysis of the target market PEPPs will struggle to compete with domestic pension products and other long term savings vehicles.

To that end we would like to see EIOPA conduct an analysis of the potential target market. This would both facilitate the design of appropriate regulation and products.

Local and tax and regulatory issues

The final area that we wish to highlight relates to the challenges of reconciling a desire for a highly-standardised pan-European pension product with local laws and regulation. These features mean there may be limits to the ability to standardise PEPPs across Europe.

The most obvious area of complexity is tax. Pension saving around the world is routinely incentivised through tax systems and while there is a broad consensus internationally that an ‘EET’ treatment is appropriate, there is significant heterogeneity at the national level on the precise design of tax incentives. Different incentive

	structures around Europe may make a PEPP more or less attractive in some countries, and this may make cross-border provision more challenging. Another area is product regulation – different markets will have different preferences for features such as guarantees and this once again puts a limit on the ability to standardise the product across Europe. It is difficult to see how these differences can be overcome and it highlights the need to focus less on standardisation of the product and more on facilitating a regulatory environment that incentivises PEPP providers to offer cost-effective and attractive products that are suitable for the target market. It is in any case not clear to us that there is a need for a high degree of product standardisation across Europe. In those countries with a developed third pillar, PEPPs will in theory compete alongside existing national pension products, which will have many diverse product features. We do not see the benefit in mandating standardisation of PEPPs alongside diverse national products. There is a danger that it can hamper the ability of PEPPs to compete in domestic markets; this brings us back to the need to identify the target markets for PEPPs around Europe.	
Question 1	As a starting point we would agree with EIOPA's view that no additional regulatory burden should be created for those institutions that are likely to run PEPPs. They should be allowed to operate as PEPP providers under the EU sectoral legislation to which they are already subject, provided that they can offer products complying with the PEPP regulation. We recognise that this may require adjustments to existing sectoral legislation. For example, asset managers regulated under AIFMD or the UCITS directive could not manage a PEPP. However, adjusting these existing directives seems less burdensome and preferable to us than creating an entirely new authorisation requirement for PEPP providers.	
Question 2	A high degree of consumer protection is clearly important in ensuring that consumers have the confidence to save for retirement. To that extent EIOPA should ensure that it	

	creates a regulatory environment that results in PEPP providers delivering products that are suitable for the target market, are transparent in their costs and charges and deliver value for money to the end consumer. On this last point, we would note that value for money should be viewed in terms of the quality of the product offering and not just the price. Beyond this, we believe there is a big role for public policy to play in increasing retirement savings around Europe. Creating the right consumer protection regime will not on its own lead to an increase in retirement saving. Behavioural economics has highlighted the inherent human biases that can militate against long term saving and the UK experience of automatic enrolment has shown that significant policy interventions may be required in order to generate step-changes in retirement saving. An additional cultural challenge faced across Europe is the relative lack of consumer exposure to to capital markets as a way of generating a future pension income. For many savers the concept of investing in market instruments to generate income and increase savings is an alien and disquieting concept and persuading individuals to take risk over extended periods of time is a challenging task, particularly given the general preference for exposure to cash across Europe. Changing these cultural norms is crucial to increasing savings in long term investment products such as the PEPP. Such norms can only be changed by educating consumers and this is an area where European governments should take the lead.	
Question 3	With regards to introducing a 2nd regime we do not feel there is enough detail as to what this would constitute to be able to form a view on it at this stage. Any further clarification that EIOPA and/or the European Commission could provide on the goal and functioning of a 2nd regime would therefore be welcome. We believe that it would be possible to create a PEPP through a “standard” regulation, which would include the product rules that a personal pension product would need to comply with in order to benefit from an EU passport. Existing national personal pensions products would not be bound by these rules, unless their providers wished them to have the PEPP label.	

	The ELTIF regulation is an example of EU regulation that is set up along similar lines – it does not apply to existing long-term investment funds that are not offered on a cross-border basis. Adopting a regulatory structure that builds upon existing regulations that are well understood by Member States and the financial services industry would also offer the best outcomes in terms of implementation and consumer protections.	
Question 4	We agree that any default investment option that contains a guarantee does not in addition require a life-cycle strategy with de-risking. To do so would unnecessarily reduce the saver's upside – unnecessarily precisely because the guarantee is protecting against downside investment risk. However, there is a broader question which relates to whether guarantees are even appropriate as the default option in a long term investment product such as the PEPP. We discuss this further in our answer to question 6.	
Question 5	The behavioural economics literature shows that too much choice can be paralysing for consumers and so we support the idea of a default with a limited number of investment options. However, we do not have a view on what is the right number of options – this is something that should ideally be tested with consumers.	
Question 6	We fundamentally believe that default strategies are a necessary feature of a PEPP – the behavioural economics literature has shown the effectiveness of such an approach. Any default strategy should have a member-focused, outcome-based objective which can then be achieved using a given asset allocation, but thereafter we are wary of being overly-prescriptive of what a default strategy should look like. It is likely to vary according to the characteristics and ability of the target market to save and bear risk. Rather than prescribe a pan-European approach to the default, we would prefer to see a principles-based approach that sets out governance standards that the provider must adhere to e.g. setting member objectives, performance measurement against the member objective, assessing suitability over time and value for money. This then	

	allows the PEPP provider to design default strategies that are appropriate for the target market; these may well differ across countries. As a practical consideration, a simple de-risking approach may not be appropriate if savers wish to continue to invest throughout retirement; but it is appropriate if savers plan to buy an annuity. Again, approaches to retirement income will vary across Europe and this needs to be reflected in the accumulation stage investment strategy. This highlights the need to be cautious in mandating an investment approach at a European level. <u>Guarantees</u> We do not believe that guarantees are appropriate as a default investment option. Guarantees are not costless and are typically only cheap when they are unlikely to be required and expensive when there is a greater probability of them being required. The cost of any guarantee needs to be factored in to any decision to purchase one. Over a 30-40 year time horizon, investing in a diversified basket of securities means that the kind of guarantees discussed (e.g. 0% real return) are unlikely to be needed. This makes it questionable whether it is appropriate for a PEPP saver to be defaulted into a guaranteed product where the guarantee is highly unlikely to be needed *and this is known in advance*. This is not to say that guaranteed products should not be offered – that is something that is best left to the market and active individual choices; but we do not believe they are suitable as default products. As we have already set out in our introductory comments, a focus on guarantees also biases provision away from asset managers towards balance sheet entities. The PEPP is a long term investment product and we do not believe that making it more difficult for asset managers to provide a product whose engine is their core business would benefit consumers, who would miss out on the expertise of the asset management industry in delivering good long-term outcomes.	
Question 7	Suitabiity is a term that has strong regulatory association with the regulation of advice and distribution. From the perspective of the product manufacturer, there are clear	

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	responsibilities with respect to ensuring that products are well designed and appropriate for the target market. In this regard, we would emphasise the importance of a transparent consumer-focused governance framework for delivery of the the default arrangement as discussed above. While outcomes cannot be guaranteed, having strong governance around the investment process in particular can maximise the likelihood of good outcomes for members.	
Question 8	We do not believe it would be appropriate for all investment options to have a life-cycle or guaranteed element to them. This is limiting consumer choice for those who do want it. As we have explained above, the most appropriate course of action is to have a well designed and governed default arrangement that is suitable for those members who make no investment choice. Thereafter pension savers should be free to exercise choice over where they invest.	
Question 9	Where a PEPP comes with a guarantee, prudential regulation should be appropriate to ensure that the guarantor is regulated to the same solvency standards regardless of the nature of the provider. If this can be achieved through the relevant sectoral legislation it would appear better to do so that way rather than create a new solvency standard simply for PEPP providers.	
Question 10	We believe that no one should be barred from buying a PEPP if they wish to. However, there may be cases where it is not appropriate for the individual and this raises the question of whether it is appropriate for the PEPP to be purchased without advice. This in turn comes down to how the PEPP is distributed – if done so via the workplace and it comes with an employer pension contribution (as deferred pay) it is hard to see how this could be detrimental to the individual (if there is no other way of accessing this deferred pay). If the PEPP is sold via a retail market and the only money that goes in is the individual’s contributions, then the advice question becomes more important. It seems to us that the issues of distribution and advice are therefore highly important and need careful thought and attention.	
Question 11		

	Individuals purchasing a PEPP could hold the product for as long as 40 years. Over such a long period it is unreasonable to suppose that consumers would be locked into products, regardless of the performance of the product. We therefore agree with EIOPA that switching products or providers should be allowed but potentially limited to avoid providers having to hold portfolios consisting entirely of liquid assets. However, we do not believe that there is necessarily a trade-off between the individual's desire to have the option of switching provider and ability of the provider to invest PEPP contributions in illiquid assets. This is because at the level of the provider, only some of the assets in the PEPP will need to be held in more liquid asset classes in order to meet potential investor demand to switch funds or providers; and the greater the scale of the PEPP the more likely it will be able to hold illiquid assets without experiencing liquidity issues caused by investors switching product.	
Question 12	As discussed above we believe that as long as the PEPP has sufficient scale in assets under management (AuM) at the provider level, there should not be a tension between the individual's desire for the option to switch and the ability of the PEPP provider to invest in long-term, illiquid assets. This is because with a large value of AuM the provider should only have to allocate a proportion of its overall portfolio to liquid asset classes in order to meet any liquidity reqirements arising from investor switching. Implicit in this is the assumption that all or the vast majority of investors do not switch products at the same time.	
Question 13	The detail of what should be the precise interval for switching without incurring additional charges is something that is likely to be determined only after observing the experience of how investors react. It is therefore appropriate to observe how the market develops before deciding whether any regulation is needed in this area. More generally, it may be helpful to make a distinction between switching funds within the PEPP and switching providers. It is not clear to us that there should be any cost to switching funds within the PEPP, particularly where there are no guaranteed or bonus features on the fund. In these cases exiting investors will bear the transaction costs of	

	fund-switching and this will impact on their returns. We do not see why an additional exit charge should be imposed. In the cases of funds that come with bonuses or guarantees e.g. 'with-profits' funds a surrender penalty may be appropriate in order to protect the interests of those investors remaining within the fund. With respect to switching providers, switching is unlikely to be consumer-driven and may be more likely to result from incentive structures provided to sales teams. Perhaps the only way to deal with this is to prohibit any commission being paid to distributors.	
Question 14	We agree that the starting point for pre-enrolment disclosure for the PEPP should be the PRIIPs regulation. In that context we would refer EIOPA to our response to this summer's PRIIPs Technical Discussion Paper for our specific views on the future shape of the PRIIP KID, particularly in relation to the presentation of charges and transaction costs. These are as relevant for PRIIPs as they are for PEPPs. In addition to this there are a number of key messages that we would like to stress in the specific context of the PEPP: • While the PEPP is, by design, an asset accumulation vehicle, its ultimate goal from an individual perspective is *to provide a retirement income*. Therefore, information around risk and projections of outcomes would be beneficial to the investor if they were **framed in terms of income** and thought should be given to how this could be achieved. • The **risk indicator** should be expanded to cover other types of risk that are relevant specifically to PEPPs and that may arise as a result of investment choices by the PEPP holder. The main ones here are inflation risk and shortfall/adequacy risk. For example, a PEPP where the individual chooses to invest fully in cash or bonds might score as low risk on grounds of investment risk, but would score as high risk in relation to inflation and shortfall risks.	

	As far as investment risk is concerned the risk indicator should be appropriate for the holding period of the product. Given the long-run nature of the PEPP, a risk indicator that focuses on short-term volatility is clearly inappropriate. It would be better to develop a risk indicator that focuses on the *risk to income* at retirement. • Where pre-enrolment communication aggregates the charges of a PEPP into a single figure, consideration should be given to whether the consumer should be able to get access to the **charge on each of the constituent elements of the PEPP**. There is clearly, however, a trade-off between simplicity and the ability to secure greater transparency. The important principle is that any disclosure must be designed to aid the consumer in choosing between PEPP products. • Calculation and presentation of **the cost** of the PEPPs should take into account the specific benefits that they could offer, for example a minimum return guarantee or a biometric risk coverage. While these features provide additional benefits to investors that will be reflected in generally lower risk indicators, they also entail costs that need to be disclosed to consumers using some form of common methodology. Without disclosure of these costs it is not possible for the consumer to evaluate the value of these benefits. • **Performance scenarios** should be based on some measure of anticipated returns. In addition, given that the purpose of the PEPP is to provide a retirement income, thought should be given to how consumers can be aided to understand the impact of these different scenarios on their income in retirement.	
Question 15	This question comes back to the fundamental issue of how the PEPP is going to be distributed. If done so via the workplace and it comes with an employer pension contribution (as deferred pay) it is hard to see how this could be detrimental to the individual (if there is no other way of accessing this deferred pay) and this means that it may be more suitable for sale via the internet.	

	If the PEPP is sold on a retail market and the only money that goes in is the individual's contributions, then there would be more questions over whether the internet is suitable as a chanel for distribution. In this case advice might be required before a PEPP is purchased and this means that any internet sales process would need to be well regulated. It is important here to stress the importance of financial education as a complement to financial consumer protection. It is widely recognised that many people lack the level of financial education required to decide how much they should save to prepare for retirement and how they should manage their savings and investments. If the general direction of travel is to distribute on the internet, individuals will only benefit if they feel they have the confidence to engage. This will require governments and the financial services industry to work together to boost the financial sophistication of their citizens and consumers. EIOPA could also play an important role in this area to increase awareness of the importance of financial literacy and promote initiatives to develop the capacity of individuals to save for the long term and invest to improve their future financial well-being.	
Question 16	Again, whether the distributor is required to apply an appropriateness test to the sale of a PEPP depends on the conditions and route to distribution. A product distributed via the workplace that comes with an employer contribution and with a well-designed default fund (e.g. UK workplace pensions) should not require an appropriateness test. The presence of the employer contribution in particular is key here – if this element of deferred pay is only available to the individual through the pension product, it is hard to see how it is to the individual's detriment to be in the product. Where these conditions do not hold it may that it is sensible for a distributor to apply an appropriateness test in the case of a non-advised sale.	
Question 17	We have already highlighted in our introductory comments that there may be limits to the ability to standardise the PEPP due to differences in local tax treatments and product regulation. However, we do not see this as a problem. Given its central role as a capital accumulation vehicle to generate an income in retirement, the necessary	

	scale in a PEPP already exists through the investment management and administration processes, both of which are integral features of the PEPP product. It is not clear what scale economy benefits further standardisation brings beyond these.	
Question 18	As a general principle we believe that where biometric risk coverage is provided there should be appropriate solvency requirements applied. Typically it is insurers that underwrite biometric risks; representatives of the insurance industry will therefore be better placed than we are to answer this question.	
Question 19	We do not support caps on charges and costs and it is hard to see the rationale for a cap in a market that does not even exist yet. Caps are a blunt policy intervention tool with a number of risks for pricing patterns – in particular the risk that charges can move up to the level of any cap. They also carry the risk of unintended consequences in terms of behaviour, extending to the investment process and the balance between expenditures on different elements of the pensions value chain. Emerging experience from the charge cap that has been in place since April 2015 and covers default strategies in UK workplace pension schemes is already confirming some of these impacts: • Within the overall product price cap of 75bps, the budget for expenditure on investment strategies is falling and driving many schemes towards passive strategies, often because other elements of the value chain are using up the budget. Such decisions should be made on the grounds of the quality of the investment offering and not cost. It is also worrying that from a member perspective, expenditure on investment - the only determinant of member outcomes after contributions have been paid – is being squeezed at the expense of other elements of the value chain that do not determine member outcomes. • Certain investment techniques that look to limit volatility are being priced out because of the cap. But guarantees, which are outside of the cap, can be used	

	freely, regardless of their cost and value. This is potentially detrimental to the consumer because no attention is paid to the value of any guarantee; it also reduces competition by biasing provision against asset managers in favour of balance sheet entities that can write guarantees. • Certain asset classes are becoming too expensive to invest in e.g. direct property investment. Members are therefore missing out on potential benefits of this asset class with decision making being driven by costs rather than the economic fundamentals of the asset class. We also do not support any cap on transaction costs on the investments inside a PEPP. Capping transaction costs will be to the detriment of the member since it will limit the manager's ability to trade on the member's behalf. Transaction costs are fundamentally different to product and service charges. The former are incurred in delivering a return, the latter are paid for the cost of a service. Regulators in the UK have recognised this and the workplace pensions charge cap does not include transaction costs. Although not in favour of a cap, we are clear that EIOPA should not allow dsitribution and advice costs to be embedded within a product charge. In the interests of transparency, these costs should be shown separately from any product charge because they are not part of the product.	
Question 20	We have already outlined above the limits to standardisation of the PEPP and that this does not create problems, in our view, for the PEPP. On the contrary, individual PEPP providers should have some flexiblity in product design – competition should be on product quality as well as price. To suggest otherwise implies that there is no value in a PEPP beyond any standardised approach. A better understanding of the target market in each country will illustrate which additional product features are desirable.	
Question 21	As we have alluded to in some of our previous answers, we recommend taking into account the best practice characteristics of European passporting regimes.	

	As with the UCITS Directive, the PEPP Regulation should contain a product passport regime, under which the provider of a PEPP can market a PEPP to investors in Member States other than its home country, upon notification to its home regulator in accordance with the process set out in the regulation. The product passport in the PEPP regulation would build on the "PEPP label", compliance with the features of which would authorise the distribution of PEPPs across the EU to investors.	