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DRAFT Questions and Answers on the proportional supervision of IORPs

Table of Contents

Question 1: What is proportional supervision of IORPs? Why does it matter?	3
Question 2: What are the minimum prudential and regulatory conditions to a proportional supervision of IORPs?	4
Question 3: What practical steps can NCAs initially take to implement a proportional supervision of IORPs?	4
Question 4: What supervisory practices can facilitate a proportional supervision of IORPs?	5
ANNEX: Illustrative list of indicators to facilitate the implementation and conduct of proportional supervision	6

The Questions and Answers (Q&A) is addressed to all NCAs responsible for the prudential supervision of IORPs. As part of EIOPA's mandate to promote a common supervisory culture, the Q&A focus on the proportional supervision of IORPs. The Q&A and accompanying Annex do not aim for completeness. Supervisory practices provided in this document are not exhaustive. The Q&A should assist NCAs with their initial prioritisation and allocation of supervisory resources before the materialisation of IORPs' risks. A significant change in IORPs' risk profile may lead to a re-prioritisation of NCAs' supervisory resources and possible review of the proportional treatment of the concerned IORPs.

Question 1: What is proportional supervision of IORPs? Why does it matter?

Proportional supervision refers to the idea that the supervisory means (e.g. resources) put in place by NCAs to supervise IORPs are appropriate to what is necessary to achieve the objective of prudential supervision set in Article 45 of the IORP II Directive.

Proportional supervision should not be confused with proportional regulation. Whilst proportional regulation, and hence degree to which proportionality is integrated in the regulatory framework, will facilitate the implementation of proportional supervision, proportional regulation and proportional supervision differ in terms of their purpose. Proportional regulation consists of regulatory measures aiming to reduce compliance costs borne by IORPs. In contrast, proportional supervision seeks to optimise the use of NCAs' scarce resources for the effective supervision of IORPs, given the qualitative and quantitative characteristics of the domestic IORP sector. The Q&A therefore focus on the latter objective.

Although proportionality will resonate most with NCAs already conducting risk-based supervision because of the size and diversity of their domestic IORP sector, proportional supervision is relevant to all NCAs responsible for the supervision of IORPs, regardless of whether they supervise other types of financial institutions in addition to IORPs.

This is because proportional supervision follows the spirit of the IORP II Directive. The proportionality principle in the IORP II Directive seeks to minimise, where applicable, IORPs' administrative burden (proportional regulation). The Directive also requires for the supervision of IORPs to be forward-looking and risk-based (Article 47 of the IORP II Directive). Thus, the application of the proportionality principle is an integral part of risk-based supervision (proportional supervision) in line with the IORP II Directive.

In Member States where the IORP sector is still in its infancy but set to grow in the future, risk-based supervision and the importance of optimising the use of supervisory resources may become more relevant over time.

Question 2: What are the minimum prudential and regulatory conditions to a proportional supervision of IORPs?

Proportional supervision must satisfy minimum prudential and regulatory requirements.

1. The prudential objective set in Article 45 of the IORP II Directive must not be compromised. Proportional supervision must ensure that the rights of members and beneficiaries between IORPs are equally protected
2. Proportional supervision does not equal deregulation. The easements provided by proportional supervision do not discharge IORPs from fulfilling their legal obligations
3. Proportional supervision should help NCAs prioritise and optimise the allocation of supervisory resources in relation to the national specificities of the IORP sector. Effective proportional supervision should indirectly help maintain the diversity of the IORP sector and level-playing field at both national and European levels
4. Proportional supervision should largely relate to IORPs' risk profile and encourage a case-by-case approach tailored to IORPs' different risk profiles

Question 3: What practical steps can NCAs initially take to implement a proportional supervision of IORPs?

NCAs can take forward the following two practical steps when considering proportionality in their supervision of IORPs:

1. Identify relevant proportionality indicators linked to national specificities and characteristics of IORPs

Proportional supervision is not confined to bringing easements to small IORPs. The IORP II Directive cites several elements underpinning proportionality which, depending on the relevant provision of the Directive, include:

- Size of the IORP
- Internal organisation of the IORP
- Size of the IORP's activities
- Nature of the IORP's activities
- Scale of the IORP's activities
- Complexity of the IORP's activities
- Inherent risks of the IORP's activities

NCAs should develop a good understanding of the main characteristics of the domestic IORP sector, the key drivers that may differentiate IORPs' risk exposure and how both IORPs' characteristics and differentiating factors in IORPs' risk profile relate to proportionality. To support NCAs' proportionality considerations in supervision, EIOPA has developed an illustrative and non-exhaustive list of possible indicators in relation to proportionality (See Annex). NCAs should consider these indicators as part of building their understanding and knowledge of IORPs' risk profile. They should also take into account of how these indicators interact with each other (e.g. interdependence between membership size and extent of outsourced activities) and altogether. Proportionality indicators may have a different purpose. Their application may also vary depending on how far NCAs are in their implementation of proportional supervision. Indicators may be qualitative or quantitative in nature.

2. Segment the IORP sector, using relevant proportionality indicators, according to national specificities and IORPs' characteristics

Segmenting the domestic IORP sector by their key characteristics including relevant proportionality indicators may help NCAs determine appropriate proportional measures to include in their risk-based supervision and hence avoiding a “one size fits all” approach.

NCAs should use their understanding of and available information on IORPs, including relevant proportionality indicators they have identified, to divide the IORP sector into key segments based on shared characteristics.

NCAs could initially use the segmentation to prioritise and efficiently allocate resources, in line with their supervisory plan as well as establish a hierarchy to facilitate:

- Discussions on what proportional considerations should be included in their supervisory framework
- Identify different types of easement applicable to some segments and the phasing and staging of NCAs’ supervisory activities (e.g. on-site visits) over the supervisory cycle

Segmenting the IORP sector should, however, not be seen as an automated exercise solely based on quantitative data (e.g. scheme demographics). Qualitative information is equally important to implement an actionable segmentation.

Question 4: What supervisory practices can facilitate a proportional supervision of IORPs?

The following supervisory practices can help facilitate proportional supervision as part of NCAs’ supervisory review process:

- i. NCAs could tailor the frequency of requests for regular information according to the characteristics of the IORP sector and relevant proportionality indicators
- ii. NCAs could consider the levels of granularity for regular and ad hoc information requests in light of the characteristics of the IORP sector and relevant proportionality indicators
- iii. NCAs could adapt the frequency and intensity of examinations and on-site inspections given the characteristics of the IORP sector and relevant proportionality indicators
- iv. NCAs could adapt the frequency and intensity of engagement with IORPs to the characteristics of the IORP sector and relevant proportionality indicators
- v. NCAs could establish a hierarchy or “proportionality ladder” which sets out different levels of supervisory intensity according to the characteristics of the IORP sector and combination of relevant proportionality indicators. NCAs could use the proportionality ladder to embed supervisory practices described in points i) to iv)

ANNEX: Illustrative list of indicators to facilitate the implementation and conduct of proportional supervision

The following list does not aim for completeness. Its purpose is to provide a snapshot of possible indicators that NCAs may consider as part of implementing and conducting proportional supervision in relation to the relevant IORP II provisions referring to the size and internal organisation of the IORP, the size, nature, scale, complexity of the IORP's activities, the inherent risks of the IORP's activities.

- IORP's legal form e.g. trust-based, not-for-profit?
- Type of IORP e.g. multi-employer or single-sponsor IORP?
- Number of sponsoring undertakings
- Number of pension schemes managed? Number of different scheme types managed?
- Type of scheme e.g. DB, DC, hybrid? Open or closed scheme (existing or future accruals)?
- Cross-border business and number of host countries?
- Inclusion of non-occupational pension related activities?
- Membership size? Membership distribution by active/deferred/beneficiaries?
- Link with Article 5 of IORP II Directive?
- Size of Assets under Management (AuM)?
- Assets in relation to GDP?
- Size of total liabilities (if relevant)?
- Balance sheet total (AuM over liabilities)?
- Percentage of reinsured liabilities?
- Size of benefit/assets per member?
- Contributions relative to pensionable salary?
- Size of IORP compared to market? Percentage of national market?
- Nature of pension benefits e.g. link to Social and Labour Law, collective agreements, link with Pillar I?
- Mandatory or voluntary membership?
- Type of security mechanisms?
- Biometric risk cover?
- Investment risk coverage?
- Number of different investment types/assets?
- Type of investment policy e.g. active/passive?
- Use of listed/unlisted assets
- Use of standard investments e.g. UCITS?
- Number of different charges applied?
- Composition and size of the IORP Board e.g. member/employer representation?
- Board qualifications/experience?
- IORP's internal capacity e.g. Number of IORP employees? availability of own supporting staff?
- Extent of outsourced activities e.g. scheme administration, fiduciary management, asset management, direct involvement of sponsor?
- Outsourcing abroad? Market concentration of outsourced activities?