



EIOPA-BoS-19-246

10 July 2019

## **Opinion on the practical implementation of the common framework for risk assessment and transparency for 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) on Common supervisory culture of Regulation (EU) No 1094/2010<sup>1</sup>. 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 by providing opinions to competent authorities.
- 1.2. EIOPA delivers this Opinion on the basis of Directive (EU) 2016/2341<sup>2</sup> (the IORP II Directive), in particular in relation to Articles 25, 28 and 49 thereof.
- 1.3. This Opinion is addressed to the competent authorities (CAs), as defined in point (i) of Article 4(2) of the 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<sup>3</sup>.

### **2. Context and objective**

- 2.1. Article 25 of the IORP II Directive requires IORPs<sup>4</sup> to have in place an effective risk-management function and system. Article 49 empowers CAs to review the strategies, processes and reporting procedures that IORPs have in place to identify, measure, monitor, manage and report within the IORP on risks. In

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<sup>1</sup> 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.

<sup>2</sup> 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.

<sup>3</sup> Decision adopting the Rules of Procedure of EIOPA's Board of Supervisors, [https://eiopa.europa.eu/Publications/Administrative/EIOPA-BoS-11-002\\_EIOPA-BoS-Rules%20of%20Procedure-Rev3.f.pdf](https://eiopa.europa.eu/Publications/Administrative/EIOPA-BoS-11-002_EIOPA-BoS-Rules%20of%20Procedure-Rev3.f.pdf).

<sup>4</sup> Including the occupational retirement provision business of life insurance undertakings subject to Article 4 of the IORP II Directive.

addition, pursuant to Article 49 CAs have monitoring tools, including stress-tests, to identify deteriorating financial conditions in an IORP and to monitor how deterioration is remedied. Article 28 requires IORPs to carry out and document their own-risk assessment (ORA), including an assessment of the effectiveness of the risk-management system.

- 2.2. On 14 April 2016 EIOPA delivered its Opinion on a common framework for risk assessment and transparency for IORPs to the EU institutions<sup>5</sup> (Opinion to the EU institutions) to strengthen EU prudential regulation of IORPs.
- 2.3. This framework is relevant for all IORPs providing occupational pension schemes where risks are shared to differing degrees between the sponsor, plan members and the institution itself. IORPs providing pure DC schemes, where risks are directly and fully borne by the plan members, are not within its scope.
- 2.4. EIOPA considered in its Opinion to the EU institutions that the introduction of the common framework would be beneficial in supplementing the national regulatory frameworks. The common framework would ensure an objective and transparent view of the financial position of IORPs and it would provide a comprehensive view of the extent to which pension promises are supported by financial assets and the extent to which they rely on sponsor support, pension protection schemes and benefit reductions. The information provided by the common framework would also allow for a better understanding of the risks and vulnerabilities of IORPs, contributing to their resilience and sustainability and improving the protection of members and beneficiaries.
- 2.5. The objective of this Opinion is to promote consistent supervisory practices by providing guidance on the practical implementation of the common framework as a tool for risk assessment. The common framework contains comprehensive principles and technical specifications, which CAs and IORPs may use on a voluntary basis.
- 2.6. This Opinion further aims to facilitate risk-based and proportionate supervision of IORPs. In this context, CAs may take into account the national specificities of the IORP sector to determine the requirements necessary for implementing this Opinion considering a risk-based and proportionate approach<sup>6</sup>.
- 2.7. To facilitate the practical implementation of the common framework, this Opinion will be accompanied by:
  - Annex 1, containing principles and technical specifications for IORPs to value the common framework's balance sheet and perform the standardised risk assessment (SRA) calculations: EIOPA has adapted the broad description of the common framework in the Opinion to the EU institutions, to provide more specific technical specifications and where possible simplifications, building on the

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<sup>5</sup> EIOPA Opinion to EU Institutions on a Common Framework for Risk Assessment and Transparency for IORPs, EIOPA-BoS-16/075, 14 April 2016, [https://eiopa.europa.eu/Publications/Opinions/EIOPA-BoS-16-075-Opinion\\_to\\_EU\\_Institutions\\_Common\\_Framework\\_IORPs.pdf](https://eiopa.europa.eu/Publications/Opinions/EIOPA-BoS-16-075-Opinion_to_EU_Institutions_Common_Framework_IORPs.pdf)

<sup>6</sup> 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>

technical specifications for the valuation of the common balance sheet in the IORP stress tests<sup>7</sup> and for the quantitative assessment of further work on solvency of IORPs<sup>8</sup>. This adaptation does not change the content of the aforementioned documents, but intends to provide all relevant technical information in one document with a uniform structure;

- a spreadsheet containing the risk-free interest rate and inflation curves for the relevant currencies end-of-year, as well as the stressed interest rate and inflation curves for the purpose of the SRA interest rate risk sub-module and the value of the symmetric adjustment for the purpose of the SRA equity risk sub-module. EIOPA will update this file every year;
- a helper spreadsheet assisting IORPs to value sponsor support and pension protection schemes using the simplifications provided in Annex 1;
- a calculation spreadsheet, assisting IORPs in calculating, including through the provided simplifications, and aggregating the SRA (sub-)modules.

### **3. Common framework for risk assessment and transparency for IORPs**

#### **Common framework as a tool for risk assessment for IORPs**

- 3.1. CAs should make IORPs aware of the availability of the common framework as a tool for risk assessment and should stand ready to support IORPs in the application of this tool.
- 3.2. The common framework consists of a market-consistent common balance sheet and an SRA, calculating the impact of pre-defined stress scenarios on the market-consistent balance sheet, including all available security and benefit adjustment mechanisms, such as sponsor support, pension protection schemes and benefit reductions. The common framework allows for the use of simplifications for reasons of proportionality, although it is acknowledged that this can result in deviations from an elaborate market-consistent valuation method to value the common balance sheet and may impact the comparability between IORPs.
- 3.3. Irrespective of the national framework in which IORPs operate, the use of the common balance sheet can provide additional information for IORPs for risk management purposes.
- 3.4. The SRA analyses the impact of a set of common, pre-defined stress scenarios on the common balance sheet, and provides insight as to what extent the IORP's excess of assets over liabilities is reduced under certain stress scenarios and to what extent security and benefit adjustment mechanisms can absorb these stress scenarios.
- 3.5. When carrying out the ORA pursuant to Article 28 of the IORP II Directive, the starting point should be the national regulatory framework in which IORPs operate. Although the ORA is an own risk assessment, the information provided by the

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<sup>7</sup> EIOPA, Annex to IORP Stress Test 2019 Specifications – Technical Specifications Common Balance Sheet, EIOPA-BoS-19/135, 29 March 2019, [https://eiopa.europa.eu/Publications/Surveys/Annex%20stress%20test%20specifications\\_common%20balance%20sheet.pdf](https://eiopa.europa.eu/Publications/Surveys/Annex%20stress%20test%20specifications_common%20balance%20sheet.pdf).

<sup>8</sup> EIOPA, Technical Specifications – Quantitative Assessment of Further Work on Solvency of IORPs, EIOPA-BoS-15/070v2, 11 May 2015, [https://eiopa.europa.eu/Publications/OIS/EIOPA-BoS-15-070v2-Technical\\_specifications\\_QA\\_IORPs.pdf](https://eiopa.europa.eu/Publications/OIS/EIOPA-BoS-15-070v2-Technical_specifications_QA_IORPs.pdf).

common framework, which includes all available security and benefit adjustment mechanisms, could further strengthen risk assessment and risk management, irrespective of how capital and funding requirements are defined at national level. Still, the assessment of the overall funding needs of the IORP, including a description of the recovery plan where applicable, has to comply with the funding requirement in the national regulatory framework.

- 3.6. The ORA includes a qualitative assessment of the protection mechanisms IORPs dispose of as well as an assessment of the risks to members and beneficiaries considering any indexation mechanisms and benefit reduction mechanisms. The common framework entails the establishment of market values for these mechanisms, if available, both in a pre- and post-stress situation. In case of sponsor support, it needs to be ascertained whether the value recognised on the common balance sheet is affordable for the sponsoring undertaking. The market values of security and benefit adjustment mechanisms constitute valuable elements which can be used as input for the more qualitative assessment required by the IORP II Directive.
- 3.7. There are further elements required in the ORA that are not (fully) covered by the common framework. For instance, the common framework only includes operational risks at an overall, quantitative level and does not consider – or at least not explicitly – ESG risks. CAs should therefore read this Opinion in conjunction with the Opinion on the use of governance and risk assessment documents in the supervision of IORPs, BoS-19-245, 25 June 2019, the Opinion on the supervision of the management of operational risks faced by IORPs, BoS-19-247, 25 June 2019, and the Opinion on the supervision of the management of environmental, social and governance risks faced by IORPs, BoS-19-248, 25 June 2019.

### **Common framework as a tool for supervisory review**

- 3.8. CAs should consider, in the context of their national specificities, using the common framework as a tool for conducting the supervisory review as laid down in Article 49 of the IORP II Directive.
- 3.9. The SRA embedded in the common framework allows CAs to gather, in a standardised manner, information on the risk profile of IORPs, and use it as input for developing their supervisory planning in the context of a forward-looking and risk-based supervisory approach.
- 3.10. The supervisory review process has to take account of the national regulatory framework in which IORPs operate. In this context, the common framework supplements national valuation and funding standards by providing a market-consistent view of the financial situation of IORPs and their reliance on security mechanisms such as sponsor support and benefit reductions.
- 3.11. The results of the common framework can provide useful information to the CA and serve to identify excessive risk exposures, possible weaknesses and deficiencies amongst IORPs. Where deemed appropriate, CAs may request IORPs to consider these weaknesses and deficiencies in their risk management process.

3.12. CAs should set the reporting frequency and determine the data to be reported by IORPs.

### **Transparency of the common framework's results**

3.13. CAs should consider the extent to which results of the common framework should be disclosed to relevant stakeholders in order to promote greater transparency of IORPs' risk assessment.

3.14. The common framework provides an explicit and objective view of all resources, such as financial assets, sponsor support and pension protection schemes, which are available to support pension obligations. Although it does not necessarily specify the level of expected intervention by the sponsor and pension protection schemes over time, it gives an indication on who might be obliged to intervene and to what extent. It also includes an indication of the extent to which benefit adjustments, either positive or negative, may occur in the future based on its valuation under the common framework.

3.15. Given the characteristics of the domestic IORP sector, CAs should weigh the potential advantages of greater transparency to relevant stakeholders (e.g. improve member trust and confidence, trigger dialogue on sponsor risk) and the potential disadvantages (e.g. to avoid creating market distortions between IORPs and other market participants providing occupational retirement benefits).

3.16. Factors for encouraging or discouraging greater transparency include but are not limited to:

- the characteristics of the occupational pension market, e.g. occupational pensions provided predominantly by not-for-profit IORPs;
- relevance of disclosing information where employee and employer representatives are part of the governance structure of the IORP;
- whether results stem from using the common framework as a risk assessment tool by NCAs to conduct the supervisory review process or by IORPs to conduct their ORA
- which information, including level of detail, could be disclosed without causing any distortion, e.g. high-level summary of the results;
- to which relevant stakeholders information could be disclosed, e.g. sponsors or their representatives, members or their representatives, possibly only upon their request.

3.17. When IORPs operate several pension schemes for different groups of members and/or sponsoring employers, it would be appropriate to apply the common framework separately for each pension scheme or for each sponsoring undertaking, as this would enable obtaining relevant information for each of the specific stakeholders.

3.18. When disclosing the results of the common framework to stakeholders or to the CA, attention should be given to describing clearly the context in which the calculations have been done, the simplifications used, the parameters set and the assumptions that have been used in modelling and the valuation of some items of the balance sheet such as sponsor support and reduction of benefits.

## **Proportionality**

3.19. The common framework includes simplifications, to ensure its proportionate application with regard to the size, nature, scale and complexity of IORPs' activities. Considering the national specificities, CAs may adopt further simplifications for the valuation of the common balance sheet, when these simplifications are proportionate to the nature, scale and complexity of IORPs' activities.

3.20. Not all elements of the technical specifications will be relevant for IORPs in all Member States. In addition, the degree of materiality of many of the elements in the technical specifications will vary depending on the nature of IORPs in different Member States. Therefore, CAs may inform their IORPs which elements are not relevant and thus may be excluded.

## **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, 25 June 2019

[signed]

Gabriel Bernardino

Chairperson

For the Board of Supervisors