The European Federation of Financial Services Users
Fédération Européenne des Usagers des Services Financiers

EuroFinUse's Response to the Consultation by DG SANCO on Consumer protection in third-pillar retirement products (Commission Staff Working Document)

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Executive Summary

The European Federation of Financial Services Users welcomes this important Consultation from the European Commission as private pensions are, in our view, one of the most problematic areas for EU consumers and individual investors. We are pleased that the European Commission is aware of some of the severe problems currently existing in the area of private pensions, such as regulatory fragmentation, lack of transparent and clear information for consumers and difficulties for consumers to choose between different substitutive products.

However, we believe that the Commission may not be aware of the extent to which these problems cause consumer detriment in the area of private pensions:

- For instance, with regard to regulatory fragmentation issues, we would like the European Commission to note that the very restricted scope of the Regulation for Key Investment Documents (PRIPS)[1] is certainly not contributing to create the very much needed level playing field for retail long term investment products. The Internal Market and Consumer Protection Committee (IMCO) of the European Parliament shared EuroFinUse's opinion on the inclusion of occupational pension products within the scope of the Regulation, in the same way as the ECON Rapporteur did for the inclusion of shares and bonds[2]. This is why we believe the proposed exclusion from the scope of the Regulation of all kinds of pension products and of several categories of life insurance by the European Council last draft[3] (Article 2a and 2d) does not go in the right direction to strengthen the confidence of consumers in the EU market for private pension products.

- Also, our recent independent research shows that too many private pension products "3rd pillar") destroyed the real value of EU citizens' pensions savings and are unfortunately quite likely to continue doing so in the years to come unless strong and long -awaited[4] action from the EU Authorities in the area of long term and pension savings takes place.

[1] Especially due to the proposed exclusion of shares, bonds and occupational pensions out of the scope of the Regulation.
[2]http://www.betterfinance.eu/fileadmin/user_upload/documents/Press_Releases/en/PR_Beres_European_individual_investors_support_the_proposals_of_the_European_Parliament_Rapporteur_on_Packaged_Retail_Investment_Products.pdf
[3] http://register.consilium.europa.eu/pdf/en/13/st10/st10111.en13.pdf
[4] *"Due to the nature of long-term savings and pension plans, particular care is needed to ensure that consumers are being offered products that are really adapted to their needs and marketed appropriately. These are major, once in a lifetime, financial decisions for consumers. Therefore, consumers must be in a position to make their choices in full knowledge of the product, correctly assessing their circumstances and needs."* (European Commission's Green paper on Retail Financial Services in the Single Market, April 2007)

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Questions 1 and 2: The definition of third-pillar pensions

As EuroFinUse stated on its [response to the previous consultation from DG SANCO on Third-Pillar Retirement Products from November 2012], there is a lack at EU level of a clear distinction between second and third pillar retirement products.

We feel that the proposed definition by the European Commission in this consultation[5] is a good start. However, we do not entirely agree with the proposed definition for third-pillar retirement products, especially as regards to the addition "either voluntary or mandatory". We understand that the "*third-pillar"* categorisation should refer to products where consumers have a certain capacity of choice. A product to which contributions are mandatory is closer to a pure tax-like charge, and should be better contained in the first-pillar as we can generally associate it to a mandatory individual account. Therefore, third pillar should only include products for which it is up to the consumer to calibrate his or her contributions to them.

More concretely, we believe that the definition of "*private pensions*" is more important; and which we developed in our Research Report "Private Pensions: The Real Returns" according to the definition from OECD on its classification and glossary document for private pensions from 2005[6] to define the scope of our research.

Question 3: What are the main risks for consumers when purchasing a third-pillar retirement product?

We believe this is one of the most important questions of this consultation document: as evidenced in our report "Private Pensions: The Real Returns", the biggest problem for consumers is that they are deemed to purchase pension products that much too often do not manage to beat inflation, once deducted all expenses borne to the consumer and taxes; and therefore lose money over the long run, as evidenced by data from OECD and EuroFinUse on the returns of pension products over the last 5 and 10 years.

Questions 6 to 12: Self-regulatory codes and EU certification schemes

[5] *"Third-pillar retirement products are defined as any type of private retirement product subscribed to by consumers on an individual basis [as opposed to occupational], either voluntary or mandatory"*, Commission Staff Working Document, "Consumer protection in third-pillar retirement products", DG SANCO of the European Commission, April 2013

[6] http://www.oecd.org/insurance/private-pensions/2496718.pdf

The Consultation Paper from the European Commission refers to the possibility of promoting self-regulatory codes for the industry industry and voluntary EU certification schemes (this is an option to which the White Paper on pensions from 2012 referred to). EuroFinUse believes that own-initiative solutions such as self-regulatory codes are soft law approaches which are not appropriate to tackle huge internal market problems such as the clearly disadvantaged position of consumers versus providers of private pensions. At the same time, certification schemes can contribute to the creation of a true internal market on private pensions (which does not exist so far), in the same way as the UCITS scheme did very successfully. However, consumers and retail investors do not need any further categories of private pensions available at retail level (there are already too many of them and it is very difficult to make a decision). We would recommend to instead fix the existing private retirement solutions by ensuring they are eventually much more transparent and aim at protecting the real value of savings, at least, in the long run.

Questions 4 and 5: Main recommendations

We refer to our key Recommendations in the area of private pensions from EuroFinUse's Research Report "Private Pensions: The Real Returns" (these Recommendations are not exclusive of third pillar pensions but also for those private non mandatory second pillar pension products):

- As a matter of urgency, public bodies must ensure:

- Fair, clear and not misleading information for all long term and retirement savings;
- Independent and competent advice; and
- Limit the increasing complexity of retail long-term investment products. Governments should support the design of a basic and simple retirement savings vehicle that would provide at least the protection of the purchasing power of those savings over the long term. It should also be easily accessible without "advice" and without heavy commission.

- Regulation needs to offer a unified framework for the marketing and sale of pension products to savers. As a general principle, regulation should adopt the perspective and interests of market users, not the perspective of market intermediaries[7].

[7] Kay Review, recommendation on the principles of regulation.

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- Thoroughly improve and harmonise the product disclosures for all long term and retirement savings products: this is in line with EuroFinUse proposals regarding the European proposed Regulation on 'PRIPs'[8]. The current levels of disclosure on fundamental aspects that define past and expected performance of an investment vehicle are missing. Under these circumstances, it is impossible to make informed investment choices or stimulate a competitive national and pan-European market in the provision of private pension products.

- In particular the disclosure of historical returns must be provided:

  - After inflation (in real terms);

  - After all charges borne directly or indirectly by the investor; and

  - After taxes (as required for all US investment funds).

  If the finance services sector is unable to agree on the shape and form of pension product disclosures, then at a minimum policy makers must mandate that disclosure of historical returns must be provide after inflation, charges and taxation.

- Regulation must consider how to fairly compensate financial advisers, so that they focus on providing advice based on suitability and not selling the product that offers the highest fees. Ideally, regulation should be consumer focussed, emphasising and promoting simple products and trusted providers, stressing product suitability and supplier integrity[9].
- Basic financial maths should be part of all school curricula as this is crucial knowledge for accessing adequate pensions. This long term investment needs to be made in the school curriculum. In general, policy makers in all Member States need to raise the standard of financial literacy of their citizens. Financial literacy is a life skill on a par with reading and writing. In an aging population, increasingly forced to make its own retirement provision, financial literacy will have a key influence on retirement outcomes.

- Taxation should incentivise long term savings and investments and not consumption and short term savings, but at least not penalise them. This could be done by favourable

[8] In general terms, occupational and non-occupational pensions should be included into the scope of PRIPS to deliver a KID.
[9] *Ibid*

tax treatment to contributions to pension schemes. The accumulation of pension wealth needs to have that, in order to encourage citizens to make private pension provision. At the very least taxation should not hurt the real value of pension savings.

- Prudential regulation must recognise that pension vehicles have potentially very long investment horizons. They have the capacity to opportunistically absorb risk, to achieve extraordinary real returns, where the non-pension insurance sector cannot. Pension investment vehicles can be contra cyclical and an important source of risk capital for the economic growth and employment opportunity. In particular, pension investments in equities must not be penalised. This is why all pension products should be -at least partially exempted from solvency regulation that forces suboptimal long term asset allocation.

- To provide protection from inflation, governments should issue inflation linked securities or promote simple inflation protected long-term savings products specifically targeted at pension savers. These securities and/or 'packaged' products should be readily accessible, without requiring the use of intermediaries. The aim should be to provide cheap access to a do-it-yourself retirement scheme that preserves the real value of the investment.

- Lastly, we believe that governments can play an important role in protecting saver interests and promoting universal pension coverage by establishing low cost public pension saving schemes for their citizens. We believe that the Danish ATP[10] scheme serves as a model example of government working effectively with social partners to achieve this goal.

[10] ATP is established by law; the Minister of Employment appoints the Committee of Representatives on recommendations offered by the social partners. The Minister also appoints the members of the Board.

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