

The Danish Financial Supervisory Authority

22 January 2019

Statement on inspection at Danica Pension A/S

1. Introduction

In March 2018, the Danish Financial Supervisory Authority (the FSA) conducted an inspection at Danica Pension, Livsforsikringsaktieselskab (Danica Pension), which focused on the company's investments in infrastructure. The inspection was part of a cross-sector review in which the FSA examined the same theme at eight life insurance companies and multi-employer occupational pension funds.

The inspection covered the company's organisation, processes and position on infrastructure investment, including its position on investments and compliance with the prudent person principle.

Under the prudent person principle, pension companies must make investments so as to safeguard policyholder interests in the best possible way. The investment strategies pursued by the companies must reflect the benefits that the companies have told the customers to expect. The individual company may invest only in assets associated with risks which the company can understand and handle, including identify, measure, monitor, manage, control and report on (see "Guidelines on alternative investments and good investment processes in the light of the prudent person principle" (*Vejledning om alternative investeringer og gode investeringsprocesser i lyset af prudent person-princippet*)).

As part of its inspection, the FSA examined five selected infrastructure investments with a view to establishing how the organisation and processes worked in practice. The inspection was conducted prior to the acquisition of SEB Pension.

2. Summary and risk assessment

Danica Pension is a commercial pension company offering its customers an average-rate product as well as a market-based product. Danica Pension has 600,000 customers and DKK 350 billion worth of pension assets (in Denmark, not including SEB Pension).

By mid-2018, the portfolio share of alternative investments in the pension sector accounted for 11% of total assets (not including properties), whereas the share of infrastructure investments accounted for 3%. The company's portfolio share of investments in alternative assets accounted for 7% of total assets, whereas the share of infrastructure assets accounted for 2%.

The company had invested primarily through private equity funds and had invested in just under 30 infrastructure funds containing a broad range of underlying infrastructure investments.

The board of directors' policy and guidelines for the investment area

The FSA observed that the company's board of directors had incorporated a risk profile in its investment policy in relation to alternative investments and had limited the acceptable risks in a number of areas in relation to alternative investments and infrastructure investments. The FSA assessed, however, that the risk profile was inadequate as were the limits laid down. The FSA issued an order to the company to ensure that its investment policy includes adequate identification and limitation of the risks that the board of directors is willing to assume in the areas in question and to revise the limits laid down in relation to alternative investments.

The company was asked to give an account of whether its fixed return targets for alternative investments for the purpose of continued assessment of realised returns were relevant targets and constituted a relevant basis for comparison.

Investment risk and risk/return assessment

The FSA observed that the company prepares detailed reporting on an ongoing basis in which the performance of the individual investments is assessed in terms of returns, investment events, covenants, etc. The FSA issued an order to the company to supplement this reporting with an update on the company's expected return and return target of the individual investments.

Valuation process

The FSA asked the company to give an account of the management of conflicts of interest in the valuation process in terms of the investment unit's involvement in the process.

Risk management

The risk management function was not presented with any material investments for comments with a view to assessing the risk profile of the investments before they were made. Consequently, the FSA issued an order to the company to ensure that the risk management function is given the opportunity to comment on risk before an investment decision is made.

Furthermore, the company was asked to give an account of how the annual report prepared by the person responsible for the risk management function provides the board of directors with a sufficient overview of the risks and risk management system of the pension fund.