	Comments Template on **Discussion Paper on Sponsor Support Technical Specifications**	**Deadline** **31 October 2013** **18:00 CET**
Name of Company:	Barnett Waddingham LLP	
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 question, 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 DP-13-001@eiopa.europa.eu** **Our IT tool does not allow processing of any other formats.** The numbering of the questions refers to Dicussion Paper on Sponsor Support.	
Reference	**Comment**	
General Comment	Barnett Waddingham LLP is a UK based firm of actuaries and consultants. In particular, we provide a range of actuarial, administration and consultancy services to trustees and sponsoring employers of pension schemes. We have therefore considered the discussion paper on sponsor support technical specifications with interest. The following represents the views of many, but not necessarily all of the actuaries and consultants working at Barnett Waddingham LLP. We favour the alternative simplified approach put forward in the discussion paper to the complex stochastic valuation previously required for the QIS. However, we remain fundamentally opposed	

	to the holistic balance sheet approach as tested in the QIS and our responding to this discussion paper should not be taken as agreement with that approach. These do not as yet strike the right balance between the interests of IORPs, sponsors and members; between small schemes and larger, more sophisticated schemes; or between cost and benefit. Further, it is still not clear how the valuation of sponsor support will be used. It is vital that potential supervisory responses are considered in conjunction with this to ensure that any revised framework is fit for purpose.	
Q01.	We question whether the stochastic method would be of enough benefit to justify the considerable costs involved, given the small number of IORPs which might choose to use this option. If IORPs indicated for the QIS that they required additional guidance, then such guidance may be necessary: however it would be difficult to produce guidance which covers all the necessary points. We expect that if more IORPs were to use this approach, rather than the small sample used for the QIS, more issues would come to light that would require additional detail. If guidance is required, we expect that national supervisors may be in a better position to produce clear guidance specific to each country's circumstances.	
Q02.	The more options which are available to IORPs, the less consistent and comparable the results will be between IORPs. The simplifications also include significant approximations which may not be appropriate for all those who choose to use them. We would prefer a more general approach, stating that IORPs or national supervisors can make their own proportionate simplifications or approximations to suit their circumstances. The alternative approach is part way there but further work should be undertaken on appropriate simplifications.	
Q03.	We do not believe that, given the lack of consensus in the method of valuing a sponsor and calculating the amount available to an IORP, the concept of maximum sponsor support can ever be meaningful. This concept should be dropped. We need to understand the use to which this information would be put before we can consider alternatives.	
Q04.	The justification given for using wages to estimate maximum sponsor support is that contribution increases represent deferred wages. Presentationally we find this difficult. Many IORPs in the UK are closed to new entrants or future accrual, and the active workforce may not be members of	

	the defined benefit IORP, or may be far outweighed by the technical provisions for pensioner members or those who have left employment. Wages in these cases will bear no relation to « deferred pay » for the pension scheme members. In addition, there may be different ways in which salary is paid (e.g. bonuses, overtime, commission, share options) which would make a comparison across different employers difficult. If this concept is to be retained, although we hope it is not, we would prefer a less prescribed measure, as assessed by the trustees or managers of the IORP with the cooperation of the sponsor, which will enable IORPs to take into account their specific circumstances.	
Q05.	We are comfortable with this concept, as long as there remains room for judgement (other factors than mechanical credit ratios should be permitted to be taken into account where appropriate). In particular, we support a move away from reliance on credit ratings where the rating agencies hold less sufficiently accurate and up-to-date information than the IORP itself.	
Q06.	While the possiblity of providing a standard table to link credit ratios with default probabilities is atractive in its simplicity, further work should be undertaken on the probabiltiies themselves. In particular, consideration should be given to the effect of different company structures, the time horizon considered and judgement where there are sponsor-specific factors that are not adequately captured by the credit ratios. The derivation of the default probabilities should be transparent and sufficiently researched. We would also like IORPs to retain the option of using a different default probability where this is appropriate, e.g. where the company is part of a heavily regulated sector, has some form of guarantee, or where expert advice indicates this.	
Q07.	We understand that there can be a difference between default probabilities for companies with similar accounting-based performances in different countries, and over different periods. For this reason, it may be better for this to be the responsibility of the supervisor in each member state. For example, the Pension Protection Fund in the UK works with suppliers such as credit rating agencies who assist it in deriving default probabilities specifically for sponsors of IORPs and the Pensions Regulator may be able to make use of this.	
Q08.	Affordability should be a consideration for the nature of recovery plans and periods, and supervisory responses, recognising that funding the pension scheme is not the sponsor's main business and that permitting the sponsor to invest in its business could improve its financial	

	position and lead to stronger sponsor support over the long term – to the benefit of the IORP. However, these issues are not considered in this discussion paper. Affordability should not be a constraint on the value of sponsor support but a matter for discussion between the IORP, the sponsor and the national supervisor (where necessary) when agreeing the pattern of funding.	
Q09.	We remain opposed to the holistic balance sheet approach as drafted. However, in the context of this consultation and while this option is not likely to be relevant for the UK, IORPs in countries such as Ireland would benefit from the inclusion of limited conditional sponsor support where the sponsor is a going concern and remains committed to funding the IORP. However, given the option of the sponsor to walk away, inclusion of this could lead to difficulties in comparing schemes. We need to understand the likely supervisory actions here, but it may be necessary for the value of limited conditional sponsor support to be identified separately. This may be a matter where national supervisors would be best placed to provide guidance.	
Q10.	Yes, we believe more detailed guidance would be needed if another QIS were to be undertaken, if the objective is to ensure consistency of approach between IORPs. However, we believe it will be difficult to develop guidance of a manageable length and simplicity that covers all eventualities. International accounting standards require recognition of discretionary practices where a constructive obligation exists. A constructive obligation is where a sponsor has no realistic alternative, for example where a change in practice would cause unacceptable damage to the employer-employee relationship. A similar approach could be applied to the valuation of limited conditional sponsor support and discretionary benefit adjustment mechanisms. However, we need to understand the use to which this measure would be put before we can suggest an appropriate method. EIOPA should give this question more thought in conjunction with the policy objectives.	
Q11.	We welcome the simplicity of the alternative approach, which will be easier for small and medium-sized IORPs to understand and adopt. In particular, we are happy to see the flexibility in the framework. We expect that the alternative approach would become the norm for UK IORPs, with few to none preferring to use a stochastic approach. However, the practical implications of the holistic balance sheet approach for funding and supervision of IORPs remain unclear and we	

	reserve judgement on the usefulness of this approach until further work has been undertaken in this area. We remain unconvinced that the benefit of valuing the employer covenant in this way will outweigh the costs of doing so, including the potential for misleading different parties. Further impact analysis needs to be taken, to include supervisory responses, and potential alternatives to the quantitative approach.	
Q12.	By itself, the alternative approach does address the concerns raised on the complexity of the valuation of sponsor support in the context of the QIS. However, this valuation cannot be considered in isolation without addressing the impact it may have on scheme funding, sponsor contributions and recovery plans. This interaction should be considered in any future QIS.	
Q13.	It is vital that we understand how this information will be used in practice and the possible supervisory actions. Further analysis of the costs and benefits of this approach should be carried out. « Going concern » IORPs with a strong sponsor could be expected to cope with reasonable risks such as investment strategy. We consider that the use of level B technical provisions, rather than level A, could be used on the holistic balance sheet in such cases without detriment to members. The solvency capital requirement would then provide a buffer against investment risk. We also consider that proportionality should be considered further, particularly for small schemes where some risks may not be material. Transition arrangements should also be considered in detail.	
Q14.	Underfunded IORPs with weak or very weak sponsor support may wish to consider the recoveries they might be able to make should the sponsor become insolvent. However we would expect that these IORPs would take professional advice, and the holistic balance sheet should not be the place for (or set a standard for) such a measurement. IORPs may wish to calculate a maximum value of sponsor support if this permits them additional flexibility in making funding decisions. Again, we need to know the use to which this information	

	is intended to be put.	
Q15.	Further adjustments may be needed, for example, for entities with a guarantee from government, or in certain regulated industries. We believe it will be difficult to provide a single, simple method that covers all eventualities.	
Q16.	We believe IORPs should be able to calculate a credit strength for a future QIS based on the information provided, although we do not believe that many small IORPs will participate. The credit strength calculated may not be appropriate for the purposes of funding and supervision.	
Q17.	Again, we believe so, although some IORPs may need to seek professional advice (leading to additional cost). There is a possibility that large IORPs may be more able to do this, whereas small IORPs will be left facing the cliff edges of the standard table.	
Q18.	We are content with the ratios as described for the purposes of the QIS. Further work should be undertaken on their appropriateness for supervision and funding.	
Q19.	EIOPA should carry out further research in this area and note that what parameters are appropriate may vary over time.	
Q20.		
Q21.	If the periods shown are for QIS work only, then they will be sufficient to produce a numerical answer. However, we are concerned that specifying these periods for a QIS may lead to them being used as a basis for a policy response. We believe the contribution payment period should not be prescribed. Even if these periods are to be used solely for the valuation of sponsor support, rather than determining the contributions to be paid, there will be a perception that this table will represent a target. In particular, we believe that any period less than 3 years will be difficult to manage due to the need for sponsors to budget in advance. IORPs in the UK are sponsored by employers who have a business to run, and the IORP will often not have the first call on the sponsor’s cash. This can be acceptable to trustees when the sponsor’s business activities are likely to lead to sponsor support strengthening in future. We would prefer to use the present value of the agreed contributions as a minimum value of	

	sponsor support, rather than using some concept of the value of the sponsor as the only determinant in deciding what contributions should be paid.	
Q22.	As set out above, affordability is a key factor in order to continue to grow the sponsor's strength. It is difficult to comment on « obligation » without further information on supervisory reponses.	
Q23.		
Q24.	While they may be suitable for providing a numerical answer for QIS work, this may not necessarily mean they are meaningful, or the most appropriate for use in policy. In particular consideration should be given to the need to review the assumed default probabilities from time to time, and the effect of cliff edges in default probabilities on the derived value of sponsor support and required contributions. This may be a particular issue for small schemes which cannot afford to take specialist advice. It may be fairer to increase the number of credit quality steps in the scale. Further, we note that for the Weak and Very Weak credit steps, the year 1 default probabilities are being used as these are higher than the long-term average rates used for the other credit steps, with the justification being that these are « conservative » despite acknowledging that the 1 year probability of default does not appear to be representative of the long term credit risk involved. There seems to be a tendency to pick the most conservative option at each individual stage of the calculation of the holistic balance sheet and we would caution against building in too much prudence, as (unlike insurance companies where profit is shared) if UK IORPs become overfunded it can be very difficult for sponsors to receive a refund.	
Q25.	It is not clear whether the contributions calculated under this stage are to be used simply to value sponsor support, or will be used to set the actual contributions payable to an IORP. Even if the former, we expect that setting out such a method would lead to a mechanical target for funding. Instead, the trustees and sponsor should be permitted (after taking actuarial advice) to negotiate a contribution pattern which reflects the needs of the business as well as the IORP. Reducing this process to a rigid table of « acceptable » recovery plans is too simplistic and artificially constrains the flexibility in the framework.	
Q26.	Likely recoveries will vary from sponsor to sponsor, and year to year. However, recoveries should	

	be allowed for as to do otherwise would underestimate the value of the sponsor support. In particular, charities and not-for-profit companies may benefit from allowance for recoveries. These organisations may have significant assets tied up in property, and few long-term creditors other than the pension scheme. EIOPA may need to undertake further work in this area.	
Q27.	We believe that sponsor support from other group companies should be allowed for for the purposes of the QIS, where the support is legally enforceable. We expect, in practice, that companies with complex group structures may wish to obtain specialist advice on how to allow for this support. The value of support by group companies where this is not legally enforceable requires further consideration.	
Q28.	It would be difficult to provide further guidance as circumstances and group structures will vary widely, and the guidance could not cover all possible scenarios. In practice we believe IORPS with sponsors with complex group structures will need to take expert advice, in particular in relation to overseas parent companies, obligations to other IORPs and the extent of any legal obligation.	
Q29.	Even if the group does not support the IORP directly, it may support the sponsor (particularly where the sponsor is a non-trading company). The value of the group's support will depend on the group structure, its relation to the IORP and legal considerations.	
Q30.	We remain opposed to the concept of the solvency capital requirement as previously proposed. We are concerned that the SCR will lead to far too conservative a balance sheet and stifle economic growth, together with accelerating the decline of defined benefit pension provision. We require further information regarding the purpose of this information and the supervisory responses.	
Q31.	The number of sensitivities required should be reduced to avoid confusing the issue. We need to understand the purpose of this sensitivity analysis before we can comment further.	
Q32.	Some IORPs may have, in addition to a sponsor, some form of support from a member state – e.g. a Crown guarantee in the UK. The value of this support should be allowed for, for example it might be appropriate to assume a much reduced, or zero, default probability on the portion of the IORP covered by any such guarantee.	
Q33.	We reiterate our opposition to the holistic balance sheet proposals as set out in EIOPA's response to the European Commission's call for advice. We consider that concentrating on such technical	

	issues as set out in this consultation is distracting from the real issues. Further work must be done on the likely supervisory approach before we can comment on the appropriateness of the methodology. The most important issue for IORPs and sponsors is likely to be the effect on contributions and funding. We would like to see work carried out on the extent to which cash contributions to IORPs might change under the framework. IORPs and sponsors will also be concerned about any increase in administration costs. We would like to see the effect of the proposed framework on IORPs', sponsors' and members' understanding of the risks and funding of IORPs, and a detailed cost-benefit analysis.	
Q34.	More attention needs to be paid to proportionality for small and medium-sized IORPs. We would also like to see EIOPA consider alternatives to needing to place a number on the value of sponsor support.	
Q35.	The solvency capital requirement remains nigh impenetrable. This area of work needs to be completely re-framed, taking into account the typical level of knowledge and understanding of trustees and managers of IORPs. In the UK, one third of trustee boards are made up of lay trustees who may have little to no finance experience. We remain unconvinced of the benefits of the suggested approach, and require further information on its purpose and likely regulatory responses.	
Q36.	We consider that the treatment of « last man standing » schemes requires further consideration as assuming an average financial strength for the industry may not be appropriate. We consider that there needs to be some weighting factor to take account of differing numbers of members from each employer.	