Comments Template on CP-12-003 – Draft Technical Specifications QIS IORP II		Deadline 31 July 2012 18:00 CET
Name of Company:	BTPS Management Ltd	
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 paragraph or a cell, 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 CP-12-003@eiopa.europa.eu. Our IT tool does not allow processing of any other formats.** The numbering of the paragraphs refers to Consultation Paper 12-003.	
Reference	**Comment**	
General Comment	Introduction to BT Pension Scheme By way of background, the BT Pension Scheme (BTPS) is the UK's largest corporate pension scheme, managing assets worth around £38 billion, paying over £2bn in pension payments per year and accountable to some 330,000 beneficiaries under a defined benefit (DB) structure. As well as being the largest scheme, we have access to significant internal resources: although investments are managed externally we have approximately 50 people in the executive arm including specialised risk and strategy teams and two in-house actuaries.	

The BT Pension Scheme is an occupational defined benefit scheme with some 75% of its liabilities relating to pensioners or former employees of BT. The Scheme is closed to new entrants and as such does not compete with other pension or similar retirement benefit providers. As the sponsor is a UK based company with limited non-UK employees it has never felt any requirement to deliver cross-border arrangements. The pension scheme is being de-risked in line with its growing maturity, and this is being done in a controlled way in close co-operation with our sponsor.

BTPS's approach to asset allocation has been focussing on diversification across asset classes and investment returns to achieve long term stable returns with positive cashflows rather than de-risking into extremely low-yielding UK or other government bonds.

Overview – impact on growth agenda and financial sustainability

We welcome the introduction of regulatory and best practice requirements which reduce risk and improve the benefit security of Scheme members. But it is crucial that any regulatory change does indeed reduce risk and enhance security, both in terms of the overarching aims of the proposals and in their detailed implementation. We are aware that the current consultation does not have the status of formal proposals, but in order to respond we need to consider them as such; we have some significant concerns that the current approach, to the extent that it can be understood at this stage, fails to deliver reduced risk and enhanced security.

In particular, we are concerned about the inflexibility of the current proposals. The single approach to the understanding of risk implied in the proposals means that there may be a further herding of investment institutions into the same narrow set of assets, further increasing their price, dramatically reducing their attractiveness as investments and increasing systemic risk. This seems particularly ill-timed when the markets are already crowding into what are perceived as safe-harbour assets. This is not a sustainable investment strategy and risks putting additional burdens on sponsoring companies to finance the additional costs this will imply due to lower future returns.

The biggest single impact of the current IORP pillar 1 proposals thus may be a significant further reduction in the availability of capital to invest in the growth and prosperity of the European economy, both by reducing the scope for investment in areas such as corporate equities, venture capital and infrastructure, and by increasing the costs of pension promises for the corporate sector. This risks making it significantly more difficult to achieve the European Commission's 'Europe 2020' targets on job creation and investment in growth.

Our clear view is therefore that in order to avoid significant adverse consequences for the European economy, and to avoid introducing new systemic risks, the IORP regime must be flexible enough to allow scheme-specific assumptions for the calculation of liabilities and must avoid in effect obliging pension schemes to match those liabilities with the same classes of assets.

Other key comments – complexity

We make a series of comments below and in response to the technical questions, but this should not be taken in any way as an expression of comfort with the overall approach, about which as we note we have significant concerns.

One concern with the overall approach is that it is predicated on the need to have a level playing field with the insurance industry so that there are not competitive distortions in the market. As an IORP established to fulfil existing pension obligations, and as we are closed to new entrants, this argument about competition does not apply to us – and neither does it apply to many IORPs across Europe. To impose such costs on schemes which do not compete in the interest of ensuring fair competition seems inappropriate.

	We are concerned that the QIS process is continuing at a time when the specific nature of the proposed IORP regime remains unclear. It is hard – if not impossible – to provide a considered view of the impact of a set of proposals which are not yet near to being finalised. Not least, it has proved extremely difficult to comment on the calculation methods when we do not know what is the intended use of the results. We note that there were a series of 5 QIS processes over several years for the insurance industry solvency proposals, and that this series was necessary in order for some of the technical complexities to be identified and resolved (we also note that even with 5 such processes there are still elements which remain to be resolved). We believe it is a significant risk to assume that the technicalities of the IORP proposals can be resolved in a single QIS process. We note that our intention is to complete the QIS ourselves and we intend to respond directly to EIOPA with the results of this work. But we understand that the UK's Pensions Regulator is intending to respond to the QIS itself on behalf of UK schemes, in part at least to minimise the burden of the process on schemes. We believe that national supervisors do not necessarily have sufficient information on all schemes – not least their access to information on sponsors is inevitably limited – to enable them to develop an accurate QIS on behalf of all IORPs. We would note that if there is a sense that the QIS is too complex for individual IORPs to respond to, this may be a fundamental failing of the QIS and trying to address it by regulators responding on behalf of IORPs merely masks the problem. The more appropriate solution would be a significant simplification of the QIS process; one way to do this might be to have a series of QIS processes as was done for the insurance industry. We are significantly concerned that the proposed application of a solvency-based approach to IORPs is too technical and uses inaccurate non-market consistent assumptions. Particularly where the sponsor retains the obligation to pay the pension liabilities and the	

IORP represents a vehicle to assist the sponsor to provide those retirement benefits, the solvency-based approach fails to reflect the underlying realities of the situation. Notably, the SCR process, a complex and expensive calculation, is therefore of no practical relevance to many IORPs. At the March 1st open meeting in Brussels, Commissioner Barnier promised that the proposed IORP directive requirements would not be a "copy and paste" of QIS 5 for insurance markets; we are concerned that this undertaking does not yet seem to have been carried through in practice.

UK pension schemes are small on average with limited resources and they thus rely heavily upon their advisers. Generally, these advisers are focussed on the UK pensions market and are unfamiliar with many of the insurance-related concepts in the proposals. The six week time-scale is too short to expect any appropriately detailed and considered response from most UK IORPs, and we do not accept the argument given for halving the usual three month timeframe for consultations. We would note that CEIOPS' research from 2008 identified the UK as having the largest exposure to this proposed approach.

In our view, the UK currently has a properly functioning regulatory regime and a sizable and sustainable Pension Protection Scheme (the PPF). The approach to risk, funding and regulation in the UK is scheme-specific and that approach copes well with the diversity of pension schemes that exist in the UK, responding not least to the varying quality of sponsor covenants enjoyed by pension schemes. It is not clear to us that the holistic balance sheet approach responds effectively to the specifics of the relevant regulatory regimes in different member states. We are also concerned that the holistic balance sheet approach could place unhelpful stress on the value of the sponsor covenant and potentially lead to increased risk to member's benefit security.

We believe that this is just one example of the way in which the Commission and EIOPA approach has been driven by a European harmonisation agenda and an unhelpful focus on competition rather than reflecting appropriately on the marked and substantial differences

	between Europe's pension systems and labour laws. We believe that this single approach is hard to justify in the context of the variety of European pension regimes and systems, and does not reflect the obligations of subsidiarity. Additionally, taking forward this approach in isolation from the other forms of European pension provision (i.e. pillars 1 and 3) as discussed in the Commission's white paper on pensions is highly questionable.	
Q1.	The approach is significantly too technical for most IORPs and we believe that more simplifications are warranted in order for the bulk of IORPs to be able to contribute effectively. We are concerned that these steps towards a QIS are taking place before there is clarity as to the underlying regime. This seems inappropriate and risks making the QIS a meaningless process. It is impossible to assess the impact of a regime whose substance is not yet clear. We would thus strongly favour holding back the QIS, and even this consideration of the technical specifications for the QIS, until there is some certainty as to the shape of the underlying IORP regime. Once this underlying regime is clear then it would be appropriate to develop the QIS process; we would favour an approach involving a succession of QIS processes which progressively develop the framework, as was done for the insurance industry Solvency II regime. Assumptions such as 2% inflation and 50% recovery rates mean that this method fails to be market-consistent and the resulting HBS numbers risk being no better than meaningless. Inflation risk is the largest risk faced by most UK pension schemes and not including a specific module on inflation means the liability number will be incorrect, the SCR number meaningless and the HBS wrong. The date chosen to run the QIS numbers means that the calculations will incorporate the most stressed market position for interest rates. This highlights one of the largest challenges to European IORPs: that of historically low interest rates. We would suggest a	

	sensitivity analysis of using different dates would be of interest and relevance, and would highlight the additional volatility introduced into the calculations by (1) using market defined risk free rates (especially as at the financial year end when the market is balancing its books) and (2) using a snap-shot method of valuation rather than smoothing. This method contrasts with recent announcements in the US and Holland of the utilisation of a long-term smoothed or adjusted discount curve and risks imposing long-term consequences from a calculation based on a single point in time of severe stress in the financial markets. We would encourage EIOPA to investigate whether a different process which considers more fully the extremely long-term nature of IORPs is suitable.	
Q2.	The security mechanisms are key for UK IORPs and are for them by far the most material part of the HBS. The valuation methods of these supports will define whether UK pension schemes are recognised to be financially sustainable over the long term. The suggested method is too complicated, with a single solution applied to an evaluation which must be scheme-specific. The methodology is poorly defined yet too complicated, and is likely to provide at best spurious accuracy considering the huge assumptions required. It seems to us that arbitrarily determined values are applied at a number of critical points in these calculations, such as: the 50% recovery rate (HBS 6.17); the assessment of future profits and sponsors' earnings (HBS 6.36); the proportion of shareholder funds available for the IORP; the 50 bp adjustment to allow for the illiquidity premium (HBS 8.12); the inflation and salary increase assumptions (HBS 8.23 and 8.24, respectively); the mortality and longevity shocks of 15% and 20% (SCR 7.17 and 7.29, respectively); and the figures in the counter-party default risk module (amongst others). These arbitrary values risk entirely undermining the relevance of the calculations; while they provide some small simplification of a highly complex process, they render the outcome essentially meaningless and valueless. In addition, there are some basic practicalities which are unaddressed, such as which is the	

	company whose shareholder funds are relevant for the calculations – the holding company as parent or the principal employer, or some combination of the various entities which undertake the liabilities; where different group companies sponsor different IORPs (frequently the case cross-border within multinational groups), there are added complexities again. These issues have simply not been adequately addressed in these proposals. We note that all these various elements are unique to IORPs and were not considered in the Solvency II proposals. To the extent that the Solvency II route is being followed the complexity of these elements is such that it appears hugely ambitious to believe that they can be addressed in a single QIS.	
Q3.	We believe that the specifications are too technical and deviate too far from any current evaluation methods for most UK IORPs and their advisers to understand. Notwithstanding this complexity and technicality, there is not enough flexibility – for small pension schemes to use a really simple model while the largest sophisticated IORPs could apply their own scheme-specific models or methodologies. We firmly believe that a significantly less detailed approach would be more suitable, which could introduce a regime flexible enough to apply across a range of different scales and types of IORPs and across the EU to reflect appropriately the different structures and natures of the relevant regimes and IORPs. This would probably require a high level set of principles which could be interpreted according to local and specific circumstances.	
Q4.	Simply put, no. Even as the largest IORP in the UK our ability to respond to such technical consultations is limited and we will only be able to do so using costly resource from our advisers. This was necessary even to respond to this current consultation – for which we relied on the support of advisers to run models based on the key material assumptions. Finding resource that understands the insurance-based questions but also understands UK	

	pension schemes was extremely difficult; just responding to the consultation has taken up a significant portion of the whole management team's resources for the past month. We expect that the burden of the QIS itself will be very similar and assume that this is the main reason why the UK's Pensions Regulator is seeking to run the QIS on behalf of UK IORPs. However, we question the accuracy of this exercise without schemes' involvement, especially in the highly complex and non-standard area of sponsor assessment. The simple fact that the Pension Regulator feels obliged to lead the QIS process on behalf of IORPs should be an indicator that the QIS process is too complex and too costly. Following some detailed discussions with our actuary, we estimate the cost of performing the technical calculations will be some 50%-100% greater than the current existing UK regulatory approach, and more if they are required more frequently than the valuations currently needed triennially. We are unclear what value is added, if any, by this process to justify this significant additional cost burden. As noted above, there are a number of unsatisfactory assumptions and approximations built into the process meaning that this significant cost will be borne to create a result that may be no better than arbitrary.	
Q5.	In many areas it is still unclear how the HBS will be constructed. Many calculations are either unnecessarily complex and if they are simplified as suggested they simply will not produce meaningful results. On sponsor support calculations there is not enough detail, for example, to provide a single value for shareholder funds – a value which could be calculated in a number of different ways with the resulting answers in our case potentially varying by a factor of 20 depending on the methodology chosen. Making assumptions of net profits of sponsors is a complex calculation to make and not all pension schemes will have the access to this sensitive information or access to an expert who can easily calculate it. It is unclear whether we should calculate the sponsor support including or excluding the recovery payments	

	contributions. We have noted that there are a number of key assumptions and factors built into the models required by the QIS. We wonder what would be the process for updating these as relevant within any regime that emerges, and who will take responsibility for doing this and ensuring the quality of the assumptions chosen to be applied. We note that there will also be significant uncertainty as to the inflation assumption, in simple terms as to which measure of inflation should be applied at any given time. In the UK, this might be either CPI or RPI; the calculation will produce very different results depending on the assumptions made. We note that many elements of the HBS are, despite undertakings from the European Commission, based extremely closely on Solvency II. We believe that many of these are simply not appropriate for IORPs. For example, the relevance of the risk margin is not apparent to us. Again, this will add to the costs of the process for no readily apparent benefit.	
Q6.	The required evidence for being allowed to simplify is extensive and will need agreement by our domestic pensions regulator which will need additional experienced resource to facilitate this. The restriction of "the IORP should carry out its own valuation which should be consistent with the general requirement" risks meaning that in practice the availability of an alternative may be of limited value. We would welcome being able to use the methods we have developed internally over the last decade and to use our existing covenant valuation advisers to avoid running two conflicting calculation methodologies, but it is not clear that in practice this will be permitted. We would like to comment on simplification 1 in 6.39 – we believe that very few IORPs will regard "stochastic valuations of sponsor support" as a simplification. It is worth noting that stochastic modelling of the sponsor covenant is likely to be beyond even many	

	sophisticated advisers in the pension scheme sector and asking them to use these (even in a 'black box' spreadsheet) is dangerous as there will be little ability to validate the output. We are concerned that we have not seen the simplification spreadsheets and hence are unable to comment on the suitability of these; this makes it impossible to give a fully considered response to this question. The most obvious simplification of the sponsor support calculation – and one that reflects the reality at least for UK defined benefit calculations – is simply that the sponsor support fills any deficit between assets and liabilities. In situations where the sponsor covenant is not sufficiently robust to cover this deficit, ultimately the Pension Protection Fund may be called on. We would not recommend the option in HBS 6.89 to exclude pension protection schemes as we believe that it is entirely appropriate that value is assigned in the HBS to the PPS. Beneficiaries take significant comfort from the existence of PPS structures. Further simplifications are necessary in the valuation of sponsor support and pension protection schemes to ensure a higher level of participation in the QIS. When we calculated the sponsor support according to the methodology, it was significantly complex and the results appeared to be extremely unclear. The inclusion of certain aspects, such as recoverables from insurance seem irrelevant to IORPs and seems to provide evidence of an inappropriate inclusion of elements of Solvency II, something which is unwelcome and is not in accordance with European Commission undertakings.	
Q7.	In the UK we are generally able to access and take into account the trends in mortality. However, it is not entirely clear what the technical specifications are requesting. If it is intended that IORPs calibrate their mortality only by reference to the most recently	

	published standard tables, we would consider this inappropriate as IORPs should be permitted to use the mortality tables that best fit the demographic profile of their beneficiaries even if that means calibrating to non-standard tables or ones which have not been updated as recently as the standard tables. In principle, we support the use of mortality tables that reflect a 'best estimate' projection of future mortality improvements.	
Q8.	The principles for calculating the best estimate cashflows seem clear. However, using a stochastic approach is likely to be onerous; so would splitting the liabilities into the different categories (discretionary, unconditional etc). Also, we consider performing separate SCR calculations for each category as overly complex and an unnecessary burden. We feel that the assumption for level A of swap bid rates less 10 bp is an unnecessary non-market consistent assumption as to the risk free rate in the UK. We currently use the Gilt curve or the Sterling swap curve. Again the 4.2% forward rate beyond 50 years will have a major financial implication as our scheme has liabilities out to 80 years. Bringing expenses into the calculations seems less material and overly complex.	
Q9.	This does not seem appropriate in the UK. While the HBS should reflect the realistic level of liabilities and should take account of scope within the IORP to reduce benefits, within the UK this does not seem relevant as a reduction in benefits occurs only following default – it is not an ongoing mechanism.	
Q10.	There is a fundamental difficulty with these: that the HBS purports to provide objective valuations of matters that are subjective and not susceptible to single point values. This is particularly true in relation to sponsor support valuation. The methods may produce precise numbers but in practice the assumptions on which those numbers are based make them largely meaningless. We would argue that EIOPA needs to look at other options for taking	

	account of sponsor support and pension protection schemes, focusing on an assessment of the maximum value of these items that could be applied to the IORP. In practice, where the pension obligations are the sponsor's rather than the IORP's itself, the sponsor support and the pension protection scheme provide the balancing item in any holistic balance sheet. Our existing approach to calculating the value of the sponsor covenant is both less precise and much more bespoke. The high level and broad scope approach employs three specialised advisers assessing all levels of the sponsor's business over the next 15 years including cashflow generation, debt coverage, dividend policy, business risk and sector risks. This produces a range not a single number, but enables us to assess the confidence we can have that the liabilities will continue to be covered to the benefit of our beneficiaries. One possibility for a few large, rated corporate sponsors with listed liquid debt is to use the CDS (credit default swap) market that in effect places a traded market view of the probability of default. However, the value of this is limited to around a five year horizon and is clearly only available for a limited number of sponsors.	
Q11.	We do not believe that credit ratings should be used in these calculations as they are limited in use to bond payment default risk. Not only will they not be available for significant numbers of sponsors, credit ratings are not necessarily a reliable guide to the probability of default on a sponsor's pension obligations as pensions are an employment-related agreement and so subject to various protections – which differ across different member states. In addition, the financial crisis has brought credit ratings into question and the regulatory community is actively working to ensure that credit downgrades do not have systemic implications by seeking to remove any hard-wiring of credit ratings into any regulatory rules. This perspective has been reflected by ECON in its recent statement (June 19th) that	

	"no EU law would be permitted to refer to credit rating for regulatory purposes, and regulated financial institutions would not be permitted to sell assets automatically in the event of a downgrade". We believe therefore that there should not be any steps to install credit ratings at the heart of these proposals. We do not believe that using a 50% assumption for the recovery rate is "market consistent".	
Q12.	No, we do not agree with the proposed calculation for the maximum value of sponsor support. It seems to us that the assumptions made for cash flows, default probabilities and recovery rates mean that the end product of these calculations risks being arbitrary at best. We believe that EIOPA should consider alternative approaches to the assessment of sponsor support and pension protection schemes. We highlight in our response to Question 10 the level of detailed work that we put in to developing a bespoke assessment of the sponsor covenant, but we do not attempt to develop a single number but rather a range which attempts to reflect this support. We again suggest that where the pension obligations are the sponsor's rather than the IORP's itself, the sponsor support and the pension protection scheme provide the balancing item in any holistic balance sheet. This accurately reflects the legal nature of the situation and is clearly a simpler as well as a more accurate calculation.	
Q13.	It will be difficult for UK IORPs to apply the matching premium methodology as liability matching assets are not segregated until an actual buy-out has occurred. Given that this is typically through an insurance company the liabilities at that stage are covered by the Solvency II regime. We are concerned about a proposal to calculate the HBS based on a single day's figure for swap bid rates. We understand that the Dutch regulatory authorities will shortly move to	

	the use of figures from the prior month, introducing some smoothing and reducing the risk of single spike figures having severe and unhelpful implications. We would go further and argue that a methodology needs to be applied which reflects the long-term nature of pension schemes and their ability to traverse cycles such as today's low interest rates – meaning that a smoothing approach should encompass more than a single month's figures. Having said this, we would add further that smoothing is not the ideal approach as even with a long-term approach the quality of the data and the quality of the markets can mean that the impact is highly variable. We encourage EIOPA to explore a more appropriate approach which recognises the long-term nature of pension schemes (as contrasted with the different nature of insurance provision), one option for which would be to take a flexible approach to recovery plans. We are also concerned about the proposal for the counter-cyclical premium which suggests that a uniform adjustment (50bp) be applied across all markets. We would suggest that to be market consistent this would need to vary across markets to take account of different yield curves and related different historical and implied volatilities in each market.	
Q14.	We strongly welcome the inclusion of this approach as an alternative to risk free rates and would argue that this method should be used as the primary method for calculating technical provisions. We believe that this approach would significantly reduce the stress to IORPs and their sponsors. It would also have the significant benefit that IORPs will be encouraged to maintain coherent and appropriate diversified investment strategies, thereby reducing systemic risk in investment markets through crowding into certain asset classes. This would reduce one significant risk of the overall proposals: that the level of capital available to invest in the growth and prosperity of the European economy would be significantly reduced (jeopardising the European Commission's 'Europe 2020' targets on job creation and investment in growth).	

	We note that this proposed method is inflexible and it could be significantly improved through allowing a more scheme-specific calculation. At the least we believe that the proposed approach for deriving level B discount rates should be refined to encompass appropriately the full range of investment strategies available to and used by IORPs, taking account both of other asset classes and the benefits of diversification. The assumption that "other investments is to be a considered non-fixed income" is very restrictive and will lead to significant changes in asset allocations away from low risk, cashflow matching investments such as infrastructure investment which growth in the European economy requires. The simplification of bond yields focussing mostly on European bonds fails to reflect the reality of IORP investment as most pension schemes have significantly larger holdings of US government and US corporate bonds, not to mention the increasing exposures to emerging market debt. The assumption of a 3% return for all other investments seems a huge simplification; UK pension schemes currently follow a similar calculation to estimate expected returns but with significantly more rigour and accuracy. We note the significant gap of there being no suggested expected return for inflation-linked bonds which are a major allocation for most IORPs, certainly in the UK, and perhaps elsewhere in Europe. When considering the two approaches, we believe that the technical, rigid market-led approach upon which the EIOPA (and ultimately Commission) proposal is founded is an unsuitable measure of a pension scheme liabilities – which are ultimately of a long term nature. This approach will also lead to increased and potentially very significant systemic risks.	
Q15.	The use of fixed value non-market consistent assumptions for inflation will potentially give rise to very significant issues of mismatches between the valuations of assets and liabilities which are in practice matched closely. For example in our case, the method suggests that our inflation-linked liabilities should be valued using this 2% assumption while our	

	inflation-linked assets will be valued according to market valuations. It also makes the calculations complex as we face a prescribed curve for interest rates yet a flat inflation value. This issue is exacerbated for us and for other UK schemes, and possibly for IORPs in other European markets, because we face two different forms of inflation for different portions of our liabilities. We are obliged to apply both RPI and CPI to different liabilities and we wonder which of these should be deemed to be 2%, or whether it is both. The practical fact is that even were one of these measures of inflation 2% at any given point the other would not be. The potential for mismatching is thus greatly increased under what is deemed a simplification. Inflation is one of the largest risks that our pension scheme faces and to assume it is fixed at a non-market level results in all the numbers calculated under the QIS as being little more than meaningless. We are also of the view that including an assumption for salary growth should be an option reflecting the specific pension scheme circumstances, and particularly any agreement with the sponsor and the associated employment contract.	
Q16.	We are unsure how to approach answering this question as we do not know how the SCR will be used and what it represents. Without this clarity we see little benefit or use for the SCR and the detailed calculations which are required in order to develop it. We believe that EIOPA needs to accept that the SCR is of at best marginal relevance for many IORPs. Given that many defined benefit IORPs are derisking with many having the intended aim of a buyout, and that the funding level required for this is below that expected under the SCR, it seems likely that many IORPs will never reach the funding level sought as they will agree a buy-out before this occurs. It thus seems to us that including a SCR in	

	the HBS will add no value. Regardless of its relevance, the approach to the SCR seems too complicated and makes the assumption that IORPs adopt a mainly fixed-income based asset mix, an approach which may have significant implications for current pension scheme asset allocations – with the potential for this to impact the scope for investment in European growth, as highlighted above under Question 14. One specific issue highlights problems with the overall calculation: a non-zero SCR arising from a fully derisked pension scheme with a sponsor guarantee seems simply incorrect. From our specific perspective, we use more bespoke calculations to develop our own assessment of the investment risks faced in our portfolio. Recognising the limitations of a VaR based approach, we supplement this measure of risk by looking at the impact on the scheme's funding position of historical stress tests and forward-looking scenario analyses. We are confused as to how EIOPA will be able to calculate meaningfully the 97.5% and 95% security levels based on calculations of 99.5% levels, given that the results are not linear.	
Q17.	We are significantly concerned at the complexity of the proposals, and we do believe that many of the risks proposed to be considered are far from material from an IORP perspective. We would strongly favour an approach which builds capacity in the sector by encouraging IORPs to build and strengthen their internal models through which they calculate their exposure to market risks rather than have to use a standardised generic 'black box' model. This risks not improving risk management in the sector as a whole because it would not help build skill and judgement; rather the standardised approach at worst would add to systemic risk by encouraging herd-like behaviours in particular circumstances. This cannot be the intention.	

	Elements of the SCR proposals appear to be directly copied from Solvency II, and thus include several risks which are in practice immaterial for IORPs. We would argue that these should be excluded. Among them are: catastrophe risk, expense risk, health risk, intangible asset risk, operational risk, pension disability-morbidity risk and pension revision risk. Our analysis of the risks to which we believe we are significantly exposed suggests that the approach is otherwise mistaken. The biggest risk we face is inflation risk - something which is ignored in the current proposals. Other risks that we consider include liquidity risk, correlation risk (changes in the correlation between the main asset classes) and country risk. We also have concerns with regards to the shock approaches. Having a single interest rate shock covering all currencies seems inappropriate given that they have different interest rate curves and face different market volatilities – all of which are also known and measurable should the calculation genuinely be needed. Similarly, the equity shock embeds an equally large assumption of 30% with no flexibility arising from the specific nature of individual IORP exposures. In practice, the impact of shocks will be very different depending on whether you are holding a specifically defined low volatility portfolio or a concentrated small cap illiquid portfolio. Having an inflexible approach will reduce the incentive for IORPs to manage their risks effectively so that any shocks that do arise have more limited impacts. Again we would note that this cannot be the intention of this process. We have specific concerns about the approach to infrastructure. This is an asset class to which we are increasing our exposure as it possesses liability-matching cashflow characteristics. Such investment will be necessary in order to create the growth and jobs which the European economy needs. However, the current treatment of such assets would act as a significant disincentive to such investment. Our target volatility is closer to 10%	

	than the treatment here which places infrastructure assets in the "other" category, implying 40%. We would encourage an approach similar to that proposed for property. Using unrealistic, non-market assumptions for the risks in long term asset classes such as infrastructure will limit any future investment into the area; we would argue strongly for a reassessment of this approach.	
Q18.	In addition to the specific concerns raised above in our answer to Question 17, we are concerned that the calculation of the SCR will be significantly complex and expensive. There seems to be an implicit assumption that the sponsor support will increase in value to absorb the factor shocks.	
Q19.	As with other elements (highlighted above under Question 17) we are concerned that the single, formula-based approach to operational risk may discourage IORPs from seeking actively to manage and mitigate their operational risks.	
Q20.	Many of these risks will be immaterial and so would be better ignored – especially given the complexity of the calculations which would be required. The cost-benefit analysis here would strongly argue that the best simplification would be for this section simply to be dropped. In addition, we would note that an instantaneous longevity shock of 20% seems wholly unrealistic given the nature and direction of demographics. A smoothed approach would be more appropriate.	
Q21.	We would strongly question the over-reliance on credit agencies for sponsor default risk for a number of reasons. We have already noted under Question 11 that regulators are moving actively to ensure that credit ratings do not have a disproportionate systemic effect, and it seems inappropriate to move in the opposite direction for IORPs. We note that many IORPs will not have a sponsor with a credit rating, and we fundamentally doubt that a	

	credit rating and related assumed default rate based on historical evidence together with a mathematical model will reliably provide a sponsor default rate that is appropriate for the long term which is needed for IORP time horizons. We are also concerned about the potential double-counting embedded in this risk. Given that the HBS already includes a risk of sponsor default we would strongly argue that this needs further consideration to ensure that there is no duplication of both effort and the risk in the calculations.	
Q22.	We do not believe that this calculation is relevant to us and so make no comment.	
Q23.	We do not believe that this calculation is relevant to us and so make no comment.	
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	Comments Template on CP-12-003 – Draft Technical Specifications QIS IORP II	Deadline 31 July 2012 18:00 CET
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	Comments Template on CP-12-003 – Draft Technical Specifications QIS IORP II	Deadline 31 July 2012 18:00 CET
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	Comments Template on CP-12-003 – Draft Technical Specifications QIS IORP II	Deadline 31 July 2012 18:00 CET
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