

**Comments Template on
Consultation Paper on Further Work on Solvency of IORPs**

**Deadline
13 January 2015
23:59 CET**

Name of Company:	EAPSPI European Association of Public Sector Pension Institutions	
Disclosure of comments:	Please indicate if your comments should be treated as confidential:	Public
<p>Please follow the following instructions for filling in the template:</p> <ul style="list-style-type: none"> ⇒ 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 <u>empty</u>. ⇒ Please fill in your comment/response in the relevant row. If you have <u>no response</u> to a question, keep the row <u>empty</u>. ⇒ Our IT tool does not allow processing of comments/responses which do not refer to the specific numbers below. <p>Please send the completed template, <u>in Word Format</u>, to CP-14-040@eiopa.europa.eu . Our IT tool does not allow processing of any other formats.</p> <p>The numbering of the questions refers to Consultation Paper on Further Work on Solvency of IORPs.</p>		
Reference	Comment	
General Comment	<p>The European Association of Public Sector Pension Institutions (EAPSPI), which covers 25 pension institutions and associations of the public sector out of 15 European countries and speaks for more than 25 million active workers and retirees throughout Europe, would like to make the following general remarks ahead of the answers in detail:</p> <ol style="list-style-type: none"> I. EAPSPI still agrees with the general aim of the Commission in the Call for Advice of April 2011, according to which a risk-based supervisory system for IORPs should be developed – but for this purpose the IORP Directive should be the starting point. 	

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Thus EAPSPI continues to be of the opinion that the supervision of IORPs requires a *sui generis regulatory regime* that truly accounts for the differences between IORPs and insurance companies. Due to the differences of pension schemes all over the EU, EAPSPI suggests respecting these differences among occupational pension systems in the different member states when amending the regulatory framework.

The development of a supervisory regime *sui generis*, which in particular differs from the Solvency II regime for insurance undertakings, is justified due to the basic differences between IORPs and insurance undertakings, as EIOPA itself has identified several times (in particular in the second consultation document on the review of the IORP Directive, EIOPA-CP-11/006, see 9.3.6 a – h as well as in other EIOPA documents and communications). EAPSPI has reservations that, in spite of this commitment, the current Consultation Paper on further work on solvency of IORPs as well as EIOPA's discussion paper on sponsor support of 2013, the technical specifications for the IORP QIS of 2012 as well as EIOPA's previous consultations on the IORP review are built on the Solvency II principles and structure.

II. The current Consultation Paper (CP) makes an attempt to improve on the shortcomings of the holistic balance sheet (HBS) in particular on the valuation of sponsor support by delivering further valuation approaches (i.e. the balancing item approach - BIA) and it tackles the urgent question of how the HBS is going to be used as a regulatory instrument. EAPSPI wants to underline the following points prior to the statements to the specific questions::

- EAPSPI welcomes that EIOPA for the first time is addressing in detail the central question of the regulatory function of the HBS (trigger points, funding requirements and EU-wide Solvency Capital Requirement (SCR), tiering of assets, recovery period) although we think that this should have been answered at a much earlier stage before the in-depth-analysis of the HBS elements.
- **EAPSPI is still of the opinion that the concept of the HBS should not be applied to IORPs.** The reason is that the HBS and the calculation of the SCR fully rest on the Solvency II structure regarding the market-consistent valuation of assets and liabilities

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and the measuring and quantifying of risks which EAPSPI regards as unsuitable for IORPs (see also part IV of this introduction below). By maintaining this structure, the HBS itself is not an appropriate approach for IORPs. The fact that security mechanisms of IORPs are considered at a later stage may not solve this basic problem.

- In general EAPSPI is of the opinion that **the qualitative requirements as proposed in the 4th IORP II Compromise Draft of the Italian Presidency (in particular Art. 29 Risk Evaluation for Pensions) sets accurate and sufficient requirements with respect to risk management of IORPs.** Minimum funding requirements and valuation standards should continue to be determined according to the current IORP directive. Regulatory consequences of the HBS analysis in risk management should only be determined by national supervisors (i.e. recovery plans with long recovery periods). It must be clearly understood that the use of the HBS will not be broadened: in a first step an introduction as risk management tool followed by the second step to use the HBS for strict harmonization of valuation and funding.

- **The HBS should not be used to lead to EU-wide harmonization of calculation of technical provisions** (Level A technical provisions), especially for the reason of putative comparability for an internal market of pensions, if this leads to a higher cost burden for employees and employers and detrimental effects for the entire IORP sector in consequence. As **EIOPA clearly analyses the result would be negative effects for occupational pensions, sponsors and economic growth (i.e. 5.86, 5.177, 5.179 and 5.188)** – thus the result is not worthwhile especially as according to the result of the answers to the Green Paper on Pensions of 2010, *“a number of respondents, mostly among the employers, suggested that, at least for the time being, a review of the current rules is not necessary or that a single approach is not possible.”* (Commission’s summary of 7/3/2011 of responses to the Green Paper, summary of Q 10, p.20; see also Q72 and Q85).

- **Within the discussion surrounding the HBS, EAPSPI in general welcomes the official introduction of the “balancing item approach” (BIA) in combination with the**

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simplified and heuristic check of sponsor strength by using PwC's "M" approach. But EAPSPI strongly suggests – if the HBS should be introduced at all – that **in case of a strong sponsor, multi-employer-scheme (MES) IORP or instances of other security mechanisms, these should constitute truly exceptional cases that should release an IORP from explicitly setting up a holistic balance sheet or Solvency II-like risk based solvency capital requirements.**

The rationale is that in the cases of the application of the BIA, the strength of the security mechanisms / sponsor support is actually proven and thus market consistent valuation (including the use of risk free interest rates) is not needed any more because the strength of the sponsor avoids the necessity of a transfer of the IORP's assets and liabilities and further specific quantifications seem to be superfluous. Especially in the case of MES, the BIA captures the notion that a large number of sponsors in the end is in charge of the settlement of pension claims (= HBS) and also serves as cushion for adverse developments (=SCR). This illustrates the flexibility of the sponsor support of MES IORPs and delivers a flexible protection of pension claims with solidarity.

III. EAPSPI welcomes that EIOPA still explicitly recognizes that the non-standard case of non-corporate sponsors, especially public sector entities and charities which are in addition mostly multi-employer-schemes (MES), deserves specific considerations. **However the range of suggested valuation approaches (except for the balancing item approach) are still not suitable / workable for not-for-profit and public sector sponsors, as EIOPA has not yet further developed solutions for quantifying the sponsor support in a reasonable and feasible way** related to these kinds of sponsors compared to EIOPA's Sponsor Support Consultation and EIOPA's Sponsor Support Event on 17th October 2013 - these problems are still unresolved. (see Q67)

With respect to the use of the balancing item approach for valuing sponsor support, **EAPSPI suggests that - multi-employer schemes with large number of employers, legally enforceable sponsor support and joint financing should automatically qualify for applying**

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the balancing item approach without reference to the strength of the individual sponsor (in addition to the listing in no. 4.4 of the consultation document). The rationale for this is that MES with a sufficient number of employers and joint financing could be seen as a means of collective pooling of default risk of individual sponsors – in analogy to the suggestions of EIOPA regarding pension protection schemes (PPS) in 4.248 of the consultation paper.

IV. EAPSPI again wants to express its **general concern with the HBS** as presented in the IORP QIS of 2012. As the present consultation paper (and earlier consultations) does not offer the possibility to address this general issue, EAPSPI is taking this opportunity to present its general reservations about applying the Solvency II principles, the SCR structure and the HBS concept to IORPs. It is not possible to answer EIOPA's question in the discussion paper on the details of the sponsor support without being able to refer to this argumentation.

- The **Solvency II regime is not necessary for IORPs**. The already existing security mechanisms have proven to be safe during the recent crisis.
 - IORPs have specific **inbuilt security mechanisms** that ensure the solvency position of pension schemes. In some pension schemes, contributions and the main benefit parameters can be modified by employers and employees' representatives.
 - Many pension schemes, especially of the public sector in the Netherlands, Scandinavian countries or in Germany, foresee **paritarian management**. Paritarian management involves social partners on the Board of Directors of the IORP or in similar internal supervisory bodies. Due to paritarian representation, the interests both of the employers and of the employees and beneficiaries are well-balanced and the benefit security can therefore be ensured.
 - Due to the fact that IORPs (especially in the public sector) are **social institutions** and therefore not chiefly for profit organizations, the possibility of a potential con-

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flict of interests between member protection and profit maximizing behaviour and dividend payments is minimised.

➤ For DB- and hybrid DB-/DC-schemes, in at least some Member States, **employers have the ultimate responsibility to fulfil the respective pension commitment**

- **The structure of Solvency II is not appropriate for the regulation of IORPs due to the differences between IORPs and insurance undertakings.** We consider the market value based approach inadequate for liabilities with such long durations as well as for valuing assets: No transfer of liabilities and assets need be permanently possible due to the tri-party-relationship (employee, employer and IORP). Because of the long-term nature of pensions, the actual risks IORPs are facing differ from those of insurance undertakings. As it is not necessary that liabilities and assets of IORPs may at all times be sold at market prices (because of the relation to sponsors) the way risk is financially measured under Solvency II (i.e. the SCR standard formula or the way the risk margin is derived) is not appropriate. Because of the long term nature of pensions, the actual risks IORPs are facing differ from those of insurance undertakings. Indeed the stable and long-term character of IORPs' liabilities has various risk mitigating effects. The methods of measuring and quantifying financially the risks of IORPs as laid out in Solvency II do not fit the nature of IORPs. These aspects should be taken into consideration when redesigning the regulatory framework for IORPs.

- Additionally EAPSPI is of the opinion that the **HBS is not able to reach the intended goal of the European Commission, namely to precisely assess and quantify the "true risk position" of IORPs** (CfA 4.1 from March 2011), because of the design and the valuation of the HBS. The valuation methods specified for the QIS still involve a high degree of arbitrariness and leads to pseudo-certainty which contradicts the notion of a neutral, objective and informative balance sheet. This problem arises in case of the various suggested methods of quantification: stochastic modelling strongly depends on the (often arbitrary) choice of parameters and models which make results hard to

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	<p>compare. With respect to the (simplified) deterministic valuation approaches it is not clear if the suggested simplifications are appropriate or even correct. Therefore, the results of stochastic modelling and the simplified deterministic approaches do not support the goal of comparable results as EIOPA clearly analyses in chapter 4.5.6 “<i>Quantitative comparison of some valuation methodologies</i>” of the CP (especially 4.244 and 4.245). This task becomes even more complex when it comes to evaluating the financial soundness of a public sector institution as employer and sponsor.</p> <ul style="list-style-type: none"> • In those cases where the HBS includes existing security mechanisms such as sponsor support, pension protection schemes, benefit reductions and where the HBS is used to trigger regulatory actions (recovery plans) the question remains: which regulatory options are available within a recovery plan at all in case of a shortfall within the HBS since all security mechanisms are already included? 	
Q1		Public
Q2		Public
Q3		Public
Q4	<p>The technical provisions should only include those contributions and benefits which are laid down in the contractual relationship between IORP and employer (4.24).</p> <p>We strongly disagree with Points 4.25 and 4.26: the basic rules which apply for IORPs are the contractually fixed rules between the IORP and the sponsors. An adequate description of the risks borne by the IORP cannot be based on rules for which there is no contractual agreement with the IORP. EAPSPI is of the opinion that “<i>risks building up for a promise to provide benefits of occupational retirement provision (primarily) via an IORP</i>” should not be recognised at all when calculating adequate financial resources for IORPs. We are concerned about Point 4.27 which relates the “<i>promise to provide benefits</i>” directly to the calculated cashflows. The second part of this paragraph rightly recognises that cashflows which have to be paid by the IORP should be included in</p>	Public

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	the technical provisions. There is no basis for the inclusion of cash flows beyond this, in particular not for parts of the “ <i>promise</i> ” which is not one or cannot be delivered by the IORP.	
Q5		Public
Q6		Public
Q7		Public
Q8		Public
Q9		Public
Q10		Public
Q11		Public
Q12		Public
Q13	<p>Only unconditional benefits should be evaluated in a risk assessment. All kinds of benefits where it is within the power of stakeholders to modify them (and in consequence avoid an increase in liabilities) should not be included in the technical provisions.</p> <p>In addition it is very complex to calculate future non-unconditional benefits that are not yet fixed. This information is not seriously comparable and of questionable use for supervisors. This leads to few benefits compared to the costs and efforts involved, in particular for smaller IORPs.</p>	Public
Q14		Public
Q15		Public
Q16		Public
Q17		Public
Q18		Public
Q19		Public
Q20		Public

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Q21		Public
Q22		Public
Q23		Public
Q24	EAPSPI is of the opinion that there is no need to make a distinction between “ <i>discretionary</i> ” and “ <i>mixed</i> ” benefits. As suggested in Q 13 we think that only unconditional benefits should be recognized when calculating technical provisions. Thus pure discretionary benefits should definitely not be included. And also other discretionary and conditional benefits seem too uncertain or too complex to model and calculate. Uncertainties of the calculations are the consequence, which worsen the transparency and comprehensibility of the results.	Public
Q25		Public
Q26		Public
Q27		Public
Q28		Public
Q29	<p>Sponsor support must be included if its function as a security mechanism is reliable. This means that legally enforceable sponsor support should always be allowed for in the HBS as this constitutes a key characteristic of occupational pensions organised by the social partners.</p> <p>But sponsor support should also be part of the HBS if it might not be legally enforceable but actually effective and practically existent. This might be the case in a multi-employer scheme with “<i>last man standing</i>” financing where legally enforceable sponsor support is only available for every employee against his/her own employer. Even if the scheme does not provide a legally enforceable “<i>last man standing</i>” principle, social partners as representatives of the sponsors act as if it was available. Thus we suggest that in these cases of a practical application of “<i>last man standing</i>”, it should also be recognized as being available to the IORP if it can be shown from historical data that the collective funding of the scheme has been applied in the past.</p>	Public
Q30		Public

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Q31		Public
Q32		Public
Q33		Public
Q34		Public
Q35	<p>In spite of its serious concerns against a possible introduction of a HBS-structure for IORPs, we want to stress that all types of available benefit reduction mechanisms (limited / unlimited, ex ante/ex post) should be recognized within the HBS. In case of an unlimited benefit reduction mechanism this should in general be treated as a balancing item as it generates the mechanism of last resort for the sustainability of IORPs.</p> <p>If more than one balancing item exists (sponsor support, pension protection scheme and benefit reduction) we are of the opinion that no separate valuation is necessary as the effort isn't worth the additional information (given the complexities for valuing sponsor support for MES in the public sector). Thus we do not agree with the approach suggested by EIOPA of valuing all other items of a holistic balance sheet first before recognizing any benefit reduction mechanisms as mentioned in 4.91.</p>	Public
Q36	<p>EAPSPI is still of the opinion that the concept of the HBS should not be applied to IORPs. The reason is that the HBS and the calculation of the SCR fully rest on the Solvency II structure regarding the market-consistent valuation of assets and liabilities and the assessing and quantifying of risks which are unsuitable for IORPs.</p> <p>But if the HBS were to be applied to IORPs, we would support a principle based approach to valuing sponsor support that leaves the specifics to be set by member states and national competent authorities. This approach would make it possible to find suitable solutions for valuation of this mechanism under consideration of the different types of sponsors and how sponsor support is organized and legally regulated (in social and labour law) within each member state. A "one-size-fits-all"-approach that doesn't fit accurately for any of the existing variants should not be applied.</p>	Public

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	EAPSPI in general wants to underline that sponsor support should be considered in a regulatory framework. Thus – given that the HBS should be introduced - the proportionality principle including the balancing item approach for the use of sponsor support in combination with PwC’s “M” approach for assessing sponsor’s strength should be part of this principle based approach.	
Q37		Public
Q38		Public
Q39	<p>In spite of its serious concerns against a possible introduction of a HBS-structure for IORPs, EAPSPI in general welcomes the official introduction of the “<i>balancing item approach</i>” (BIA) in combination with the simplified and heuristic check of sponsor strength by using PwC’s “M” approach because the BIA reflects the essential notion of the function of sponsor support as a flexible asset to call upon when needed.</p> <p>However, EAPSPI strongly suggests – if the HBS should be introduced at all – that in case of a strong sponsor (or other security mechanism) or multi-employer-scheme (MES) IORPs this should constitute a truly exceptional case that should release from explicitly setting up a holistic balance sheet or Solvency II-like risk based solvency capital requirements. The rationale is that, in the cases of the application of the BIA, the strength of the security mechanisms / sponsor support is actually proven and thus market consistent valuation (including using risk free interest rates) is not needed any more because the strength of the sponsor avoids the necessity of a transfer of the IORP’s assets and liabilities and further concrete quantifications seem to be superfluous. The BIA describes simply that sponsor support is a flexible asset that fills the gap if needed. This approach is also described by EIOPA (see 4.114.): “<i>In some circumstances the strength of the sponsor may be sufficient so that a detailed approach to valuing that unlimited sponsor support may be disproportionate. In addition, the set up and legal structure of IORPs may mean that the valuation is unnecessary and does not provide useful information to the IORP and/or supervisor. In these circumstances, IORPs could follow the balancing item approach such that the value of sponsor support is simply the required amount to balance the holistic balance sheet.</i>” Especially in the case of MES the BIA captures the notion that a large number of sponsors in the end is in charge of the</p>	Public

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settlement of pension claims (= HBS) and also serves as cushion for adverse developments (=SCR). This illustrates the flexibility of the sponsor support of MES IORPs and delivers a flexible protection of pension claims with solidarity.

To explain our position in more detail: The *“balancing item approach”* in particular for sponsor support shows the paradoxical character of the HBS as it reveals that the HBS in case of MES IORPs with strong sponsors and strong solidarity elements will always balance. The very fundamental notion behind the BIA is that the sponsor in the end is in charge of the settlement of pension claims (= HBS) and also serves as cushion for adverse developments (=SCR) illustrating the flexibility of the existing security mechanisms. With the suggested principle 2 (PwC’s *“M”*) to apply the proportionality principle it can be demonstrated that the sponsor(s) will be indeed able to step in when needed – thus the HBS is not needed any more, neither will market consistent valuation for the case of transfer as this transfer will not be necessary.

Thus we draw a different conclusion based on these notions: namely, if the quality of sponsor support is proven by the PwC criteria, no HBS and SCR for IORPs is needed because the security mechanisms of IORPs as *“holistic assets”* or – speaking with EIOPA’s terminology – as balancing items, deliver a flexible insolvency protection. The existing security mechanisms of IORPs should therefore not be seen as a part of the balance sheet or the solvency capital to fulfil the SCR within the Solvency II structure – they have a *substitutional character* that replaces the HBS and the SCR. Therefore this constitutes truly exceptional cases that should release IORPs from a Solvency II-like risk based regulatory regime.

Using EAPSPI’s suggested approach would avoid several problems:

- No concrete measurement is necessary if more than one mechanism is available to be used as balancing item (see 4.5 of Consultation Document which suggests that i.e. the sponsor support of a strong sponsor must be concretely valued using one of the other valuation methods if also a pension protection scheme (PPS) as balancing item of last resort security mechanism exists)
- the specific characteristics of IORPs would not be conceptualized and quantified inadequately as additional financial assets leading to procedures which are much too complex:

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- 1) The HBS perspective generally equates IORPs with insurance undertakings, respecting differences only as new assets put on top of the same basic structure. However, this perspective neglects the structural differences between IORPs and insurance undertakings due to the fact that in the case of occupational pensions there is a 3-party relationship (employer, employee and IORP) providing for a flexible and efficient structure for securing employees' claims.
- 2) This structural difference changes the starting point for regulating IORPs: The idea of the "back up facility" sponsor support and pension protection scheme is that they step in when they are needed no matter if the development is "normal" (HBS) or "stressed" (SCR). The differentiation of the value of the security mechanisms in the HBS in "normal times" and their loss-absorbing capacity in "stress situations" in the SCR seems artificial. This dichotomy is necessary only because of conceptualizing sponsor support and pension protection scheme as financial assets that have to fit into the Solvency II structure and once more underlines that this structure is not adequate for the regulation of IORPs. Dividing the security mechanisms in this way is unnecessary and leads to avoidable complexity.

In spite of its fundamental concerns against the HBS for IORPs, EAPSPI in general endorses the concept of the "balancing item approach" (BIA) in combination with the simplified and heuristic check of sponsor strength by using principle 2 (= PwC's "M" approach). We think this approach is practicable and efficient to implement, in particular with respect to using total wages as proxy for sponsors (public sector, charities, etc.) that do not have values like market capitalization or other suitable financial metrics (see 4.127, 4.200 and the rationale in 4.229). Using the wage sum as a proxy is a suitable approach particularly for MES with joint financing as the risk of sponsor default is covered within the scheme.

But EAPSPI is critical with respect to the requirement that IORPs shall demonstrate that the default rate of the sponsor (see 4.124) or PwC's M valuation of the sponsor (4.131) is likely to be stable over time. The stated examples are not sufficient and it is really questionable how IORPs can practically fulfil this requirement.

Public

Q40

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	The actual value of M should be determined taking into account the valuation results of the 2 nd IORP QIS in 2015. In addition also principle 1 may be used if reliable data is available and principle 3 for sponsors with PPS.	
Q41	With respect to the use of the balancing item approach for valuing sponsor support EAPSPI suggests that multi-employer schemes with large number of employers, legally enforceable sponsor support and joint financing should automatically qualify for applying the balancing item approach without referring to the strength of the individual sponsor (in addition to the listing in no. 4.4 of the consultation document). The rationale for this is that MES with sufficient number of employers and joint financing could be seen as a means of the collective pooling of default risk of individual sponsors – in analogy to the suggestions of EIOPA regarding pension protection schemes in 4.248 of the consultation paper.	Public
Q42	In spite of its fundamental concerns against the HBS for IORPs, EAPSPI in general endorses the concept of the “ <i>balancing item approach</i> ” (BIA) in combination with the simplified and heuristic check of sponsor strength by using principle 2 (= PwC’s “ <i>M</i> ” approach). Using the value “2” for M seems to be appropriate as a starting point for the 2 nd IORP QIS in 2015 .The final value of M should be discussed taking into account the valuation results of the 2 nd IORP QIS.	Public
Q43	Yes, agree. Pension protection schemes should definitely be considered either via backing up sponsor support or directly as balancing items on the HBS. Otherwise this important security mechanism for safeguarding the pension promise from the beneficiaries’ perspective would be neglected.	Public
Q44		Public
Q45		Public

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Q46	<p>EAPSPI is still of the opinion that the concept of the HBS should not be applied to IORPs as the HBS and the calculation of the SCR fully remain on the Solvency II structure regarding the market-consistent valuation of assets and liabilities and the assessing and quantifying of risks. We regard this approach as unsuitable for IORPs and the long term nature of pensions because it delivers inadequate management incentives.</p> <p>But if the HBS were to be applied to IORPs, we would agree to a principles-based and IORP specific approach to valuing sponsor support instead of an inadequate “one-size-fits-all”-approach for all types of IORPs. This enables to cover a broad range of different types of IORPs and sponsors as well as country specific differences and to find suitable solutions. Thus the regulatory specifics should be set by member states (see Q36) including a variety of equivalent approaches and leave it up to the IORP to decide which approach to choose (including particularly the balancing item approach). In addition further deterministic simplifications by member states to consider national circumstances should be allowed for. A stochastic modelling or explicit cash-flow-modelling should not be compulsory.</p>	Public
Q47	<p>EAPSPI is of the opinion that no guidance of EIOPA is needed.</p> <p>As suggested in Q36 and Q46 the regulatory specifics as well as practical guidance should be set by member states to make sure that a broad range of different type of IORPs and sponsors as well as country specific differences are adequately covered. This approach would most likely produce suitable solutions for valuation of sponsor support.</p>	Public
Q48		Public
Q49	<p>EAPSPI’s answer relates to Q49 – Q56: The HBS and the increasing number of suggested valuation approaches are not appropriate to reach the intended goal of the European Commission namely to precisely assess and quantify the “true risk position” of IORPs (CfA 4.1 from March 2011), because of the design and the valuation of the HBS. The valuation methods specified for the QIS and since then involve a high degree of arbitrariness and lead to pseudo-certainty which contradicts</p>	Public

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	<p>the notion of a neutral, objective and informative balance sheet. The newly introduced valuation approaches aggravate the problem of comparability of the HBS and SCR values determined by different valuation approaches (see 4.145 and EIOPA' s own analysis in section 4.5.6. stating huge differences between resulting values of the sponsor support given the modelling approach). This problem arises in case of the various suggested ways of quantification: Stochastic modelling essentially depends on the (often arbitrary) choice of parameters and models which make results hard to compare (also stated by EIOPA). With respect to the (simplified) deterministic valuation approaches it is not clear if the suggested simplifications are appropriate or if there are systematic biases in the valuation. Therefore, the results of stochastic modelling and the simplified deterministic approaches are not comparable and we simply do not believe that EIOPA will be successful in delivering models with comparable outcomes (see 4.145): <i>“When developing simplified methods or methods using deterministic approaches, EIOPA will consider carefully how to ensure that these methods and stochastic models produce comparable outcomes.”</i></p>	
Q50		Public
Q51		Public
Q52		Public
Q53		Public
Q54		Public
Q55		Public
Q56		Public
Q57		Public
Q58	<p>Given that the HBS would be applied to IORPs we agree to a principles-based and IORP specific approach to valuing sponsor support where specifics of the approach are set within member states instead of an inadequate <i>“one-size-fits-all”</i>-approach for all types of IORPs and sponsors. Therefore EIOPA should not define parameters to use for maximum sponsor support as this should be done at member state level and by national supervisory authorities.</p>	Public

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	<p>We agree with the procedure suggested by EIOPA in 4.199 in that sense that as a first step sponsor support should be checked with PwC's "M" criteria for sponsor strength. If the sponsor support is strong given this criteria (e.g. M equals 2 or bigger) sponsor support qualifies as a balancing item which should release the IORP from setting up a HBS, etc. as the balancing item is able to "balance technical provisions and reduce SCR to zero" (EIOPA 4.187).</p> <p>With respect to cases where the "M" criteria is not fulfilled, EIOPA suggests that IORPs should calculate the sponsor support more precisely and make "a quantitative assessment of the maximum amount of support the sponsor is capable of affording" (meaning a more detailed assessment with respect to the values checked within the "M" approach such as market cap, shareholder funds, discounted future cash-flows or total wages; see 4.200). We think the check of the appropriateness of the assessment should be left to national competent authorities (as is likely suggested by EIOPA in 4.201 to 4.203) and should also allow for a qualitative assessment.</p> <p>But in general the attempt to precisely calculate the value of (maximum) sponsor support is still questionable as there are no "universally recognised standards" for calculating it (stated by EIOPA in the 2013 Discussion Paper on Sponsor Support) and the calculation very quickly becomes (too) complex. Thus an explicit quantitative calculation should not be compulsory.</p>	
Q59		Public
Q60		Public
Q61		Public
Q62		Public
Q63		Public
Q64	<p>EAPSPI recognises that in particular the presented principle 2 (PwC's "M") for the use of the balancing item approach and the calculation of the sponsor support facilitates the valuation, especially if this needs to be done only for the suggested sample of the 5 largest sponsors. The suggested approach seems to be more appropriate than previous suggestions i.e. as applying the Alternative Simplified Approach procedure (incl. collecting the numbers for the two credit ratios,</p>	Public

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	<p>asset cover and income cover; to determine reasonable payment periods; to calculate the loss-absorbing capacity and to perform sensitivity analysis) for all the sponsors of multi-employer-schemes (suggested in EIOPA’s 2013 Discussion Paper on sponsor support). Thus, we think that this approach fits if the actual value of the sample of larger sponsors exceeds the required PwC value (M times the required HBS value) and therefore the balancing item approach can be used (see also EAPSPI’s suggestions for a full exemption in this case in Q39).</p> <p>But in other cases if the PwC criteria is not fulfilled (see 4.231) EIOPA’s approach seems to be unclear and needs further exploration: Should the IORP increase the sample of sponsors which are analysed with one of the valuation approaches (except for the balancing item approach) as long as the maximum value of the sponsor support is larger than the required HBS value? If this reading is correct this procedure seems to be still too complex particularly for multi-employer IORPs involving mostly large numbers of sponsors (especially in the public sector).</p> <p>Multi-employer IORPs by nature are not exposed to a default risk of all sponsors at the same time and it must be recognized consequently that the calculation / separation of liabilities for each employer in case of the “<i>last man standing</i>” arrangement of the IORP is quite complex and laborious.</p>	
Q65	<p>With respect to the use of the balancing item approach for valuing sponsor support EAPSPI suggests that multi-employer schemes with large number of employers, legally enforceable sponsor support and joint financing should automatically qualify for applying the balancing item approach without referring to the strength of the individual sponsor (in addition to the listing in no. 4.4 of the consultation document). The rationale for this is that MES with sufficient number of employers and joint financing could be seen as a means of collective pooling of default risk of individual sponsors – in analogy to the suggestions of EIOPA regarding pension protection schemes in 4.248 of the consultation paper.</p>	Public
Q66		Public

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EAPSPI welcomes that EIOPA still explicitly recognizes that the non-standard case of non-corporate sponsors, especially public sector entities and charities which are in addition mostly multi-employer-schemes (MES), deserve specific consideration.

We recognise that in particular the presented principle 2 (PwC's "M") for the use of the balancing item approach and the calculation of the sponsor support facilitates the valuation for not-for-profit sponsors, especially if this needs to be done by using total wages as proxy and for MES only for the suggested sample of the 5 largest sponsors. The suggested approach seems to be more appropriate than previous suggestions as applying the ASA procedure (incl. collecting the numbers for the two credit ratios, asset cover and income cover; to determine reasonable payment periods; to calculate the loss absorbing capacity and to perform sensitivity analysis) for all the sponsors of multi-employer-schemes (suggested in EIOPA's 2013 Discussion Paper on sponsor support).

With respect to the range of (partly new) simplified valuation methods presented by EIOPA, EAPSPI is of the opinion that these approaches (except the balancing item approach) are still not suitable / workable for not-for-profit and public sector sponsors as all these approaches focus on financial data / metrics of corporate sponsors. EIOPA has not yet further developed solutions or amendments for quantifying the sponsor support related to not-for-profit-institutions and for public sector IORPs (see No. 4.235 to 4.237) compared to EIOPA's Sponsor Support Consultation (see No. 64 to 67 and 101 to 102 of the 2013 Discussion Paper) and EIOPA's Sponsor Support Conference in 2013 – thus these problems are still not resolved.

Although EIOPA states (see 4.236) that assessing the ability of the sponsor(s) to provide financial support to the IORP is in principle not different for not-for-profit sponsors compared to corporate sponsors, no specific suggestions of how to do so can be found:

- EIOPA still mentions with respect to **charities, etc.** that a relaxation with respect to the income ratio but an increased value for the asset cover / balance sheet ratio within the ASA might be suitable. But we are of the opinion that it would be rather challenging to discov-

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er a serious (data) base for the deduction of how much relaxation is appropriate (i.e. to develop an adjusted credit ratio matrix for not-for-profits). Valid data on default probabilities for not-for-profit entities seems to be lacking. If no serious deduction is possible, the procedure as a whole becomes questionable. In addition, there is some doubt that financial ratios for not-for-profit entities have the same explanatory power as those of profit-oriented corporations always paying attention to their financial metrics. Therefore, the output of the simplified alternative approach for not-for-profit entities might not be comparable with the output for “normal” profit-oriented corporations.

- **Public sector sponsors** are not mentioned any more by EIOPA, although they were explicitly tackled in the Sponsor Support Discussion Paper of 2013 stating that the credit quality of the public sponsor may be assessed using the credit ratios analogue to the income and the asset cover ratio (see No. 67, Discussion Paper 2013). This seems to indicate that EIOPA realized that a thorough assessment of these mostly very complex financial arrangements and safeguard mechanisms of many public sector entities is time-consuming and can hardly be handled while the approach itself is already questionable (e.g. an attempt to precisely qualify). Multi-employer public sector IORPs in particular will face obstacles. For example, a German public sector IORP with municipalities as sponsors would have to assess the structure and the various dimensions of the revenue equalisations in Germany that governs the financial distributional system between the different administrative levels: municipalities, regions, and federal level. This system involves a distinction between the primary and secondary revenue equalisation (the formal allocation of proportions from certain tax revenues vs. hardship case adjustments) as well as between the horizontal and the vertical revenue equalisation (from one municipality/state to another municipality/state vs. from the federal state to the states or from the states to the municipalities). The German system of revenue equalisation is very complex and a thorough assessment seems to be unworkable in practice.

Q68

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Q69	<p>In EAPSPI's opinion pension protection schemes should definitely be considered either via backing up sponsor support or directly as balancing item on the HBS. If a PPS covers 100% of benefits and is sufficiently strong (i.e. large number of sponsors joining) it should be able to cover liabilities as well as SCR due to the loss-absorbing function. Otherwise this important security mechanism for safeguarding the pension promise from a beneficiaries' perspective would be neglected and the aim of the European Commission (similar level of protection irrespective of the security mechanisms used) would not be met.</p>	Public
Q70	<p>EAPSPI thinks it is important that the effect of a PPS as a balancing item is considered at all in the HBS either via modelling it indirectly as backing up sponsor support to function as balancing item by reducing sponsor default probability to zero or directly as balancing item. Therefore if relevant IORPs should be able to choose between both variants.</p> <p>One advantage of using the indirect approach of considering a PPS via the effect on sponsor support would be that it is less effort to model: in this case the sponsor support would not have to be modelled explicitly because sponsor support functions as a balancing item. In the case of considering PPS directly as an asset in the HBS, sponsor support would have to be modelled / valued concretely using one of the other suggested valuation methods although afterwards the PPS is included as a balancing item in the HBS (see also EIOPA's suggestions in 4.5).</p>	Public
Q71	<p>Yes, we agree, a PPS in principle should be allowed as a balancing item on the HBS. What is important is that <i>the effect of an PPS as a balancing item is considered at all</i> either via modelling it indirectly as backing up sponsor support to function as a balancing item by reducing sponsor default probability to zero or directly as a balancing item. A separate explicit valuation of sponsor support if also another balancing item (PPS, benefit reduction) is available is definitely not appropriate as it is complex and costly to generate (if possible at all, especially for public sector MES IORPs) and the additional information is not necessary.</p>	Public
Q72	<p>EAPSPI is of the opinion that the current rules of the existing IORP directive regarding funding and capital requirements are adequate. A market-oriented HBS and risk-based SCR should not be introduced. BUT if nevertheless more Solvency II-oriented concepts were introduced, the existing</p>	Public

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security mechanisms of IORPs (sponsor support, PPS, benefit reductions) should definitely be considered within the HBS. But EAPSPI suggests that in this case the balancing item approach should play an adequate role without the need for complex and time consuming calculations (see EAP-SPI's answer to Q39).

EAPSPI also wants to mention that those examples for the use of the HBS where real financial assets are required against Level A technical provisions and only SCR may be covered by Sponsor Support or PPS (i.e. example 1) the main driver of the quantitative impact of the proposed regulations will be market consistent valuation and the risk free discount rate used to calculate the best estimate of liabilities. The remaining items are less influential. The consequences would be – as analysed by EIOPA too, see 5.86 –enormous cost increases for sponsors (and not only recognized as balance sheet items for IORPs) as well as detrimental macroeconomic effects:

- increased call on business funds, due to the role of employers as guarantors of 'defined benefit' pensions in several EU states
- Consequences of this additional funding: significant negative impacts on capital spending, corporate cash flow, corporation tax payments, wages and employment
- more modest impacts on employee pension contributions, procurement, prices and dividend payments

See also EAPSPI'S answer to Q85 on this topic.

EAPSPI is of the opinion that - if ever the HBS were to be introduced at all – the HBS should be used exclusively as a risk management tool (i.e. EAPSPI prefers option 3 or example 6 of EIOPA's suggestions on how to use the HBS) without public disclosure and in combination with the use of the balancing item approach. Minimum funding requirements and valuation standards should continue to be according to the current IORP directive. Regulatory consequences of the HBS analysis within the risk management should be determined by national supervisors (i.e. recovery plans with long recovery periods).

It must be ensured that the use of the HBS will not be extended step by step to be finally used to assess quantitative requirements: in a first step an introduction as risk management tool in pillar II

Public

Q73

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	followed by the second step to use the HBS for strict harmonization of valuation and funding.	
Q74	No, HBS information should only be disclosed to supervisors as this information is only relevant for IORPs and supervisors but not for beneficiaries. Especially if there is other balance sheet information of pillar 1 according to national standards in addition to the risk assessment in pillar 2 it will not be easy to understand how these values relate to each other. In general EAPSPI is of the opinion that the valuation of assets and liabilities and risk-based SCR according to Solvency II are not appropriate for IORPs and therefore we do not support this option (see introduction part IV).	Public
Q75	No. Competent authorities should continue to use the locally established rules. EAPSPI is of the opinion that the qualitative requirements in the Fourth IORP II Compromise Draft of the Italian Presidency, in particular Art. 29 (Risk Evaluation for Pensions) is more than sufficient with respect to risk management requirements for IORPs. -But if the HBS should be introduced at all, it should be used exclusively as a risk management tool (i.e. EAPSPI prefers option 3 or example 6 of EIOPA's suggestions on how to use the HBS) without public disclosure and in combination with the use of the balancing item approach. Regulatory consequences of the HBS analysis within the risk management should be determined by national supervisors (i.e. recovery plans with long recovery periods).	Public
Q76		Public
Q77	If the concept of the HBS were introduced, Pension Protection Schemes (PPS) should definitely be considered as one of the core elements of the HBS. Otherwise this important security mechanism for safeguarding the pension promise from the beneficiaries' perspective would be neglected and the aim of the European Commission (similar level of protection irrespective of the security mechanisms used) would not be met. It is important that the effect of a PPS as a balancing item is considered at all in the HBS either via modelling it indirectly as backing up sponsor support (to function as a balancing item by reducing	Public

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	<p>sponsor default probability to zero) or directly as a balancing item. Therefore, if relevant, IORPs should be able to choose between both variants.</p> <p>One advantage of using the indirect approach of considering a PPS via the effect on sponsor support is that it is easier to model: in this case the sponsor support would not have to be modelled explicitly because sponsor support functions as balancing item. In the case of considering PPS directly as an asset in the HBS, sponsor support would have to be modelled / valued concretely using one of the other suggested valuation methods although afterwards the PPS is included as a balancing item in the HBS (see also EIOPA's suggestions in 4.5).</p>	
Q78	Yes, EAPSPI agrees, pure discretionary aspects should not be included.	Public
Q79		Public
Q80		Public
Q81		Public
Q82		Public
Q83		Public
Q84		Public
Q85	<p>Level B technical provisions should be the minimum requirement for the level of liabilities.</p> <p>Calculating technical provisions on a market consistent basis including a risk free interest rate is not necessary and not appropriate for IORPs. A mark-to-market valuation of liabilities for IORPs as envisaged under Solvency II would be counterproductive for long-term investments. Such a valuation would be extremely volatile, pro-cyclical, and based on a cut-off date; it would use the modelled view of an external investor and would therefore not take into account the specific feature of most IORPs. The one-year-perspective and a consequent mark-to-market valuation of liabilities would lead to a completely wrong assessment of the situation. Mark-to-market sets short-term and therefore undesirable incentives for the management. This type of valuation could harm solid and long-term planning, as well as risk analyses and related calculations. It would therefore not contribute to more security for the beneficiaries. And in addition a transfer of liabilities to other</p>	Public

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market actors (see i.e. EIOPA 5.83) is – unlike the case in the insurance sector – not relevant because of the existing security mechanisms of IORPs which are actually to be assessed by the HBS. Thus we think that especially in cases where the balancing item approach is justified, a mark-to-market valuation is neither appropriate nor necessary, given its harmful consequences as the function of a market-valuation (= transfer to other IORP or market actor) for reasons of beneficiaries protection is extremely unlikely as shown by the HBS. So the HBS with a strong sponsor as balancing item shows that no market consistent valuation is needed.

The result would be in addition an **enormous increase in liabilities** (without being a more accurate assessment) **to be covered by the sponsors** (for future promises and possibly for existing ones) will discourage sponsors from offering especially DB-schemes sponsored by employers. We therefore support EIOPA's analysis (i.e. 5.86, 5.177, 5.179 and 5.188) of the negative consequences of Level A technical provisions as funding requirements for existing promises for sponsors, employees and defined benefits and also with respect to growth and macroeconomic aspects.

These **consequences are confirmed by the IORP QIS in 2013 as well as other comprehensive studies**, i.e. the study "*The economic impact for the EU of a Solvency II inspired funding regime for pension funds*" by UK's employer association CBI together with Oxford Economics that analysed economic consequences of a 30% increase of liabilities to be covered by additional delivered funds by sponsors and the SCR covered by sponsor support or PPS (= corresponds to Level A technical provisions to be covered by financial assets). The main results of the study are an increased call on business funds and in consequence significant negative impacts on capital spending, corporate cash flow, corporation tax payments, wages and employment as well as more modest impacts on employee pension contributions, procurement, prices and dividend payments. To give some numbers:

- 30% increase of technical provisions = €440 billion (£350 billion) = cost increase for UK Businesses
- Up to 2.5% reduction of GDP for longer period
- Up to 180,000 job losses p.a.

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	<p>Similar results are given by the Report commissioned by UK's Pensions Minister Steve Webb (<u>Webb-Report</u>) indicating a funding shortfall in the UK of</p> <ul style="list-style-type: none"> • £400 billion (i.e. increase in technical provisions of £500 bn, less estimated sponsor support of £350bn, plus a net SCR of £250bn. The net SCR also allows for sponsor support). • £150 billion (i.e. increase in technical provisions of £500bn, less estimated sponsor support of £350bn) 	
Q86	<p>Our first option would be that all IORPs are in general allowed to calculate Level B technical provision as the rationale in Q85 is in general applicable. Alternatively it should be applied as a member state option.</p>	Public
Q87		Public
Q88		Public
Q89		Public
Q90		Public
Q91		Public
Q92		Public
Q93	<p>EAPSPI is of the opinion that there is no need for harmonizing the recovery period (for meeting the SCR or the technical provisions) as this is best regulated on national grounds given the national requirements with respect to calculating liabilities. Due to the long-term nature of pensions it is absolutely necessary to have long recovery periods: The principle should be that the length of the recovery period should be suited to the duration of the liabilities.</p>	Public
Q94	<p>Due to the long-term nature of pensions it is absolutely necessary to have long recovery periods for the SCR: The principle should be that the length of the recovery period should be suited to the duration of the liabilities and this should also be relevant for the SCR as a long term cushion or, as formulated by EIOPA, as "<i>longer-term</i>" capital requirement.</p>	Public

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Q95	Due to the long-term nature of pensions it is absolutely necessary to have long recovery periods: The principle should be that the length of the recovery period should be suited to the duration of the liabilities and this should also be relevant for the SCR as long term cushion or, as formulated by EIOPA, as a “ <i>longer-term</i> ” capital requirement.	Public
Q96		Public
Q97	EAPSPI is in favour of a strict grandfathering for existing pension promises and schemes (or at least long transitional periods) as otherwise increased call on business funds would cause great harm to occupational pensions (extreme case: closing of already existing schemes) as well as negatively affecting economic growth. As mentioned in Q85 the negative consequences are confirmed by comprehensive studies, i.e. the study “ <i>The economic impact for the EU of a Solvency II inspired funding regime for pension funds</i> ” by UK’s employer association CBI together with Oxford Economics which gives an analysis of likely consequences. If no extensive grandfathering were implemented the main results would be an increased call on business funds and in consequence significant negative impacts on capital spending, corporate cash flow, corporation tax payments, wages and employment as well as more modest impacts on employee pension contributions, procurement, prices and dividend payments.	Public
Q98		Public
Q99	EAPSPI highlights that those examples for the use of the HBS where financial assets are actually required against Level A technical provisions and only SCR may be covered by Sponsor Support or PPS (i.e. example 1), the main driver of the quantitative impact of the proposed regulations will be market consistent valuation and the risk free discount rate used to calculate the best estimate of liabilities. The remaining items are less influential. The consequences would be – as analysed by EIOPA too, see 5.86, 5.177, 5.179 and 5.188 – an enormous cost increase for sponsors (and not only recognized as balance sheets items for IORPs) as well as detrimental macroeconomic effects: <ul style="list-style-type: none"> • increased call on business funds, due to the role of employers as guarantors of ‘defined benefit’ pensions in several EU states • among the consequences of additional funding: significant negative impacts on capital spending, corporate cash flow, corporation tax payments, wages and employment 	Public

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	<ul style="list-style-type: none"> more modest impacts are likely on employee pension contributions, procurement, prices and dividend payments <p>See also EAPSPI'S answer to Q85 on this topic.</p>	
Q100	No. Explanation see in Q 99.	Public
Q101		Public
Q102	No.	Public
Q103		Public
Q104	No.	Public
Q105		Public
Q106	EAPSPI would agree that example 4 could be used for IORPs in the EU only in the unchangeable case that the use of the HBS would have to exceed the risk management tool function within pillar II	Public
Q107		Public
Q108	No.	Public
Q109	See Q73 – Q75.	Public
Q110	Yes.	Public
Q111	EAPSPI – given its general rejection of the HBS based on the Solvency II structure for IORPs – welcomes the balancing item approach as it represents a workable heuristic for the notion of IORPs' flexible security mechanisms with respect to sponsors, pension protection schemes and benefit reduction mechanisms. But we think in case of the application of a balancing item the IORP should be totally exempt from other HBS requirements (see Q39).	Public