Comments Template on **Discussion Paper on Sponsor Support Technical Specifications**	**Deadline 31 October 2013 18:00 CET**

Name of Company:	GDV - The German Insurance Association	
Disclosure of comments:	Please indicate if your comments should be treated as confidential:	Public

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The numbering of the questions refers to Dicussion Paper on Sponsor Support.

Reference	**Comment**	
General Comment	The German Insurance Association (GDV) welcomes the opportunity to comment on EIOPA's Discussion Paper on Sponsor Support Technical Specifications, particularly in view of the substantial difficulties emerged in the application of these technical specifications. The GDV supports the introduction of a **risk-based solvency regime** for the regulation of occupational pensions, while still recognising the specific characteristics of IORPs, such as sponsor support. German insurers are in favour of more **transparency on the risks** and greater security for members and beneficiaries. For the different types of IORPs the **capital requirements should** sufficiently **reflect the true risk profiles** when evaluating the sponsor support.	

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The GDV fully supports the commitment by EIOPA to improve the general sponsor support methodology and to look at some new approaches. In particular, the simplifications proposed and some features of the new approach, such as an alternative solution for the maximum sponsor support, are very useful particularly for small and medium-sized IORPs and IORPs with many employers.

The GDV welcomes EIOPA's intention to undertake quantitative analysis of various possible evaluation methods and to elaborate on the approaches and directions put forward in this discussion paper, taking into account the feedback received from stakeholders.

First of all, **it is not possible for small, medium-sized and multi-employer IORPs to apply the introduced alternative simplified approach** of calculating sponsor support.

On the one hand, the calculation of the financial strength of sponsors is not always possible, since many IORPs do not have the necessary data. In this case we would suggest a determination of the default probability of the sponsors without the use of income statements and balance sheets of each employer. This could be done on the basis of **publicly accessible collective data**. On the other hand, if a sufficient data base for the evaluation of sponsor support is given for a certain sponsor, then this data should be used. Moreover, the consistency of accounting methods should be secured and changes should be made transparent.

Furthermore, **materiality aspects** have to be considered as well. If there is a sufficient pension protection scheme (PPS) in place, then even simpler approaches for the valuation of sponsor support might be appropriate: When both PPS and sponsor support are taken into account, the overall HBS, and therefore the protection of members and beneficiaries, are not affected negatively. However, due to transparency reasons a partition into both components is necessary.

Finally, some stages of the alternative simplified approach of calculating sponsor support have limited added value. For example, the dependency of the payment periods of sponsor support on the financial strength and the testing of different payment periods could be omitted.

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The German insurers hope that our suggestions and simplifications will be taken into account by EIOPA. If these difficulties can be solved, the GDV believes that EIOPA's proposed approach will lead to better protection of the members and beneficiaries of IORPs.

Special features of German IORPs

Since the alternative simplified approach of calculating sponsor support did not lead to the desired objective for the German IORPs, the GDV would like to take the opportunity of describing some of the special features of its members. In order to evaluate the sponsor support, the IORPs need to be able to assess the financial strength of each sponsor and the legal enforceability of its sponsor support, where the latter is stipulated by the German labour law (BetrAVG).

One special feature of the German IORP market is the existence of multi-employer schemes. A notable number of IORPs is backed by more than hundred sponsors and this number is increasing steadily. Even with the improved alternative method it is very challenging and not always possible to evaluate the value of sponsor support particularly in the case of a large number of sponsors. The reason for this is that the methods presented require in-depth insight into individual data on the sponsors. In order to be able to assess the financial strength of the sponsors, the IORPs have to analyse and assess the income statement and the balance sheet of each sponsor which is very complex and extensive, and not always possible (e.g. no standardised accounting methods and data formats for different sponsors, different time-lines of reporting by different sponsors, low priority for the sponsors to provide data). Moreover, there were several discussions in Germany in the past about the introduction of risk-based premiums for the pension protection scheme PSV. As a first approach, the valuation of premiums should have been based on the individual risk of each sponsor. But this approach was dismissed by the same reasons mentioned above.

Therefore, it is of utmost importance, that a valuation of the financial strength is possible without the use of income statements and balance sheets of each employer. The sponsors could instead be divided into groups on the basis of publicly accessible collective data. Since this is a special

	feature of the German market, the principle of subsidiarity should apply. Next to the number of sponsors, the necessary resources and know-how have to be taken into account. Particularly small and medium-sized IORPs do not always have sufficient additional resources and know-how for an assessment of the income statement and the balance sheet of each sponsor. This also leads to additional cost burdens. The principle of proportionality should apply in this case.
Q01.	**Should IORPs be provided with additional guidance for conducting stochastic valuations of sponsor support?** Many IORPs, particularly small and medium-sized, will not be able to develop a stochastic model with their own resources. They will, therefore, rely on a standard model. Thus, a development of a well-functioning standard deterministic model is more important than additional guidance for conducting stochastic valuations of sponsor support. Furthermore, for some (homogeneous) risk profiles further simplifications are possible.
Q02.	**Should IORPs be provided with additional guidance for conducting valuations of sponsor support using either Simplification 1 or 2? Should either of these simplifications be removed or should any other simplification be developed?** In general, both simplifications are easy to implement. The real problems are that the maximum value of the sponsor support and the default probability / financial strength of sponsors are not always possible to assess as it has been previously pointed out. As long as IORPs have no sufficient information on the income statement and the balance sheet of some sponsor, there should be general uniform principles to assess the maximal value of sponsor support and its default probability / financial strength. Simplifications, also based on the principle of proportionality, are necessary.
Q03.	**In the stakeholders' view what role should the concept of maximum sponsor support play in the general valuation principles for sponsor support?** Especially in case of multi-employer schemes it is very complex and extensive to evaluate the maximum value of the sponsor support. Therefore, the maximal value should not be included in the standard deterministic model, unless an IORP possesses all the necessary information to assess the income statement and the balance sheet of the sponsor.

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Q04.	**Is wage an appropriate additional measure for estimating the maximum amount of sponsor support? If so, please explain why? Are there any other measures which could be used to assess the maximum sponsor support?** a) Wage can, at best, be used as an additional factor for the assessment of the maximum value of sponsor support. Factors that can be put up as capital if necessary are more important. b) An appropriate assessment is only possible if the detailed income statement and the balance sheet of the sponsor are accessible to the IORP and the required know-how for the assessment of the data is available. Therefore, wage should not be included in the standard deterministic model, unless an IORP possesses all the necessary information to be able to assess the income statement and the balance sheet of the sponsor.	
Q05.	**Are stakeholders comfortable with the concept of linking default probabilities, credit ratios and sponsor strength?** An appropriate assessment is only possible if the detailed income statement, the balance sheet of the sponsor and the required know-how for the assessment of these data are available. Therefore, in case of multi-employer schemes it is a very complex and extensive calculation, which is almost impossible to perform, because IORPs do not have these data. It is, moreover, certainly too costly for small and medium-sized IORPs to acquire the necessary know-how regarding the valuation of default rates and credit ratings/ratios.	
Q06.	**Do stakeholders agree with exploring the possibility of including a standard table in the technical specifications that links credit ratios with default probabilities?** It can be assumed, that the standard tables in the technical specification are more objective than the assessments that are performed by IORPs with or without the assistance from the sponsors. This would also lead to a higher transparency of the underlying evaluation methods. Any standard model is helpful, particularly for small or medium-sized IORPs.	
Q07.	**Do stakeholders have other suggestions to derive default probabilities of the sponsor and to reduce reliance on credit ratings?** The use of statistics, clustering, sector-specific data or any other standardised default data should be used instead of individual default probabilities.	

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	Furthermore, if there is a sufficient PPS in place, then even simpler approaches for the valuation of sponsor support might be appropriate: When both PPS and sponsor support are taken into account, the overall HBS, and therefore the protection of members and beneficiaries, are not affected negatively. However, due to transparency reasons a partition into both components is necessary.	
Q08.	**Do stakeholders agree that timing of sponsor support reflecting the affordability of making additional payments could be an improvement to the general principles for valuing sponsor support?** It is, in principle, appropriate to use the timing component when calculating the value of the sponsor support. However, the model might become more complex.	
Q09.	**Do stakeholders think that limited conditional sponsor support should be valued and included on the holistic balance sheet? Should it be included separately?** By German labour law, the subsidiary responsibility (Subsidiärhaftung) makes the employers always liable for the provision of occupational pensions. Therefore, limited conditional sponsor support is not common in Germany. Only the legally enforceable sponsor support should be included.	
Q10.	**Should more detailed guidance be provided in future technical specifications to value sponsor support that is subject to discretionary decision – making processes? If yes, please explain in what way. Could the suggested detailed guidance also be applied to benefit adjustment mechanisms that contain discretionary elements?** In view of the diversity of occupational pension schemes across Europe, each additional detailing would lead to a high complexity.	
Q11.	**Please provide your general comments on the alternative approach.** The presented simplifying approach for the valuation of the sponsor support should be viewed critically from the point of view of IORPs with many sponsors and small and medium-sized IORPs. The method requires the assessment of the financial strength of each sponsor which is based on individual data of the sponsors such as income statements and balance sheets. • This is not feasible for IORPs backed by many sponsors. • It is questionable, whether the sponsors will provide the required data for the calculation	

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	of the necessary indices. • Small and medium-sized IORPs might not have the adequate know-how and the necessary data. • The assignment of assets and provision for premium refunds to single sponsors is not possible (no ring-fenced funds at employer level in general). Thus, a determination of the financial strength, and therefore, of the default probability of the sponsors should be possible without the use of income statements and balance sheets of each employer or any other assistance from the sponsors. This could be done on the basis of publicly accessible collective data. The discussion paper does not take into account the principle of proportionality, since there are neither simplifications nor a possibility to neglect some steps due to immateriality.	
Q12.	**Does the alternative approach address the concerns raised during the previous consultation on the technical specifications?** The GDV welcomes, that the requirement of calculation of maximum value of the sponsor support is not needed in the alternative approach. The approach of using publicly accessible data without the need of an own thorough assessment of the default probability of a sponsor is on the right lines. This approach could be suitable if it would use clusters of sponsors instead of individual assessment of each sponsor, particularly for small and medium-sized IORPs and for IORPs backed by many sponsors.	
Q13.	**Are there any areas that have not been addressed adequately enough?** Some of the sponsors of small size are not liable for disclosure. Thus, individual data is not available for such companies. The approach of using clusters of sponsors instead of individual assessment of the financial strength of each sponsor could also solve this problem. Additionally, it could also be a suitable approach for multi-employer IORPs.	
Q14.	**Are IORPs still likely to want to calculate a maximum value of sponsor support (even if not required under the alternative approach)? If so, for what purpose?** In case of multi-employer schemes it is very complex and extensive to evaluate the maximum value of the sponsor support. Therefore, the maximal value should not be included in the standard deterministic model, unless an IORP possesses all the necessary information to assess the income statement and the balance sheet of a sponsor.	

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Q15.	**Do stakeholders have other suggestions to adjust these ratios to cater for different sectors?** The valuation could be done on the basis of publically accessible aggregated data. Moreover, a high level of detail is not necessary.	
Q16.	**Does Stage 1 contain enough information and guidance for IORPs to calculate a credit strength that is proportionate for QIS purposes?** The assessment of the financial strength of each sponsor based on individual data of the sponsors such as income statements and balance sheets is not feasible for many IORPs. In this case, the determination of the financial strength of the sponsor could be made at an aggregate level (clustering of sponsors). This could be done on the basis of publicly accessible collective data.	
Q17.	**Does Stage 1 contain enough guidance for IORPs to do their own calculations if they believe this is appropriate for them to do so?** If for some sponsor an extensive and stable data base is available, stage 1 could be appropriate. However, the assessment of the financial strength of each sponsor based on individual data of the sponsors such as income statements and balance sheets is not feasible for many IORPs. The appropriateness of the indices should be reviewed regularly.	
Q18.	**Are Income Cover and Asset Cover suitable credit ratios to use for Stage 1?** This method could be applicable for sponsors, where the necessary data is easily available. Generally, it is more appropriate to deduce the financial strength of the sponsor and its default rate from publicly accessible collective data. By doing so, it would be unnecessary to evaluate the numbers Income Cover und Asset Cover, for which deep insight into the individual data of the sponsor is necessary.	
Q19.	**Are the parameters used to determine sponsor strength in Table 4 appropriate?** If for some sponsor an extensive data base is available, then Table 4 could be applied. However, in general, a less detailed classification, especially under the consideration of table 7, is more appropriate for the assessment of the financial strength of the sponsors. The groups medium strong, strong and very strong sponsors could be combined to one group. For weaker sponsors, however, the detailed differentiation is appropriate.	
Q20.	**What other definitions of earnings or net assets could be used in sectors where the standard definitions are not appropriate?** There is no need for isolated assessment of each employer if clusters of employers are used	

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	(publically accessible aggregated data).	
Q21.	**Are the periods shown in Stage 2 appropriate (bearing in mind this is for QIS work only, and not to determine a policy response)?** For simplification reasons, we suggest to keep the period of payment of sponsor support constant and independent of the financial strength of the sponsor. This refinement, which leads to a lower present value of sponsor support for weaker sponsors in comparison to strong sponsors, is not considered to be important. We suggest a single length of the period equalling ten years. A payment of the sponsor support within the first year or a payment uniformly distributed over the first 3/5 years is not appropriate since the payment can occur at a random time in the projection in the present value of the deficit. Taking this into account, a uniform distribution of the payment over the first ten years appears to be more appropriate and conservative enough.	
Q22.	**Do you agree that time periods for contributions for the QIS calculations for sponsor support should be based on affordability or should they be based on willingness/obligation to pay?** Yes, the evaluation of sponsor support should be based on affordability.	
Q23.	**To what extent are there any IORPs whereby sponsor contributions cannot exceed certain limits (even if contributions are affordable)?** To our knowledge, there are no limits that the sponsor contributions cannot exceed in Germany.	
Q24.	**Are the annual probabilities of default appropriate for future QIS purposes? If not, why not?** It could be a possibility to adjust the default probability of the sponsor due to the assumption of a zero recovery rate. Moreover, a diversification effect could be taken into account since not all of the sponsors default at the same time.	
Q25.	**Do stakeholders have any comments on stage 3?** For simplification reasons this step could be omitted. As an alternative, the above mentioned simplification with recovery rate of zero and duration of payment period of ten years could be used analogously to the valuation of sponsor support with simplification 2. (Thus, the present value of the deficit (PVD) would be divided into equally high contribution payments according to the duration of payment period (d). The present value of the sponsor support (PVSS) is then determined by the multiplication with the survival probability $p=1-q_{def}$, where q_{def} is a one-year default probability: $PVSS=PVD/d*[(p^{(d+1)}-1)/(p-1)-1]$.)	

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Q26.	Is it reasonable to not allow for any recoveries from sponsor defaults? Please provide examples where this could increase the calculated value of sponsor support. For simplification reasons, it is reasonable to not allow for any recoveries from sponsor defaults. However, similarly to our answer to question Q24, the default probabilities might need a downward adjustment.	
Q27.	Is it appropriate to do separate calculations to allow for sponsor support from other group companies (both for legally enforceable and not legally enforceable support by group companies)? This simplification approach seems to be very complex. On the other hand, the support should be included if it is legally enforceable.	
Q28.	Should any other guidance be included on how to allow for sponsor support from other group companies? If the sponsor support is not legally enforceable, it should not be included.	
Q29.	What could be other valid reasons why the IORP should or should not take the financial position of the wider sponsor group into account when assessing the sponsor's financial position? Only legally enforceable sponsor support should be included. First of all, the "main" legal sponsor of the IORP is responsible for its pension commitment. It depends on group's internal agreements whether and to what extent the support is provided by other companies of the group. These internal agreements can also change over time. Thus, an IORP, particularly if backed by many sponsors or sponsor groups, is hardly able to assess the value of this commitment. External credit ratings and default probabilities usually implicitly take into account the membership within a group of companies. Therefore, caution is necessary to avoid double gearing between group entities.	
Q30.	Is the approach to determining the loss absorbing capacity appropriate? This approach seems to be appropriate only if an IORP has an extensive data base for an assessment of the financial strength of each sponsor. However, many IORPs, especially small, medium-sized, and multi-employer IORPs, cannot assess the income statement and the balance sheet of each sponsor. As previously pointed out, the standard model should include an assessment of the financial strength of the sponsors based on publicly accessible collective data.	

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	Consequently, stage 6 also needs to be adjusted accordingly, since the financial strength of employers cannot be adjusted after the calculation with the SCR (minus the loss-absorbing capacity of benefit adjustment mechanisms that take precedence over sponsor support). For simplification reasons, the default probability could be left unchanged. If the stage 3 could be omitted (see Q25), the loss-absorbing capacity of sponsor support could be evaluated as $SCR/d*[(p^{(d+1)}-1)/(p-1)-1]$, where the default risk of the sponsor is not included in the SCR. The assignment of assets and provision for premium refunds to single sponsors is not possible (no ring-fenced funds at employer level in general) and not appropriate. Therefore, a separate calculation of SCR for each sponsor is not possible. A general approach for the valuation of a single SCR for all employers should be used instead.	
Q31.	**Should any other sensitivity analysis be considered?** From our point of view, additional sensitivity analysis is not necessary. At least the general simplified approach should not take the sensitivity analysis into account. If the financial strength of the sponsors is assessed on the basis of publicly accessible data, then it is difficult to take the change of the financial strength of the sponsors into account. Also the change of the discount rate (+/-1% and +/-1,5%) without an adjustment of the cash flow has limited added value.	
Q32.	**Are there any other types of sponsors that should be included?** None	
Q33.	**What additional work should be carried out if this methodology was to be used for determining sponsor support in a regulatory or supervisory environment?** The possible additional work has been mentioned in the previous questions.	
Q34.	**What other improvements could be made to the suggested approach?** The possible improvements have been mentioned in the previous questions.	
Q35.	**Are there any aspects of the suggested approach which are unclear?** It would be helpful to have some tools or measures for checking whether the results from the model are plausible or not. This is of particular importance for small and medium-sized IORPs or those with many sponsors.	
Q36.	**How could the average financial strength of an industry be determined?**	

Template comments

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	Generalised and publicly accessible collective data should be used. These data should already include information about the strength of an industry.	