<table>
<tr><td colspan="2">Comments Template on EIOPA-CP-11/006
Response to Call for Advice on the review of Directive 2003/41/EC: second consultation</td><td>Deadline
02.01.2012
18:00 CET</td></tr>
<tr><td>Company name:</td><td colspan="2">HM Treasury/Department for Work and Pensions</td></tr>
<tr><td>Disclosure of comments:</td><td>EIOPA will make all comments available on its website, except where respondents specifically request that their comments remain confidential.

Please indicate if your comments on this CP should be treated as confidential, by deleting the word Public in the column to the left and by inserting the word Confidential.</td><td>Public</td></tr>
<tr><td></td><td colspan="2">The question numbers below correspond to Consultation Paper No. 06 (EIOPA-CP-11/006).

Please follow the instructions for filling in the template:
⇨ <u>Do not change the numbering</u> in column “Question”.
⇨ Please fill in your comment in the relevant row. If you have <u>no comment</u> on a question, keep the row <u>empty</u>.
⇨ There are 96 questions for respondents. Please restrict responses in the row “General comment” only to material which is not covered by these 96 questions.
⇨ Our IT tool does not allow processing of comments which do not refer to the specific question numbers below.
o If your comment refers to multiple questions, please insert your comment at the first relevant question and mention in your comment to which other questions this also applies.
o If your comment refers to parts of a question, please indicate this in the comment itself.
Please send the completed template to CP-006@eiopa.europa.eu, <u>in MSWord Format</u>, (our IT tool does not allow processing of any other formats).</td></tr>
<tr><td>Question</td><td colspan="2">Comment</td></tr>
<tr><td>General comment</td><td>We appreciate the opportunity to respond to the consultation, and note the time pressures under which EIOPA have been operating. That said, we have a number of general comments relating to our strong concerns with the proposal to apply Solvency II rules to IORPs, as well as the process through</td><td></td></tr>
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which this is being examined.

We have a serious concern with the overall approach to the consultation. The default position throughout the consultation - both at a general level, and at the level of individual details - is that Solvency II should be applied to IORPs unless there are good reasons not to do so. This places the burden of proof on those who do not agree to change. However, legislation should only be introduced, or proposed, where there is a demonstrated need for it. It is not appropriate that legislation is proposed unless a good case can be demonstrated against it – the default must be that no legislation is proposed unless it is demonstrated to be of benefit, and the burden of proof must be on those proposing legislation. Our very strong view is that no good case has been made for new maximum-harmonising solvency rules along the lines of Solvency II, and no evidence has been offered that these proposals will create a net positive benefit for scheme members, employers, or the wider economy.

The rationale for change is described as:

- creating a level playing field with insurers, on the principle of substance over form; and
- facilitating the market in cross-border IORPs

Neither of these arguments stand up to scrutiny:

- Occupational pensions are fundamentally different in substance to apparently similar insurance products, but the approach to the consultation has led to these differences being down-played. One of the fundamental differences – at least with respect to UK schemes – is that unlike insurance products, occupational pension benefits are prescribed by social and labour law. Benefits are therefore not guaranteed in the same way, which means that concepts that are core to Solvency II (such as valuation of liabilities on the basis of their transfer value) are simply not appropriate for IORPs. More generally, the promise is owed not by the IORP but by the sponsoring employer. This means that the relationship between IORP and scheme member is fundamentally different to that between insurer and policy-holder, and there is no comparable relationship between the IORPs and its sponsor in the insurance sector – for example, an insurers' only option to address a shortfall is to raise capital from external investors, which is entirely different from the IORPs position. Furthermore, IORPs are not-for-profit vehicles operating on behalf of scheme members. They are not trading, and they are

not in competition with insurers, so there is no legitimate level playing field issue here.

- The consultation acknowledges that the reason for the low level of cross-border trade may be simply a result of lack of demand. However, this is not explored in any detail, and no evidence is provided that any of the measures in the consultation will have any impact on the volume of cross-border trade.

In any case, neither argument provides a good reason for proposals of such magnitude, that carry such a high risk, and are therefore highly disproportionate to the problems they purport to address.

We are particularly concerned with the very high risks and costs of the proposals. The combination of introducing a risk-free discount rate, alongside a new Solvency Capital Requirement, would – if applied on Solvency II basis – increase in the notional capital requirements for UK provision by 30% of GDP or more. However, there is a fundamental lack of detail about how or whether the main mitigant – the sponsor covenant – might be valued, or treated on the balance sheet, meaning that we need to assume a very high increase in the capital that sponsors will need to put into their IORP schemes. This will significantly reduce the capital available for other purposes, with a major knock-on effect on economic growth and employment. Furthermore, as DB schemes are entirely voluntary, this will have the effect of incentivising the closure of existing schemes on a large scale as capital requirements reach the buy-out level. This is the opposite of what the Commission have set out to achieve.

We are also profoundly concerned with the lack of any impact assessment other than a very brief note of the potential issues relating to individual measures. It is not possible to determine whether any particular option should be preferred when there is no idea of scale of positive and negative effects. But more importantly, no effort has been made to assess the scale of the impact of the overall package of proposals. A quantitative impact assessment is needed <u>before</u> recommendations are made – not afterwards.

Finally, as a general point on process, we are concerned that EIOPA have been given insufficient time to complete this work, and that the consequent lack of an impact assessment and detail on some of the most fundamental aspects of the proposals, necessarily restricts the strength of the conclusions that can be drawn at this stage.EIOPA should therefore make clear to the Commission that any recommendations at this stage are only tentative, and may be subject change following the outcome

	of the impact assessment and further work on the feasibility of certain key aspects such as valuation of the sponsor covenant, and that the recommendations cannot be finalised until this work has been completed.	
1.	We agree that the scope of the Directive should not be extended. In particular, we agree with the conclusion that Book Reserve schemes should not be included, on the basis that Member States are required to protect employees rights in the event of insolvency of the employer. However, as per our response to Q2, we are of the view that if EIOPA recommends new solvency arrangements along the lines set out in the consultation, it must consider narrowing the scope to exclude sponsor-backed IOPRs, which have much more in common with Book Reserve schemes than with insurance products. That said, our overall position is that the case for new maximum harmonising solvency requirements has not been made, and that if the solvency position is not changed we do not see an argument for changing the scope of the Directive.	
2.	If Book Reserve schemes are excluded from scope, the argument is equally strong for excluding all occupational pensions with an employer standing behind the scheme, regardless of whether it is a Book Reserve scheme, or a sponsored IORP. In the UK, the employer sets up a pension scheme and stands behind it. The IORP is the mechanism that delivers the benefit - but only exists in law as a separate structure because the Government requires it as a precondition of benefiting from tax advantages. However, **the obligation to pay remains on the employer** and the "pension promise" is part of the employment relationship, **not a contract** between the IORP and the member. The only **material** difference between a Book Reserve scheme and a sponsored IORP is the existence of assets held in trust to meet the liabilities, but this does not change the fact that the employer retains the obligation to pay. The scheme member of a sponsored IORP therefore has more protection than the scheme member of a Book Reserve scheme in the event of insolvency, not less. On that basis, if Book Reserve schemes remain excluded, then EIOPA should equally set out the case for (and against) amending the scope of the Directive to exclude sponsored IORPs. Furthermore, the immense difficulties of estimating the value of the sponsor covenant should provide EIOPA with ample evidence that alternative, more natural, approaches to the treatment of sponsored IORPs should be explored. EIOPA acknowledges that decisions on scope are of a political nature, and therefore beyond its remit. However, to preserve its political neutrality, EIOPA must explore and set out the case for (and against) all reasonable options - excluding certain options entirely from	

	consideration would have the practical effect of taking a political stance.	
3.		
4.		
5.	We have no particular view on the options. However, in the analysis, EIOPA should explore the purpose of promoting cross-border IORP activity – in particular looking at the intrinsic link to the employer, rather than considering IORPs as a financial product for which there is a direct market. Legislation, and the definition of cross-border IORPs, should be designed to support employers that operate across EU borders and that wish to establish a single IORP across their business. Whether the definition and subsequent legislation does so effectively should be the success criterion for the review.	
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10.	The proposal to define prudential regulation is likely to have an indirect limitation on member state competence over social and labour law. While we cannot determine the precise impact, we do not agree that this proposal is necessary, and the risks of limiting Member State competence are such that we do not agree to this proposal.	
11.		
12.	Without prejudice to our view that a harmonised solvency regime for IORPs is neither necessary or practical, the proposal for an evaluation tool that would enable supervisors to include all security mechanisms in the overall solvency assessment, may look like an attractive idea in theory. However, EIOPA has not demonstrated that this is workable in practice, and the UK govt is not convinced that – the holistci balance sheet will turn out not to be a practical or viable approach. In particular, we have serious concerns that methods for valuing either the sponsor covenant, or pension protection schemes, have not been explored, and no concrete proposals have been tabled. These methods are fundamental to whether the holistic balance sheet is even possible as an approach. Without knowing whether it is possible to value these two mechanisms in practice, it is extremely premature to invite views on the holistic balance sheet as a formal proposal. Given the critical role of the sponsor covenant and pension protection schemes in offsetting what	

	would otherwise be a totally unaffordable and unnecesary increase in capital requirements, we are highly concerned that EIOPA appears to be committing to a holistic balance sheet without any evidence that it is a practical proposition. **EIOPA should therefore work up valuation methods to a level of detail that allows assessment of how this might work in practice before, not after, it responds to the Commission with a recommendation that a holistic balance sheet should be pursued.**	
13.	We agree that any valuation of assets should be based on current market value. However, we have deep concern about the underlying assumption that viability of pension schemes should be judged solely on the basis of a point-in-time calculation comparing the current market value of assets with the net present value of liabilities. The critical issue with respect to IORPs is to ensure that current and future assets are sufficient to cover current and future cash-flows. However, given the predictable, illiquid, and very long-term nature of most IORPs liabilities, a point-in-time comparison is by itself of limited value in assessing the risk that those future cash-flows may not be met. It needs to be used cautiously as an indicator of future risks that informs the actions of the supervisor, not as the final measure of solvency, with certain prescribed consequences. This is in stark contrast to liabilities for most insurance products, where liabilities are mostly very short-term, and the current market value of assets is therefore an essential determinant of whether those short-term liabilities can be met. It is noticeable that the application of market-consistent valuation of assets and liabilities to long-term products has been by far the most difficult aspect of Solvency II. The introduction of a number of complex (and controversial) mechanisms aimed at eradicating "artificial volatility" (ie. volatility on the balance sheet that does not reflect changes to the underlying risks) in Solvency II is itself evidence that a point-in-time market valuation does not provide an accurate or complete reflection of risk for certain long-term products. Any fundamental review, such as this purports to be, should look at the fundamental issues, and it is therefore unfortunate and disappointing that EIOPA have not yet taken the opportunity to explore the merits and demerits of applying this approach to IORPs, or looked at potential alternatives.	
14.	The starting point for calculation of technical provisions under Solvency II is not appropriate for occupational pension funds. The Solvency II approach is based on the premise that liabilities can be transferred to a third party without changing those liabilities. However, the liabilities of an occupational pension scheme are simply not tradeable without alterning the pension. Unlike transfers between insurance books, if you transfer a DB pension through a buy-out	

	mechanism, you fundamentally alter the nature of the pension promise. This is because a DB pension is not a pensions saving scheme that happens to be run by the employer for the employee: instead it is part of the "employment" package, which incentivises the employee to have a long-term relationship with the employer. This relationship is something that needs to be fully recognised in the solvency requirements as a critical feature. A transfer of liabilities away from the sponsor's pension fund would alter the offer by: • Fundamentally altering the" pension promise". In the UK, although the IORP is the mechanism that delivers the benefit, the obligation to pay remains on the employer and the "pension promise" is part of the employment relationship, not a contract between the IORP and the member. • Weakening the employer/employee relationship (companies that do DB schemes best are those that have a long-term view. If you break the DB link by insisting that DB schemes are just another savings scheme, like any other insurance, you sever that whole set of incentives and long-term mindset); • And most importantly, by fundamentally changing the promise by changing the legal basis on which the it is based. Sponsored schemes are governed by domestic legislation setting out the conditions, level of return, annual uprating etc which inform the level of liabilities. These conditions can be amended by amending domestic legislation, meaning that liabilities of IOPRs with a sponsor are, substantially, a function of domestic legislation, <u>and are not fixed in the same way as the liabilities under a contract</u> For these reasons, the concept of transfer value cannot be applied – at least to sponsored IORPs. However, without a notional market (ie. potential to transfer to a third party) the idea of a market consistent valuation is empty. The consultation does not offer an alternative view of market consistent valuation – instead implying that it is synonymous with the use of a fixed, risk-free discount rate. However, this is circular, and simply begs the question. We are therefore strongly of the view that Option 2 is not appropriate, and that Option 1 is the only option that should be pursued.	
15.	We agree the credit standing of the IORP is not applicable in this context (ie. the funding level of the IORP should not alter the valuation itself), but the position of the sponsor as separate from the IOPR should be taken into account. Pension Funds with a robust sponsor standing behind them can invest in assets with a higher return but greater volatility without a risk to the pension scheme member. This is because the ultimate risk is born by the sponsor, not just the pension fund.	

16.	We do not agree to this recital. Accounting standards have a different purpose to supervisory valuation standards, so may evolve in ways that are inappropriate for these purposes.	
17.	The application of 76(1) is not problematic in itself as a stand-alone amendment, although the language on "insurance and reinsurance obligations" would need to be amended as well as language on "insurers" and "policy-holders" to avoid treating pensions as insurance products. On article 76/3, we strongly disagree with the introduction of market consistency for the valuation of technical provisions. The concept of transfer value is not appropriate for occupational pension funds (see above). But, any market-consistent valuation method will inevitably introduce a high level of volatility into pension fund balance sheets that does not reflect changes to the risk to the scheme members (artificial volatility). This is likely to have very profound effects on the investment behaviour of pension funds (eg. pushing them away from investment in equities), with a significant knock-on effect on the availability of equity capital, and ultimately on economic growth. Therefore we strongly reject option 2. Furthermore, it is not clear that there is any market information that is relevant to establishing the level of technical provisions, other than that necessary to determine the discount rate. We cannot therefore see the purpose of introducing 76(3) option 1. On 76(5), this would require calculation of technical provisions under a harmonised methodology. The current Directive is fully consistent with actuarial practice, and allows for the adjustments necessary to take into account the different national legislative requirements underpinning the pensions promise (for example, national legislation governing uprating requirements, which impact significantly on technical provisions). A harmonised, centrally prescribed, approach is not appropriate given that the nature of pensions liabilities are a function of national legislation which differs greatly between Member States.	
18.	The IORPs Directive includes "if applicable, an appropriate margin for adverse deviation". This is a fundamentally different concept to the Solvency II risk margin, which is based on the additional capital a 3rd party would require to take over the obligations. As stated above in response to question 14, it is not appropriate to use the concept of a transfer value. On that basis, the "no change" option is the only option that is appropriate for occupational pension funds. However, the margin for adverse deviation should not be treated as a Risk Margin (with any further connotations with respect to solvency requirements), but rather as the inclusion of an appropriate margin for adverse deviation.	

19.	Future accrual of benefits should be disregarded for valuation purposes, but guaranteed future increases should be taken into account.	
20.		
21.	We are very disappointed that option to retain the approach based on return on assets (Option 1) appears to have been discounted – particularly for those pension funds with a strong employer covenant. No good reason for this is given. The rationale is simply that "Option 1 is not compatible with the holistic balance sheet". However, it is not clear at all why this is incompatible with the holistic balance sheet. The holistic balance sheet is only a mechanism by which all assets and liabilities can be valued. It does not follow that all assets and liabilities need to be assessed using precisely the same criteria. Furthermore, the long-term, illiquid, and fixed, nature of pension fund liabilities means that it is entirely appropriate and prudent to expect those pension funds to invest in equities and other higher-yielding instruments without introducing a risk that cannot be covered by the sponsoring employer. In that light, the UK Govt is particularly concerned that the option of using a discount curve more akin to the actual risks faced by – ie. based on the curve for AA corporate bonds as prescribed in the current IORPS Directive – as been omitted from any consideration. With respect to the two options EIOPA do put forward, both are based on use of a risk-free discount rate. The negative impacts from imposing a risk-free discount rate under either option far outweigh any potential positive effects. We feel unable to comment specifically on Option 3, given that there is no clarity on what the consequences would be for sponsor-backed IORPs in terms of the assets they would need to hold. In the absence of clarity over how Option 3 might work, both the options put forward by EIOPA will be overly prudential and lead both to increased capital requirements on a very large scale , and introduction of massive artificial volatility on the pension fund balance sheet as movement in assets valuations is no longer reflected in changes to the valuation of liabilities. While this could be mitigated to an extent by hedging, this is expensive (with all additional costs inevitably passed to scheme members) and unnecessary as the volatility is artificial in the sense that it does not reflect volatiltiy in risks to the scheme. This will strongly incentivise all sponsoring employers who can to close their pension scheme to new members and new contributions and "buy out" their existing liabilities. Remaining pension funds will be strongly incentivised to derisk on a large scale to avoid artificial volatility. Given the €500bn invested in equities, and a further €2-300bn invested in corporate bonds, the resultant shifts in investment behaviour will reduce capital available to the	

	corporate sector by over €500bn, significantly reducing prospects of growth, and destabilising capital markets. These damaging behavioural effects are likely to be seen equally for option 3 even if assets were only required to meet Level B technical provisions. The approach would quantify the additional pressure on the sponsor covenant, creating an incentive for pension funds to avoid the subsequent artificial balance sheet volatility which would create very large (albeit notional) pressures on the sponsor, which would be evident to investors, during stressed markets. We have serious concerns that the consultation does not identify the positive and negative impacts of these options, and certainly does not explore the negative effects in any depth in the EIOPA. In the absence of any benefits on a comparable scale to these massive costs,and the absence of any clarity of how option 3 might work in practice, neither option 2 or 3 should be considered. The "No Change" is the only option that should be included. The hitherto unexplored option of using the AA corporate bond curve is the only other option that might avoid these huge costs.	
22.	Expenses incurred by the IORP should be taken into account.	
23.	TPs should include all guaranteed benefits. We would not want to see a requirement to include discretionary benefits, or a requirement to not include them. A method that allows IORPs to make this judgement on discretionary benefits (in line with long term plans) would be appropriate.	
24.	Financial guarantees must be accounted for. Contractual options do exist but are mostly negligible in their effects. We would support the principle of this Article, but on the basis that proportionality applies such that if the effects ere expected to be minimal, we would not expect schemes to spend a lot of time on this issue	
25.	No. We do not agree that this would be useful. It would create an additional burden, with no additional benefit – as the draft advice notes. Given that EIOPA's draft advice acknowledges that any change will be "overly burdensome with little or no additional gain" the draft advice should have immediately ruled out any change, and it is disappointing that it has not done so.	
26.		
27.	Allowing use of approximations where data is not available is a common-sense approach that should not need to be legislated for, and is therefore an indicator of the downsides of maximum harmonisation and a further reason to avoid unnecessary change.	
28.	As with Q27, requiring regular comparison against experience is again a common-sense approach that should not need to be legislated for.	

29.	As the draft advice notes, this power is already implicit in the IORPS Directive, and no reason why new legislation should be introduced is actually given. This proposal is further evidence of the general approach of the draft consultation in which Solvency II is applied unless a strong counter reason can be identified. This places the burden of proof on those who do not agree to change. However, legislation should only be introduced where there is a demonstrated need for it. <u>It is not appropriate that legislation is proposed unless a good case can be demonstrated against it –the default must be that no legislation is proposed unless it is demonstrated to be of benefit, and the burden of proof must be on those proposing legislation.</u>	
30.	As with the response to Q29, the draft advice notes that this power is already implicit in the IORPS Directive, and no reason why new legislation should be introduced is actually given. This proposal is further evidence of the general approach of the draft consultation in which Solvency II should be applied unless there is a sound reason for not doing so.	
31.	No – we disagree. Although the calculation of technical provisions involves a number of technical aspects, it is also profoundly political – indeed in Solvency II it has involved some of the most difficult political choices of the process (for example, the choice of the risk-free discount rate). Political issues need to be agreed in the level 1 Directive, not in level 2 implementing measures.	
32.	No – we strongly disagree. It would only be possible to remove the right of individual Member States or national supervisors to set additional rules if maximum harmonisation was introduced. However, no case for maximum harmonisation has been made, and it is clear that the costs of doing so would massively outweigh any benefits. We therefore strongly disagree with either the introduction of maximum harmonising rules, or the removal of the power of individual Member States to set additional rules.	
33.	The analysis is welcome, but there is no real evidence as to whether this approach is viable, and a lot more further work is needed before any firm recommendations are made. It is critical to any prudential system that all forms of support are properly assessed and treated, and for the UK, where the sponsor covenant is a fundamental feature of the system, it is clearly of utmost importance that the high level of security provided by the sponsor covenant, backed by the	

	Pension Protection Fund, is given due recognition. Currently in the UK – and as far as we know in other Member States – all forms of support are properly assessed and treated within national frameworks. Clearly, given the wide range of security mechanisms in different member states, any move to harmonise treatment would require that all forms of support continue to be properly recognised and taken into account. To do otherwise would result in either too much or too little prudence in the system. Either of these results would be equally damaging. In that context, and without prejudice to the UK's general opposition to maximum harmonisation for IOPRs, **if** the Commission were to propose a maximum harmonised system, and **if** that was based on a holistic balance sheet along the lines proposed by EIOPA, then it would be necessary, EITHER: - to value the sponsor covenant as an asset on the balance sheet, OR; - to waive the requirement for funded schemes that are backed by a sponsor covenant to calculate a solvency capital requirement, or to hold more assets than technical provisions discounted on a reasonable return on the investment portfolio. It is disappointing that the second option has not been explored in EIOPA's draft consultation, and we are firmly of the view that this option should be included in EIOPA's final advice. With respect to the first option, the UK has profound concerns with lack of clarity as to how the sponsor covenant could be valued in practice. Under a holistic balance sheet approach as proposed by EIOPA (without a waiver for schemes backed by a sponsor covenant), the valuation of the covenant would be the only aspect of the system that could prevent a very large, and unecessary, increase in capital requirements (by as much as 30% of GDP). However, there is very little clarity as to how the covenant might be recognised, and no clarity whatsoever as to how it might be valued – a particularly difficult task, given that sponsor covenants tend to be unlimited. <u>This is approach is absolutely unacceptable, is it provides no confidence that a suitable way to value the sponsor covenant would be found, and means that it is not possible to assess the impact of any proposals in any meaningful way. However, given the scale of likely negative effects, a proper quantitative impact assessment is critical before any further steps are taken.</u> Finally, the comparison with reinsurance misinterprets the point of sponsor support, and the relationship between the IORP and the sponsor where a covenant is in place. The sponsor covenant is a reflection of the fact that the ultimate liability rests with the sponsoring employers, not the IORP. There is a direct relationship between the sponsoring employer and the employee, and the employer does not divest itself of its liabilities when establishing a pension fund. Attempts to view relationship between the IOPR and its sponsor as similar to reinsurance are therefore inappropriate.	

34.	We do not agree that articles 87-99 on the classification and tiering of Own Funds should be applied to IORPs. In particular, the long duration and predictability of liabilities, are sufficiently different to those for insurance products, and the standing of IORPs is sufficiently different to that of insurance undertakings, that there is no prima facie case for applying any tiering of capital to IORPs. The Call for Advice specified that EIOPA should "include an assessment as to whether there is an advantage to keep a three-tier system". The UK Govt is concerned that EIOPA has not carried out such an assessment, and instead looked only at what adjustments might be made to the tiering applied to insurance undertakings through Solvency II. The case for tiering IORPs capital has therefore not been made, and EIOPA should not therefore include such a recommendation in its final advice without exploring the case, and the positive and negative impacts.	
35.		
36.	Pension schemes and security mechanisms in different Member States differ greatly, and provide very different types of security that are not directly comparable. A uniform confidence level will not be able to take these different types of security mechanism into account. Application of a uniform confidence level is therefore certain to result either in too high a level of prudence in some Member States, or too low a level of prudence in others. Neither of these approaches is acceptable. Furthermore, there is little benefit to be gained in harmonising security levels: the level of benefits being provided differs so makes little sense to harmonise the security; and in some Member States benefits can be reduced (or could be reduced were social and labour legislation to be amended) so harmonising a security level makes little sense when comparing to MS where this is not possible. In other words, without harmonised employment legislation, it is not possible to compare like with like. We therefore strongly disagree with the proposal that the security level for IORPs should be uniform across the EU.	
37.	UK Govt is of the view that this is the wrong question. Whatever the confidence level, applying it over a specific time horizon is not an appropriate approach for pension liabilities. The case for a specific VaR over a specified time horizon only arises when preparing a point-in-time comparison of assets and liabilities. However, as set out in the response to Q13 (above), the critical issue with respect to IORPs – given their highly predictable and long-term cash-flows - is to ensure that current and future assets are sufficient to cover current and future cash-flows – not to provide a cushion against the possibility of a short-term deficit.	

38.	UK Govt is strongly of the view that Solvency II rules for calculating the SCR are not appropriate for IORPs – and in particular that it is not appropriate for sponsor-backed IORPs. The draft response argues for application of Solvency II rules for solvency capital requirement on the basis that "the promises made to members and beneficiaries by IORPS and/or employers are comparable to those made by life insurance companies" (para 10.3.53). However, this is not the case, and EIOPA's assessment ignores certain key differences: • An insurance contract is a legal agreement between the insured, or policyholder, and the insurance company. The insurer's promise to pay these benefits is legally binding. On the other hand, a "pensions promise" is part of the employment contract, and the scope for amending the terms of that promise is subject to domestic employment legislation. Pension fund liabilities are therefore subject to change (depending on domestic legislation), whereas insurance obligations are fully guaranteed; • For sponsor-backed schemes – at least in the UK - the obligation to pay the scheme member remains with the employer, not with the IORP. To require the IORP to calculate a (notional) solvency capital requirement would therefore not result in increased security for the scheme member, and would therefore create an additional (and significant) burden without any identifiable benefit. Furthermore, the draft response notes the "additional cost for IORPs and sponsors which could undermine the cost-efficiency of occupational retirement provision" and the "risk of employers reducing occupational retirement provision". The scale of these negative impacts is likely to be **extremely material** and, given the challenges of an ageing population extremely concerning. However, the only benefits identified are an increase in transparency and a level playing field with insurance companies, neither of which are likely to deliver any quantifiable benefit. **It is essential that EIOPA properly assess and quantify these positive and negative impacts before they respond to the Commission with any recommendation.**	
39.	Our view is that the current 3-yr review period (with more frequent reviews for weaker schemes) is sufficient.	
40.	Govt's view is that there is no case for an MCR for IORPs. The primary purpose of the SCR/MCR split in Solvency II is to provide for a ladder of intervention that enables supervisors to intervene while	

	the insurance undertaking is still a going concern, avoiding the need to remove the undertaking's licence to trade. The situation for IORPs is fundamentally different: • IORPs are not trading and therefore do not stand to have their licence withdrawn. The response to a breach of MCR would therefore never be the same as for insurance undertakings; • The absolute need for a long recovery period if technical provisions are breached means that there is plenty of scope for gradual supervisory intervention. The MCR would therefore serve no additional purpose. More generally, it is concerning that the consultation does not address the consequences of breaching the SCR, the MCR or the level of technical provisions, or what the consequences might be for sponsor-backed IORPs that fail to recover their position during their agreed recovery period. This issue is fundamental, and reflects the key difference between IORPs and insurance undertakings, and should not be dismissed simply by saying that it "would have to be carefully considered", as para 10.3.205 suggests.	
41.		
42.	We do not agree that capital should be held to cover operational risk for DC schemes – particularly for sponsor-backed schemes. Product and service providers will already hold capital to cover operational risks. The additional costs – both of capital requirements and the additional administrative burden - would be passed straight on to scheme members, without any obvious improvements to the scheme's security (particularly for sponsored IORPs where the sponsor bears the risk anyway). Given the current low returns on DC schemes, even small additional costs are likely to reduce their attractiveness at a point in time where a significant expansion of DC schemes will be critical in helping Member States respond to the challenges of the ageing population. We are therefore strongly in favour of Option 1.	
43.		
44.	The length of the recovery plan should be determined on the basis of the level of risk that the IORP will not be able to meet its liabilities (ie. cash-flow requirements) while it is under-capitalised. Although, in general, shortfalls should be eliminated as quicky as the sponsor can reasonably afford, given the long duration and high level of predictability of IOPRs liabilities, long recovery periods are entirely appropriate. This is completely different to insurance, where liabilities tend to be much more short term, and there is therefore always a risk of being unable to meet those liabilities during any period in which they are undercapitalised.	

	Furthermore, long recovery periods are essential to preventing a temporary deficit hitting the balance sheet of the sponsoring employer during stressed markets, which would lead to unnecessary insolvencies of the sponsoring employer. The worst way to enhance short-term security of the IORP would be to force the sponsor into insolvency. This would then put the IORP – and any backing Pension Protection Scheme - under even greater pressure (in the worst case scenario, in the UK it could create a downward spiral whereby increasing insolvencies create unsustainable pressure on the Pension Protection Fund which then requires a large increase in contributions from solvent IORPs which pushes more IORPs and sponsoring employers into insolvency). It would also have a strongly pro-cyclical effect. At least for sponsor-backed IORPs, the recovery period for any shortfall in technical provisions should therefore be as long as the sponsor reasonably needs in order to ensure affordability, consistent with ensuring that the IORP can meet its cash-flow requirements during the recovery period. National supervisors need to retain the flexibility to set a reasonable recovery period based on their assessment of the risk both to the scheme members and to the sponsoring employer.	
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47.	We believe that the prudent person principle has served IORPs well and should be retained in its current form	
48.	We believe that Article 18(5) of the IORP Directive provides adequate discretion for Member States to lay down more detailed rules.	
49.	We do not believe such distinctions are necessary or desirable given the in provisions of Article 18(1) the IORP Directive (the prudent person principle) and Article 18(5)	
50.	It is difficult to ascertain from the draft what the practical effect of inserting wording from Article 132(2) of the Solvency II Directive would be.	
51.	We accept that it may be advantageous to clarify the definition of “borrowing” to relate to direct borrowing only.	

52.	Application of Solvency II to IORPs has the potential to be profoundly pro-cyclical – much more so than the application to insurers. This partly because the critical dampening effect IOPRs have on pro-cyclical behaviour (due to their ability to hold on to equities and other non-risk-free assets in a financial crisis) is highly likely to be severly damaged.And because the asset portfolios of IORPs in some member states (including the UK) are far greater than those for insurers - the claim at 12.3.13 that the impact would be limited compared to insurers is factually incorrect. The counter-cyclical mechanisms in Solvency II are far from adequate in countering this negative effect. The only measure that would have an impact is the equity dampner, but the impact of this is likely to be minor as IORPs will be strongly incentivesed to derisk their portfolios and invest instead in risk-free instruments. None of the other counter-cyclical measures – the pillar II dampner, or the ladder of intervention – would have any effect. And it is far from clear that the counter-cyclical premium or the Matching Premium being developed in Solvency II level 2 would have the necessary effect. In the event that EIOPA recommend application of Solvency II solvency requirements to IORPs, it should recommend a comprehensive examination of the pro-cyclical nature, and the further counter-cyclical mechanisms that would be needed.	
53.	We broadly concur that supervision of IORPs should be prospective and risk based, and different to that for insurance firms. However, we consider that this can be accomplished within the framework of the current Directive. For example, in keeping with the general principle that regulatory bodies are most effective if they adopt a risk-based approach – UK legislation provides the Regulatory Authority with the flexibility to take a proactive, risk-based approach to regulation, with discretion in how it interprets and implements its main statutory objectives to: ▪protect member benefits; ▪promote good scheme administration; and ▪reduce the risk of situations arising that may lead to claim for compensation from the Pension Protection Fund (the UK Guarantee Scheme. This flexibility allows the Regulatory Authority to focus resources on those areas where it identifies greatest risk to members' benefits.	
54.	See response to Q53	
55.	Whilst we accept the important role that stress testing plays in terms of certain financial institutions, including insurance firms, we do not consider that stress testing per se is applicable to IORPs. The current technical provisions requirements in Article 15 of the IORP Directive, and investment requirements in Article 18 of that Directive have proved robust and flexible enough to deal with recent economic trends, recognising that pension schemes are very long-term undertakings. Requiring stress-testing along the lines of banking and insurance would	

	effectively treat IORPs as going concerns that are at risk of insolvency, forced sale of assets, or significant capital raising, under certain economic or market scenarios. However, this misses the purpose and status of IORPs as vehicles by which the employer carries out its pensions promise. They are not trading bodies. Furthermore, the existence of long recovery periods means that short-term stresses will not create any risk for IORPs. Stress-testing would therefore at worst demonstrate that an IORP would require a long recovery plan. We therefore strongly disagree that authorities should have the powers to carry out stress tests on IORPs.	
56.	We note that the current IORP Directive has no provisions for a sanctions regime. The UK Government agrees that the general supervisory power at Article 34(2) of the Solvency II Directive provides a suitable starting point, although in accordance with the principles of subsidiarity, we see no purpose in a common sanctioning regime across the EU, other than perhaps for schemes that operate across borders.	
57.	We consider that this matter should be left to the discretion of member states and their Regulatory Authorities. The UK Regulatory Authority already has discretion to make the imposition of penalties public.	
58.	The UK Government would prefer the agreement between the supervisory authorities in question	
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60.	The UK Government sees no reason to apply these requirements to IORPs	
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64.	The UK Government agrees that at their broadest, the general governance requirements in the Solvency II Directive could be applied to IORPs.	
65.	The UK Government questions the need for such a change given that the requirements in Article 9(1)(b) of the IORP Directive are already very close to those subsequently adopted for Article 42(1) of the Solvency II Framework Directive.	
66.	UK law requires IORPs in the private sector to be set up under trust, and as part of the fit and proper person requirements, requires trustees to have (inter alia) appropriate knowledge and understanding of the law relating to pensions and trusts, and the principles relating to scheme funding and investments. The UK has a tradition of voluntary trusteeship, and trustees may be nominated by members. Consequently, newly appointed trustees have a	

	6 month period of grace to acquire the knowledge and understanding to carry out their role (the period of grace does not apply to professional trustees). This period of grace should be retained. Given the diversity of pensions systems and design across the EU, we consider that procedures and controls to enable supervisory authorities to assess fitness are best left to national Regulatory Authorities.	
67.	The UK Regulatory Authority has wide powers from the issue of improvement notices (that identify areas of weakness that must be addressed) through civil penalties (fines) to the appointment of professional trustees and ultimately the removal of trustees.	
68.	The UK Government welcomes EIOPA's view that given the heterogeneity of IORPs across the EU, the throughout the EU, the principle of proportionality must apply to all elements of the governance system of IORPs (including internal controls, internal audit, outsourcing).	
69.	UK concurs with the view that the purpose of ORSA is adequately covered by scheme funding requirements. In terms of UK institutions, it is not clear what value is added by requiring institutions to calculating discretionary benefits, which are after all discretionary.	
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72.	The UK already has extensive legislative requirements on whistle-blowing in the case of non-compliance with any enactment or rule of law, or where the failure to comply is likely to be of material significance to the Regulatory Authority in the exercise of any of its functions.	
73.	As noted in the response to question 16, the heterogeneous nature of the IORP sector requires a proportionate internal control system that should be proportionate to the nature, scale and complexity of the IORP. It is axiomatic that an IORP should comply with all relevant legislation, but we consider that a requirement at EU level should be restricted to those schemes operating across borders.	
74.	The UK Government agrees that at their broadest, the general requirements in the Solvency II Directive could be applied to IORPs.	
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77.	We consider that the current IORP Directive is sufficient,	
78.	We consider that the independence of the actuarial function is vital and that such independence is best maintained	

	through professional standards set by the profession.	
79.	Given the context as set out in the draft response, we merely note that the framework of the current Directive has proved adequate	
80.	We consider that the current requirements on outsourcing (Article 13(1)(b) of the IORP Directive are adequate to ensure that Regulatory Authorities can call in information on outsourcing where needed)	
81.	We concur that some standardisation of outsourcing may be needed for schemes operating across borders	
82.	We consider that bodies or individuals to whom functions are outsourced should be appropriately qualified or authorised to carryout their functions	
83.	We consider that the appointment of custodians and depositaries should remain voluntary for IORPs	
84.	On questions 84 – 88 we have not had time to carry out such an impact assessment	
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89.	We would favour retention of the provisions of Article 14 of the IORP Directive.	
90.	We see no value in the convergence of information provision to regulatory authorities, given the diverse nature of IORPs across member states.	
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95.	In terms of the questions 91-95, UK legislation already requires the provision of very similar information. We emphasise, however, that: • there is a fundamental difference between UCITS and IORPs because IORPs are not commercial products; • comparisons between IORPs are irrelevant as members and prospective members are not faced with making a choice between competing products; • any legal requirements on information provision must be relevant, and proportionate, both in relation to the costs	

	imposed on the scheme (which may ultimately be borne by the member) and the risk of actively discouraging individuals from joining schemes.	
96.	See general comments	