Comments Template on EIOPA-CP-11/006 Response to Call for Advice on the review of Directive 2003/41/EC: second consultation		Deadline 02.01.2012 18:00 CET
Company name:	Mercer	
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The question numbers below correspond to Consultation Paper No. 06 (EIOPA-CP-11/006).

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Question	Comment	
General comment	Mercer is a leading global provider of consulting, outsourcing and investment services. Mercer works with clients to solve their most complex benefit and human capital issues, designing and helping manage health, retirement and other benefits. It provides benefits, actuarial, investment and	

governance consulting advice to IORPS throughout the European Union and is a leader in benefit outsourcing. Its investment services include investment consulting and multi-manager investment management.

Mercer recognises that there is scope to improve standards of governance and risk management in many IORPs and welcomes the review that is taking place with regard to the IORP Directive. However, we are concerned that the review process might result in undesirable, and perhaps unintended, outcomes. This is for two reasons:

First, the objectives behind the review of the IORP Directive and the adoption of Solvency II principles are unclear and short term. Depending on how they are applied, we agree that many of the principles underlying Solvency II could result in stronger risk management and so better outcomes for scheme members, but the consultation document provides no clarity about how EIOPA expects regulation to operate in the proposed new framework. It seems clear that, in some cases, a complete adoption of Solvency II could have severe (negative) financial consequences on many IORPs, their sponsoring employers and members. However, since it is unclear where amendments to Solvency II might be made in the amended IORP Directive and in its implementation, and without an impact assessment of the consequences, it is difficult to be clear about the practical implications of the proposals.

If the objective is to introduce a stronger regulatory regime, this might be appropriate in relation to future liabilities. However, some countries have substantial accrued liabilities that could become materially underfunded if Solvency II principles are applied without amendment. This appears to conflict with member state subsidiarity in relation to social and labour law and could undermine existing arrangements made under company and contract law.

Secondly, harmonisation with Solvency II does not seem a legitimate objective for review of the IORP Directive. The implementation of Solvency II has been a difficult and expensive process, resulting in trade offs between different member states and different types of insurance, so that the outcome is not necessarily the best and most transparent or coherent regulatory regime. Like most professions, we expect that regulation is an evolving discipline, so it should be possible to learn from the

	experience of Solvency II, the existing IORP Directive, and other regulatory models to develop a system that is proportionate and fit for retirement provision in the 21st century. In particular, regulation needs to respect the nature of the underlying contract between the employer and employee, be proportionate to the risks posed at a macro, as well as micro, level and sensitive to the disincentive effects created by imposing too heavy a regulatory burden. Our answers to the specific questions asked in the consultation are appended to this letter. We have also entered them on the web based service provided.	
1.	We consider that clarifying the scope of the IORP Directive is fundamental to the EC's objectives to achieve a harmonised regulatory regime across all employer sponsored pension provisions. Because of this, we do not entirely agree with the analysis presented in Chapter 4 of the consultation. For example, paragraph 4.3.7 suggests book reserve schemes should remain outwith the scope of the IORP Directive because they are subject to Directive 2008/94/EC. But all employee remuneration, including funded occupational pension provision, is subject to that Directive. We respect individual member states' right to determine their own approach to social security, including how retirement provision should be established. However, since the way employers provide occupational provision necessarily takes into account the pension provided by the state, different models of employer provision have developed in different countries. These target different benefits using different benefit designs and different funding models. As the consultation document notes, this makes any attempt to determine which schemes should be in scope a political decision, but necessarily also, it means that attempts to 'harmonise' the prudential regulation of those schemes that are in scope will also be political, particularly in relation to those schemes that are outwith the scope of the Directive. If the premise is that pension provision that employees have contributed to directly or indirectly should be subject to a minimum level of prudential regulation, and this is not forthcoming from the member state, then we do not see why there is a distinction between how the provision is established (that is, whether it is implemented by the state or the employer), or how it is financed	

	(that is, whether it is provided on a funded, notionally funded, book reserve or pay as you go basis). If there is to be a distinction, then the regulation applied to those in scope of the Directive must be constructed in the knowledge that there is no level playing field and 'harmonisation' cannot be achieved. In particular, it must be sensitive to the anomalies created by the definition of 'scope' and the differences in provision created by each member state's social provision.	
2.	As mentioned, there is a case for EIOPA considering how the scope should be widened to include any scheme established by an employer, and any scheme that employers contribute to on their employees' behalf. There will, of course, be a financial impact on those brought into scope which, in the absence of a quantitative assessment on the current set of proposals, we are unable to detail. However, if the presumption in relation to those schemes within the scope of the Directive is that the benefit to members outweighs the cost of what is being proposed, then the argument must apply equally to other arrangements brought within scope. Our experience of book reserve schemes in Germany, for example, is that they are straightforward to provide, partly because they are subject to rules based regulation that is fairly light touch. There is a balance to be struck between simplicity and security. Our view is that simplicity is desirable, but that if this is a regulatory objective it needs to be applied consistently to all employer sponsored pension provision; similarly, clear targets for security might be desirable, but this also needs to be applied consistently.	
3.	None of the options presented in the consultation document appear to us to address the questions we have raised about the appropriate scope, in our answers to the previous questions.	
4.	Yes, for the following reasons: ▪ Some member states mandate a level of employer sponsored 'state' provision that is far greater than in other countries, so that additional, voluntary, employer sponsored retirement saving is at a far lower level. The circumstances in which provision should be considered as 'state' or 'employer' provided is therefore blurred. ▪ For historic reasons, some member states have permitted employers to establish occupational	

	provision on a pay as you go or book reserved basis. Often employers establish reserves to ensure that they are likely to have sufficient cash to pay benefits as they arise, so in fact they are, implicitly, at least partially funded. Similarly, some funded employer provision is only partially funded. It seems inconsistent to treat these different arrangements differently, from the point of view of prudential regulation.	
5.	We do not agree that the proposed Option 2 will result in clear definitions across all member states. The difficulties in relation to the current definition of 'host member state' have arisen due to the different ways in which member states transposed the IORP Directive into their national legislation. Our view is that the similar issues are likely to arise if the IORP Directive is amended as suggested: the structure of employment relationships and agreements and the ultimate liability to contribute to pension schemes in respect of shortfalls, for example, are potentially very complex. In addition, the suggested approach will remove the link between social and labour law and where the members work. This is likely to produce further negative impacts not highlighted in EIOPA's draft response. For example: ▪ Some schemes where the IORP and the members are in a single member state will become 'cross border' because the sponsoring undertaking (for example a bank with a local branch structure) is located in another member state. ▪ Employees in one member state could be members of an IORP with its main administration in another member state and with an employer in a third member state. In this example, neither the regulation nor the social and labour law applying to the IORP would have any connection with the members. ▪ In the previous example, if the sponsoring entity was based outside the EEA, then even though the members and the IORP were based in different member states, it would not be considered cross border; and if it were, then what social and labour law should apply to the members? Other potential negative impacts include: ▪ Removing the link between the location of the member and the "host country" by redefining host country as the location of the sponsoring undertaking presents the possibility of employers	

structuring their cross border arrangements to choose the host country on the basis of perceived less onerous social and labour law. Any such arbitrage would be likely to damage the image of cross border pension provision.

- Removing the link between the members' location and applicable social and labour law (SLL) risks producing scenarios where members in one country are covered by the SLL of another country. The design of the section of the scheme covering these employees however will still be shaped by the need to meet local requirements for tax approval, and the need to reflect local social security and mandatory provision. The likelihood is that the SSL of one country will not sit well with a scheme section designed for locals of another country.
- This would make the task of clearly communicating members' benefits and rights more difficult. Rights with which members are familiar in their own country (for example indexation) may not apply, and other features more appropriate to entirely different pension regimes (such as rules around transfer values) may apply.

The suggestion to address these concerns is that Article 20 could be amended "to give the ability to the authorities of the member state of the SLL (i.e. another member state than the home and host member states) the right to take measures against the IORP, and the introduction of a requirement that the IORPs should respect the applicable social and labour law, irrespective of whether that is the law of the Host Member State". However, this would add further significant layers of complexity, undermining the objectives of providing clarity and encouraging the establishment of cross border schemes.

We consider that the IORP Directive should consider member interests in establishing the rules that underlie cross border provision: that is, it would be preferable to institute a regime that provides appropriate protection to scheme members' benefits, regardless of where the scheme is located, whilst respecting the social and labour law members are subject to because of the member state they are legally resident in. This would also reflect employers' objectives when establishing pension arrangements for employees. The location of the employer seems irrelevant to this.

Consequently, the provisions in Article 20 seem to us to make more sense if the 'host member state' for the sponsoring undertaking is associated with the legal residence of the employees, rather than

| | the undertaking's location. In our view, the current definition of host member state achieves this, by implicitly referencing the legal residential status of the employee, rather than the employer. If it is unclear in that respect, then our preference would be for this to be clarified, rather than for it to reflect the employer's status.

We also observe that the distinction drawn between cross border IORPs in paragraph 7.2.2 of the consultation issued in July 2011 on the first draft response to the Call for Advice is not as clear cut as was suggested. For example, where there is a distinction between the IORP and the 'scheme' (for example, the Netherlands), this generally vests the scheme around the members' employment contracts, so that defining cross border schemes in relation to the nationality of the scheme can be identical to defining it in relation to the relevant social and labour law. | |
| 6. | Although we agree that, in many circumstances, it is valuable to be able to identify different members' shares of a pooled investment fund, we do not agree that it is always necessary to ring fence assets and liabilities in all circumstances. For example, in defined contribution schemes it is absolutely necessary to be able to identify the assets underlying individual member's accounts and, if there are separate investment funds, these also need to be identifiable to be sure that they meet their mandates. It is also possible that, if some member states continue to prescribe additional investment restrictions on IORPs, then the assets underlying the liabilities of members based in that member state will need to be identified separately. However, circumstances are likely to arise where, if individual sections of a scheme are completely segregated from other sections, inefficiencies could arise that hinder, rather than enhance, the likelihood that members will get their expected benefits. For example:

▪ If sections are permitted to share administration costs, then the scheme will have easier access to benefits of scale;
▪ If defined benefit sections accrue surplus funds, then it could be legitimate for those funds to be shared across other sections of the scheme. We agree that this would need to be regulated, but provided the surplus cannot be explained solely by member contributions, we can see no detriment to members in making this possible. | |

	These circumstances are most likely to arise where all the sponsoring employers are members of the same group of companies, but we see no reason for limited sharing of assets to be prevented at the level of the Directive. In particular, they can be achieved without exposing members of one section to risks that could emerge due to the underfunding of another.	
7.	As discussed in our answer to question 6, we consider there could be more negative outcomes if ring fencing is imposed in too restrictive a way than included in the consultation document.	
8.	The introduction of additional requirements attaching solely to cross border IORPs should be proportional, to avoid acting as a disincentive to establishing cross border arrangements. The principle should be that national (home member state) legislation on ring fencing should already be appropriate to cross border IORPs as far as possible (except to deal with cases where different member states are permitted to introduce additional regulation under the IORP as is the case for investments). So, in our view, the member state of the home country should only have to introduce ring fencing in cases of cross border activity (over and above national rules on ring fencing) in cases where the host member state has imposed investment rules that are in line with the IORP Directive (Article 18(7)) but not compatible with those of the home member state.	
9.	We do not see this as an issue only relating to cross border schemes. We agree that, where schemes are legally separate, albeit managed and/or administered by the same IORP, they should be provided with "a full legal and financial separation of assets and liabilities". This should be part of the protection rules provided by the legal framework of a member state. However, where the scheme is a single legal entity with different sections, then in most cases, as described above, we consider it to be sufficient for the assets and liabilities to be 'administratively' ring fenced, so that legal separation might only apply in limited circumstances. Where, for example, cross border schemes are single schemes with many sections, where the employers participating in those sections are owned by a single entity, we consider that the introduction of stronger ring fencing rules could be excessive, and result in less efficient outcomes for members and for employers.	

10.	The options presented, to do nothing, or to define the scope of prudential regulation, seem complete and we agree with the analysis. We agree with the recommendation to adopt option 2.	
11.	We would not expect an adverse impact on any stakeholders as a result of explicitly determining the scope of prudential regulation in the manner recommended. We would expect the adoption of option 2 to bring an increased level of certainty to all stakeholders in the context of cross border activity, which could encourage an increased level of market activity in this area (while recognising that the lack of certainty on prudential regulation and social and labour law is only one, and not the most important, of the current barriers to the adoption of cross border arrangements).	
12.	Although the idea of a holistic balance sheet that presents the value of the scheme's liabilities against all the sources of capital available to the scheme seems attractive, in practice it could be difficult to achieve a useful outcome. Since it is unclear from the consultation how the concept will be used in practice, it is difficult for us to form a strong view one way or the other. Our particular concern is largely in relation to the valuation of the company covenant, but also the accounting treatment of contingent assets. The proposal seems to be that the scheme managers would place a value on the extent to which the company covenant is available to them. This will be, at best, an extremely complex exercise. Even in the simple case where there is a single sponsoring employer, the employer's 'spare' capital is likely to have prior calls on it, some contractually constrained and others tied to the needs of shareholders and internal business plans. Also, quite reasonably there is a requirement for asset valuations to be 'market consistent'. In the case of employer covenant, there is no market, so the best to hope for is "mark to model", but corporate finance models are generally not transparent and incorporate many subjective elements. For example, in some cases it might be possible to use bond spreads or the cost of credit default spreads could be used to construct a proxy measure, but it would be far from perfect, since these	

	only reflect the specific bond holders' positions, which will be very different from the IORP's. In addition, where there is no legal access to sponsor covenant (for example, the sponsors legal commitment is only to pay the cost of ongoing accrual), then as well as ability to pay, willingness must be taken into account, and this may prove particularly challenging to value. Perhaps the best that can be hoped for is that the liabilities are fully determined (so, in particular, Component 3, which is described as 'excess of assets over liabilities', is determined – if deemed necessary – using some specific formula). Then, the difference between the calculated liabilities and the aggregate of the scheme's financial assets and its 'known' prospective assets (recovery plan and, where possible to value, contingent assets and protection funds) could be described as 'excess of liabilities over assets'. In principal, it would then be clear the extent to which member security relies on the company covenant. There could be a consequent responsibility on IORPs to consider whether the extent of reliance is realistic, give the information available to them about the sponsoring employers and, for example, their future business plans and prospects. In practice, there are also difficulties in measuring liabilities consistently, since different scheme designs provide members with different levels of security or expectation. Whilst valuing fixed benefits might be relatively straightforward, contingent or indexed benefits create more problems and conditional benefits, which effectively introduce risk mitigating features onto the liability side of the equation, raise another level of complexity. Since one of the EC's objectives is to achieve harmonisation throughout the EU, we also observe that the circumstances and extent to which IORPs have access to the employer covenant varies, depending on local member state legislation. Depending on whether, and how, the requirement to place an auditable value on the company covenant is used in the amended IORP Directive, it is possible that a material additional cost of pension provision could be placed disproportionately on pension schemes registered in a very small number of member states (that is, directly on the employers that sponsor those schemes). Since the UK is the only member state where employer covenant has come to form part of the funding regime, it is possible that the idea of the holistic balance sheet was devised to address some of the practices adopted by UK schemes. However, we feel our alternative presentation addresses exactly the same points made in Chapter 8, but without imposing the cost and complexity	

	determining an actual value would require. In particular, we agree that the employer covenant should be taken into account in some form when determining the amount of financial assets defined benefit schemes are expected to target as part of the regulatory regime. Ultimately, the effectiveness of the concept depends on how it will be used by EIOPA and member state supervisory authorities: the consultation is silent, for example, on the steps it might expect an IORP to take if the assets measured using the holistic balance sheet approach are insufficient to meet the IORP's total liabilities, which could include solvency capital requirements. If the presentation is to be made available to IORPs to consider whether they are appropriately financed, given the information it provides about the quantity of risk the liability and asset profile imposes, then this seems a useful exercise; however, we would find it far more difficult to accept if the intention is for supervisors to impose onerous funding obligations on employers as a consequence of a shortfall on the asset side of the balance sheet against the total liabilities, including the Solvency Capital Requirement (SCR). We do not comment on the different components it is suggested could be included in the holistic balance sheet in this question, since they are considered further under Call for Advice 5. 12. (contd) We agree that the difference between IORPs that target defined benefits or investment returns, without recourse to the sponsor in the event of underfunding (Article 17(1) IORPs), should continue to be distinguished from those IORPs that do rely on the sponsor. For example, in the former case, it would be unreasonable for the scheme to consider that the employer's covenant served as a contingent asset available to the scheme, particularly following adverse experience. However, we do not understand the description of IORPs where the regulatory regime draws on the permissive nature of Article 17(3), as 'different' from other IORPs. In this case, it is the regulatory regime that is different, so we do not think the distinction is needed. Indeed, retaining Article 17(3) could undermine the EC's objective of harmonising regulatory standards throughout the European Union. It would create a more level playing field if the schemes established by employers on the understanding that the company covenant must be made available to the scheme to cover shortfalls in funding whilst the scheme and employer are ongoing, and/or in extremis, all had to be regulated	

	consistently, rather than enabling the supervisory authorities in some member states to regulate differently than others.	
13.	In theory, market consistent valuations seem attractive because they appear to provide an objective measure. However, in practice, they do not necessarily achieve this: generally, for example, market valuations can be affected by investor preference, but more specifically, for some assets and liabilities, a 'market' does not exist. In particular, there is no market for the liabilities of ongoing pension schemes. Although the question relates to the measurement of asset values, consistency is a fundamental accounting principle, so it is important to consider the extent to which this can be achieved. Paragraph 9.3.13 points to 9.3.8 for an explanation of a 'market consistent basis' for pension scheme liabilities, but the consultation document makes a clearer statement about what is intended in the proposed EIOPA advice on possible amendments to Article 77. Here it says that the technical provisions (best estimate of liabilities plus risk margin) should be the amount one IORP would need to take over and meet another IORP's obligations. Although we believe this could achieve a good outcome in the case of IORPs that carry their own risks, it will not work well in relation to schemes that rely on company covenant. In this case, there is no consistent measure of the amount required, since schemes will often take into account the employer's interests and covenant when deciding whether, and on what basis, to accept a bulk transfer of another scheme's liabilities. It is certainly not the case that a risk free, or matching cash flow, approach would be used to determine the amount of assets transferred between each IORP. It is possible that references to a 'transfer value' in the consultation document are made in relation to the cost of transferring IORP liabilities to an insurance company. However, in our view this is not necessarily an appropriate measure for a scheme except in wind up, so at best represents an upper bound for where to set technical provisions, rather than a market valuation. On the other hand, it could be argued that, when agreeing to accept a bulk transfer from another IORP, schemes do consider the employer covenant available to them (not the covenant available to the transferring scheme). For example, they might be prepared to accept a lower transfer of assets	

	where they had evidence that their sponsoring employer’s covenant was strong enough to support the risk inherent in the amount transferred. Another consideration arises from pension schemes’ non-profit nature: generally: ▪ the receiving scheme will be interested in ensuring it receives sufficient assets in relation to the transferred liabilities so that, in conjunction with the employer covenant, it has not undermined the security of its existing members; whereas, ▪ whilst taking relative levels of security in the two schemes into account, the transferring scheme will be concerned that the assets transferred do not undermine the security of its remaining members, in conjunction with its employer’s covenant. In an insurance context, when a transfer takes place, both parties are concerned about the profitability of the exercise for their shareholders. Although they could have different books of business that mean their interests are not identical, they will take similar matters into account, It seems that, in the absence of a real market and under pressure to determine a market consistent approach to be consistent with Solvency II, EIOPA has devised an artificial construct that does not seem coherent. In particular, a quasi-transfer value approach might impose short termism on IORPs that is inconsistent with the long term nature of the liabilities that, for example, do not require immediate liquidity or even full funding on a least risk basis to be secure. It is possible that, when negotiating sales and purchases, employers assume a value for the pension scheme liabilities (net of scheme assets) that are being transferred, adjusting the sale price accordingly. However, even if this is the case, we do not believe it would give rise to a consistent measurement, because it is likely to be affected by the other value the purchaser sees in the target entity. Rather than introducing a false impression that, on transfer, there is a ‘market’ price, we would prefer that alternative approaches to calculating technical provisions are considered. Our preferred approach depends on how the information will be used for regulatory purposes. For example, IORPs are likely to be better placed to manage the risks in their scheme if they are aware of the market	

	price of purchasing financial instruments that match their expected future cash flows. Our view is that this is the closest many ongoing IORPs will be able to get to a 'market consistent' measure. However, we think it would not be appropriate to mandate this calculated amount as a minimum threshold for the level of financial assets that all IORPs must hold. Finally, because markets are imperfect and often short-term, and IORP liabilities are generally long term and not directly 'marketable', market consistent measurements should only be part of the information used by IORPs and regulators to manage the risks they face. In particular, if the intention is to operate a counter cyclical regulator regime (CfA 8) relying solely on market consistent measures will create difficulties.	
14.	Our answer to this question depends on how the liability value will be used by regulatory authorities. EIOPA's draft advice is not clear what the first Option entails. We assume it would result in Article 15(1) and 15(2) being retained. We consider that the requirement in the IORP Directive to establish technical provisions (Article 15) is adequate: it provides for a principles based approach that enables the scheme to take into account all matters relevant to it (including, for example, the cost of transferring liabilities to an insurance company) in determining a prudent approach to the calculation. Option 2, however, requires a market consistent approach. As discussed in our answer to question 13, if this is construed in terms of a transfer to another IORP, we believe this is a false concept in relation to pension scheme liabilities. Our view is that Option 1 is more meaningful in the context of occupational pension provision and so is preferable, but that some of the underlying concepts relating to the measurement of technical provisions, as set out in the Solvency II Directive, could be relevant to IORPs and add value to the valuation process. To achieve this, if Article 15 is retained unamended, at the implementation stage EIOPA and the supervisory authorities of individual member states might consider that more specific guidance is	

	needed. For example, there could be guidance about how schemes should 'take into account' their underlying investments in the context of the future payment of the accrued liabilities. This could set out the extent to which IORPs should consider the risk profile of their assets and liabilities and the extent to which they are unmatched, in the context of determining whether additional margins should be held to reduce their risk profile and then quantifying those margins. There could also be help for schemes to interpret what is meant by 'prudence'. However, prudence is not an immutable concept: that is, the outcome of following a prudent decision making process will differ, depending on circumstances. Thus, having a principle that requires a prudent approach but then mandating a particular measure for certain aspects of the approach could result in outcomes that could be considered imprudent, given the circumstances of the scheme and its sponsoring employer. Where technical provisions are to be used to determine minimum levels of financial assets held by the IORP to meet the scheme's liabilities, we consider that the amount of risk that can be taken into account in determining that measure should depend on the extent to which the members' security relies on the employer covenant. Where the employer covenant is not available as a real or contingent asset, then it is reasonable to target higher levels of financial assets than cases where the employer covenant is available to the IORP. Nonetheless, we agree that it is important for IORPs to understand how the price of purchasing matching assets might be different from their measure of the financial assets that they need to hold to cover a (risk related) value of technical provisions. The use of Value at Risk (VaR) techniques, for example to indicate the risk margins that might be needed to protect members from certain worst case scenarios, or just the effects of having a mis-matched investment strategy, would also add to some IORPs' risk management capabilities, although we do not feel it is necessarily proportionate to mandate these approaches in all cases.	
15.	We assume that the credit standing of the IORP would be taken into account on the asset side of the holistic balance sheet, in which case there could be double counting if it was also used to determine and appropriate measure of the liabilities.	

16.	We do not see what is achieved by this. Accounting standards have different objectives from those of a prudential regulatory authority. Since insurance companies are subject to both corporate accounting standards and prudential regulation, the principle might serve some purpose in Solvency II. However, since IORPs are not for profit entities, it is less relevant. In particular, unless the European Commission considers a risk free discount rate similar to a corporate bond approach, the principle seems redundant. A general requirement for EIOPA and member state supervisory authorities to act proportionately and not unnecessarily impose administrative burdens on IORPs would be preferable. If EIOPA is suggesting IORPs' financial statements should be revised to encompass the holistic balance sheet, then it would be sensible if the accounting standards that apply to IORPs are amended to be consistent with the regulatory framework. However, given the uncertainty we have with measurement of, for example, employer covenant, we are not convinced that this is practicable.	
17.	If Article 15 is retained, then we cannot see the purpose of also transposing Article 76 of Solvency II into the IORP Directive. However, for consistency, the EC might prefer that rather than retaining the opening sections of Article 15, subparagraphs (1), (3) and (4) are substituted. However, if Option 2 of question 14 is adopted, then we can see that these parts of Article 76 follow logically.	
18.	As discussed under question 13, we do not consider that the concept of a transfer of liabilities between IORPS provides a consistent measure, nor one likely to meet a regulatory purpose. Instead, we prefer the existing provision, with amendments as suggested in our answer to question 14, where IORPs have to explicitly consider including risk margins to allow for adverse experience relative to the assumptions they use to value the liabilities. Thus, our preferred approach would be the status quo. However, Option 3 might be an acceptable alternative, depending on how funding requirements are derived in relation to it. Other measurements (for example, VaR techniques) are also useful for supporting risk management discussions, but again, our view is that there are some models for IORPs in the EU where such	

	calculations could, depending on the confidence level used, risk overstating the financial capital required to provide an adequate level of security for scheme members' benefits.	
19.	We think it is necessary here to distinguish between 'future accruals', by which we would mean pension entitlements that will only arise if future service is completed, and existing undertakings, which might be entitled to enhancements in future (for example, revaluation of past service accruals where this is a statutory requirement or provided for in scheme rules). Making this distinction, we do not think that future accruals should necessarily be included in the calculation of technical provisions (that is, we do not think it should be mandated, but IORPs should be able to choose to do so). The key feature here is that, even when future contributions and the associated accrual are pre-defined, the accrual is generally also contingent on members remaining in service with the employer and so will not happen in respect of members that leave service. Where future increases in benefit (and payment of contributions) will occur regardless of the member's future service, then we agree that it would be reasonable to allow for this in the technical provisions calculation. Our understanding of Article 77(2) is that it recognises that, to be entitled to the full benefit under some insurance policies (for example, endowment policies) premiums have to continue to be paid, perhaps for the full policy term. This concept does not translate neatly into most pension provision. Instead, it might be clearer to require IORP technical provisions to include at least all cash flows in respect of benefits that have accrued, or that the IORP is committed to pay, in relation to service at the calculation date (for example, the benefit members would be entitled to if they left the scheme on the calculation date).	
20.	Yes.	
21.	Option 3 appears to us to be the optimum solution. It would mean that: ▪ Schemes had to present technical provisions calculated on a consistent basis (the risk free, Level A, calculation); and	

	▪ There would be flexibility about the different asset classes available for financing Level A technical provisions so that the way benefit security was achieved would reflect the legal construct of the IORP. We do not agree that Option 2 would lead to better transparency than any of the other options. In each case the scheme could be required to illustrate the calculation of future cash flows using a risk free rate and show the difference between the calculated technical provision and the 'risk free' calculation. So Option 2 provides no greater transparency than the others. We agree with the positive impacts listed for Option 3 and consider that, by providing a flexible regulatory regime that can respond to market cycles, EIOPA will enable continued defined benefit provision and so greater stability of retirement benefits for occupational pension scheme members. The alternatives are likely to result in a faster decline of defined benefit provision, and greater reliance on defined contribution arrangements, leaving employees with greater uncertainty about their pension outcomes. We do not agree that, if Level B technical provisions were not the same across all member states, this would mean full harmonisation had not been achieved; in our view, harmonisation, in terms of a similar calculation, would be achieved via the Level A measure. Then, provided the assumptions and methodology for calculating Level B technical provisions are required to be chosen prudently, a concept that could be further developed via the implementation measures, although the calculation would not lead to the same measure for Level A in all cases, it should lead to similar degrees of security for all scheme members.	
22.	Yes, although there are different ways of achieving this, which are recognised by various different accounting standards. For example, it could be considered as a deduction to the return on assets, or as an explicit cost of providing the benefit. The approach adopted by different IORPs partly reflects the way they are established, so it would be proportionate to permit different approaches, provided the approach adopted by the IORP is made clear to its supervisory authority.	
23.	No. We distinguish here between members' accrued benefits and entitlements, and between	

discretionary and conditional benefits:

- Members' accrued benefits and entitlements are those benefits, some of which might be in payment, that cannot be reduced or otherwise altered without member consent;
- Discretionary benefits are benefits that have not been granted and that might not be granted;
- Conditional benefits are benefits where the payment is conditional upon a rule being met. These include, for example, benefits in payment that can be withdrawn if funding levels fall below a prescribed level, and benefit that will be paid if a prescribed test is met.

We agree that the first and last type of benefit should be included in the technical provisions calculation but consider that discretionary benefits are fundamentally different and should not be included.

In some countries, employers sometimes agree that schemes can award discretionary benefits when funding levels are high, where the test of 'high' is a subjective one left entirely to the employer's discretion. If discretionary benefits were included in the technical provisions calculation, the calculation would produce a larger result which is likely to have adverse consequences:

- Members' expectations might be raised unreasonably, and they might misunderstand the status of the 'discretion';
- Discretions would become less likely to be granted;
- Employers might request trustees to remove the power to make discretionary increase from the scheme rules.

In none of these cases is the members' interests defended.

In addition, including an allowance for discretionary benefits in the technical provisions would increase the cost of the scheme to the employer, even if ultimately IORPs become able to offset the liability by including subordinated liabilities amongst the assets disclosed on their balance sheet. It would be unreasonable for regulation to impose a cost on employers for benefits they have no intention of awarding.

24.	We agree that schemes should reflect the value of member options in their calculation of the technical provisions, in the way described.	
25.	We agree that, in calculating technical provisions, schemes should take into account the various different risk groups they are exposed to. However, the word ‘segment’ means something specific in some member states’ legislation, so we suggest that a more general principle might be preferable. For example: ▪ IORPs shall take into account the different risk groups in the scheme when calculating technical provisions. At a minimum, DB and DC liabilities should be treated separately.	
26.	We agree that an amended Article 81 might have a place in the IORP Directive. In line with the holistic balance sheet, it might be appropriate for the value placed on reinsurance recoveries or the benefit of special purpose vehicles to be treated as a contingent asset, rather than a negative liability. From the members’ perspective, presenting liabilities gross of any recoveries is likely to present a clearer picture, than a net calculation.	
27.	Yes, except it should be recognised that it is not possible to have accurate data at all times, so this requirement should be implemented proportionately. There will often be a lag between an event happening and the scheme being notified and, in the case of deferred members, it is sometimes difficult to be sure that up to date addresses have been notified.	
28.	We agree that this principle would be appropriate for an IORP, if applied proportionately. However, as drafted it could introduce a logical inconsistency. The proposal is that technical provisions should be calculated using a risk free discount rate, but Article 82 would require schemes to disclose where assumptions have not accorded with experience and amend them appropriately. Where schemes invest in risk seeking assets, this would require schemes to move to a risk related basis for technical provisions, which the IORP Directive might forbid.	
29.	We agree that supervising authorities should be able to request IORPs to provide information setting	

	out and justifying the approach they have adopted for their technical provisions calculation. However, inevitably there will be some subjectivity in the appropriateness of the assumptions and methodology adopted. Supervisor authorities might need some constraints so that they do not impose their own views on schemes, when to all intents and purposes the IORP has complied with the legislation and regulation that applies to it. For example, the paragraph could be amended to say 'Upon reasonable request'.	
30.	In principle this seems reasonable, although before doing so the supervisory authority should be required to demonstrate why the position reached by the IORP does not comply with the regulatory requirements. However, this raises the question about the actions that must follow from the increase in the technical provisions and highlights a fundamental difference between insurance companies and IORPs. For example, if the Directive requires IORPs to hold financial assets at least equal to their technical provisions at all times, then the increase in measurement creates a need for additional capital. IORPs generally cannot access capital from financial markets, in the same way that insurance companies can. There are different models throughout the EU for dealing with shortfalls: ▪ In some countries, benefits can be reduced until funding has been restored; ▪ In others, the 'safety valve' is reliance on the employer covenant. In the latter case, currently, it is not possible for IORPs to require employers to finance shortfalls regardless of their own financial circumstances. Instead, these are met over a period of time agreed between the IORP and the employer, often subject to regulatory oversight. The consultation document suggest this flexibility will remain, although one interpretation of the proposals is that the measure of financial assets required could be higher than under the current IORP Directive and a maximum period of 15 years would be mandated. These two pressures could result in a decision by a member state regulator causing an employer to, at the very least, break banking and other covenants it has with its other creditors and stakeholders,	

	and, at the worst to become insolvent. The knowledge that regulators have these powers is likely to make future shareholders and lenders very nervous about companies that sponsor defined benefit schemes, to the extent that they become unviable. The effect of the proposals could be to fundamentally alter the legal status of IORPs in relation to the sponsoring employer and to undermine the effect of existing company law and individual contracts. Until EIOPA and the EC are clear about the consequences of the revised measures of technical provisions that could result following amendments to the IORP Directive, in particular, how these will be used by the IORP and by regulators, we are unable to take an informed view in relation to this question.	
31.	We agree that, depending on the decisions taken by the European Commission following receipt of the information provided to it by EIOPA in relation to Call for Advice 5, there might need to be provision for EIOPA to negotiate implementing measures with the member states supervisory authorities. However, this should be applied proportionately, respecting the different sizes and types of IORPs that are found in different member states, and should be subject to the same degree of consultation that would apply to Level 1 regulation.	
32.	If the rules are intended to address differences in the member state's provision and help the Directive meet its objectives, then we have no objection to this.	
33.	We agree that paragraph 9.3.194 lists the main forms of sponsor support. However, we are less certain about the analysis that follows. For example, whilst members might be indifferent about the source of their benefit payments (forms A and B), the different structures impose different disciplines on employers and are triggered by different contingencies. For example, under Form A, once a shortfall in funding has been identified, the recovery plan agreed between an IORP and the employer can form a legally binding commitment. However, our understanding of Form B is that it only becomes relevant once the IORP is (effectively) insolvent, which means the contingency on which it becomes payable is different and, once it is in payment, its accounting treatment must be different since the IORP is technically insolvent. In that sense, it is a contingent asset similar to Form C, where the trigger is (for example) related to scheme	

funding rather than employer insolvency.

Regardless of this, we agree that the support can be divided into the three categories in paragraph 9.3.212, and that the category the support falls into is likely to influence its value to the IORP.

33. (contd) Do stakeholders agree with EIOPA that IORPs should value all forms of sponsor support as an asset and take account of their risk-mitigating effect in the calculation of the solvency capital requirement?

We understand from the statement 'take account of their risk-mitigating effect in the calculation of the solvency capital requirement' that EIOPA is suggesting that a strong employer might result in a lower SCR.

The suggestion that the SCR should be lower when the employer covenant is strong highlights a weakness or circularity in the proposed approach to the holistic balance sheet. Our preferred regime would be for IORPs to be able to take the employer covenant into account when determining their approach to calculating and financing the scheme's technical provisions (Option 2) or, if preferred, the subsidiary 'Level B' calculation of the liabilities suggested in paragraph 9.7.36 of the consultation. The Level A calculation then achieves the EC's objective that different IORPs should disclose similar measures of technical provisions, and Level B would achieve harmonisation in security by reflecting the different types of benefit structure, and the different types of assets that IORPs can access to provide them.

As proposed in the consultation document, the SCR represents resources the scheme would be expected to have access to in the event that an extreme event occurred. Given the proposed level of the technical provisions calculation, except in those schemes with no recourse to the employer in the event of underfunding against technical provisions, the most likely extreme event will be the employer's insolvency. However, IORPs are expected to place a value on the employer's covenant to demonstrate that they have access to sufficient financial resource should an extreme event occur. This makes the information provided via the holistic balance sheet relatively meaningless.

Our preferred alternative, as suggested in our answer to question 12, would be to:

	▪ State a least risk liability measure on the liability side, with risk margins to allow a reserve for mismatching (called technical provisions); ▪ Include a lower liability measure (Level B), against which the IORP is expected to hold financial assets (including any recovery plan contributions); ▪ State the value of the financial assets on the asset side; ▪ Explicitly add to the financial assets the value of any recovery plan contributions and, if appropriate, financial contingent assets (noting that prudent accounting principles suggests contingent assets should have no value unless the contingency has occurred or become highly probable); ▪ Illustrate the reliance on the company covenant by the difference between the total asset and liability values. Where employers have a weak covenant, the Level B measure would be close to the technical provisions and reliance on the covenant should be low.	
34.	We agree that, where relevant, the principles of 'own funds' applies equally to IORPs as to insurance companies.	
35.	We consider that any assets available to the IORP should be allowed for, following the principle of the holistic balance sheet. The issue will be in the valuation of the asset, and how it is allowed against the SCR.	
36.	We do not agree that a 'uniform security level' is necessarily imposed just by mandating a similar approach to the calculation of technical provisions on all IORPs, since this ignores the fact that different IORPs protect against different risks. For example, some defined benefit schemes target lump sums, so members are left with mortality and interest rate risk at retirement; regardless of the financial measures imposed, members of these schemes have less security than members of schemes that target income related benefits; and similarly, members of schemes where indexation is mandatory face less risk than members of schemes where it is not.	

	A uniform measure therefore only considers one degree of risk, whereas the risks faced by scheme members are multi-faceted. Differences in the benefit structure adopted by IORPs in different member states have arisen largely as a result of local social and labour law. Ignoring this in setting the security level for members' benefits risks interfering with the objectives adopted by national governments when establishing the legal framework within which occupational pension schemes must operate. For example, in the event of involuntary wind-up of an IORP, beneficiaries may rank equal to unsecured creditors of the sponsor in some countries (e.g. the UK), while in others (e.g. Ireland) this is not the case. Also, having established a 'uniform security measure', there is no information about the action supervisory authorities could take if it were not met. Depending on the level it is struck at, and the actions that follow, this could have severe financial impacts on IORPs and their sponsoring employers, so that a long implementation period might be required before the proposed new Directive could come into force.	
37.	There is no right answer to this question. We agree that the results produced using Value at Risk (VaR) analysis become increasingly weak, the longer the time horizon used. However, one year is a short time horizon for a pension scheme. On balance, if IORPs are to be required to hold solvency capital and it is to be measured using a statistical approach, a one year VaR approach is probably satisfactory. Decisions in relation to the confidence level are likely to be more material.	
38.	We are concerned that applying statistical models to many pension schemes could result in spurious outcomes, given their size. In addition, the risks carried by most small schemes are generally more straightforward than those carried by larger schemes, since their benefit structure, membership, investment policy and employer relationships are less likely to be complex. Consequently, it is likely to be disproportionate to impose Solvency II models directly onto most IORPs. In addition, the process of implementing Solvency II has been resource intensive: few IORPs will have the resource, and few of their sponsoring employers will have the will, to engage at the level that insurance companies have. The process therefore risks being influenced by a small number of	

	large schemes, resulting in outcomes that are inappropriate across the board. EIOPA could have considered different options: for example; ▪ Article 100 of Solvency II could be transposed into the IORP Directive but only in respect of those IORPs that are within the scope of Article 17(1) of the IORP Directive. ▪ Article 100 could be applied to all IORPs, but the methodology could be simpler, for example, based on scenario testing. In the UK, the Pension Protection Fund has introduced this type of measurement for determining the investment risk different IORPs pose to it. Regulation is an evolving discipline. Although Solvency II has some attractions relative to the effect of the IORP Directive, it is not a perfect model and was developed with a particular form of legal entity in mind. The broad principles underlying Solvency II could be retained and applied to IORPs without carrying over the complexity and resulting bureaucracy that has resulted.	
39.	If a simple, proportionate regime is imposed, annual testing might be appropriate. However, given the long term nature of most defined benefit provision, in line with the current regime we expect that three yearly would normally be adequate and unlikely to provide materially lower protection to members.	
40.	In Solvency II, the purpose of the MCR is to determine a point at which member state supervisory authorities are given stronger powers to intervene in the operation of an insurance company. For example, they can prevent the insurer from writing new business and take steps to transfer books of business to alternative providers. The position in the case of IORPs is less clear. Is it expected that supervisory authorities should force the immediate funding of an IORP without sufficient assets to meet its MCR; or that sponsoring employers should be required to transfer the liabilities to another provider? Both of these could be difficult for employers, particularly since they are likely to have prior calls on their available capital. A decision about a MCR is impossible without understanding its implication. 40 (contd) What adjustments to the Solvency II rules are needed regarding the structure and	

	frequency of the calculation? See above.	
41.	In principle, and in the context of our previous comments in relation to the holistic balance sheet, we agree that there is a place for pension protection schemes. Our preference would be for it to be valued as a separate asset.	
42.	No. It might be sensible to require DC schemes to carry reserves (over and above the value of members' funds) related to short term future administration costs and the cost of winding up the scheme in the event of employer insolvency. However, where the investment risks are borne by members, the only other operational risk the members should face that could affect them financially is fraud: to ask IORPs that are managed fraudulently to carry additional funds against this risk seems unlikely to provide material protection to members. As the consultation document notes, in the UK a separate arrangement to protect members against fraud has been established, which is financed by a levy imposed on all UK registered IORPs. This seems a more reasonable protection regime for this type of arrangement.	
43.	We agree with the principles that IORPs should monitor their financial position and be prepared to take steps for its recovery in the event that it falls below certain levels that could be predetermined. We also agree that some notification requirements would be appropriate, although without information on the way the holistic balance sheet approach could affect the way schemes are financed it is difficult to determine what would be proportionate. Broadly, we understand that supervisory authorities will want more information about schemes with greater risk profiles (including lower funding levels), but do not agree that they should be able to access information arbitrarily. Thus, we would suggest that a requirement for information requirements to be proportionate to the risk should be included in any amended IORP Directive. However, we also wonder what role supervisory authorities will have. IORPs generally have different mechanisms for managing the risk of underfunding than those available to insurance companies. For example, IORPs with no recourse to contributing employers in relation to underfunding can often reduce benefits (so there is explicit conditionality in the benefit structure); where the sponsor	

	covenant is of value to the IORP, future contributions might be forthcoming. Taking the timing of these payments entirely out of the hands of the employer would risk undermining its ability to operate profitably and attract shareholders or other entities prepared to finance it.	
44.	We agree that, where IORPs are underfunded relative to a particular target measure, they should be required to put in place plans to reach the target. However, the nature of these plans is likely to differ depending on the sources of capital available to the IORP in relation to accrued rights. Where IORPs have no recourse to contributing employers in respect of accrued rights, they can often treat certain benefits as conditional and make reductions; where there is recourse to the employer, additional contributions are often requested. Both models are legitimate, but both risk imposing costs on particular generations due to risks adopted in respect of other generations. Of course, in an ideal world the new risk that emerges due to underfunding would be removed as quickly as possible, but this could result in unfair outcomes to members and to employers, their employees and shareholders. So the speed over which the recovery plan is met should be proportionate: nothing is served by pushing employers into insolvency, or cutting one cohort of members' benefits more severely than necessary, just because rules impose too short a recovery plan. Transitional measures will also be relevant to this. If the revised Directive is implemented when funding levels are low relative to the standard required and short recovery plans are imposed, then there will be immediate and possibly inadvertent consequences.	
45.	Yes.	
46.	We do not agree that the requirements in Article 142 should be transposed directly into a revised IORP Directive, in the context of the holistic balance sheet. The nature and value of the assets available to IORPs could change materially over the period of a recovery plan, so, in particular, predicting future balance sheet entries would be spurious as could be the estimate of SCR if more complex calculation models are imposed. However, it would be reasonable for IORPs to consider future cash flow requirements over the period of the plan, provided it is understood that, given their conditional and contingent natures and the member options that might be available, these are no more than indicative best estimates.	

47.	Yes. Our view is that many of the subsidiary requirements set out in the Solvency II Directive just indicate what could be viewed as 'prudent' investment behaviour and so might sit better at a lower level of legislative prescription.	
48.	We do not see the purpose of this, in particular in the context of the EC's objective to achieve a consistent regulatory regime across all member states.	
49.	Although the overarching objectives behind setting investment strategy for defined benefit and defined contribution schemes can be constructed to be the same (for example, to ensure members' expected levels of benefits are achieved with a high degree of certainty) the steps needed to meet the objectives are likely to be different, given the way risk is shared. However, provided the prescription in the revised IORP Directive remains centred on 'prudent person' investment principles, we think its provisions should remain the same for both sorts of provision. In particular, we do not think the Directive is the place for directing DC IORPs towards, for example, particular designs of default fund. The design and naming of investment strategies developed with the aim of supporting members of DC schemes to meet their objectives at retirement is continuing to develop; since Directives are not reviewed frequently and can only change following in depth consideration and consultation, there is a risk that DC schemes would be prevented from taking advantage of new investment products that could provide better targeting or security for members, just because the wording in the Directive does not accommodate their structure.	
50.	• We agree that many of the additional requirements in the Solvency II Directive, relative to the IORP Directive, do not impose materially different obligations on IORPs. On that basis, although there may be no harm in amending the IORP Directive to include them, similarly nothing will be lost by not including them: on balance, then, since nothing is gained by their inclusion we suggest they are not included. Instead, it might be appropriate for Level 2 guidance to clarify, where appropriate, what is meant by the prudent person principle, for those member states where the principle is not so well understood. • We do not agree that cross border DC schemes necessarily place more risk on members (indeed,	

	if the EC believes that is the case we wonder why it is keen to encourage them) and so do not agree that there should be more prescription over the choice of default fund in their case. • We agree that the provision under Article 132(3), that (broadly) the assets held by DC funds should match the associated investment mandate.	
51.	We agree that IORPs' ability to borrow should be restricted, but also consider that there could be some circumstances when they would legitimately choose to borrow. For example, it might be appropriate to borrow to achieve risk management objectives or efficient portfolio management, but not solely for the purposes of investment.	
52.	We are not comfortable with the suggestion that Article 27 of the SII Directive should be transposed into the IORP Directive without amendment. Our view is that regulatory supervision should ensure that IORPs are operated in line with legislative requirements, and those requirements imposed by their own rules, and to provide members and beneficiaries only with the protection these afford. If there is a requirement to protect members and beneficiaries without this caveat, supervisors are then able to impose additional requirements that could subvert the intended relationship between state, members and the IORP providers and/or employers. We do agree that: ▪ supervisors should take into account the effect their actions might have on the stability of financial systems and the ongoing provision of different pension scheme designs; and ▪ an important tool in relation to counter cyclical regulation will be to extend the period over which shortfalls need to be recovered. The circumstances covered in Articles 106, 138 and 304 (smoothing equity returns, adjusting recovery plans following exceptional market movements and allowing for the long term nature of liabilities, respectively) are all relevant to this. However, because the sources of capital available to IORPs are often restricted, either because they do not have recourse to external funding, or because employers' ability and/or willingness to pay is likely to be reduced in market down turns, supervisors will need to be flexible about how they exercise their powers. Cross subsidies will be created regardless of whether they exercise their powers in this regard, or not. For example, in schemes	

	where shortfalls in funding are met by reducing benefits, one generation will lose differently to another, depending on how the reduction is made; similarly, where employers are available to meet underfunding, demanding extra contributions could weaken the employer and expose its employees to risk, ultimately undermining members long term security to achieve a short term recovery. There is also the question of how the holistic balance sheet will operate in a counter cyclical world. For example, in the absence of other measures, if economic conditions deteriorate then this is likely to lead to a reduction in the value of the employer covenant on the asset side (and possibly other assets), whilst the increased uncertainty could require less risk to be taken on the liability side, exacerbating the size of any shortfall.	
53.	It is worth remembering that there are considerably more IORPs than there are insurance companies, and that they are very different in terms of risk exposure and legal structure, so the resource required to regulate them is likely to be greater. For it to be possible for the general supervisory principles of the Solvency II regime to be applied to IORPs, we consider that the provision of IORPs might need a fundamental review. If more member states' regulatory regimes facilitated the provision of multi employer or 'master trust' IORPs, then the resulting economies of scale within some IORPs could result in better management of risk, more accountability and less onerous regulatory supervision. Implementing a Solvency II type regime in relation to IORPs without easing the transition of small IORPs into larger structures seems to put the cart before the horse.	
54.	We do not agree that the object of all pension supervision should be to improve members' benefit security: there is a point at which benefit security is sufficient and providing greater security can be counter productive. For example, if too onerous obligations are placed on one form of provision, providers will move to a different, less regulated form of provision, in which case member security is actually reduced. EIOPA should consider what an appropriate level of security for benefits is, taking into account all risks and how information, good governance and benefit design can be used to manage these risks, as well as financial measures. Although the level of security to target via the Directive is likely to be political decision, EIOPA and other parties involved in providing and regulating the financial products have a responsibility to make it clear that complete security of all financial products is not a	

	realisable objective. The question of how security can be delivered does not appear to have been addressed at all in the consultation. Similarly, although the way administrative differences between IORPs and insurance companies should affect amendments to the drafting of Solvency II principles, before they can be translated into the IORP Directive, other more fundamental differences have not been addressed. In particular, IORPs often serve a social aim, by ensuring employees have access to incomes once they are too old to participate in labour markets. For this social aim to be met it is important that all types of employer are able to provide, and all types of employee are able to access, occupational pension provision. Otherwise, those most in need of employer sponsored retirement provision will be unable to access this form of saving and the social aspect of the IORP will be lost. Insurance companies are not part of a similar social contract: if regulation results in certain products being too expensive for some people to access, then they do not buy them, just as they do not buy other 'luxury' goods. Our view is that this model does not translate well to pension provision and that, certainly, some member states have established a relationship between state and employer sponsored provision that assumes that it will not translate. So, whilst we agree that at an administrative level EIOPA's draft response appears to recognise some differences between IORPs and insurers, we see no evidence that the more important differences have been considered.	
55.	The answer depends on how the information will be used and the requirement would need to be applied proportionately. We agree that stress testing gives rise to useful information: for example, where an IORP has no recourse to the employer covenant, then stress testing could be useful information for indicating the likelihood that conditional benefits might have to be reduced; where an IORP does have recourse to the employer covenant, then it can help it understand the extent to which, for example, investment risk is correlated with risk that the employer covenant will fail. So stress testing would enable supervisory authorities to consider whether IORPs need to take additional steps in relation to their risk management policies or disclosures to members. However, because IORPs have limited ability to demand additional funds from external sources, we do not see the usefulness of a test that triggers this requirement.	

56.	We do not believe a case has been made in the consultation document for this. Member states already have sanctions in place if IORPs are not managed in accordance with local legislation, which includes measures taken to implement the requirements under the IORP Directive. There seems to be no evidence that these provisions are inadequate, so no need for them to be strengthened.	
57.	This will depend on the events that gave rise to the penalty. We would not support 'naming and shaming' for minor breaches.	
58.	It seems appropriate that host states can apply sanctions on an IORP that fails to meet (for example) relevant aspects of its requirements. Although it does not seem necessary for the host state to go through the home state to achieve this, we would expect there to be some collaboration between the two states' supervisory authorities. Otherwise the home state might not have sufficient information to carry out its responsibilities.	
59.	We agree that supervisory authorities would need to be able to collect some information from IORPs in relation to the measures they take to implement the requirements under a revised IORP Directive. However, there are considerably more IORPs than there are insurance companies, so the review process provided for under Solvency II is likely to be onerous, without resulting in much improved outcomes. Because the resource challenge is likely to differ between member states, it might be appropriate for member states to be able to determine the most suitable ways of achieving regulatory oversight, within high level principles set in the Directive, that are proportionate to the risk and take into account the resources available to each IORP in providing the information that could be required.	
60.	We cannot see the purpose achieved by capital add-ons since IORPs are unable to access additional capital in financial markets. Even if this were restricted to apply solely to schemes where members bear all of the risk, the effect of the add on would just be to reduce members' conditional benefits further.	

61.	We agree that it is reasonable for IORPs to expect any providers of outsourced services to provide them with adequate information and that the providers themselves should have to cooperate with supervisory authorities in carrying out their duties in relation to the IORP. However, any rights the supervisory authority has to request information and demand access to premises should be proportionate and reasonable, in connection with its regulatory responsibilities. EIOPA should also consider how it will treat cases where the entity providing third party services to the IORP is separately regulated, perhaps by supervisory authorities implementing standards produced by EIOPA itself under the Insurance Directive. In that case, revisions to the Directive should not duplicate the supervisory role: it should be possible to look through from one set of regulation to the other, to minimise the risk of regulatory overload.	
62.	We would be concerned that changes in the definition of 'home state' could create difficulties with existing structures and we are not aware of any problems created by the existing interpretations of the definition. However, if it is considered that clarification would materially improve the quality of regulation, then we agree that the home state should be where the IORP is registered or authorised, and that 'main administration' should refer to the place where the main strategic decisions are taken. In particular, the definition should not interfere with decisions IORPs could legitiamtely take to outsource the administration function (in the sense of managing payrolls and dealing with day to day member events) to locations outside of the member state the IORP is registered in. In relation to chain outsourcing, we agree that the IORP and the supervisory authorities should be able to look through to the actual entity carrying out tasks in relation to the IORP and that supervision should not stop at the level of 'first outsourcer'. However, if functions are outsourced offshore, then this could create logistical difficulties. We would not consider it appropriate for the regulatory regime to prevent outsourcing to countries other than the IORP's home country, but agree that chain outsroucing, particularly to offshore locations, is likely to place additional governance responsiblities on IORPs that the regulatory regime could be used to indentify, although not necessarily at the level of the Directive.	
63.	Yes, we support the application of strong governance principles to IORPs, provided the principle of proportionality is applied appropriately and the associated information requirements imposed on IORPs (for example, to meet the measures proposed under CfA11) are not onerous.	

	However, rather than mandating regular reviews of IORPs' governance documents, we feel that, in many cases, supervisory authorities should be able to rely on self-certification of processes by those responsible for the IORP. In particular, where the processes have been introduced following advice from an individual or entity already subject to regulation, the IORP's supervisory authority might be prepared to accept certification from the regulated individual or entity. However, 'proportionality' needs to take risk into account as well as size. There could be some circumstances where it is not reasonable to subject smaller IORPs to lighter regulation, in which case, if the regulatory burden is perceived as onerous, member states should consider whether the delivery model selected by the IORP is fit for purpose. Enabling alternative structures that create the economies of scale necessary for strong risk management and governance (for example, creating federations of smaller IORPs under a common governance structure) might meet the objectives underlying the Directive better, as well as achieving better member outcomes.	
64.	We believe so, but the Directive should be amended in such a way that does not prevent new forms of IORP being developed for which other requirements might be inappropriate.	
65.	It seems reasonable to require those with control over the way an IORP is managed or administered to meet 'fit and proper' criteria, regardless of whether the benefits provided are defined benefit or defined contribution. However, whilst agreeing that some level of knowledge and understanding is essential, we are less concerned that they have necessary qualifications. Often, having a range of diverse skills and backgrounds on a governing body, rather than a narrow group of 'experts', creates an environment that is more likely to challenge the status quo so, in our view, even if the main principles from Solvency II Directive are transposed into the IORP Directive, it is important to retain the existing provision in Article 9, which permits those running the scheme to rely on advisers. Where an IORP's management relies on advisers to support it to make key decisions, it seems appropriate that the 'fit and proper' test should apply to those advisers, and the senior management in those advisers' firms, as well as the requirement for appropriate qualifications and experience.	
66.	We consider that the knowledge requirements should apply to the group of people (the 'board') who	

	effectively run the IORP at all times, but need not apply all the time to individuals. This enables lay people to join the board and subsequently acquire the necessary knowledge about the scheme: otherwise it could be difficult to attract the right mix of people, which in some cases includes scheme members.	
67.	If decision makers at an IORP fail collectively or individually the fit and proper requirements, it should be possible for the supervisory authorities to replace them with alternative representatives. However, because of the different legal frameworks for IORPs we consider it most appropriate for these measures to be determined at the member state level.	
68.	We agree that principles in relation to the need for risk management should apply to IORPS similarly to how they apply to insurance companies. However, IORPs generally are unable to select members, do not necessarily have to market themselves and do not have to meet shareholders' objectives, so their risk profiles are likely to be different. Consequently, the matters likely to drive risk management strategies could be different. Provided this is taken into account in the transcription of the Solvency II requirements into the IORP Directive, we are supportive of this initiative. However, it is not possible to comment on the consultation document's statement of the positive or negative impacts of introducing these new requirements into the IORP Directive without knowing what actions supervisory authorities will be expected to take in response to the information that emerges from these exercises. In relation to this, and to other aspects of the consultation, without this information and a quantitative impact assessment, the actual effects of the proposals are impossible to assess.	
69.	Our view is that the requirement for risk management policies, the framework underlying the holistic balance sheet including the need to establish how an IORP's measurements of a scheme's technical provisions relate to the different forms of security, including financial assets and employer covenant, should be sufficient. Overlaying an additional process for IORPs seems unlikely to add additional value. ORSAs might be valuable in an insurance company context, since it encourages company management to consider how the risk management and other regulatory processes imposed by	

	Solvency II affect their ability to attract new business and shareholder capital. The ORSA can be used to establish a position that marks a company as different from its competitors but, because it is part of the regulatory process, it enables supervisory authorities to monitor how companies ORSAs relate to other aspects of Solvency II’s capital and governance requirements. However, these tools do not seem useful to IORPs, which do not have to satisfy the same market disciplines. The risk management and financial measures imposed via the supervisory regime ought to be adequate to achieve the objectives set out by EIOPA in Chapter 21 of its consultation, for an IORP’s ORSA.	
70.	Our answer to question 69 applies equally to IORPs where members bear all the risks. In both cases the only circumstance in which we can see value to IORPs carrying out an ORSA is where the regulatory regime does not enable them to manage their risk properly, or to establish sufficient financial or other assets to achieve adequate levels of member security. If the regulatory regime prevents that, then we view it as a failure of the regulatory regime, rather than a reason for IORPs to establish additional and different risk management techniques. However, it will be necessary to ensure that, as far as necessary, the risk management and other aspects of the regulatory regime apply to defined contribution as well as defined benefit schemes.	
71.	As discussed previously, we consider there to be no need.	
72.	Mercer agrees that IORPs should be required to establish internal controls and to monitor compliance with their regulatory and other responsibilities. Also, particularly because IORPs often rely on external advisers and outsourced investment management, administrative functions and other services, there need to be measures to ensure the compliance of these external providers. Establishing whistleblowing responsibilities on these other entities that are associated with the IORPs is a way of ensuring the supervisory regime is complied with at all levels. Not least, it creates a mechanism for self regulation, helping supervisory authorities to carry out their responsibilities. Consequently, we believe that mandating whistleblowing, rather than leaving it to member states to decide whether to provide for these obligations, would produce a more proportionate regime and result in a lesser regulatory burden over all.	

73.	Whilst we agree that IORPs need to monitor their compliance with all the legislation that applies to them, in most cases this will not be a negligible task. Therefore, the Directive should not be prescriptive about how this is achieved.	
74.	We agree that there is likely to be value to IORPs establishing an internal audit function, but consider that the Directive should not be prescriptive about how it is achieved.	
75.	We consider that whistleblowing responsibilities should be applied to all bodies and individuals with responsibilities towards the IORP.	
76.	The actuarial function as currently described in the IORP Directive is limited relative to those in Solvency II. The requirements in Solvency II add some context and also impose additional responsibilities, including responsibility for judging whether the approach adopted by the IORP is compliant (currently, the requirement is solely for advice to be provided, rather than for opinion to be stated). In most EU countries, actuaries are likely to be regulated by local professional institutions, so this additional layer of compliance should give additional reassurance to the supervisory authority, similar to an audit function. Ultimately it must be the IORP that is responsible for taking decisions with regard to the operation and risk management of the scheme: requiring the adviser to comment on how effectively IORPs have carried out their duties in relation to the technical provisions calculation could introduce conflict into the client relationship if the knowledge, understanding and behavioural skills of the IORP’s decision making representatives are not fully proficient. However, overall, we agree that the requirements are likely to make the application of the regulatory regime more rigorous. Regardless of how the requirements for an actuarial function are implemented, we consider that member states should be given flexibility over how they implement this principle (subject to ensuring that the skills and experience of the person carrying out the function meet certain minimum standards).	
77.	We believe so, with the suggested amendments in relation to underwriting policy and reinsurance.	

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	We agree that the actuarial function should have whistle-blowing responsibility to the Board of the IORP and to the supervisory body. We also agree that actuaries should be able to make a strong contribution to the risk management function.	
78.	Although we agree that, in principle, it is important for the actuarial function to be independent of the IORP, in practice this is unlikely to be possible. Whether the holder of the actuarial function is directly employed by the IORP, or appointed as an adviser, he or she will have a pecuniary interest in maintaining a relationship with the IORP, which could affect the advice provided; where the holder is an external adviser, he or she could have other clients that are not independent of the IORP. Our view is that, in many cases, the risk of the quality of advice provided being affected can be managed by having robust conflict of interest protocols so that all parties are aware of the risks and have agreed steps to mange them. That is, although independence cannot be guaranteed, it should be possible to ensure that the quality of advice provided can be relied upon.	
79.	We support the proposed introduction of Option 2 and agree with the analysis of the options presented.	
80.	We agree with the principle that IORPs should be permitted to outsource most aspects of their management to third party providers whilst retaining the responsibility for ensuring any functions are provided effectively. We are concerned about the effects of the proposal in paragraph 25.5.2(c), that Supervisory Authorities must 'remain sighted of the outsourcing and … able to monitor the compliance'. Although clearly service providers should not be appointed with a view to avoiding supervision, in our view, the prime consideration should be that outsourcing cannot hinder the effective running of the IORP – provided this is the case, then Supervisory Authorities should be able to organise themselves to operate effectively in relation to any third party arrangements. It is likely that EIOPA's proposal will achieve this, but it will depend on how 'remains sighted' is interpreted during the implementation process.	

	We also do not understand the need for IORPs to notify supervisory authorities in 'a timely manner', of any decisions taken with respect of outsourcing. We expect supervisory authorities will become aware of this through normal disclosure requests and requirements, and that should be sufficient. In relation to the powers being given to supervisory authorities, in this case, as in previous parts of the consultation, we suggest that supervisory authorities' ability to request information is limited to cases where it is reasonable for them to do so and that the information they are able to demand is proportionate.	
81.	We are not sure what is referred to here. Outsourcing contracts will be driven by the relationship between the IORP and its service provider, which in turn is likely to depend on the size and legal structure of the IORP and the benefits targeted. So standardisation might not be appropriate. In addition, in our experience outsourcing contracts do not create any obstacles in relation to cross border provision: the obstacles are met long before arrangements for outsourcing are considered, and arise in relation to tax and other legislative restrictions.	
82.	We consider this a matter for the IORP and its service provider. Since its approach to outsourcing will be part of an IORP's risk management and internal controls policies, proposals elsewhere in the consultation already cover any special risks associated with outsourcing contracts adequately.	
83.	We agree that, in the absence of member state regulation, the provisions in the current IORP Directive risk leaving some scheme members exposed to the risk of operational failure in relation to the scheme's assets. However, we are not sure that the distinction made in the consultation between IORPs with a 'legal personality' and those without is necessarily helpful. Instead, we would support an amendment to the IORP Directive that introduced the general principles of good governance in relation to safe keeping of assets, as set out in paragraph 26.3.35 of the consultation document. Then, member states could decide whether more prescription was required, based on the different models for IORPs in their countries. In particular, many IORPs will invest via entities subject to either the UCITS or the AIFM Directives, so to carry the principles in those Directives directly into the IORP Directive would risk duplicating regulation.	

84.	We agree that having stronger principles than those in the current IORP Directive could make scheme members' benefits more secure. However, inconsistent outcomes could arise if what seems to us to be an artificial distinction between those IORPs considered to have 'legal personality' and those that are not, is used to impose different regulatory standards.	
85.	Currently, many IORPs invest a significant proportion of their assets in collective investment funds, so proposals to require IORPs to appoint a depositary will need to consider the relationships and responsibilities of those that act as an IORP's accounting book of record for investments in collective investment funds, but do not act as the collective fund's depositary. Moves to increase depositary's liability for investments in collective investment funds will increase the cost of investments and could create an economic incentive for IORPs to purchase units direct from fund managers as opposed to holding units in the custodian's nominee name. Consideration needs to be given to the treatment of different classes of investment instruments. For example, some financial instruments, such as securities which can be registered in an account opened at the depositary's books or physically delivered to the depositary (e.g. bearer securities), can be held in custody. However, others, such as over the counter derivative instruments, real estate and private equity investments, cannot, and more thought should be given to the responsibility and liability the depositary bears in these cases. We do not consider it would be desirable or practicable to require IORP appointed depositaries to undertake due diligence of other service providers, such as fund accountants, custodians and auditors appointed by investment managers or investment funds. This could make it more difficult for IORPs to access new, or change existing, fund managers. Because IORPs often contract with other regulated entities with regard to investment management, there is a risk that regulatory measures will be duplicated, with no additional benefit for members and superfluous resource implications for supervisory authorities.	
86.	Custodians and Depositories commonly only enter into business with entities after completing know your customer, anti money laundering and contract negotiations, so we do not consider the	

	requirement to agree contractual terms will add materially to most IORP's existing costs. Extending a depositary's liability to include investments in commingled investment funds or assets not in safekeeping is likely to incur substantial additional costs which may be disproportionate to the additional protections offered. Extending oversight functions to cover areas such as valuation, cash flow, liquidity forecasting and accounting goes beyond the current remit of the depositary or custodian function. Since this is likely to result in additional fees, a detailed cost-benefit analysis should be undertaken to ensure it is in the best interests of investors. We consider the commonest source of conflicts of interest will arise from combined prime brokerage / custodian appointments. Such conflicts are currently commonly managed by fire walls within organisations, including, but not limited to, staff access rights between trading floors and asset servicing areas, in addition to physically segregated servers for house positions and positions in administration. Our preference would be for regulation to be implemented at the level of the prime broker or other potentially conflicted organisation as opposed to individual IORPs. In practice, prime brokerage and similar services are provided by a small number of globally active organisations, so regulation could then be implemented more effectively. Where it is deemed necessary to appoint a depositary, we agree that the terms of engagement should cover the general requirements set out here. We do not distinguish between the cost of having to appoint a depositary, and the cost of entering into a robust contract with the depositary.	
87.	We consider that the principles set out in paragraph 26.3.35 are sufficient.	
88.	In our experience, the majority of smaller IORPs are not currently required to appoint a depositary. We estimate industry average minimum fees to be in the region of €40,000 - €70,000 and therefore question whether the mandatory appointment of a custodian for IORPs fully invested in commingled investment funds constitutes value for money. However, if individual member states are able to implement the general principles in a proportionate	

	way, reflecting the legal construct of the IORPs under their jurisdiction, and their relationship with the assets and the entities used as investment managers, it should be possible for the costs to be proportionate to the advantages achieved for scheme members.	
89.	We agree with the analysis. In particular, we agree that it is important to strike a balance between the provision of information and the cost imposed on schemes as a result.	
90.	We would welcome some convergence between the IORP Directive and Solvency II in relation to disclosure of information to supervisor authorities. For example, the IORP Directive gives supervisory authorities wide power to gather information, whereas Solvency II specifies only information relevant to the supervisory body’s responsibilities: this would enable a more proportionate outcome. However, there are considerably more IORPs than there are insurance companies, and we would not feel it an appropriate outcome if supervisory bodies had to become much larger (and therefore costly) solely to manage the amount of information that could be required. So the implementing measures need to ensure that supervisory authorities are supported in identifying the information that is most relevant to their duties, and are able to exercise data requests in a proportionate way.	
91.	We do not think it is necessary to prescribe additional information requirements on DB schemes in Level 1 regulation. However, the stark distinction between DB and DC made in the consultation document does not reflect reality: in fact, there is a continuum of provision, with some DC schemes providing rules based benefits (for example, a minimum annual rate of return) and some DB schemes sharing investment risk with members (for example, via conditional indexation). Consequently, there should be some basic information requirements that apply to all schemes, and additional information provided depending on the type and size of the risk borne by members.	
92.	Yes. We think it is important for members to be given information that enables them to understand the investment choices available, but they should also know where the responsibility for choosing investment funds and operating the scheme lies, for example. However, we do not agree it is sufficiently important for members to be able to compare different IORPs that this should become part of the information prescribed in the Directive.	

93.	Members need to be provided with sufficient information that they can, perhaps with some support, understand the risk reward profile of the choices available to them. But this equation will vary according to the member's own risk preferences and characteristics, so to be most useful the information provided will need to be tailored to individual member's circumstances. In practice, this is expensive to achieve and so it might not be proportionate to prescribe this in Level 1 regulation, but we do think it important that investment mix and duration are taken into account. The answers to the questions asked here are non-trivial and a considered response would fill several pages, but some suggestions are: ▪ Risk and reward can be shown using sliding scales, or summary, descriptive, phrases. These should be related to different objectives, so that those approaching retirement understand the different investment horizon available to them, and the different risks they face. This is not as simple as saying that equity works better over longer time horizons. ▪ Performance scenarios need to be carefully conceived and communicated so as not to raise members' expectations. One approach would be to include an example with no future growth, but continued contributions, for comparison. ▪ The choice of risk premium should be left to member state supervisors, since access to deep investment markets differs throughout the EU. Although we agree that it is important for members to be provided with sufficient information that they should be able to take a view about the risk reward profile of the funds available to them, we think it unlikely that all members will use the information.	
94.	It should contain information about the current level of costs and the ability of the provider to alter the costs charged. It should cross refer to the KID, but not have to be co-ordinated, since the KID content is likely to change with time.	
95.	Since there is such a variety of IORPs, including structure, legal status, and designs, throughout the EU, harmonisation should be at a very high level. For example, prescribing the basic content and perhaps a risk related approach would seem adequate.	

96.	Until a quantitative impact assessment is provided, it is hard to have an opinion. We agree that more cost will be imposed on DC schemes, and there will be some benefit, but we are not sure the extra cost will be worth the likely marginal benefit achieved.	