<table>
<tr><td colspan="2">Comments Template on EIOPA-CP-11/006
Response to Call for Advice on the review of Directive 2003/41/EC: second consultation</td><td>Deadline
02.01.2012
18:00 CET</td></tr>
<tr><td>Company name:</td><td colspan="2">OECD Secretariat to the Working Party on Private Pensions</td></tr>
<tr><td>Disclosure of comments:</td><td>EIOPA will make all comments available on its website, except where respondents specifically request that their comments remain confidential.
Please indicate if your comments on this CP should be treated as confidential, by deleting the word Public in the column to the left and by inserting the word Confidential.</td><td>Public</td></tr>
<tr><td></td><td colspan="2">The question numbers below correspond to Consultation Paper No. 06 (EIOPA-CP-11/006).

Please follow the instructions for filling in the template:
⇨ Do not change the numbering in column “Question”.
⇨ Please fill in your comment in the relevant row. If you have no comment on a question, keep the row empty.
⇨ There are 96 questions for respondents. Please restrict responses in the row “General comment” only to material which is not covered by these 96 questions.
⇨ Our IT tool does not allow processing of comments which do not refer to the specific question numbers below.
o If your comment refers to multiple questions, please insert your comment at the first relevant question and mention in your comment to which other questions this also applies.
o If your comment refers to parts of a question, please indicate this in the comment itself.
Please send the completed template to CP-006@eiopa.europa.eu, in MSWord Format, (our IT tool does not allow processing of any other formats).</td></tr>
<tr><td>Question</td><td colspan="2">Comment</td></tr>
<tr><td>General comment</td><td></td><td></td></tr>
<tr><td>1.</td><td></td><td></td></tr>
</table>

2.		
3.		
4.		
5.		
6.		
7.		
8.		
9.		
10.		
11.		
12.		
13.		
14.		
15.		
16.	**What is the stakeholders' view on inserting a recital in the IORP Directive saying that supervisory valuation standards should, to the extent appropriate, be compatible with accounting standards?** The suggestions proposed by the Response differ from accounting standards in various ways (for example by proposing a risk margin, using a different discount rate, the existence of an asset ceiling under IAS 19, the use of prudent vs. best estimate assumptions, the calculation of technical provisions, etc.), so it is unclear what practical meaning any such statement would have. For a further discussion, see the OECD note "The New IAS 19 Exposure Draft" (http://www.oecd.org/dataoecd/44/56/45929995.pdf) and "Recent Developments in Pension Accounting" (http://www.oecd.org/dataoecd/60/54/40954137.pdf).	

17.		
18.		
19.	**Do stakeholders agree with the proposed conditions defining in what cases IORPs should take into account future accruals or not when establishing technical provisions?** The CfA response proposes the following on page 151 with respect to the “definition of cash-flows relevant when calculating technical provisions”: *In cases where there are predefined contributions set in advance for the pre-retirement period and where there is a direct relation between contributions paid to the IORP in a certain part of this period and the pension rights accrued in this part of this period then all cash in-flows and outflows…shall be considered when calculating technical provisions.* *In other cases technical provisions shall be calculated based on future cash-flows resulting from accrued rights.* The full implications of this proposal are difficult to determine without further clarification and analysis. However, based on the wording above, it would seem that two DB plans that promise identical DB benefits at retirement age (e.g. 1.5% of final average pay times years of service) could be valued in completely different manners based on the accrual patterns of the benefits within the two DB plans, for example, if the retirement benefits in one of the DB plans accrue on a straight-line basis and the retirement benefits in the other DB plan accrue using an insurance company-type accrual pattern. The potential impact of having significantly different technical provisions for ultimate retirement benefits that are identical would need to be explored.	

	Furthermore, would pure defined contribution schemes fall under the first paragraph above and would that mean that all future cash flows would need to be taken into account to determine the technical provisions? Having technical provisions that differ from the market value of plan assets in pure defined contribution plans would raise a number of issues.	
20.		
21.	**What is the stakeholders' view on the two options presented regarding the interest rate used to establish technical provisions (including positive and negative impacts)?** Use of a spot market discount rate for purposes of determining capital requirements may encourage a short-term investment horizon or encourage pro-cyclical behaviour. For a further discussion, see the answer to question 36 and the OECD Working Paper on "The Impact of the Financial Crisis on Defined Benefit Plans and the Need for Counter-Cyclical Funding Regulations" (http://www.oecd.org/dataoecd/22/11/45694491.pdf).	
22.		
23.	**Do stakeholders agree with the analysis regarding the inclusion of unconditional, conditional and discretionary benefits in technical provisions as introduced by Article 78 of Solvency II? Do stakeholders find that discretionary benefits should be included in the best estimate of technical provisions? Is the Solvency II article on surplus funds useful for IORPs in this respect?** If a best-estimate approach were to be used, then it would seem reasonable to also value discretionary benefits on the best-estimate probability that those benefits would be paid out in the future. However, if benefits truly are discretionary, then care must be taken that any provision for such	

	benefits and any asset accumulation to cover such benefits do not in effect turn discretionary benefits into mandatory benefits. IAS 19 requires taking into account future salary increases when valuing technical provisions. However, this would not typically be consistent with an insurance company's valuation of a similar product. Furthermore, as recognised in the OECD Guidelines for Funding and Benefit Security the funding requirements of discretionary or conditional benefits should be more flexible than those for non-discretionary or guaranteed benefits.	
24.		
25.		
26.		
27.		
28.	**Do stakeholders believe that it would be useful to introduce Article 83 of Solvency II with appropriate amendments into a revised IORP Directive regarding the need for assumptions to calculate technical provisions to be regularly compared against experience and adjustments made when appropriate?** Many IORP's are too small to have plan specific demographic assumptions and, with the help of their actuaries and auditors, use demographic assumptions based on industry or country averages or approximations made by their actuaries. It is unclear whether the requirement for regular experience study reviews would be appropriate or reliable for small and medium-sized IORP's. For a further discussion, see the IOPS Principles of Private Pension Supervision, Principle 6 on Proportionality and Consistency (http://www.oecd.org/dataoecd/51/9/44495715.pdf).	

29.		
30.		
31.		
32.		
33.	**What is the stakeholders' view on the analysis regarding sponsor support? 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?** In principle, valuing different forms of sponsor support seems reasonable (as outlined in paragraph 9.3.194). The contingent assets of the plan sponsor described in paragraph 9.3.194(C) typically back book-reserved obligations which the CfA states are covered by the Directive 2008/94/EC on the protection of employees in the event of employer insolvency. Including these types of contingent assets for funded plans when book-reserved plans which pay benefits due based on these same types of contingent assets seems to be inconsistent.	
34.		
35.		
36.	**What is the stakeholders' view on the analysis whether to introduce or not a uniform security level for IORPs across Europe? Do the stakeholders agree with EIOPA's decision not to recommend a specific probability? If not, what specific probability should be imposed upon IORPs?** A harmonised solvency regime would ideally encourage and respect the diversity of pension systems that exist in Europe.	

	As stated in the OECD Working Paper on "The Impact of the Financial Crisis on Defined Benefit Plans and the Need for Counter-Cyclical Funding Regulations" (http://www.oecd.org/dataoecd/22/11/45694491.pdf), broadly speaking, the goals of solvency regulations for defined benefit plans should be to • encourage deficit reduction contributions and appropriate build up of surplus when plan sponsor finances are strong; • help maintain predictable costs and dampen volatility; and, • give plan sponsors more control to manage risks and costs. Furthermore, solvency regulations for defined benefit plans should • Avoid excessive reliance on current market values for purposes of determining contributions. • Set minimum funding levels or targets that are consistent with the goal of benefit security. • Allow appropriate levels of over-funding in good economic times via more flexible tax ceilings. • Limit contribution holidays and plan sponsor access to surplus. • Encourage stability of long-term contribution patterns via appropriate actuarial methods. • Incorporate flexibility into funding rules to reflect the overall volatility of funding valuations. • Avoid over-regulation and maintain a stable regulatory environment.	
37.	**Do stakeholders agree that the confidence level should apply to a one-year time horizon?** Measuring value-at-risk over a one-year time horizon can be problematic given the long-term nature of IORP obligations. The CfA's proposed solution to this short time horizon by giving a lower confidence interval than the 99.5% required by Solvency II could be a practical work-around, but does not necessarily fully address the issues of counter-cyclicality and potential short-termism that may arise with the use of such quantitative, risk-based funding rules.	

	Short-term value-at-risk type models combined with fair value principles and market discount rates may incentivise pro-cyclical funding behaviour and shorten the investment horizon. Furthermore, it is important to take note that in sponsored-backed IORPs, the most important risk is not necessarily annual fluctuations in the funding level, but the possibility of sponsor bankruptcy, as recognised in the OECD Working Paper on "The Impact of the Financial Crisis on Defined Benefit Plans and the Need for Counter-Cyclical Funding Regulations" (http://www.oecd.org/dataoecd/22/11/45694491.pdf). Finally, model risk should also be taken into account as it is unclear to what extent the various risks that IORPs are exposed to can fully be modelled and quantified in a value-at-risk type solvency framework.	
38.	**What is the stakeholders' view on applying the Solvency II-rules for calculating the solvency capital requirement (SCR) to IORPs, taking into account their specific security and benefit adjustment mechanisms?** See answer to question 37. It appears as if some countries' private pension systems will be affected by the proposals made in the CfA response to a much greater extent than others. Given the voluntary nature of occupational pension plans, a concern is that overly onerous capital requirements would incentivise plan sponsors to further transfer risk to individuals. If capital requirements are similar to those required for insurance companies, then it would seem reasonable to expect that plan sponsors could find buying out their obligations with an insurance company an appealing option, even though this may be ultimately a more costly form of provision, without necessarily leading to greater benefit security, or higher expected benefits.	

	Care must also be taken so that any risk-based solvency rules based on the Solvency II framework do not work to the detriment of the long-term investment horizon and do not encourage pro-cyclical behaviour.	
39.		
40.		
41.		
42.	**Do stakeholders agree that capital requirements for operation risk should be applied to DC schemes where investment risk is borne by plan members? Should these capital requirements be uniform or tailored to the actual risk profile? Do stakeholders find it sensible to distinguish between DC and other schemes in the area of operation risk?** Capital requirements for operational risk in DC plans are not common practice in OECD countries. Compulsory insurance to cover the risk of, for example, fraud is a more common approach.	
43.		
44.	**What is the stakeholders' view on the analysis regarding the submission of recovery plans and the length of recovery periods as introduced by Articles 138 and 139 of Solvency II? Should the recovery periods – with regard to the SCR and possibly the MCR – for IORPs be flexible, fixed or a combination of both? What would be the reasons – if any – to allow IORPs longer recovery periods than prescribed by Solvency II?** Recovery periods should take into account the long-term nature of IORP obligations. Furthermore, the OECD believes that supervisory oversight should be proportionate, flexible and risk-based.	

	During the 2008 financial crisis, regulators and supervisors in many countries allowed flexibility in recovery rules in order to avoid materialising losses at the bottom of the market and put undue burden on cash-strapped plan sponsors. See the OECD Working Paper on "Private Pensions and Policy Responses to the Financial and Economic Crisis", http://www.oecd.org/dataoecd/37/54/42601323.pdf.	
45.		
46.		
47.	**Do stakeholders believe that the prudent person principle is a sufficient basis for the investment of IORPs or is additional provision needed?** The OECD believes that the basic regulations should be built around the concept of the "prudent person" standard. The OECD Core Principles of Occupational Pension Regulation state that *The governing body of the pension plan or fund and other appropriate parties should be subject to a "prudent person standard" such that the investment of pension assets is undertaken with care, the skill of an expert, prudence and due diligence. Where they lack sufficient expertise to make fully informed decisions and fulfil their responsibilities the governing body and other appropriate parties should be required to seek the external assistance of an expert.* *The legal provisions may include maximum levels of investment by category (ceilings) to the extent that they are consistent with and promote the prudential principles of security, profitability, and liquidity pursuant to which assets should be invested. Legal provisions could also similarly include a list of admitted or recommended assets. Within this framework, certain categories of investments may be strictly limited. The legal provisions should not prescribe a minimum level of investment (floors) for any given category of investment, except on an exceptional and temporary basis and for compelling prudential reasons.*	

48.		
49.	**To what extent do stakeholders believe the investment provisions of the Directive should differ between defined benefit and defined contribution pensions?** Generally, OECD guidelines on asset management consider the prudent person standard as appropriate for both defined benefit and defined contribution plans. The OECD Core Principles of Occupational Pension Regulation state that *Where members direct their own investments in an occupational pension plan, they have the right to a number and diversity of investment choices sufficient to permit them to construct an appropriate investment portfolio in light of their own individual circumstances and in the context of the particular pension programme.* Members in a defined contribution scheme should be provided with a robust default investment option with an appropriate level of risk exposure that incorporates a life-cycle investment approach.	
50.	**Do stakeholders agree with the analysis of the options (including the pros and cons) as laid out in this advice? Are there any other impacts that should be considered?** The CfA Response proposes that "IORPs shall only invest in assets and instruments whose risks the institution concerned can properly identify, measure, monitor, manage, control and report". It should be examined whether this would prohibit IORPs from investing in assets such as infrastructure and private equity which may in principle be attractive to long-term investors due to a potential illiquidity premium. For a further discussion, see the OECD paper "Pension Fund Investment in Infrastructure: A Survey" (http://www.oecd.org/dataoecd/59/33/48634596.pdf).	

51.		
52.	**What is the stakeholders' view on the analysis regarding the objective of supervision and the measures to avoid pro-cyclical behaviour?** The OECD believes that funding rules should aim to be counter-cyclical. For a further discussion, see the answer to question 36 and the OECD Working Paper on "The Impact of the Financial Crisis on Defined Benefit Plans and the Need for Counter-Cyclical Funding Regulations" (http://www.oecd.org/dataoecd/22/11/45694491.pdf).	
53.		
54.		
55.		
56.		
57.		
58.		
59.		
60.		
61.		
62.		
63.		
64.		
65.		
66.		
67.		
68.		

	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
69.		
70.		
71.		
72.		
73.		
74.		
75.		
76.		
77.		
78.		
79.		
80.		
81.		
82.		
83.		
84.		
85.		
86.		
87.		
88.		
89.		
90.		
91.		
92.		
93.		

94.		
95.		
96.		