

**Comments Template on
Discussion Paper on Sponsor Support Technical Specifications**

**Deadline
31 October 2013
18:00 CET**

Name of Company:	Lincoln International Pensions Advisory Limited (LIPAL)	
Disclosure of comments:	Please indicate if your comments should be treated as confidential:	Public
<p>Please follow the following instructions for filling in the template:</p> <ul style="list-style-type: none"> ⇒ Do not change the numbering in the column "reference"; if you change numbering, your comment cannot be processed by our IT tool ⇒ Leave the last column <u>empty</u>. ⇒ Please fill in your comment in the relevant row. If you have <u>no comment</u> on a question, keep the row <u>empty</u>. ⇒ Our IT tool does not allow processing of comments which do not refer to the specific numbers below. <p>Please send the completed template, in Word Format, to DP-13-001@eiopa.europa.eu</p> <p>Our IT tool does not allow processing of any other formats.</p> <p>The numbering of the questions refers to Discussion Paper on Sponsor Support.</p>		
Reference	Comment	
General Comment	<p>We welcome the Discussion Paper and, in particular, believe the "Alternative Simplified Approach" represents a useful development to the original QIS.</p> <p>Lincoln International Pensions Advisory Limited (LIPAL) is one of the largest leading independent providers of employer covenant advice to sponsors and trustees of pension schemes in the UK. We advise on all aspects of the employer covenant, including assessments, monitoring and advice on corporate transactions. We currently advise schemes with assets exceeding £80bn in aggregate.</p> <p>LIPAL is part of the global firm, Lincoln International LP. Our pensions team draws on corporate</p>	

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	finance and other expertise from the circa 300 professionals located throughout the world. LIPAL acts for both trustees and sponsors on a wide range of pensions issues.	
Q01.		
Q02.		
Q03.		
Q04.		
Q05.		
Q06.		
Q07.		
Q08.		
Q09.		
Q10.		
Q11.	<ul style="list-style-type: none"> • We are in favour of a “proportionate approach” and believe the “Alternative Simplified Approach” could provide a useful baseline with schemes retaining the flexibility to carry out additional tailored analysis as they see appropriate and as envisaged by Para 62 of the Discussion Paper. • We believe Solvency 2 provides a useful precedent in this case allowing insurers to implement a “standardized approach” whilst giving them the option to build an “internal model” where this is merited. In addition, we believe useful parallels can be drawn with the FtK standardized approach used in the Netherlands for determining solvency cover. • Owing to the many potential complications associated with valuing sponsor covenant (highlighted in Section 2 of the Discussion Paper and reflecting many of our comments made during the Actuarial profession’s London discussion of the PwC and Barrie & Hibbert papers in January 2013) it is important for the approach in the first instance to be relatively simple and proportionate, so that all IORPs can comply. 	

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	<ul style="list-style-type: none"> • Therefore, our view is in favour of a two-phased approach: <ul style="list-style-type: none"> ○ Partial adoption over a transition period during which the calculations are carried out for disclosure purposes only; followed by ○ Full implementation, but only once all the practical issues encountered during transition are addressed and the remedies / penalties for failing the solvency test are clear (at present time, this clarity is some way off). • We believe the introduction of the FRS17 accounting standard serves as a useful precedent in this case: giving users and practitioners time to get used to it before the standard was finalized and implemented in full. • During this transition period no penalties would be imposed on schemes if they were to find themselves in breach of the guidelines. • The transition period should help unearth key risk management themes for IORPs and help ensure the new approaches are applied consistently to IORPs across different jurisdictions (who may have very different social contracts). • From our discussions in other jurisdictions outside the UK, there will be very different levels of practical expertise when dealing with assessing sponsor covenant which will take time to acquire in many jurisdictions. • Moreover, the transition period should allow advisors to reconcile any covenant work already undertaken in the relevant jurisdictions (e.g. the UK) for funding purposes with the new approaches. 	
Q12.		
Q13.	<ul style="list-style-type: none"> • An answer to this question requires clarity over how EIOPA intends to use this material. • For example, if EIOPA intends to implement a prescriptive covenant valuation approach intended for a new solvency regime for IORPs, significant additional information is required to properly define the approach. • We believe a prescriptive approach could be counterproductive if it oversimplifies covenant valuation and produces misleading results. • If the sponsor covenant calculations are to be carried out for disclosure purposes only and giving IORPs scope to adjust the methodology to fit their specific requirements, we believe 	

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	the Discussion Paper is in many regards adequate.	
Q14.		
Q15.	<ul style="list-style-type: none"> We believe other ratios may need to be considered, in particular when analyzing sponsor support provided by financial institutions and utilities, among others. 	
Q16.	<ul style="list-style-type: none"> It would be useful for IORPs and their advisors to have access to some case studies for different types of schemes and sponsors. We note that the calculations envisaged by the “Alternative Simplified Approach” are backward-looking in nature (para 61 suggests using credit ratios based on the average of the most recent 3 years). We believe covenant assessments should be forward-looking, consistent with the forward-looking nature of the liabilities to be met. Users of the information will need to be aware of the discrepancy between the likely period of sponsors’ financial forecasts and the duration of the scheme liabilities. The methodology does not address on what basis covenant valuations should be carried out. We note that QIS typically favours best estimate approaches but we note that best estimate projections are rarely derived from backward-looking calculations. 	
Q17.	<ul style="list-style-type: none"> It would be useful to have additional clarity on the application of the quantitative ratios. For example: <ul style="list-style-type: none"> Asset Cover: It is not clear whether any adjustments are made to the ‘net asset’ value used in the calculation to allow for the quality of the asset, security, etc. Income Cover: The calculation appears to assume that all EBITDA after debt costs will be available to fund an IORP. In the UK this seems inconsistent with the Pension Regulator’s principle of promoting growth. It would be useful for IORPs and their advisors to have access to some case studies for different types of schemes and sponsors. 	
Q18.	<ul style="list-style-type: none"> We believe there are a number of ratios (other than Income Cover and Asset Cover) that are key to covenant assessments but which may not easily map to historical default probabilities. For example, we believe the ratio of Free Cashflows to Level A deficit is an important ratio to consider. 	
Q19.	<ul style="list-style-type: none"> We see potential dangers in relying on only two credit ratios (Income Cover and Asset Cover) 	

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	<p>when valuing sponsor covenant.</p> <ul style="list-style-type: none"> We believe qualitative factors will play a very important role in sponsor covenant assessment. 	
Q20.		
Q21.	<ul style="list-style-type: none"> To determine the appropriateness of the proposed mapping of contribution period to sponsor covenant rating we would need to understand how the suggested periods are calculated. We believe sponsor affordability and contribution periods require projection of sponsor free cashflows. The contribution periods will then be a function of what percentage of free cashflows can realistically be diverted to pension deficit contributions. 	
Q22.	<ul style="list-style-type: none"> We agree the time periods for contributions for the QIS calculations for sponsor support should be based on affordability unless there is a stated obligation to pay. 	
Q23.		
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Q36.		