

OPSG Feedback Statement
to
EIOPA QIS Preliminary Results

(Publication of EIOPA-BOS-13/021

“QIS on IORPs – Preliminary Results for the European Commission”)

Executive summary

- The EIOPA report on preliminary results provides a good and useful overview of the relevant issues of the valuation of a Holistic Balance Sheet (HBS);
- EIOPA puts forward many disclaimers to the reliability of the outcomes of this first QIS. It is not possible to come up with an appropriate proposal for quantitative requirements (Pillar 1) based on this QIS;
- From the beginning the OPSG has had doubts if the Holistic Balance Sheet approach could be a useful tool for pension fund supervision. After this QIS, there are much more doubts if it will be possible to use the HBS as supervisory tool;
- More studies are necessary in order to improve the valuation of the HBS and to test what would be the appropriate place of the HBS in a future European supervisory framework, if at all;
- EIOPA and the European Commission should come up with a clear timetable – with sufficient (time for) interaction with stakeholders to improve the outcomes – for these future studies. It should be made clear what the (final) goals are of these studies.

EIOPA OCCUPATIONAL PENSIONS STAKEHOLDER GROUP

OPSG FEEDBACK STATEMENT TO EIOPA “QIS ON IORPs – PRELIMINARY RESULTS FOR THE EUROPEAN COMMISSION” – MAY 2013

1. General remarks

The OPSG welcomes the publication of EIOPA’s report “*QIS on IORPs - Preliminary Results for the European Commission*” (EIOPA-BOS-13/021). This document provides the preliminary results of the quantitative impact study (QIS) conducted by EIOPA on Institutions for Occupational Retirement Provision (IORPs). Central element of this QIS was the valuation of the so-called Holistic Balance Sheet (HBS). EIOPA intends to publish the final report in mid-2013.

The publication of the preliminary results of the QIS enables the OPSG to provide some feedback to EIOPA for the final report. In paragraph 2 of this reaction, the OPSG comes up with some concrete suggestions for the final report. The OPSG would like to record its appreciation to this well written report. It provides a good and useful overview of the relevant issues of the valuation of a HBS and the report contributes to a more fact based discussion on the quantitative aspects of the revision of the IORP Directive across Europe.

The proposed Holistic Balance Sheet approach is not only a new kind of framework, but also highly complex. Not surprisingly, EIOPA mentions – justly – a lot of disclaimers to the reliability of the outcomes of this first QIS and highlights the preliminary nature of the QIS results. IORPs may have used different assumptions, interpretations and simplifications and the outcomes also show substantial variation between participating countries as a result of differences in assumptions. Therefore, there cannot be an appropriate comparability of results of IORPs between and within different Member States. EIOPA also concludes that this QIS cannot be considered a full assessment of a comprehensive supervisory framework and therefore the real impact cannot be measured. Furthermore, EIOPA puts forward that some significant issues have not been resolved yet (sponsor support, valuation of long-term guarantees, valuation of discretionary benefits, other confidence levels than 99.5%).

The OPSG recognises and underpins these comments, which were also mentioned in the OPSG responses to the consultations of the Call for Advice and the Technical Specifications of the QIS (EIOPA_OPSPG_12_08). From the beginning the OPSG has had doubts if the HBS approach could be a useful tool for pension fund supervision. After this QIS, these doubts are intensified. It will be very difficult to achieve the aim of the European Commission to come up with a common level of security for all IORPs.

After reading the report on the preliminary QIS results, the OPSG concludes that it will not be possible to come up with an appropriate proposal for quantitative requirements (Pillar 1) based on this QIS. As EIOPA clearly states in the draft report, this QIS is not a complete assessment of the HBS approach. More QISs will be necessary in order to complete the assessment of the practicability and feasibility of the HBS and to identify what would be the appropriate place of the HBS in a future European framework, if at all. Independent from the question whether the HBS is technical feasible and desirable, EIOPA has also stated that ‘further information is needed in the feasibility of a common level of security and its effectiveness in terms of costs and benefits’. The OPSG advises to make such an assessment after more research (for instance a second QIS) and to leave open the question whether the HBS should be implemented at all.

EIOPA OCCUPATIONAL PENSIONS STAKEHOLDER GROUP

OPSG FEEDBACK STATEMENT TO EIOPA "QIS ON IORPs – PRELIMINARY RESULTS FOR THE EUROPEAN COMMISSION" – MAY 2013

EIOPA has an important task to come up with an adequate final report on the QIS and further advices with respect to the revision of the IORP Directive. The OPSG is ready and willing to be engaged in these technical exercises. The OPSG would like to contribute to further research (e.g. valuation of sponsor support) and QISs in order to test and to improve the HBS approach. In paragraph 3, the OPSG gives some recommendations for the next steps which could be taken after this first QIS. The possibility should not be ruled out that the final conclusion will be that the practicability and feasibility of the HBS approach will be insufficient and there will not be an appropriate place of the HBS in a future European framework or that the HBS will not be used for capital requirement (Pillar 1), but possibly only in Pillars 2/3.

2. Recommendations for final report

The background, the process and the results of the QIS are well described in the report. In order to improve the understanding of the report, the OPSG suggests to add more explanation (and education) of the results. We need a better understanding of what is calculated and what are the main drivers behind the differences in and between Member States. This is essential information for answering the question what will be the appropriate place – if any – of the HBS in a potential harmonised and unified solvency regime for IORPs. Furthermore, the OPSG has some general suggestions to provide more guidance to stakeholders, which enables them to have a better overview and understanding.

More explanation and education

- The draft paper gives many explanations for outcomes. It would be helpful to have general overview of the biggest factors impacting a possible transition of the current regime to the HBS, preferably be decomposing this transition. The OPSG could imagine that that overview will show the impact of switching to market consistent valuation, the value of steering and adjustment mechanisms in the HBS, the gross SCR and the impact of the steering and adjustment mechanisms on the net SCR;
- In the draft report it is stated that IORPs may have used different assumptions, interpretations and simplifications in the QIS. It would be helpful to map the most important differences and provide insight what the impact is of these different assumptions (also to improve the comparability and transparency of the results);
- There could be more explanation what the main drivers are of the differences between the current regimes and the three scenarios. The differences are currently shown by the figures and graphs, which are quite clear. There could be more attention for the explanation and interpretation of these figures;
- There could be more insight in the differences in the value of sponsor support and the maximum value of sponsor support. There are large differences between different Member States (see table). It would be helpful to have more explanatory text on the reasons of these differences.

EIOPA OCCUPATIONAL PENSIONS STAKEHOLDER GROUP

OPSG FEEDBACK STATEMENT TO EIOPA "QIS ON IORPs – PRELIMINARY RESULTS FOR THE EUROPEAN COMMISSION" – MAY 2013

	BE	DE PF	DE PK	IE	NL	NO	SE	UK
Pension protection scheme	0	2	0	0	0	0	0	1
Sponsor support	1	20	16	0	8	0	2	31
Maximum value of sponsor support	550	820	290	0	57	0	28	127

- More attention could be given to benefit reduction:
 - In Germany benefit reduction is part of conditional benefits, but it is not clear what the level of the benefit reduction is within the conditional benefits;
 - Substantiation should be given why benefit reduction is not taken into account in UK;
 - In the Netherlands, IORPs took benefit reduction into account, but these values were not shown in the report. The exclusion of benefit reduction has an impact on the value of other adjustment and security mechanisms, but this is not taken in to account. It would be helpful if EIOPA would provide information on the impact on the other adjustment and security mechanisms.
- It is desirable to also present the figures on the gross SCR and compare these numbers with the net SCR. This is especially relevant for other confidence levels than 99.5%;
- Comparability of the decomposition of asset mix could be improved by a split-up between fixed income instruments and non-fixed income instruments and include a better explanation/description of "other equities" and "other bonds".

General suggestions:

- Add an executive summary;
- Add a roadmap for the follow-up: which steps should be taken according to EIOPA after this QIS;
- Add opinion/feedback of EIOPA on feedback given by IORPs in the qualitative questionnaire;
- Some National Supervisory Authorities might come up with an own report on the QIS. There could be a reference to the(se) report(s).

If EIOPA will not be able to honour all OPSG requests within the remaining time until the delivery of the final report, the OPSG suggests to table further research that EIOPA wants to deliver based on OPSG's and other suggestions.

3. Next steps after the first QIS

The report on preliminary results clearly shows that more studies are necessary. The OPSG suggests that EIOPA comes up with a planning with appropriate timelines. This planning should include which steps should be taken in the future and, preferably, at what moment in time. According to the OPSG there are additional studies necessary on the following four issues:

1. Clearer definition and better understanding of discretionary benefits and benefit reductions;
2. Technical issues (improve valuation of the HBS);

EIOPA OCCUPATIONAL PENSIONS STAKEHOLDER GROUP

OPSG FEEDBACK STATEMENT TO EIOPA "QIS ON IORPs – PRELIMINARY RESULTS FOR THE EUROPEAN COMMISSION" – MAY 2013

3. Supervisory issues (how could and should the HBS be used);
4. Fundamental issues (also related to the current economic and financial situation).

An adequate planning and coherence between these studies is necessary, also because there will be an interaction among elements out of the different studies: a holistic approach is desirable. EIOPA and the European Commission should prevent that the burden of doing these studies will be too high for IORPs (e.g. not at the same moment different kind of studies). If any further quantitative modelling arises from this work, the process must allow adequate time for all concerned to understand and explore these important issues before technical specifications are finalised.

3.1. Clearer definition of benefits

It is clear from the preliminary report that there are differences among Member States about the definition and treatment of important issues, especially discretionary benefits and benefit reductions. It is understandable that these differences can arise given historic and social differences in pension practice in different countries. It is also understandable that the differences might not emerge fully until a QIS/further research is actually undertaken.

Nonetheless, comparable results cannot be produced unless there is a common understanding and definition for the different approaches. EIOPA must explore further these problems and agree a common basis for comparability and description.

3.2. Technical issues

As mentioned by EIOPA, there are still some important issues which need to be resolved¹ or where further work is needed². According to the OPSG, new consultations on technical specifications could contribute to solve these issues and so to improve the valuation of the HBS. These technical consultations could contribute to more harmonisation or convergence of assumptions, interpretations and models between and within Member States.

For these consultations and future QISs an appropriate timetable is recommended (in too many EIOPA reports there is the remark that the timetable was too tight). The quality and breadth of the responses will improve with an appropriate timetable giving stakeholders more time which will improve their responses, and consequently also the quality of the final outcome. More time for QISs will contribute to more and better involvement of stakeholders. At first sight it might seem that more interaction between stakeholders, EIOPA and National Supervisory Authorities could lead to a loss of time, but it could end up with a shorter time period and an improvement of the quality. EIOPA and the European Commission will benefit from better and more cooperation between IORPs, National Supervisory Authorities and EIOPA. This could contribute to the harmonisation and/or give an impression of the difficulties to come to a harmonisation of the level of security for IORPs.

¹ Supervisory framework, multi-employer IORPs and expenses borne by employers (Section I.5.12 of EIOPA's revised draft technical specifications (EIOPA, Draft Technical Specification QIS of EIOPA's Advice on the Review of the IORP Directive, EIOPA BOS) 12/085, 2 October 2012, Frankfurt).

² Sponsor support, pension protection schemes, confidence levels other than 99.5%, parameters and correlation matrices, MCR, Long-term guarantees, risk margin, pension scheme / contract boundaries, segmentation of pension obligations, discretionary benefits, level B expected returns, inflation and proportionality (Section I.5.13 of EIOPA's revised draft technical specifications (EIOPA, Draft Technical Specification QIS of EIOPA's Advice on the Review of the IORP Directive, EIOPA BOS) 12/085, 2 October 2012, Frankfurt).

EIOPA OCCUPATIONAL PENSIONS STAKEHOLDER GROUP

OPSG FEEDBACK STATEMENT TO EIOPA "QIS ON IORPs – PRELIMINARY RESULTS FOR THE EUROPEAN COMMISSION" – MAY 2013

At the same time the OPSG would like to remark that timely clarity on the usability of the HBS concept is warranted to reduce the uncertainty for employers and social partners in offering pensions. In many situations they are currently hesitant to offer new forms of occupational pensions or to change the current pensions since the outcome of the IORP revision and the introduction of the HBS is unclear. A too long process of revision could be very detrimental for occupational pensions. Another disadvantage of an intensive process is that the costs of further QISs and consultations/research will become a financial burden.

In general, the OPSG would like to state that more (intense) interaction between the European Commission, EIOPA, National Supervisory Authorities and other stakeholders will be beneficial for all. The OPSGs welcomes that EIOPA plans to have a public meeting on the final QIS report and invites the Commission and EIOPA to seek for more involvement of stakeholders.

3.3. Supervisory framework

In addition to the question if it is possible to have a meaningful valuation of the HBS, also the question how the HBS could be used as supervisory tool needs to be answered. What would be the appropriate place of the HBS in a future European framework? How could a supervisory regime look like?

The European Commission is primary responsible for coming up with proposals for the supervisory framework. It will be useful if the European Commission will test timely if – and how – the HBS approach can be used as supervisory tool. This in order to prevent a lot of possibly unnecessary QISs and consultations (to solve the technical issues), if the conclusion would be that the HBS approach is not suitable as supervisory tool. Assessments to test the supervisory framework, should also test what the possible impact of a revised IORP Directive is on the policy of IORPs (change of asset allocation, other set up of financial policy, etc.). This because changes of the policy of an IORP will also affect the valuation of the HBS again.

3.4. Fundamental issues

The principles out of the technical specifications of the methodology which are used in the QIS are most of the time directly coming from the Solvency II framework. It could be questioned if some of the fundamental principles are still adequate and relevant. The underlying principles are based on highly price efficient markets, normal distribution curves and stable correlations. The events of the last few years have shaken confidence in these assumptions. Furthermore, there is an on-going discussion on how long-term pension liabilities should be valued: what is an appropriate balance between market-based valuation, stability and countercyclicality? In different Member States, this is currently discussed and even within Solvency II there is not (yet) a consensus how to discount long term guarantees. Also the question could be raised how suitable a one-year horizon confidence level is for (very) long-term obligations. A debate about the underlying fundamental principles of the HBS is recommendable.

Furthermore, the OPSG would like to highlight that the revision of the IORP Directive should be seen in a broader perspective. Especially, there should be attention for the (unintended) consequences that a revision of the IORP could have on Long Term Investing. Recently, the European Commission published a Green Paper on Long Term Investing. The OPSG advises to have an integrated assessment in order to investigate the impact of a revised IORP Directive on Long Term Investing.

EIOPA OCCUPATIONAL PENSIONS STAKEHOLDER GROUP

OPSG FEEDBACK STATEMENT TO EIOPA "QIS ON IORPs – PRELIMINARY RESULTS FOR THE EUROPEAN COMMISSION" – MAY 2013

Finally, in OPSG's response to the consultations of the Call for Advice and the Technical Specifications of the QIS, the OPSG suggested that alternatives to the HBS could be considered not targeting full harmonisation but still using a holistic framework (EIOPA_OPSPG_12_08). Such a holistic framework could still take into account the steering and adjustment mechanisms, but leave freedom to National Supervisory Authorities to calibrate the system with a view on the national practices.

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Adopted by the EIOPA Occupational Pensions Stakeholder Group at Frankfurt am Main, 17 May 2013.

The Chairperson of the EIOPA Occupational Pensions Stakeholder Group

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