



EIOPA-OPSG-15.01  
13 January 2015

**OPSG opinion**

**Input to EIOPA Consultation Paper on  
Further Work on Solvency of IORPs**

**EIOPA-CP-14-040**

## **1. General Remarks**

The OPSG has considered the consultation paper, prepared at its own initiative by EIOPA, which poses 111 questions on the possible use of the Holistic Balance Sheet (HBS), and detailed issues regarding the valuation of items which may be included in the HBS. A number of the issues considered were raised during the previous consultation and QIS, and the OPSG welcomes the further research undertaken and the additional policy options now being considered.

The OPSG considers that the most important section is that dealing with the possible uses of the HBS, and the related questions 72 to 98. The key points which the OPSG makes in response to these questions are

- I. The HBS cannot be used in Pillar 1 to set capital requirements or technical provisions or to determine the length of recovery periods in cases of "underfunding"
- II. The HBS could be a useful tool for risk management under Pillar 2
- III. The HBS could provide useful information for members and beneficiaries on the security of the pension promise but this would have to be presented in a meaningful way.

The OPSG is of the view that if an HBS is to be constructed, the technical provisions to be covered by financial assets (Q85) should in general be determined by reference to the expected return on assets (Level B) rather than by using a risk free rate (Level A). The OPSG considers that if Level A technical provisions were imposed on an EU wide basis, there would be a significant impact on existing "contractual agreements" in many Member States (Q97) and that lengthy transitional periods, and/or grandfathering provisions, would be necessary in this scenario (Q98).

The OPSG is supportive of proposals that the approach to valuation of elements of the HBS, and its use, should be at the option of Member States, subject where appropriate to overarching UE principles (e.g. Q37 and 46 re sponsor support). This would enable the specificities of IORPs in different member states, and the relevant national social and labour law to be appropriately taken into account.

The OPSG is also strongly of the view that the proportionality principle must be applied where possible, especially given the high number of small and medium sized IORPs in the EU, for whom lengthy and complex calculations would impose an excessive burden. Simplifications should also be permitted where possible and appropriate e.g. by treating sponsor support and/or pension protection schemes as balancing items (Q39 and 71).

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Note: This input was developed by the OPSG Occupational Pensions Stakeholder Subgroup on "Solvency Issues" in line with mandate approved at 07/07/2014 OPSG meeting: [https://eiopa.europa.eu/Publications/Meetings/20140718-EIOPA-OPSG-14-01\\_OPSG\\_Subgroup\\_Solvency\\_issues\\_Mandate-cl.pdf](https://eiopa.europa.eu/Publications/Meetings/20140718-EIOPA-OPSG-14-01_OPSG_Subgroup_Solvency_issues_Mandate-cl.pdf)

## 2. Contract boundaries

*Q1: Do stakeholders think that the word “contract” is an adequate description of the characteristics of the set of rules and arrangements governing the provision of benefits to members and beneficiaries by an IORP?*

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Contract is not an adequate description for IORPs. There is not, in general, a legal "contract" between a member or beneficiary of an IORP and the IORP itself, nor in trust based jurisdictions, between the trustees and fiduciaries of the IORP and the members and beneficiaries: an employee of a company is required to, or has the right to, become a member of an IORP sponsored by that company as a consequence of either an individual or collective contractual agreement with their employer. In some jurisdictions that contractual right is then expressed as subject to the rules of the IORP, and the contract therefore includes a right to terminate or amend the benefit promise. In a trust based jurisdiction the trust deed and rules rather than the contract will establish the employee's entitlement if he or she joins the IORP, and the entitlement is enforceable against the trust and not necessarily against the employer. Accordingly, the OPSG does not think that the word "contract" is adequate or appropriate in the context of an IORP.

*Q2: Do stakeholders think that the word “boundary” is suitable here?*

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The term "contract boundary" has been taken from Solvency II for (re)insurance undertakings, and the reason for its use in this context has been clearly explained in 4.13 to 4.20. An IORP takes on additional risks as members accrue additional benefits and does not usually have the unilateral right to terminate the accrual of benefits or the payment of contributions to finance those benefits. However, where the financing of those future benefits is subject to ongoing review, so that the additional risks to be taken on will be met by the contributions to be received, or alternatively the sponsoring employer can exercise its right to terminate accrual of benefits (having where appropriate consulted and agreed with employees/employee representatives), there is no need to calculate technical provisions in respect of these future benefits as such technical provisions would be fully covered by the contributions receivable. Technical provisions should be established in respect of benefits accrued up to the current date, and in some jurisdictions there is also legal and statutory protection in place for benefits accrued up to the current date, which might therefore be considered the "boundary". However, the OPSG does not consider this term to be meaningful in this context.

*Q3: If not, please provide an expression more suitable for IORPs which could replace the expression “contract boundaries”.*

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The OPSG suggests that the Directive requires that technical provisions be established for benefits accrued up to the date of the holistic balance sheet (HBS), but not after that date, except where no party has the unilateral right either to terminate the accrual of benefits or to adjust the level of contributions paid into the future. The legal protection given to the accrued rights of members is often determined by reference to benefits earned before the date of any proposed change or termination, and so it should not be assumed that rights to accrual of benefits and payment of contributions continue on the basis applicable as at that date. In cases where no party has the right to adjust future contributions, technical provisions should be established in respect of all benefits due to be accrued by existing members up to their expected retirement date, and the present value of future contributions due over that period should be accounted for as an asset in the HBS.

### *Q4: Do stakeholders have any general comments on the above section?*

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The OPSG notes that if Solvency II were to be applied without amendment, this would imply that all future cashflows would be recognised in technical provisions, except in NL which currently is the only MS where the IORP itself has a unilateral right to terminate. This would not be appropriate as it is recognised in 4.26 that an IORP is a vehicle used to provide benefits as determined by others i.e. social partners. In the UK for example the sponsoring employer, occasionally the trustees, sometimes both sponsoring employer and trustees jointly, may have rights of termination.

*Q5: Do stakeholders think that unilateral rights (or obligations) of an IORP to terminate the contract/agreement/promise or reject additional contributions to the contract/agreement/promise or modify the promise in a way that contributions fully reflect the risk should be the basis for a definition of contract boundaries for IORPs? Are there cases where such rights (or obligations) should be the basis for a definition of contract boundaries for IORPs even though they are not unilateral rights (or obligations) of the IORP, but can be exercised unilaterally or jointly by other parties (possibly together with the IORP)?*

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As noted above, this would apply in only one MS. It would therefore seem more appropriate to recognise cashflows only in respect of benefits accrued to date where some entity/person or combination of parties i.e. the IORP, the social partners (or the employer acting unilaterally) can terminate or amend the future accrual of benefits.

*Q6: Do stakeholders agree with the analysis above of the different ways of liabilities of IORPs arising?*

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Along with the two ways described, the OPSG notes that liabilities can also arise from the single event of a person becoming a member of an IORP (e.g. if, immediately on joining, a member is entitled to a lump sum or dependant's pension should they die while a member, and the formula determining this lump sum or pension is independent of the member's length of service). Such benefits do not "build up due to continued service of the member", but the OPSG assumes that it was intended that the liabilities due to these benefits would come under this description 4.30.ii. The OPSG therefore suggests that the wording of this section is modified to make this explicit (or explicitly rule out such liabilities, if that is the intention).

The OPSG notes that the definition proposed in 4.33 is intended to apply where the IORP does not have a unilateral right to cease or modify benefits and that the promise be recognised "on an ongoing basis" which the footnote explains means that the promise to pay benefits continues to exist as at the valuation date. The OPSG interprets this as meaning that unless the other parties who have a right to terminate/amend the benefits have done so by the valuation date, it should be assumed that accrual of benefits and payment of contributions continues on the basis applicable as at that date. If this is a correct interpretation, the OPSG would not agree with this approach as outlined above. Making this assumption would render meaningless the key powers retained to parties within trust or contract, to amend or terminate future accrual for reasons of affordability.

***Q7: Do stakeholders think that there should be a distinction between incoming cash-flows which are considered as “regular contributions” to finance (the accrual of) benefits on the one hand and sponsor support on the other hand? What is the view of stakeholders regarding the practicality of such a distinction?***

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Yes. There may be practical difficulties identifying the difference between the two types of contributions in some circumstances e.g. where contributions are determined on a smoothed basis (as for example in the Netherlands). More generally, the distinction would depend on the assumption basis used to value the liabilities so it would be possible for the same future contribution cashflows to be split differently depending on the basis used to value the accrued liabilities.

***Q8: Do stakeholders agree, that, if there was a distinction as described in question Q7, “regular contributions” should be recognised in technical provisions while sponsor support should be treated separately?***

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No. For the avoidance of doubt, the OPSG is taking "regular contributions" to mean those required to finance the ongoing accrual of benefits and not contributions (which may be regular in the normal meaning of the word) due to be paid in the future to amortize a deficit or surplus arising on past service. In this case (assuming the contract boundary relates to past service), the OPSG would envisage that future “regular contributions” would relate to benefits that are outside the contract boundary, and therefore they should not be recognised in the HBS. The OPSG would agree that the present value of the future promised contributions that are not to fund accrual of future benefits (but are based on the current funding position of the IORP) should be treated as sponsor support. The OPSG notes that the part of future contributions calculated to fund risk benefits (i.e. those benefits that do not accrue due to contributions paid or continued member service) would here be treated as “regular contributions” and so be excluded from the technical provisions.

***Q9: Do stakeholders agree that payments by the IORP to the sponsor related to a surplus of the IORP (in case such payments are allowed for in the scheme) should not be recognised in technical provisions of the IORP? If not, how/where should they be recognized/presented in the holistic balance sheet?***

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Yes, the OPSG agrees that the present value of potential future payments from the IORP to the sponsor should not be included in the technical provisions. The OPSG suggests they should be shown either as a reduction of sponsor support in the assets, provided the value of the refunds to the sponsor is smaller than the value of the sponsor support or separately on the HBS as a claim on the IORP and therefore as a (conditional) liability. A refund of surplus to the employer is very unlikely to arise in practice and may not be permitted under the rules of the IORP or by legislation in any case.

***Q10: Are stakeholders aware of cases in which there would be an obligation of the IORP to pay out benefits without having received any contributions/payments to finance those benefits (e.g. because the obligation is constituted by social and labour law)? If yes, please describe.***

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In the Netherlands, this can be the case for industry-wide IORPs (e.g. in the case of bankruptcy of one of the (many) sponsors). In those cases the IORP has not received contributions or has received only part of the contributions whilst the pension obligation to the employees remains.

In Sweden, there could be situations where there are payments from an IORP, even if the employer has gone bankrupt or not paid contributions, due to labour organisations/guarantees.

If legislation is brought in to modify accrued benefits to increase them in a way that had not been financed for, or in the case of administrative error or fraud, the answer could also be “yes”. The OPSG would consider these as future risks to the ability of the IORP to pay benefits as they fall due, rather than to be accounted for within the technical provisions. It is of course the case that IORPs frequently pay out benefits where there is insufficient payment received to continue to finance the same benefits going forward, which reiterates the points made above about the contract boundaries.

Unanticipated cases may indeed occur, since the pension promise is influenced by social legislation. For example, gender or age equality requirements may direct or indirect repercussions on the benefits originally envisaged and provided for in the initial financing plan.

***Q11: Do stakeholders believe that the contract boundaries could be defined based on future benefit payments rather than contribution or premiums?***

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Yes, as per our answer to question 5, the OPSG would define the contract boundary as the future cashflows only in respect of benefits accrued to date where some entity/person or combination of parties i.e. the IORP, the social partners (or the employer acting unilaterally) can terminate or amend the future accrual of benefits.

***Q12: Do stakeholders have any general comments on the above section?***

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No.

***Q13: Do stakeholders have any general comments on the above section?***

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If consistency is to be achieved across all IORPs in determining whether surplus is potentially payable to the sponsor (and so included as negative sponsor support) or as surplus participation to the members (and so included as extra technical provisions), the OPSG feels that further direction is needed in this area than is given in this section.

***Q14: Do stakeholders think that the above definition of contract boundaries for IORPs is in line with the general idea that cash-flows should be recognised if and only if they lead to risks building up in the IORP as described in section 4.2.4 (all those cash-flows should be in technical provisions; no cash-flows where all risks could be avoided should be in technical provisions)?***

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While the OPSG has reservations about the use of the term “contract boundaries” for IORPs (see answers to questions 1, 2 & 3), the definition is helpful in clarifying the cashflows that should be included, and the principle that they should only be recognised if they lead to unalterable risk.

***Q15: In case more/higher cash-flows than appropriate (compared with the general idea) are included in technical provisions according to this definition, how should the definition be amended to exclude them?***

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One key item missing from the definition is the reference to the unilateral right of the sponsor which is frequently the case, (e. g. Ireland) and less frequently the unilateral right of trustees (there are

some UK examples) to terminate the accrual of benefits. The OPSG suggests that this point be captured in 2d.

In Germany 1) the sponsoring employer is entitled to stop at any time the contributions to a Pensionskasse or Pensionsfonds in the case that he decides to replace these "financing vehicles" and to deliver future benefits within the pension promise via a direct pension pledge or a support fund or terminate the pension plan as such, with the latter having some legal restrictions; 2) the Pensionskasse will be entitled to adjust for future contributions the benefit level being provided; for example to use more conservative interest rates or biometric tables.

In Sweden, the sponsoring employer can, under some circumstances, change/terminate accrual of benefits/adjust future contributions.

*Q16: In case not all cash-flows which lead to risk building up in the IORP, as explained in section 4.2.4, are included, with which wording could they be included?*

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The OPSG suggests these be covered in the first sentence of 2. by inserting "(unless they do not lead to risk building up in the IORP)" after "dates".

*Q17: Is the wording of the definition appropriate for IORPs?*

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The OPSG believes the wording should be extended to at least capture the unilateral right of the sponsor and/or other parties. As mentioned in our answer to question 3, our preference is that the Directive requires that technical provisions be established for benefits accrued up to the date of the holistic balance sheet (HBS), but not after that date, except where no party has the right to terminate the accrual of benefits or to adjust the level of contributions paid into the future. In this latter case, technical provisions should be established in respect of all benefits due to be accrued by existing members up to their expected retirement date, and the present value of future contributions due over that period should be accounted for as an asset in the HBS. Termination in some countries (e.g.UK) is also not the same necessarily as winding up the IORP, and it may be necessary to make it clearer in the text that termination means termination of accrual of future benefits, not necessarily termination of the IORP.

*Q18: Is it necessary to have both 2. a. and b. in the above definition, or could a. be restricted to cases where a termination of the agreement leads to a stop of additional contributions and/or the repayment of contributions received/payment of a surrender value (and then maybe a. and b. could be combined)?*

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It would be preferable if 2. a. and b. were combined. In any event 2.a. should also include IORP (and sponsor) rights to terminate or amend the agreement with the plan members to provide the pension benefits e.g. Germany, Ireland, UK. Amendment rather than termination is frequently used to reduce future accrual.

*Q19: Are there additional rights of the IORP or another party (unilateral or not) which should be considered in the definition (see section 4.2.4)?*

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As mentioned earlier, the main item missing is the unilateral right of the sponsor, or the unilateral right of trustees, or their joint exercise of the power to terminate. There may be instances where the rights of other interested parties may be relevant i.e. regulator, social partners.

*Q20: Is it clear from the proposed wording of the definition that in principle not only benefits (out-going cash-flows), but also contributions (incoming cash-flows) have to be recognized in technical provisions?*

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Yes. However, it would be helpful to clarify this point (where relevant) as technical provisions are associated more with out-going cash-flows.

*Q21: Are the cases described in parts a) and b) of the definition clearly distinguishable in practice?*

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Yes.

*Q22: Are the conditions mentioned above for making unilateral rights of the sponsor part of the definition of contract boundaries sufficient, or should further conditions be included? How could those rights and conditions be merged into the proposed definition of contract boundaries?*

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The OPSG believes the conditions are sufficient and suggests they are captured in 2d. by specifying that where the sponsor (or other party) has the unilateral right to cease payment or accrual of benefits, then future accrual and contributions need not be recognised.

*Q23: Do stakeholders agree that the proposed adapted definition of contract boundaries for IORPs (above) leads to the results described in this section? If not, please explain.*

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Yes.

Example 8 is closest to the typical situation in UK and Ireland and it would be the sponsor acting unilaterally or acting with the IORP that would most likely terminate the contract.

### **3. Discretionary decision-making processes**

*Q24: Do stakeholders consider the above definitions workable? If not, please explain why not and how you would suggest to improve the definition(s).*

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The definitions are a bit confused and should be set out in much clearer language. The OPSG suggests a simpler message e.g.:

1. IORPs can provide for discretionary benefits. The conditions for awarding these may be:
  - a. Funding permits i.e. there are sufficient reserves to award say a pension increase where the rules specifically allow for this
  - b. Rules provide that in a certain event the fiduciary exercises discretion on how or to whom benefits are paid – for example on the death of a member.
  - c. Discretion that is allowed but requires an augmentation of benefits (which may require financing). In these circumstances the fiduciary pays a defined benefit at its discretion.
  - d. Precedent / custom and practice. As these are not provided by the rules the awarding of these benefits should always include an augmentation payment to finance these additional benefits.



- e. Surplus sharing should be possible but only if the rules permit. It should not be used through collective bargaining arrangements outside of the IORP.
2. Where overall funding of the IORP is in deficit, no discretionary benefits may be awarded.
3. Discretionary decision making process should only be a consideration where the IORP is in surplus. Where used to bring the IORP into surplus (by reducing benefits) then this should require local regulatory approval.

### *Q25: Do stakeholders have any general comments on the above section?*

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Our general comments are:

1. The IORP rules should specify the nature of the benefits.
2. Where the benefit is known but the recipient is not (in the event of death distributions) then technical provisions should be established in respect of the expected cashflows.
3. Where the benefit is conditional on funding then the IORP will need to have an agreed policy. If that policy is that, say, pensions will increase by inflation then technical provisions should be established in respect of the expected cashflows and benefits only provided if the funding position permits.
4. Once benefits have been awarded then they have to be reserved for as they cannot be assumed to be discretionary in the future.

Care needs to be taken to ensure that where benefits are conditional on funding e.g. in Netherlands, the process does not become circular by requiring additional funding which in turn may require additional conditional benefits to be provided.

### *Q26: Would it be possible, in the views of stakeholders, to properly quantify the relation between the funding position of the IORP and elements of discretionary decision-making (the pattern) in order to take the pattern into account in the valuation process? If so, how?*

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The OPSG believes that the following framework would address the issue.

1. The IORP rules should specify the nature of the benefits.
2. Where the benefit is known but the recipient is not (in the event of death distributions) then technical provisions should be established in respect of the expected cashflows.
3. Where the benefit is conditional on funding then the IORP will need to have an agreed policy. If that policy is that, say, pensions will increase by inflation then technical provisions should be established in respect of the expected cashflows and benefits only provided if the funding position permits.
4. Once benefits have been awarded then they have to be reserved for as they cannot be assumed to be discretionary in the future.

Care needs to be taken to ensure that where benefits are conditional on funding e.g. in Netherlands, the process does not become circular by requiring additional funding which in turn may require additional conditional benefits to be provided.

Discretionary powers and decision making should be considered separately. The discretionary power is defined in the rules of the IOPRP and sets out what can or will happen. The decision making process is then:

1. Does the IORP have to provide this benefit? – if so then the benefit must be reserved for and paid when it is due
2. If the IORP does not have to provide the benefit then it comes down to
  - a. Is there a surplus? – if yes then it can be provided (without additional financing)
  - b. Is there a deficit? – then either the IORP is brought up to 100% funding or the benefit is not provided

*Q27: Do stakeholders agree that IORPs need to produce a best estimate of expected future payments (under different scenarios), if pure discretionary benefits were to be recognised in a holistic balance sheet? If not, what alternative would you suggest?*

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The OPSG notes that EIOPA expresses the opinion in paragraph 5.56 that pure discretionary benefits should not be included in an IORPs balance sheet. The OPSG agrees in principle with this view as pure discretionary benefits cannot be considered part of the pension promise and in any event it would be difficult to establish a best estimate of the future cashflows where there is no defined basis on which the discretion might be exercised in future.

*Q28: Do stakeholders agree that IORPs need to produce a best estimate of expected future payments (under different scenarios), if mixed benefits were to be recognised in a holistic balance sheet? If not, what alternative would you suggest?*

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The OPSG agrees. This should follow the IORP's policy on the mixed benefit. If there is a policy or intention to provide these benefits (even if not strictly required), they should be reserved for.

It is also important to establish a process in relation to the awarding of these benefits. They should not be awarded if the IORP is in deficit at the time. To do otherwise would reduce funding ratios and put a greater strain on the sponsor.

*Q29: Do stakeholders agree that IORPs need to produce a best estimate of expected future sponsor payments (under different scenarios), if non-legally enforceable sponsor support was to be included on the holistic balance sheet? If not, what alternative would you suggest?*

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If non-legally enforceable sponsor support was to be included on the holistic balance sheet, the IORP does need to produce a best estimate of future contributions and these should be agreed in a schedule as part of the valuation process or recovery plan. Where this is the case then the full value of these contributions should be included in the HBS, perhaps with some adjustment to reflect whether these would be obtainable in an insolvency situation. An agreement to pay should be sufficient to include in the HBS.

*Q30: Do stakeholders agree that these are the two options for valuing off-balance capital instruments? If not, what alternative options would you suggest?*

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Yes.

*Q31: Which option do you support? Please explain why you support this option.*

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The OPSG prefers option 4.80 as:

1. It focuses on situations where there is a loss which needs to be managed.
2. It has a cash flow value.

*Q32: Do stakeholders agree that surplus funds should be valued for their nominal value? If not, how would you suggest to value surplus funds?*

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The OPSG agrees with the proposal.

*Q33: Do stakeholders agree that these are the three options for valuing subordinated loans? If not, what alternative options would you suggest?*

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Surplus funds are part of an IORP's own funds and should therefore be accounted for by their nominal value. A discussion about further valuation options is thus not required.

*Q34: Which option do you support? Please explain why you support this option.*

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Option 3 is the preferred option as it is realistic and allows for changes in the funded position.

#### 4. Benefit reduction mechanisms

*Q35: Do stakeholders agree with these two approaches to valuing benefit reduction mechanisms? If not, what alternatives or amendments would you suggest?*

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The balancing item approach would seem to be the most practical approach to adopt for ex-post reductions and reductions in case of sponsor default. The extent of the reduction required to make the HBS balance, having taken all other mechanisms into account, should be determined and compared with the maximum amount permitted, if any limit exists. This information would enable the IORP or supervisor to form a view on what steps to take.

For ex-ante reduction mechanisms where the extent of the reduction can be determined precisely depending on the circumstances, a direct approach may be more appropriate, although it would still be desirable to identify separately the impact on the HBS of the reductions anticipated.

Careful consideration should be given in both cases as to how the information should be communicated to members and beneficiaries.

#### 5. Legally enforceable sponsor support

*Q36: Do stakeholders agree that at the EU level, there should only be a principle based approach to valuing sponsor support with the specifics being left to member states/supervisors and/or IORPs?*

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Characteristics of IORPs can differ a lot from one Member State (MS) to another.

For example, differences exist in the following areas:

- Size
- Legal structure
- Governance

- Parties involved in the day-to-day management

Inside one MS, different IORPs exist. For example:

- IORP with 1 sponsor
- IORP with several sponsors, belonging to the same group or not, with solidarity between sponsors or not
- 1 sponsor with several IORPs

Also, on the sponsor's side, differences are present. For example:

- Multinational companies
- Rated companies
- Unrated companies
- Not-for-profit organizations

Because of all these specificities, it seems difficult to capture sponsor support in one single formula all over the EU. The logical step is then to go for a principle based approach on EU level offering the opportunity to the Member States of adequately taking into account the national characteristics especially on the valuation of sponsor support.

Consequently, the OPSG believes that the specifics for the valuation of sponsor support should be left to the MS, i.e. to national supervisors in collaboration with IORPs. The national supervisors know their market and they also know the IORPs they are supervising, probably from the date of creation of the IORP. Apart probably from cross-border IORPs established by large multinational companies, the national supervisors also know the sponsoring companies and their obligations in relation to their IORP.

Any kind of "one size fits all"-approach in this area should be prevented. One guiding principle for the valuation of sponsor support should especially be the opportunity for IORPs to use the sponsor support as a balancing item where appropriate.

***Q37: Do stakeholders agree with the overarching principle that the valuation of sponsor support should be market consistent? If not, what principle(s) would you suggest?***

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The OPSG agrees with a principle based approach for the valuation of the sponsor support and in general with the market consistent approach as overarching principle. In this context, the OPSG would like to point out that EIOPA identified that "the balancing item approach would therefore render the market-consistent value of the element [being used to balance the HBS]"(page 10 EIOPA Consultation, part 4.3).

The OPSG however insists on the importance of the application of the proportionality principle in this area as well, and the use of the simplified approaches proposed means that in some cases the market consistent approach would not be applied.

***Q38: Do stakeholders agree that in order to achieve this market consistent valuation, the expected cash flows required by the IORP should be valued allowing for affordability and credit risk of the sponsor? If not, what approach(es) would you suggest?***

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The OPSG considers that a separate and explicit valuation of the sponsor support using expected cash flows is not necessary in cases when the balancing item approach is applicable, noting that EIOPA has identified that "the balancing item approach would therefore render the market-

consistent value of the element [being used to balance the HBS]" (page 10 EIOPA Consultation, part 4.3).

If the balancing item approach is not appropriate, the OPSG agrees with the allowance for affordability of the sponsor while valuing expected cash flows using the market consistent approach. Credit risk of the sponsor should be taken into account as well; however, default rates may not be available for all types of sponsors. Simplifications in this area could lead to inexact outcomes.

***Q39: What is the general view of stakeholders with regard to sponsor support as a balancing item?***

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The OPSG is of the view that the "sponsor support as a balancing item" should be the starting point of any valuation in the holistic framework because it is the most practical and feasible approach, as well as being compatible with the market consistent valuation, as identified by EIOPA.

Rules would have to determine in what cases this starting point could be accepted without any further valuation, based on the proportionality principle. For example, in the case where the sponsor support is less than M times the value of the sponsor (M to be defined).

***Q40: Which conditions should apply for sponsor support to be treated as a balancing item?***

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The OPSG supports the overall approach set out in paragraphs 4.115 to 4.133 to treating sponsor support as a balancing item. All conditions are legitimate in certain circumstances and should therefore equivalently be considered in the regulatory framework.

***Q41: Are there other cases beyond the cases mentioned above in which sponsor support could be treated as a balancing item?***

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One might consider that where the sponsor sets up a provision on the liability side of its balance sheet, this could be taken as equal to the sponsor support as a balancing item.

Currently some sponsors have the legal obligation to provide unlimited sponsor. However, this obligation is not always reflected in the sponsor's accounts. If, in the future, the IORP has to provide a Holistic Balance Sheet (HBS) to the national supervisor, with the amount of sponsor support clearly reflected, will this lead to pressure to include this figure in the accounts of the sponsor?

***Q42: Do stakeholders have a view as to what value of M would be appropriate?***

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More detailed analysis is required in order to establish an appropriate value for M. The OPSG is of the opinion that a figure lower than 2 should be acceptable e.g. 1.25.

***Q43: Do stakeholders think a pension protection scheme could in principle be considered as impacting on sponsor support to allow it to be a balancing item if it is considered financially strong and based on a sufficiently permanent and certain legal arrangement?***

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The OPSG believes that the existence of a Pension Protection Scheme (PPS) should be considered a sufficient condition to allow for sponsor support to be the balancing item on the HBS, if and only if all liabilities are recognised by the PPS. However, it seems to be even more appropriate to take into

account the existence of a PPS directly as a balancing item on the HBS, if and only if all liabilities are recognised by the PPS.

Where a reduction of benefits may arise even after the intervention of the PPS (i.e. where the PPS does not protect 100 % of the benefits) and on the condition that this is clearly defined, the OPSG agrees that allowance for this possible reduction in benefits should be included in the HBS i.e. OPSG supports the comments of EIOPA in paragraphs 4.135 to 4.137.

The OPSG stresses that MS should put sufficient measures in place to “supervise” the strength of their PPS.

***Q44: Should considering a pension protection scheme as a balancing item be restricted to cases where a pension protection scheme protects 100% of benefits or is it appropriate to allow for the reduction in benefits in case of sponsor default where there is a pension protection scheme in place?***

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The OPSG believes that the existence of a Pension Protection Scheme (PPS) should be considered a sufficient condition to allow for sponsor support to be the balancing item on the HBS, if and only if all liabilities are recognised by the PPS. However, it seems to be even more appropriate to take into account the existence of a PPS directly as a balancing item on the HBS, if and only if all liabilities are recognised by the PPS.

Where a reduction of benefits may arise even after the intervention of the PPS (i.e. where the PPS does not protect 100 % of the benefits) and on the condition that this is clearly defined, the OPSG agrees that allowance for this possible reduction in benefits should be included in the HBS i.e. OPSG supports the comments of EIOPA in paragraphs 4.135 to 4.137.

The OPSG stresses that MS should put sufficient measures in place to “supervise” the strength of their PPS.

***Q45: Do stakeholders believe that it is appropriate that where a pension protection scheme is used as the balancing item, a separate minimum level of funding with financial assets and/or sponsor support should be required?***

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The OPSG is of the opinion that there is no need to define a separate minimum level of funding with financial assets where a PPS is in place i.e. all IORPs should be required to have the same minimum level of funding with financial assets.

The OPSG is of the view that this level would be up to the national supervisor to define.

***Q46: Do stakeholders agree that technical specifications should allow for a principles-based, IORP specific valuation of sponsor support? Please explain.***

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Yes. A standard approach prescribed by EIOPA is unlikely to be suitable in all cases. A principle-based and IORP specific approach for valuing sponsor support instead of an inadequate "one-size-fits-all" approach for all types of IORPs would be appropriate. This would enable supervisors to adopt suitable approaches for different types of IORPs and sponsors as well as facilitate country specific differences.

Requiring all IORPs to comply with a standard approach is likely to result in unnecessary complexity and additional costs without necessarily producing more appropriate outputs. A principles-based approach allowing for the specific features and circumstances of IORPs will be more flexible.

Supervisory authorities can ensure that IORPs adopt appropriate approaches that are consistent with the principles set out by EIOPA.

*Q47: In what areas of valuation of sponsor support would it be most useful for EIOPA to specify guidance? Please explain and describe the possible contents of such guidance.*

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The OPSG does not have sufficient technical experience of valuing sponsor support using stochastic techniques to comment on this but accept that guidance may well be useful to practitioners in some areas. It is important that any guidance does not detract from the principles-based approach EIOPA is minded to adopt.

*Q48: Are there any other issues in relation to stochastic models, which you believe should be covered?*

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No.

*Q49: Do you believe that this approach is a suitable simplified method for determining sponsor support? In what circumstances is it appropriate? In what circumstances might it not be appropriate?*

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This approach (QIS1) is a suitable method for determining sponsor support in a simplified manner. As with any simplified approach there will be issues with interpreting the output in some cases but overall the approach will produce results that are useful in many cases. This approach will be most suitable for those IORPs who do not have the resources to adopt a stochastic approach but who have the necessary inputs for this simplification readily available. It may not be appropriate to use this approach where negative contributions are possible.

It is worth noting that simplified methods generally seem to produce lower estimates of sponsor support than full stochastic models (and within the set of simplified methods the simpler the method the lower the estimate of sponsor support seems to be). While this might be considered to be an incentive to invest in risk management tools it might also be considered an undue burden on smaller IORPs.

It is not clear whether EIOPA intends to take a number of alternative options forward to a further QIS and ask IORPs to calculate results on each basis or whether it is intended that a full menu of options be available for IORPs to pick and choose from.

*Q50: As EIOPA has provided a model for IORPs to derive a value using this specification as long as they provide the input data, what more should EIOPA do to encourage use of this approach where appropriate?*

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It is more important for there to be sufficient suitable approaches for IORPs to be able to adopt one that does not impose an unreasonable burden rather than for EIOPA to encourage the use of a specific approach.

***Q51: Do you believe that this approach is a suitable simplified method for determining sponsor support? In what circumstances is it appropriate? In what circumstances might it not be appropriate?***

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As with QIS1, this approach (QIS2) is a suitable method for determining sponsor support in a simplified manner. As many IORPs participating in the QIS used this method, it was clearly felt to be an appropriate and simple/applicable approach in many cases. As with QIS1 it is likely to be appropriate for IORPs which do not overly rely on sponsor support, or do not have the resources to adopt a stochastic approach but which would have the necessary inputs for this simplification readily available.

***Q52: As EIOPA has provided a model for IORPs to derive a value using this specification as long as they provide the input data, what more should EIOPA do to encourage use of this approach where appropriate?***

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As per our response to Q50 above it is more important for there to be sufficient suitable approaches for IORPs to be able to adopt one that does not impose an unreasonable burden rather than for EIOPA to encourage the use of a specific approach.

***Q53: Do you believe that this approach is a suitable simplified method for determining sponsor support? In what circumstances is it appropriate? In what circumstances might it not be appropriate?***

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This approach is a suitable simplified method for determining sponsor support. It has a strong theoretical underpinning and captures many features of IORPs and their funding that are important in any use that the HBS might be put to. It would be appropriate to use in circumstances where IORPs felt that it was appropriate to their circumstances and could be applied with relative ease. This method does not include an affordability check which would have to be done separately. It is unlikely to be appropriate for smaller IORPs.

***Q54: Should EIOPA produce spreadsheets to enable IORPs to use this simplification?***

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Yes.

***Q55: Do you believe that this approach is a suitable simplified method for determining sponsor support? In what circumstances is it appropriate? In what circumstances might it not be appropriate?***

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This approach is a suitable method for determining sponsor support. It will be particularly appropriate for smaller IORPs for whom no credit assessment or insolvency probability would otherwise exist. It may not be appropriate in cases of current full funding. It may not be appropriate for larger IORPs who have the resources to adopt other approaches.

***Q56: Do the proposed adaptations to this option overcome the criticisms? Should EIOPA produce spreadsheets to enable IORPS to use this simplification?***

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The proposed adaptations deal with many of the issues raised but cannot completely resolve all of these. A simplified approach by its nature will never produce completely appropriate outputs in all



circumstances. However the approach has many advantages to many forms of IORP and EIOPA should produce spreadsheets to enable IORPs to use this simplification.

*Q57: Do stakeholders agree that a simplified one-size-fits-all approach for the calculation of maximum sponsor support is not possible and so the best approach is the proposed principles-based approach for including sponsor affordability? If not, please explain.*

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The OPSG agrees. Because of all the specific characteristics of the IORPs in the different Member States, it seems difficult to capture sponsor support in one single formula all over the EU. The logical step is then to go for a principle based approach on EU level offering the opportunity to the Member States to adequately take into account the specific national characteristics also on the calculation of maximum sponsor support.

*Q58: In respect of a further quantitative impact assessment, would stakeholders like EIOPA to define the parameters to use for maximum sponsor support? If yes, how could EIOPA improve the approach set out in the previous QIS?*

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For the purpose of a further QIS, it would seem helpful for EIOPA to define the parameters but if the approach is ultimately adopted, the parameters should be determined by the IORP and approved by the local regulator (consistently with EIOPA prescribed principles). The OPSG has no views on the approach EIOPA should adopt for the QIS.

*Q59: Do stakeholders think that other options should be considered to determine a value to be used to assess overall sponsor affordability?*

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The options presented appear sufficient for this purpose.

*Q60: Do stakeholders believe that the approaches presented cover the full range of possibilities? If not, what specific alternative approaches would stakeholders propose?*

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The options presented appear to cover a full range of possibilities. Not all of the options presented will be appropriate in all circumstances.

*Q61: What in stakeholders' views is the appropriate time period on which to consider possible payments from sponsors for the calculation of sponsor support? Please explain.*

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The OPSG notes the discussion in 4.217 to 4.220 and supports the comment quoted from the response to the July 2013 consultation that "sponsor affordability, growth and investment plans should be a consideration" and that "the right balance is struck between the funding needs of the IORP and allowing the sponsor to invest and grow its business". In the OPSG's view, the decisive factor will always be the financial position of, and thus the economic capability of, the sponsor.

The two possible timings suggested in 4.220 both have merit and each might be appropriate in different circumstances.

The OPSG suggest that the appropriate time period be determined by the IORP subject to approval of the national supervisor, consistent with principles established at EU level.

### *Q62: Please provide your views on this suggested approach.*

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The suggested approach is a first attempt to deal with a particularly complex issue. In practice companies may sponsor multiple IORPs including IORPs with multiple sponsors and with implicit or explicit guarantees. As an example, German corporations often sponsor multiple types of IORPS available under German SLL, some of them multi-employer. In case of multinationals the same German corporations may assume all risks of a UK pension scheme via an unlimited guarantee.

The suggested approach tends to favour the ASA method as the simplest one. However, already this method creates challenge of apportionment of maximum sponsor support. Each of the proposed parameters of apportionment has its advantages and disadvantages. Nevertheless, to account for very diverse cases as many options as possible should be available. This however creates a regulatory arbitrage as IORPs will likely select an option that produces the most favourable result.

### *Q63: Are there any other suggestions on how to deal with single sponsors with multiple IORPs?*

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No.

### *Q64: Please provide your views on this suggested approach.*

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The suggested approach is unclear. First, it underestimates the complexities of IORPs with multiple sponsors. In practice there are many cases of such IORPs with sponsors of various size and profitability levels. Secondly, it is unclear from 4.229 how the total wages approach could be used in practice. How would an assessment of relative scale of the IORPs' demands and relative scale of their sponsors allow anything but a rather qualitative type of assessment? Thirdly, selecting just a sample of biggest IORPs or any other approach to arrive at a sample, especially as suggested here based on availability of data, would likely create biases and lead to results that would not be representative.

It is unclear in 4.232 what is meant by refined assessment and which additional measures could be delivered in practice to address the situation of insufficient sponsor support.

### *Q65: Are there any other suggestions on how to deal with multiple employer IORPs?*

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No.

### *Q66: Please provide your views on this suggested approach.*

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In general, sponsors with parent guarantees could fulfil the same purpose as a regular sponsor providing sponsor support to the respective IORP in cases where all the additional requirements to qualify for sponsor support on the HBS are met. Nevertheless, the suggested approach fails to take into account the complexities of parent guarantees. The guarantees are often customized to fit the exact circumstances of a given scheme. French parent companies for example may give only limited guarantees to the UK pension schemes of their affiliates, often with various additional conditions.

### *Q67: Please provide your views on this suggested approach.*

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The suggested approach constitutes the first attempt to address complex and diverse situations of “not-for-profit” institutions. However, it is unclear which measures and how could be used for these entities. Treating them differently than “for-profit” sponsors limits the comparability between the

two types of sponsors and potentially creates different levels of protection for plan members. The OPSG does not see any justification from a member/beneficiary perspective of permitting a lower standard to be applied for “not-for-profit” institutions than for other employers.

*Q68: Are there any other suggestions on how to deal with not-for-profit entities?*

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No.

## 6. Pension protection schemes

*Q69: Do stakeholders agree with the above comments on the options to value pension protection schemes? If not, please explain.*

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PPS are safeguarding members and beneficiaries against a loss of entitlements and benefits in case of a default of the sponsoring undertaking, thus serve as a security mechanism and should therefore be taken into account on the HBS.

In this context, the OPSG agrees that the issue is complex. The discussion is a first “brainstorming” attempt showing different options of addressing the issue but it raises more questions than answers. The OPSG considers that what is additionally required is a comparative analysis of fundamental differences between existing pension protection schemes in various MS.

*Q70: Which of the options to value pension protection schemes do stakeholders prefer?*

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The OPSG understands that the options to which this question refers are the alternative approaches of separate valuation and presentation of the PPS (4.249) and using the PPS to reduce (possibly to zero) credit default risk of the sponsor (4.250). The different PPS within the Member States operate as separate institutions or tools and should thus also be valued on the Holistic Balance Sheet as a separate asset and not by reducing the default risk of the sponsor.

The OPSG notes the disadvantage of this approach identified by EIOPA that it would not be cost effective or worthwhile for each IORP to have to determine a value of the PPS applicable to them, and the OPSG recommends that some simplified and consistent approach be acceptable.

*Q71: Do stakeholders think a pension protection scheme could in principle be considered a balancing item on the holistic balance sheet, if considered as a separate asset on the holistic balance sheet?*

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Yes, but if and only if all liabilities are recognised by the PPS. Where a reduction of benefits may arise even after the intervention of the PPS (i.e. where the PPS does not protect 100 % of the benefits) and on the condition that this is clearly defined, the OPSG agrees that allowance for this possible reduction in benefits should be included in the HBS i.e. OPSG supports the comments of EIOPA in paragraphs 4.135 to 4.137.

## 7. Components of supervisory framework

*Q72: If it was decided to establish EU capital/funding requirements as part of pillar 1, would there in the stakeholders' view be a role for the holistic balance sheet? Please explain why and, if yes, what that role should be.*

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The OPSG sees no role for the HBS to be used in pillar 1. There is more justification for application of the HBS for pillar 2 than for pillar 1, if it should be used at all. When it would be applied in pillar 2, it would make more sense to include all security and adjustment mechanisms, even if these are not legally binding, than in pillar 1. In pillar 1, on the one hand, only the inclusion of "hard" balance sheet items seems defensible, but on the other hand, the exclusion of other elements would make the HBS "un-holistic". Therefore, in pillar 2 a fuller picture of the financial position of the IORP and a higher level of market consistency can be reached than in pillar 1, where there is ample ground to exclude "softer" steering mechanisms (like benefit cuts).

The issues with regard to the specifications of the HBS, especially the valuation of balance sheet items on the HBS and more consistency across the EU, need to be solved before it can be decided whether the HBS can be used in any risk based framework at all. Achieving consensus on these issues would probably already be a great challenge, but even if successful, the HBS would not need to be imposed to achieve EU capital/funding requirements.

Proportionality will also be an issue. Since the HBS is a complex method, even if the information could have added value, the calculations can be so complex and costly that it is not a cost effective instrument to use for supervision.

Since the HBS seems to be cost ineffective, the OPSG would give in consideration also to investigate other possible instruments like ALM, stress test, continuity analysis to test the financial position of IORPs. Another reason to develop other instruments is that it is very unlikely that – if the HBS can be properly developed and would have added value – the HBS will be the sole supervisory instrument.

The market consistent valuation poses a problem. Either a full stochastic valuation is used or simplifications. On the one hand, the stochastic valuation is complex, expensive and would use concepts like risk-neutral valuation. The concept of risk-neutral valuation makes providing insights in the future development of the IORP too complicated and is therefore not useful to calculate the capital requirements over one year. The HBS cannot easily be used to project the future funding position and give probabilities on the likelihood of possible outcomes. On the other hand, the simplifications by their nature will, at best, give approximations of the market value, with as a consequence that the capital requirements will be a proxy as well.

The use of HBS in a risk based supervisory framework may lead to undesirable behaviour from the perspective of the IORP and from a supervisory perspective. Based on this framework an IORP would take extra risk in poor times, because an IORP that is highly underfunded could improve the HBS by taking extra risk. This extra risk would not have a big impact on the conditional benefits (like conditional indexation) that is part of the HBS. The benefit reduction option on the other hand would increase with risk taking as this option will get more "in the money".

*Q73: Do stakeholders believe that the holistic balance sheet should be used as a risk management tool as part of pillar 2 requirements? Please explain.*

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The OPSG thinks there would be more justification for application of the HBS for pillar 2 than for pillar 1, if it should be used at all. When applied in pillar 2, it would make much more sense to include all security and adjustment mechanisms, even if these are not legally binding, than in pillar 1. Therefore, in pillar 2 a fuller picture of the financial position of the IORP and a higher level of market

consistency can be reached than in pillar 1, where there is ample ground to exclude "softer" steering mechanisms (like benefit cuts).

Risk management should provide insight in the development of the solvency situation of the IORP over time. However, the HBS only provides insight in the current valuation and not in the projections of capital requirements. The valuation of all kind of options on HBS, like sponsor support (conditional on future funding status), conditional benefits (like conditional indexation) and benefit cuts (conditional on too low future funding), requires complex valuation methods like risk-neutral valuation. Risk-neutral valuation only is able to give a current valuation of the cash flows, but cannot be used to predict future cash flows. Since predicting future cash flows is impossible, the HBS cannot be used to project the future funding position and give probabilities on the likelihood of possible outcomes.

In the Netherlands however, the concept behind the HBS is used to look at fairness of the pension deal across stakeholders (especially across generations). This would be a possible use of the HBS or of its underlying concept. Therefore the implementation of the HBS is not possible in pillar 1 and has a very limited use in pillar 2 and 3.

*Q74: Do stakeholders agree that the outcomes of a pillar 2 assessment should be publicly disclosed as part of pillar 3 requirements?*

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The OPSG underlines the importance of disclosure of information about the benefits and the financial position of the IORP to members and beneficiaries; they are entitled to information which assists their understanding of the security of their pension promise (i.e. as set out in 5.34). It is important that the information provided to members and beneficiaries in this regard is clear, fair and not misleading, and is understandable to those who do not have detailed knowledge of financial issues.

As mentioned in our answer to question 73, the HBS could possibly be used for risk management purposes (in pillar 2). The OPSG has serious concerns though about disclosing the outcomes of a pillar 2 assessment to members and beneficiaries under pillar 3. The HBS is a complex method and even experts possibly do not have a full understanding of the HBS and the underlying calculations. The OPSG doubts whether the HBS will provide information in a meaningful fashion for the members and beneficiaries. For example explaining a value of 20 for mixed benefits and at the same time 10 for benefits cuts will be too difficult and the same will hold true for having a value for the PPS on the HBS.

The HBS only provides insight in the current valuation of assets and pension promises and does not provide an insight to a participant in for example to what extent the pension is likely to keep up with inflation. In order to get an idea of the perspective and risks of the future pension, one should simulate with real world scenarios. The HBS cannot be used to do that.

The question refers to "public disclosure" of the Pillar 2 results which appears to be broader than disclosure to members and beneficiaries e.g. to media and to unrelated employers and their employees. 5.35 suggests that such "public disclosure" would "encourage reforms" where an IORP is shown to be unsustainable. The OPSG would strongly reject any requirement to make publicly available the financial results of an IORP, as this could lead to "naming and shaming" of some IORPs/employers and might actually hinder an appropriate resolution of issues between the employer/members/supervisor.

*Q75: Do stakeholders agree that competent authorities should be empowered to take supervisory action based on the pillar 2 assessment of the holistic balance sheet? Please explain and, if yes, what action?*

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The OPSG would like to stress that the issues with regard to the valuation base of the HBS need to be solved before the HBS can be used in any risk based framework, if at all.

If the HBS would be used as a base to initiate supervisory action, the IORP would possibly be double charged for risk taking: as a result of the inclusion of all loss absorbing elements in the HBS an IORP has to build up buffers for both risks and soft benefits. This can be envisaged by the way the HBS is set up. By increasing the investment risk, the downside risk is reflected in a higher SCR requirement. Higher risk also increases upward potential and therefore the indexation option. If the HBS would be used for a minimum funding requirement, the IORP would be required to hold extra funding for this increased indexation option. This effect of double charging could be resolved if prudential supervision would focus on unconditional promises.

If the concept of HBS requires the inclusion of all steering instruments, there are no further instruments available for recovery if the funding would be too low. In this case the recovery plan cannot be set up; it is already included in the HBS in the form of the steering instruments available to the IORP. The conclusion then is that the financial policy of the IORP is possibly unsustainable and that the sponsor, employees, (deferred) members and other relevant stakeholders should reconsider the pension deal.

As a general remark the OPSG would like to stress that a useful concept of recognising certain elements in the HBS depends crucially on the supervisory response. The responses to the following questions do not take this into account.

*Q76: Which of the two options for recognising non-legally enforceable sponsor support do stakeholders support? Please explain why you support this option.*

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The OPSG considers application of the HBS more sensible for pillar 2 than 1 and 3 (also see our answer to question 72). If the HBS will be used for pillar 2, any relevant information should be reported in one way or another to scheme members and beneficiaries (pillar 3). In pillar 2, preferably all steering instruments that will have a (market) value should be included, also non-legally enforceable sponsor support. If this would have a positive value, it should not be disregarded. So when applying the HBS to pillar 2, the OPSG would prefer option 1.

The existence of some form of non-legally enforceable sponsor support will contribute to the safety of the pension promise as the employer may make additional contributions to meet underfunding when it arises. Therefore one could be in favour of the option to include the non-legally enforceable sponsor support in the HBS. However, individual IORPs are best suited to decide if and how to include this, subject to approval of the national supervisor. As there is a link to IFRS in the sense there is a need for a realistic picture of liabilities of a sponsor, the IORP should be able to address this issue with their sponsor(s). The local supervisor should then assess the method used and the viability of the assumptions and resulting outcome.

*Q77: Which of the two options for recognising pension protection schemes do stakeholders support? Please explain why you support this option.*

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The OPSG considers application of the HBS more sensible for pillar 2 than 1 and 3 (also see answer to question 72). In pillar 2, preferably all steering instruments that will have a (market) value should be included, also the PPS. If this would have a positive value, it should not be disregarded.

Also the existence of a pension protection scheme (PPS) will contribute to the safety of the pension promise. Therefore one could be in favour to include the value of the PPS on the HBS. However, in the case of the inclusion of the PPS, EIOPA has to monitor the financial strength of these PPSs. This has to be done on a macro scale, otherwise the systematic risk of such schemes are not taken into account in the value.

In general, PPS should be valued as a balancing item on the holistic balance sheet – but if and only if all liabilities are recognised by the PPS. Where a reduction of benefits may arise even after the intervention of the PPS (i.e. where the PPS does not protect 100 % of the benefits) and on the condition that this is clearly defined, the OPSG agrees that allowance for this possible reduction in benefits should be included in the HBS i.e. OPSG supports the comments of EIOPA in paragraphs 4.135. to 4.137. – for the following reasons as expressed in the Consultation Paper:

- PPS protects members and beneficiaries against insolvency of their employers. In a holistic view, it should therefore be included in the HBS. The Consultation paper describes conditions a PPS would have to fulfil (4.139), which the OPSG supports.
- There is a close link between sponsor support and pension protection schemes. Pension protection schemes could be seen as a form of collective sponsor support. Therefore they should, like sponsor support, be included in the holistic balance sheet.
- PPS is a mechanism, established under national social and labour law, which protects members and beneficiaries against insolvency of their employers. A European prudential framework should not aim at changing the level of security which is accepted under national social and labour law.
- PPS fulfil their task on a regular and ongoing basis. They are not a last resort mechanism, like insurance guarantee schemes. So they cannot be excluded from the HBS on the grounds that they are similar to insurance guarantee schemes, even if one accepts a need for consistency with the insurance framework.
- PPS can be financed by tens of thousands of sponsors of different industry sectors and nationwide, which gives them a very strong financial basis, comparable to the strength of a whole national economy.
- In cases where a strong PPS is in place, the benefits of members and beneficiaries would be protected with a sufficient level of security. A sufficient level of security can therefore be achieved in those cases, without applying short recovery periods or requiring an IORP to hold financial assets at least of the amount of Level A technical provisions.

EIOPA rightly considers individual sponsor support as an important security mechanism. It therefore would not make sense not to include pension protection schemes as a form of collective sponsor support like for example for over 90,000 employers in Germany. In addition, if it was not recognized, the security level in Germany would be systematically higher than in many other EU Member States.

Not taking pension protection schemes into account in the HBS would therefore remove it even further from the reality of occupational pensions in European Member States.

***Q78: Do stakeholders agree that pure discretionary benefits should not be included on an IORP's pillar 1 balance sheet, as these do not represent a part of the benefit promise that needs to be protected by quantitative requirements? If not, what alternative options would you suggest?***

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The OPSG considers application of the HBS more sensible for pillar 2 than 1 and 3 (also see the answer to question 72). In pillar 2, preferably all benefits that will have a (market) value should be

included, also pure discretionary benefits. If these would have a positive value, it should not be disregarded.

Any quantification of these discretionary benefits will be a difficult, possibly (very) unreliable estimate. Especially any extrapolation of previously taken discretionary decisions will ignore the fact that a different position or economic circumstance will probably lead to a different outcome. Therefore recognising discretionary benefits on the HBS could not be possible, but inclusion by the IORP should be done if possible and with evidence to support the valuation.

***Q79: Which of the three options for recognising mixed benefits do stakeholders support? Please explain why you support this option.***

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The OPSG would prefer a fourth option, related to option 3. The OPSG considers application of the HBS more sensible for pillar 2 than 1 and 3 (also see answer to question 72). In pillar 2, preferably all benefits that will have a (market) value should be included, also mixed benefits. If these would have a positive value, it should not be disregarded.

If the HBS were to be used for pillar 1, as a result of the inclusion of all loss absorbing elements in the HBS an IORP has to build up buffers for both risks and soft benefits. This effect of double charging could be resolved if prudential supervision would focus on unconditional promises. Therefore the OPSG is in favour of not recognising mixed benefits in the HBS, especially not if the HBS would be used for capital requirements in pillar 1.

Another issue is whether there is a legal or contractual obligation to provide these benefits. If there is no such obligation, the character of these benefits is very similar to the character of discretionary benefits.

***Q80: Which of the three options for recognising benefit reduction mechanisms do stakeholders support? Please explain why you support this option.***

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The OPSG considers application of the HBS more sensible for pillar 2 than 1 and 3 (also see the answer to question 72). In pillar 2, preferably all steering instruments that will have a (market) value should be included, also all benefit reduction mechanisms. If these would have a positive value, it should not be disregarded. Therefore, the OPSG supports option 3. The OPSG does not see any rationale for making a distinction between ex ante and ex post reductions.

If the HBS would become the base for risk based supervisory framework in pillar 2, all options in a pension contract having impact on the benefits, including benefit reductions, should be included. The HBS is supposed to provide insight into valuation of all steering instruments available to the IORP. Excluding elements such as ex-post benefit reduction will corrupt this purpose.

If the HBS were to be used for pillar 1, consistency with the approach of discretionary and conditional benefits as mentioned in 5.65 may be economically valid, but the legal perspective might be different, i.e. granting discretionary benefits in addition to hard basic benefits is different from cutting benefits from the same hard basic benefits.

In a PBS like benefit statement, there will be no difference for member's (expected) benefits between ex-ante and ex-post benefit reductions. Making explicit the possibility of benefit reductions will certainly promote realistic perceptions with beneficiaries, sponsor(s) and other stakeholders of IORPs.

***Q81: Are there any additional options that stakeholders believe should be considered?***

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In view of the OPSG, there are no other options which should be considered.



***Q82: Do stakeholders agree that off-balance capital instruments should always be eligible to cover the SCR? If not, what alternative options would you suggest?***

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The OPSG considers application of the HBS more sensible for pillar 2 than 1 and 3 (also see the answer to question 72). If the HBS were to be used for pillar 1, the OPSG does agree that off-balance sheet capital instruments should be eligible to cover the SCR. The OPSG would like to restate though, that the concept of the HBS, requiring inclusion of all steering instruments (and thus the recovery plan) in the balance sheet and not allowing for projections/simulations, cannot be combined with the concept of SCR.

***Q83: Do stakeholders agree that surplus funds should always be recognised on an IORP's balance sheet and could always be used to cover capital requirements? If not, how would you suggest to treat surplus funds in this respect?***

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The OPSG considers application of the HBS more sensible for pillar 2 than 1 and 3 (also see the answer to question 72). If the HBS were to be used for pillar 1, the OPSG does agree that surplus funds should be recognised on an IORP's balance sheet and could be used to cover capital requirements. The OPSG would like to restate though, that the concept of the HBS, requiring inclusion of all steering instruments (and thus the recovery plan) in the balance sheet and not allowing for projections/simulations, cannot be combined with the concept of SCR.

***Q84: Do stakeholders agree that subordinated loans should always be recognised on an IORP's balance sheet and could, bar possible future decisions to introduce restrictions, be used to cover capital requirements? If not, how would you suggest to treat subordinated loans in this respect?***

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The OPSG considers application of the HBS more sensible for pillar 2 than 1 and 3 (also see the answer to question 72). If the HBS were to be used for pillar 1, the OPSG does agree that subordinated loans should be recognised on an IORP's balance sheet and could, bar possible future decisions, be used to cover capital requirements. The OPSG would like to restate though, that the concept of the HBS, requiring inclusion of all steering instruments (and thus the recovery plan) in the balance sheet and not allowing for projections/simulations, cannot be combined with the concept of SCR.

***Q85: In the stakeholders' view should the minimum requirement for the level of liabilities to be covered with financial assets be based on the Level A technical provisions or the Level B best estimate of technical provisions? Please explain.***

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The OPSG considers application of the HBS more sensible for pillar 2 than 1 and 3 (also see the answer to question 72). If the HBS were to be used for pillar 1, the OPSG would at the one hand like the concepts used to be (market) consistent and at the other hand like that the nature of the pension deal and purpose should be recognised.

The discount rate should reflect the nature and certainty of the benefits. If the benefits are guaranteed/hard, level A would be most appropriate, but this will possibly not reflect the financial policy of the IORP to fund these benefits. Whilst coverage of Level A technical provisions by financial assets provides greater alignment and consistency with the nature of hard (guaranteed) benefits, the reality is that in the case of many IORPs this would require significant additional capital contributions from the sponsoring employer which it may not be in a position to make without seriously damaging

its business, and hence would require the closure of the IORP and/or a reduction in benefits. This would change the nature of the pension promise. The sponsor may be able to provide support over the long term which will enable, with a high degree of probability, the benefits to be paid as they fall due but will retain the ability to invest in the business to underpin the value of this sponsor support, thereby maintaining the pension promise.

For "soft" benefits, where the pension promise is not guaranteed, level B is appropriate, especially when the benefits depend on the investment returns achieved.

In addition, the risk of using level A reserves is that it could disincentivise IORPs from investing in real assets to the long term benefit of the (EU) economy: the option to reduce risk and the level of sponsor support required (i.e. move to a self-sufficiency basis) is available to those IORPs/sponsors who want to do so by investing in low risk bonds, in which event level A and level B coincide. Whilst the use of Level B reserves as the appropriate measure might seem to encourage IORPs to invest recklessly, in practice this would be restricted by the requirement to invest in accordance with the "prudent person principle" and with the IORP's Statement of Investment Policy Principles.

***Q86: If the Level B best estimate were to be used, in the stakeholders' view should it apply to all IORPs or should its use be restricted to IORPs which dispose of certain security and adjustment mechanisms, be subject to prior approval of the national supervisor or applied as a member state option? Please explain.***

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As noted above, the OPSG considers that Level B would be appropriate in cases where the benefit promise is considered "soft" and dependent on the investment returns achieved, regardless of other security or adjustment mechanisms. Where the benefit promise is hard, Level B would only be appropriate if there are other security or adjustment mechanisms to bridge the gap to the Level A provisions, if these are not fully covered by financial assets.

The OPSG suggests that this should be a member state option, possibly subject to some overarching principles to be set out in the Directive to facilitate a base for harmonisation if and when harmonisation is warranted. Prior approval of the national supervisor should not be required under the Directive, but could be a requirement of the supervisor in some Member States.

***Q87: In the stakeholders' view should the level of technical provisions that needs to be covered with assets (incl. security mechanisms), and that potentially serves as a basis for the SCR, be based on Level A technical provisions or on the Level B best estimate of technical provisions? Please explain.***

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The OPSG considers application of the HBS more sensible for pillar 2 than 1 and 3 (also see the answer to question 72). If the HBS were to be used for pillar 1, the OPSG would at the one hand like the concepts used to be (market) consistent and at the other hand like that the nature of the pension deal and purpose should be recognised (also see the answer to question 85).

If the HBS were to be used for pillar 1, the OPSG would like to restate though, that the concept of the HBS, requiring inclusion of all steering instruments (and thus the recovery plan) in the balance sheet and not allowing for projections/simulations, cannot be combined with the concept of SCR.

As noted above, the OPSG considers that Level B would be appropriate in cases where the benefit promise is considered "soft" and dependent on the investment returns achieved, regardless of other security or adjustment mechanisms. Where the benefit promise is hard, Level B would only be appropriate if there are other security or adjustment mechanisms to bridge the gap to the Level A provisions, if these are not fully covered by financial assets.

The OPSG suggests that this should be a member state option, possibly subject to some overarching principles to be set out in the Directive to facilitate a base for harmonisation if and when harmonisation is warranted.

Q88: If the Level B best estimate were to be used, in the stakeholders' view should its use be restricted to IORPs which dispose of certain security and adjustment mechanisms, be subject to prior approval of the national supervisor or applied as a member state option? Please explain.

As noted above, the OPSG considers that Level B would be appropriate in cases where the benefit promise is considered "soft" and dependent on the investment returns achieved, regardless of other security or adjustment mechanisms. Where the benefit promise is hard, Level B would only be appropriate if there are other security or adjustment mechanisms to bridge the gap to the Level A provisions, if these are not fully covered by financial assets.

The OPSG considers that this should be a member state option, subject perhaps to some overarching principles to be set out in the Directive.

*Q89: Do stakeholders believe it would be a sensible approach for member states to specify additional requirements regarding the funding with (financial) assets through national social and labour law, instead of through national prudential regimes? Please explain.*

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It is too early to decide on this as the general approach should first be specified before discussing the need to allow for additional requirements. However, this would be a pragmatic way to retain MS options within an EU wide prudential framework, allowing for an adequate consideration of national characteristics of IORPs. At the same time, such an approach might also help to encourage the establishment of cross border schemes where there may be national concerns about regulatory arbitrage.

*Q90: Do stakeholders believe that there is scope for harmonising the recovery period regarding the level of technical provisions to be covered with financial assets on the EU level? Please explain.*

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If the concept of HBS requires the inclusion of all steering instruments, there are no further instruments available for recovery if the funding would be too low. In this case the recovery plan cannot be set up; it is already included in the HBS in the form of the steering instruments available to the IORP. As noted by the OPSG in previous responses, this is a major problem in relation to the use of the HBS in practice: the IORP appears to be in an impossible situation if all mechanisms have been taken into account and the HBS still does not balance, whereas in practice some solution must (and can) be found.

There is scope for harmonised principles on the recovery period for the sake of the protection of the beneficiaries. Such harmonisation will permit a fair establishment of cross-border IORPs as opposed to regulatory arbitrage with IORPs moving to countries applying lower requirements (race to the bottom). However, if the HBS is not used for pillar 1, as we suggest all along in our response a recovery period linked to the HBS will become irrelevant.

On balance, the OPSG considers that it Option 3 is most appropriate i.e. that it should be a member state option to set the length for the period (i.e. the plan horizon) over which the level of technical provisions should be covered with financial assets, subject perhaps to some overarching principles to be set out in the Directive.

***Q91: Do stakeholders think that the recovery period regarding the level of technical provisions to be covered with financial assets should be short or cover an extensive period of time? Please explain.***

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If the concept of HBS requires the inclusion of all steering instruments, there are no further instruments available for recovery if the funding would be too low. In this case the recovery plan cannot be set up; it is already included in the HBS in the form of the steering instruments available to the IORP. However, if the HBS is not used for pillar 1, as we suggest all along in our response, a recovery period linked to the HBS will become irrelevant.

The usually long duration of pension liabilities allow for a long-term approach to risk management. However, a recovery period must not be so long that the IORP is not able to pay out pension benefits as they come due.

The OPSG considers that it should be a member state option to set the length for the period (i.e. the plan horizon) over which the level of technical provisions should be covered with financial assets, subject perhaps to some overarching principles to be set out in the Directive.

***Q92: In the stakeholders' view how long should the more extensive recovery period be and should it be restricted to IORPs which dispose of certain security and adjustment mechanisms and/or be subject to prior approval of the national supervisor? Please explain.***

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If the concept of HBS requires the inclusion of all steering instruments, there are no further instruments available for recovery if the funding would be too low. In this case the recovery plan cannot be set up; it is already included in the HBS in the form of the steering instruments available to the IORP. However, if the HBS is not used for pillar 1, as we suggest all along in our response, a recovery period linked to the HBS will become irrelevant.

The OPSG considers that it should be a member state option to set the length for the period (i.e. the plan horizon) over which the level of technical provisions should be covered with financial assets, subject perhaps to some overarching principles to be set out in the Directive.

Also, once set a recovery period must not be revised, except in extreme circumstances, to avoid putting the IORP in a situation of complacency or uncertainty with regard to fulfilling the agreed recovery plan.

Finally, the recovery plan should be subject to prior approval of the supervisor and should take into account the security mechanisms insofar as the absence thereof should lead to a shorter recovery period.

***Q93: Do stakeholders believe that there is scope for harmonising the recovery period for meeting the SCR on the EU level? Please explain.***

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If the concept of HBS requires the inclusion of all steering instruments, there are no further instruments available for recovery if the funding would be too low. In this case the recovery plan cannot be set up; it is already included in the HBS in the form of the steering instruments available to the IORP.

If the HBS were to be used for pillar 1, the OPSG would like to restate though, that the concept of the HBS, requiring inclusion of all steering instruments (and thus the recovery plan) in the balance sheet and not allowing for projections/simulations, cannot be combined with the concept of SCR.

There is scope for harmonised principles on the recovery period for the sake of the protection of the beneficiaries, to the extent that a recovery period is useful, which the OPSG doubts as stated before. Such harmonisation will permit a fair establishment of cross-border IORPs as opposed to regulatory arbitrage with IORPs moving to countries applying lower requirements (race to the bottom). In addition, as the SCR is the required capital derived from a prudential framework based on harmonisation at EU level, it would be logical to allow for harmonised principles on the recovery period.

On balance, the OPSG considers that it should be a member state option to set the length for the period (i.e. the plan horizon) for meeting the SCR, subject perhaps to some overarching principles to be set out in the Directive.

*Q94: In the view of stakeholders should the recovery period in the event of non-compliance with the SCR be short or cover a more extensive period of time? Please explain.*

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If the concept of HBS requires the inclusion of all steering instruments, there are no further instruments available for recovery if the funding would be too low. In this case the recovery plan cannot be set up; it is already included in the HBS in the form of the steering instruments available to the IORP.

If the HBS were to be used for pillar 1, the OPSG would like to restate though, that the concept of the HBS, requiring inclusion of all steering instruments (and thus the recovery plan) in the balance sheet and not allowing for projections/simulations, cannot be combined with the concept of SCR.

To the extent that the EU should set standards for recovery periods, which the OPSG questions, as long as the IORP is able to meet its commitments at the time of pay-out, relatively long recovery periods should be allowed.

There is scope for harmonised principles on the recovery period for the sake of the protection of the beneficiaries, to the extent that a recovery period is useful, which the OPSG doubts as stated before. Such harmonisation will permit a fair establishment of cross-border IORPs as opposed to regulatory arbitrage with IORPs moving to countries applying lower requirements (race to the bottom).

On balance, the OPSG considers that it should be a member state option to set the length for the period (i.e. the plan horizon) in the event of non-compliance with the SCR, subject perhaps to some overarching principles to be set out in the Directive.

*Q95: In the view of stakeholders how long should the more extensive recovery period be and should it be restricted to IORPs which dispose of certain security and adjustment mechanisms and/or be subject to prior approval of the national supervisor? Please explain.*

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If the concept of HBS requires the inclusion of all steering instruments, there are no further instruments available for recovery if the funding would be too low. In this case the recovery plan cannot be set up; it is already included in the HBS in the form of the steering instruments available to the IORP.

There is scope for harmonised principles on the recovery period for the sake of the protection of the beneficiaries, to the extent that a recovery period is useful, which the OPSG doubts as stated before. Such harmonisation will permit a fair establishment of cross-border IORPs as opposed to regulatory arbitrage with IORPs moving to countries applying lower requirements (race to the bottom).

To the extent that the EU should set standards for recovery periods, which the OPSG questions, the recovery period in the case of the SCR should be longer than the one set for Technical Provisions owing to the fact that a breach of the SCR does not result in an immediate threat for Technical Provisions, so that members and beneficiaries are still protected.

Also, once set a recovery period must not be revised, except in extreme circumstances, to avoid putting the IORP in a situation of complacency or uncertainty with regards to fulfilling the agreed recovery plan.

Finally, the recovery plan should be subject to prior approval of the supervisor and should take into account the security mechanisms insofar as the absence thereof should lead to a shorter recovery period.

On balance, the OPSG considers that it should be a member state option to set the length for the period (i.e. the plan horizon) in the event of non-compliance with the SCR, subject perhaps to some overarching principles to be set out in the Directive.

***Q96: Do stakeholders agree that IORPs should be required to submit a recovery plan if capital/funding requirements are not met or should more specific supervisory responses be specified on the EU level? Please explain.***

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If the concept of HBS requires the inclusion of all steering instruments, there are no further instruments available for recovery if the funding would be too low. In this case the recovery plan cannot be set up; it is already included in the HBS in the form of the steering instruments available to the IORP.

However, if the HBS is not used for pillar 1, as we suggest all along in our response, a recovery period linked to the HBS will become irrelevant.

As noted in 5.132, there are many components which could be included in a recovery plan, and consequently the OPSG is of the view that it should be a member state option to determine the content of the recovery plan, subject perhaps to some overarching principles to be set out in the Directive. In practice, the process would involve dialogue between the IORP and the supervisor as solutions would depend on the circumstances (e.g. the size of the shortfall, its cause, its potential duration, etc.).

***Q97: What is the view of stakeholders on the potential impact of a possible future European prudential framework for IORPs on existing contractual agreements and national social and labour law?***

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This is analysed very well in 5.134 to 5.139. It is too early to assess the consequences on existing "contractual agreements" without knowing the details of the framework.

However, the OPSG believes that existing contractual agreements and national social and labour law would be negatively impacted by a maximum harmonisation EU wide framework and that it is essential to retain MS options to enable the different pension structure to be maintained, albeit with a greater degree of harmonisation in relation to governance and risk management as proposed in IORP II.

*Q98: In the stakeholders' view is there scope for transitional measures in order to mitigate the potential impact of a possible EU prudential regime on existing contractual agreements and national social and labour law?*

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The OPSG thinks it would be essential to have transitional measures if significant changes were proposed to the existing regime, and at an extreme this could take the form of applying any new structure to new members of IORPs ("new contracts") or possibly future accrual for existing members, with the existing regime applying to pension rights built up to date.

Transitional periods and/or grandfathering rules depend also on the supervisory framework chosen. Very long transitional periods are not recommended but in some cases may be absolutely necessary under some supervisory frameworks. Therefore the choice of the supervisory framework should be evaluated also compared to the duration of transitional periods.

Nevertheless, any kind of implementation of transitional periods and/or grandfathering has to go hand in hand with an adequate consideration of all the specific mechanisms like the sponsor support or PPS within the HBS and cannot be seen as a substitute for the inclusion of such mechanisms.

## **8. Analysis of examples of supervisory frameworks**

*Q99: Do stakeholders have any general comments on (the description of) example 1?*

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This approach does not seem feasible in MS where the existing prudential framework is not already closely aligned to the insurance framework.

As pointed out in the discussion:

- This solvency framework seriously interferes with existing pension schemes contracts and national social and labour law in a number of member states;
- It will discourage sponsors from providing pension promises for future membership in many countries and may lead to the reduction of accrued pension rights;
- Due to exclusion of protection schemes there is a misstatement of the level of protection.
- The short term recovery period could lead to a possible increase in sponsor insolvency
- This approach could have a negative impact on long term investment and the EU growth agenda.

In addition it requires a very long transitional period and/or grandfathering measures.

The OPSG would comment that:

- Whilst in theory this approach would facilitate the use of cross border IORPs, this would probably be more than counteracted by the withdrawal of defined benefit provision by employers who might otherwise have considered establishing a cross border or pan-European IORP.
- Whilst member protection would clearly be improved, in many cases the level of the pension promise may have to be reduced to remain affordable, and it is questionable whether members are better served by a lower benefit promise with a high levels of security, or a higher benefit promise with a greater risk that this will not be delivered (provided the risks are fully disclosed and managed appropriately).
- The treatment of conditional and mixed benefits seems inappropriate: the requirement that assets held are sufficient to hedge mismatch risk on financial markets in relation to these benefits is impractical so in practice these would have to be capable of being transferred to

another undertaking (probably an insurance company) in which event they may become guaranteed (or at least subject to different conditions/discretions) so that there would be a change in the pension promise.

Some negative impact of this approach could be overcome if:

- Level B technical provisions are considered;
- Long term recovery period are admitted;
- Protection schemes are accounted for.

### *Q100: Could example 1, in the view of stakeholders, be used for all IORPs in the EU?*

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OPSG does not think that this approach could be used for all IORPs in the EU, in relation to existing promises. If these were grandfathered, and this approach introduced for future employees/accruals (after a transitional period), it is likely that there would be a significant reduction or even complete disappearance of defined benefit IORPs. Benefit promises could only be provided in a Pillar 1 system, a fully insured pension contract, or an unfunded (private or public sector) approach.

### *Q101: Do stakeholders have any general comments on (the description of) example 2?*

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This approach seems workable.

As pointed out in the consultation paper:

- This solvency framework interferes with national systems by imposing an SCR with a harmonized confidence level, but the impact may be limited in some countries;
- IORPs would not be required to take into account pure discretionary and mixed benefits, in line with the current IORP directive;
- Member states have the discretion to allow for considerable recovery periods;

However:

- IORPs would not be required to have sufficient assets to be able to hedge mismatch risk on financial markets, which reduces the level of member protection;
- Due to exclusion of protection schemes there is a misstatement of the level of protection;
- Some (limited) inconsistencies with the Solvency II framework are introduced. The OPSG does not consider this to be a fundamental problem.

### *Q102: Could example 2, in the view of stakeholders, be used for all IORPs in the EU?*

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The OPSG thinks that this approach could be used for all IORPs in the EU, provided there will be a transitional period. The OPSG is of the view that an SCR is inconsistent with the use of the HBS in Pillar 1. However, if there were to be an SCR, the requirement to cover it with a harmonised confidence level is in our view inappropriate as the confidence level should be set at Member State level. In addition, the OPSG disagrees with the exclusion of PPS in this example.

The OPSG would require further detail of the proposed approach and consideration of worked examples e.g. from QIS 2 before forming a view on its applicability across the EU.



### *Q103: Do stakeholders have any general comments on (the description of) example 3?*

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This approach is complete as it also considers a forward looking assessment. However, modelling technical provisions, security and benefit adjustment mechanism with a forward looking perspective could be too complex for many IORPs.

More generally, it is not clear why the holistic balance sheet should have a different approach to evaluate technical provisions. Only Level B (or level A with appropriate adjustments) should be considered in HBS.

In this approach the IORP is initially able to deliver on the pension promise, without ex-post benefit reduction, with a probability corresponding to the SCR confidence level.

The impact on National IORP systems is expected to be “limited” by EIOPA. However, this seems not the case, especially for the SCR requirement and the pillar 2/3 forward looking assessment.

### *Q104: Could example 3, in the view of stakeholders, be used for all IORPs in the EU, taking into account national specificities?*

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This approach attempts to recognise the importance of the ongoing ability of the IORP to provide the benefits as they fall due, rather than just focussing on the short term solvency requirements. It is however complex and the interaction between the pillar 1 and pillar 2/3 supervisory actions is unclear. The OPSG sees no room for applying the HBS in pillar 1 and would require further detail of the proposed approach and consideration of worked examples e.g. from QIS 2 before forming a view on its applicability across the EU.

### *Q105: Do stakeholders have any general comments on (the description of) example 4?*

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This approach seems feasible although the OPSG is of the view that an SCR is inconsistent with the use of the HBS in Pillar 1. The logic is that pure conditional benefits (excluding benefit reduction) should be covered by financial assets. With respect to example 3 also ex-post benefit reduction and reduction in case of sponsor default is introduced for SCR. Meeting SCR capital requirement is simpler, so a lower impact on IORPs is expected and a shorter transition period could be introduced (compared with example 3 which introduces also a pillar 2 requirement).

### *Q106: Could example 4, in the view of stakeholders, be used for all IORPs in the EU?*

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This approach addresses some of the concerns expressed in relation to earlier examples. The OPSG would require further detail of the proposed approach and consideration of worked examples e.g. from QIS 2 before forming a view on its applicability across the EU.

### *Q107: Do stakeholders have any general comments on (the description of) example 5?*

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This approach also attempts to recognise the importance of the ongoing ability of the IORP to provide the benefits as they fall due, rather than just focussing on the short term solvency requirements. No SCR capital requirement is introduced in Pillar 1 but a more harmonized approach based on Level A estimate is introduced. The use of a level A TP estimate could lead to a strong impact on IORPs for whom technical provisions are currently calculated on a Level B approach, as permitted under the IORP Directive and national legislation, requiring a very long transitional period and/or recovery period.

### *Q108: Could example 5, in the view of stakeholders, be used for all IORPs in the EU?*

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This example is less complex than Example 3, but would require a long transitional period if it were to be implemented for all IORPs in the EU, and might lead to a significant reduction in defined benefit IORPs. The OPSG would require further detail of the proposed approach and consideration of worked examples e.g. from QIS 2 before forming a view on its applicability across the EU.

### *Q109: Do stakeholders have any general comments on (the description of) example 6?*

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This reflects the current IORP directive for Pillar I with the full Holistic Balance Sheet introduced only as a risk management tool in Pillar 2. The OPSG considers that the use of an HBS type framework could be useful in pillar 2, provided that costs for IORPs necessary to introduce the HBS are not excessive, compared to other simpler risk management tools that may be used at MS level which can account for country-by-country IORPs characteristics and which can be implemented with lower costs.

### *Q110: Could example 6, in the view of stakeholders, be used for all IORPs in the EU?*

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This example is closest to the existing position, and may therefore be easier to implement than a more complex approach. The existing requirements of the IORP Directive are maintained in relation to technical provisions and capital requirements (for Article 17 IORPs) but are overlaid with a more structured supervisory regime in relation to Pillar 2 /3 to assess the sustainability of the pension promise. The OPSG would require further detail of the proposed approach and consideration of worked examples e.g. from QIS 2 before forming a view on its applicability across the EU.

## **9. Possible simplifications**

### *Q111: Do stakeholders agree that there is scope for simplifications with regard to drawing up the holistic balance sheet? Which simplifications would you consider most important and in which situations?*

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The OPSG is not yet convinced by the arguments in favour of an implementation of the HBS, and will await the outcome of the consultation and the QIS before finalising its position.

If it is decided to implement such an approach, there should be a broad scope for simplifications. In this context, it would for example be reasonable to include an exemption from calculating the HBS in cases where either a comprehensive or a strong sponsor is providing for a high and thus adequate level of security.

The OPSG would also urge that appropriate simplifications be made in relation to the calculations underlying the elements of the HBS, and in particular the SCR if this were to be introduced, to reflect the characteristics of IORPs where these differ from the insurance products for which the Solvency II framework was developed.