

Comments Template on EIOPA-CP-11/006 Response to Call for Advice on the review of Directive 2003/41/EC: second consultation		Deadline 02.01.2012 18:00 CET
Company name:	Association of Consulting Actuaries (UK)	
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<p>The question numbers below correspond to Consultation Paper No. 06 (EIOPA-CP-11/006).</p> <p>Please follow the instructions for filling in the template:</p> <ul style="list-style-type: none"> ⇒ <u>Do not change the numbering</u> in column "Question". ⇒ Please fill in your comment in the relevant row. If you have <u>no comment</u> on a question, keep the row <u>empty</u>. ⇒ There are 96 questions for respondents. Please restrict responses in the row "General comment" only to material which is not covered by these 96 questions. ⇒ Our IT tool does not allow processing of comments which do not refer to the specific question numbers below. <ul style="list-style-type: none"> ○ If your comment refers to multiple questions, please insert your comment at the first relevant question and mention in your comment to which other questions this also applies. ○ If your comment refers to parts of a question, please indicate this in the comment itself. <p>Please send the completed template to CP-006@eiopa.europa.eu, in MSWord Format, (our IT tool does not allow processing of any other formats).</p>		
Question	Comment	
General comment	We thank EIOPA for the diligence and expert nature of the consultation document and the chance to respond. Whilst we understand that EIOPA were constrained by the nature of the request from the EC we would have preferred if the nature of the questions in some areas had been more open and we	

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	have made reference where appropriate below to wider issues of particular importance.	
1.		
2.		
3.	Option 1	
4.	None	
5.	<p>It is unfortunate that the question being asked of EIOPA does not have a wider scope to capture all the potential options set out in 5.2.2, but the following comments can be made:</p> <p>(a) If we look back at the spirit of the original directive, cross-border activity was envisaged to refer to situations where a sponsoring employer was in a different country from the IORP, i.e. where the sponsoring employer was using an IORP in a different country and therefore not subject to the regulation applicable to IORPs in the employer's own country.</p> <p>Therefore, the following should not be considered cross-border activity: an employer and an IORP both registered in State A with employees based in State B as well as in State A. After all, this was not cross-border activity requiring additional regulatory approval before the Directive was introduced. Instead, cross-border activity should in principle be where the sponsoring undertaking and the IORP are located in different countries, i.e. the first of the three approaches mentioned. This was the new option permitted and encouraged by the introduction of the Directive: the option for sponsoring undertakings to sponsor IORPs in countries other than their own.</p> <p>Accordingly, we support Option 2 in principle ("Amend the wording of the IORP directive to reflect the position that cross-border activity arises only when the sponsor and the IORP are located in two different Member States").</p> <p>(b) However, the situation where a small number of internationally-mobile employees are sent to work in another country on a local contract unintentionally triggers the cross-border provisions of the Directive, and this has been a constant concern of employers. (Example: employer and IORP both registered in State A, employer sends an employee to work in State B on a local employment contract with its sister company in State B.)</p> <p>It may be advisable to insert "predominantly" into the appropriate place or places in Article 20 to "carve out" situations where the number of such employees is proportionately small.</p>	

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	<p>(c) The point made in 5.3.27 and 5.3.37 (IORP and members in State A, sponsoring undertaking in State B) should be dealt with, by having an appropriate definition of "sponsoring undertaking" that would be flexible enough to be able to be interpreted as being in State A in that case (e.g. by allowing branches of a parent company to be considered to be located in the State where the employees are located).</p> <p>(d) We support the addition of a requirement that the IORP should respect the applicable social and labour law</p> <p>(e) Prior to the implementation of any option there should be a thorough impact assessment to avoid unintended consequences. An example of an unintended consequence of the position as outlined by EIOPA would be the proposed definition of 6 (c), where the suggested wording would mean that if for instance, the French parent company of a British company provided a parental guarantee to the Trustees of the British pension fund (which provided benefits only to British employees) then the fund would be considered cross-border in nature. This is likely to deter foreign parent companies from providing such guarantees, thus reducing member security which is hardly the intention of the Directive.</p>	
6.	We believe that this is largely an appropriate response, subject to our comment on question 8 below. However, we note that under item 7 dealing with administrative ring-fencing "in principle no allowance for transfer of assets" there needs to be allowance for the transfer of assets within an IORP from one section to another when an individual changes country of employment and wishes to transfer his assets and liabilities within the IORP (other situations can be envisaged). Also we note that the different interpretations of the concept of IORPs undertaking cross-border activity being fully funded at all times is not dealt with in any detail in the response and we would be keen to have EIOPA reflect on this discriminatory treatment of cross-border IORPs compared to single country IORPs (either here or elsewhere in the response).	
7.		
8.	We would be strongly against any such mandatory ring-fencing approach since it would negate many of the advantages of cross-border activity for multinational employers and consequently impact their employees.	
9.	We believe that the structure and principles of privilege rules should rest with the Member State given subsidiarity considerations.	
10.	Yes	

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11.		
12.	<p>IORPs are not insurance companies. Employers wish to remunerate their employees with pension in retirement for many reasons that have built up over the years, but including a wish to have orderly succession planning so that employees are adequately provided for at a time of life when they may be becoming less productive and they may wish to retire themselves. Other means of providing for retirement are available, but the employer-sponsored system is one that has worked well over the years.</p> <p>The employers that establish IORPs are, for the vast majority, not in the business of running insurance companies. They are not, certainly in the UK, in competition with insurance companies or each other, in that they are not trying to win IORP members from insurers or other IORPs. If the IORPs that they sponsor become subject to the full capital requirements for insurance companies, there is no doubt that the current trend away from funded defined benefit pension provision will accelerate. The replacement defined contribution schemes that are established instead lead to all investment and other risks falling on the employee.</p> <p>The difficulties with placing formal monetary value on the strength of the sponsor covenant are massively understated in the consultation. Practical experience in the UK (given the range of sponsors from asset-rich to asset-light, cash generative commercial organisations to non-profit organisations etc) demonstrates such assessments are prone either to be hugely expensive, multi-disciplinary and time-consuming exercises, or to be shallow, for example the Dun & Bradstreet analysis used for the UK Pension Protection Fund, which we assume is the arrangement referred to in paragraph 9.3.202, or incomplete, for example relying on corporate bonds or credit default swaps to give an indication of default risk, when many sponsors are not the subject of such instruments.</p> <p>Even a limited exercise such as the valuation of intangible assets such as "brand" is fraught with difficulty and subjective opinion. In addition consider for example a sponsor which has substantial free cash reserves on its balance sheet at the date of the valuation but where the parent could "sweep" the cash overnight (c.f. Lehmans, where billions were transferred to the USA very shortly (hours) prior to collapse). What is the value of such a covenant? And if you cannot legally and formally count on it, why attempt to account for it? You could very easily paint a misleadingly gloomy or rosy picture. Either would be equally bad. Consider also the difficulties of disclosure, particularly with overseas (e.g. Japanese) parent companies in private ownership, who are and continue to be wholly supportive of the IORP but which will not make (wide) disclosure of their</p>	

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	<p>management accounts?</p> <p>We would agree it may be appropriate to retain the distinction between the two types of IORP. The Article 17(1) IORPs have the greatest similarity to insurers, in that there is no external body to which they can turn for support if their assets prove to be insufficient to fund their promised benefits. Sponsor-supported IORPs can turn to the sponsor, an entity involved in producing profits, if they need support to meet members' benefits.</p> <p>In retaining this distinction, it will be necessary not to introduce any de facto end-point, where sponsor-supported IORPs ultimately have to fund as per 17(1) IORPs, owing to a contingent risk of insolvency. It is this false premise that appears to underlie the desire to impose insurance style solvency on IORPs. The primary protection against insolvency is the Pension Protection Fund in the UK, or various other insurance mechanisms in other countries. To insist that IORPs are effectively similar to insurance companies, thus compelling sponsors to move funds out of economically effective working capital and into economically ineffective risk-free assets, is misplaced, highly damaging and counter-productive.</p>	
13.	Yes but see also our response as regards reinsurance in question 20	
14.	<p>The concept of "transfer value" solvency, which assumes the need to aim for a world where a (distressed) sponsor can readily transfer its IORP in full to an insurer, is misplaced and is rejected. In practice, in the UK we have the Pension Protection Fund, meeting the requirement for insolvency protection under long-standing EU law (article 8 of the 1980 insolvency directive). This additional concept of transfer to an insurance company is inconsistent, unnecessary and overly onerous. (See 9.2.4 etc). Furthermore for decades it has been possible to transfer individuals, blocks of membership and indeed whole schemes from IORP to IORP. Portability is already enshrined in the UK.</p> <p>We would support an approach based on a transfer value only if this was the Level A in a Level A/Level B approach, where Level B was the target funding level and Level A was just provided as an item for disclosure.</p>	
15.	Yes, we agree with this EIOPA recommendation.	
16.	Our view is that where practical advantages can be gained (e.g. reducing actuarial costs to IORPs) by aligning standards then such advantages should be exploited, but accountancy standards were designed for a fundamentally different purpose to funding.	
17.	For the reasons described in our response to question 12, we believe that it is appropriate for	

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	<p>sponsor-backed IORPs to continue to be able to calculate technical provisions based on the yield on the corresponding assets held by the institution and the future investment returns, with a prudent margin. We do not support a "best estimate market consistent" calculation as Solvency II defines these terms. The wording in Article 76(3) is appropriate if the underlying calculations are redefined as we suggest, i.e. the factors allowed for in the calculations should be set taking account of market and other observable conditions</p>	
18.	<p>We strongly prefer Option 1, to maintain the current rules of the IORP Directive. This is in line with the approach successfully used for pension schemes in the UK, where technical provisions may be based on expected asset returns, with a prudent estimate of these assumptions as a risk buffer, and where there is additional protection for members through the Pension Protection Fund.</p> <p>We do not agree with the calculation of technical provisions underlying Option 2. It is unworkable because it is unaffordable. As described in the paper it will also result in volatile funding levels. It will also cause major disruption in the securities markets, with many IORPs selling equities, causing difficulties for companies in raising finance, and creating excessive demand for bonds.</p> <p>We believe a version of the Option 3 could be of interest but that it would need considerable adaption such as:</p> <ul style="list-style-type: none"> -the detailed implementation should be left to Member States (and not prescribed on a pan-European "one size fits all" basis). - "Level A" technical provisions (a new term which the consultation proposes be assessed on a risk-free basis to be prescribed in detail by the EU, a process not without difficulty in current market conditions) could in many jurisdictions simply be benchmarked to insurance buyout rates for all of the IORP's accrued non-conditional benefits as an adequate proxy, with the details left to the Member States. -Level A technical provisions would be used only as a disclosure item with no associated capital requirements. The funding target would thus be "Level B" technical provisions which, as proposed, would be assessed using a discount rate based on expected investment return, the detailed implementation of which would be left to Member States. 	
19.	Yes	
20.	Generally we agree that calculations should be based on the gross benefit and with sums recoverable from elsewhere shown separately. But this should be subject to proportionality and accuracy considerations, for example permitting the net position to be shown where the expected cashflows by	

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	an IORP are matched by payments to the IORP from a regulated insurer or allowing the value placed on such assets to be consistent with the market (not based on a surrender value).	
21.	<p>The use of a risk-free interest rate will, in the UK, in most cases result in a significant increase to the technical provisions calculated, as they are currently, based on a prudent estimate of future investment returns. Plan sponsors have alternative options, either to adopt unfunded book reserve pension plans, or to move from defined benefit to defined contribution pension plans. Both of these moves will result in a reduction to the level of financial security provided to employees, compared to the existing situation where defined benefits are funded.</p> <p>Not only would risk free rates have (potentially disastrous) economic consequences, the rationale for their use is wholly misplaced as IORPs are not insurance companies, do not compete for pension "business", and, in the UK for instance, benefit from an adequate protection mechanism (the Pension Protection Fund).</p>	
22.	<p>We believe that the word "expenses" here refers to the costs, in addition to the payments to IORP members, which are incurred in operating the IORP. For an Article 17(1) IORP, the assets of the IORP clearly need to cover expenses as well as pension payments, and so projected expenses should be included in technical provisions. For a sponsor-backed IORP, where sponsor contributions can be increased to cover rises in expenses, we see less need to include future expenses within technical provisions.</p> <p>It is worth noting that the International Accounting Standards Board has recently finalised its update to the international pension accounting standard for companies, IAS19. After extensive discussions, the Board's final version of IAS19 does not require companies to include expenses in the Defined Benefit Obligation (the value of the company's accrued pension obligation), but instead includes them either, in the case of investment expenses, within a net investment return figure, or in the case of other expenses, recognizes them in profit as they are incurred.</p>	
23.	<p>This question further exposes the major differences between IORPs and insurers. An IORP can be set up with benefits that are</p> <p>fully unconditional, or</p> <p>conditional (possibly conditional on internal factors such as actual IORP investment returns, or on external factors such as the performance of an investment index), or</p> <p>discretionary (with varying possible degrees of discretion e.g. with the sponsor and/or trustees having unfettered discretion, or with a well-established practice that discretion is almost invariably</p>	

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	<p>exercised, or perhaps with a customary exercise of discretion where there are surplus funds available)</p> <p>It is noteworthy that some of the types of discretionary benefits that are offered by IORPs would not be offered by insurers (e.g. salary linkage), and that the parallel between the two types of institution is stretched to a point where it is difficult to apply the same rules to both types.</p> <p>We think that this is an area where there are significant differences in practice between different IORPs and between different Member States. We think that there is value in using the IAS19 term "constructive obligation". Informal practices give rise to a constructive obligation where the entity has no realistic alternative but to pay employee benefits. An example of a constructive obligation is where a change in the entity's informal practices would cause unacceptable damage to its relationship with employees.</p> <p>A suitable structure might run as follows:</p> <p>IORPs are required to include unconditional benefits in their technical provisions, including any benefits that arise out of a constructive obligation</p> <p>They would be required to disclose the existence of any other discretionary benefits in the report on technical provisions, with the value of these additional benefits that would be paid if the discretionary practices continued.</p> <p>The supervisory bodies in each Member State would have freedom to introduce specific rules on top of this to reflect local circumstances, for example to deal with specific exercises of discretion that are unique to that country.</p> <p>It would be counter to social objectives to require IORPs to include all discretionary practices in technical provisions. One of the reasons for adoption of discretionary practices is that it gives the employer the option not to exercise discretion, for example in years with poor profitability. As things stand, employers sometimes exercise discretion: if the company is required to make a significant addition to its technical provisions, one can be sure that the discretionary practice will stop.</p>	
24.	We agree that guarantees and options should be taken into account in calculating technical provisions.	
25.	We believe that benefits within an IORP are typically more homogeneous than the liabilities of insurers. We see value in separating out components of the technical provisions where the underlying risks are substantially different (e.g. within a plan with DB and DC sections). Any such	

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	introduced requirement must be subject to proportionality / materiality considerations. Overall, while this segmentation has meaning within the context of a multi-line insurance company, it has little meaning within the context of many IORPs.	
26.	As stated above in question 20, we believe that there is no value in including IORP liabilities in a calculation of technical provisions where these are matched by contracts with a regulated insurer. Subject to this amendment, we have no difficulties to include gross liabilities and reinsurance as separate items in the IORP's calculations.	
27.	Yes	
28.	Yes as a measure of the effect of experience diverging from actuarial assumptions, and as information that may be relevant for adjusting future actuarial assumptions. However proportionality is key here, with, for example, little point in detailed mortality analysis where, because of the size of the IORP, no credible conclusions can be drawn from this analysis.	
29.	Yes, subject to the overriding requirement for implementation of the rules to be proportionate.	
30.	Yes, provided that this power is to be exercised by the supervisory authority in each Member State.	
31.	<p>We agree with EIOPA that there may be a need for Level 2 implementing measures, but that this depends on the wording of the new IORP directive. We suggest avoiding or minimizing the extent of Level 2 guidance where possible and ensuring that there is open process in determining and reviewing such measures.</p> <p>As is apparent from this consultation, there are different designs of IORP in different Member States. An attempt to set detailed rules centrally is doomed to failure – without familiarity with the local position, there is far too great a risk of introducing rules which are at best inappropriate and at worst positively harmful to local IORPs. Our preferred position would be for a new IORP directive to be principles-based, with implementation by the local supervisory authority in each Member State, and with oversight and experience sharing within EIOPA, with the aim of identifying any problematic inconsistency of approach between Member States.</p>	

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32.	Given the issues about differences in IORP design between Member States, we suspect that there will need to be some additional guidance by each Member State to deal with specifically local issues.	
33.	<p>We notice that the relevant conclusion section in the EIOPA consultation, paragraph 9.3.223, does not contain an impact assessment.</p> <p>As described in our response to question 12, the "holistic balance sheet" as proposed is, in practice, unworkable. The difficulties with placing formal monetary value on the strength of the sponsor covenant are massively understated in the consultation. Practical experience in the UK demonstrates such assessments are prone</p> <ul style="list-style-type: none"> - either to be hugely expensive, multi-disciplinary and time-consuming exercises, - or to be shallow, for example the Dun & Bradstreet analysis used for the UK Pension Protection Fund, which we assume is the arrangement referred to in paragraph 9.3.202, - or to be incomplete, for example relying on corporate bonds or credit default swaps to give an indication of default risk, when many sponsors are not involved in such instruments. <p>Even a limited exercise such as the valuation of intangible assets such as "brand" is fraught with difficulty and subjective opinion. In addition consider for example a sponsor which has substantial free cash reserves on its balance sheet at the date of the valuation but where the parent could "sweep" the cash overnight (c.f. Lehmans, where billions were transferred to the USA very shortly (hours) prior to collapse). What is the value of such a covenant? And if you cannot legally and formally count on it, why attempt to account for it? You could very easily paint a misleadingly gloomy or rosy picture. Either would be equally bad. Consider also the difficulties of disclosure, particularly with overseas (e.g. Japanese) parent companies in private ownership, who are and continue to be wholly supportive of the IORP but which will not make (wide) disclosure of their management accounts?</p> <p>Finally we would note that there is no evidence that the current UK system of covenant assessment is so flawed as to require an EU approach to be prescribed.</p>	
34.	No. "Own funds" is not a concept that maps onto many IORPs, particularly sponsor-supported IORPs in the UK. The sponsor has a legitimate interest in any "excess" funding, particularly because it can be (to an extent) symmetrical to its acceptance of the risk of underfunding. We have already made the point that the IORP is not and does not bear comparison with an insurance company. The	

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	<p>sponsor does not bear comparison with the insurer's shareholders. The undertaking (of providing pensions) is not a competitive one. A risk-free SCR, above which own funds can be defined, is inappropriate. By extension therefore, the concept of own funds itself is inappropriate within the context of an IORP with sponsor support.</p>	
35.	<p>Yes, with suitable protection from potential abuse, and clarification of the interplay with the Employer Related Investment requirements in the UK for instance.</p>	
36.	<p>To impose a blanket solvency level on all IORPs risks being either:</p> <ul style="list-style-type: none"> -meaningless (so low as to be worthless for a number of Member States) -damaging (so high as to cripple sponsors and cause lasting economic damage by diverting capital away from economic growth and into risk-free investments, simultaneously causing long term overall lowering of pension provision) <p>We have also pointed out that such an approach may be practically impossible and inappropriate (due to the entirely different nature of the "external" mechanisms for protection such as the Pension Protection Fund, other insurance arrangements, ability to reduce benefits, conditional or discretionary funding etc).</p> <p>Finally it should be borne in mind that most IORPs are very small compared with any insurance company, and it is wholly disproportionate to compel (most) IORPs into a system that makes them value such mechanisms as part of a solvency assessment.</p> <p>It is not so much that we agree that EIOPA should not be recommending a specific probability at this time. It is more that we believe the whole concept of a specific pan-European harmonised "probability" is inappropriate.</p>	
37.	<p>We refer to the answer to question 36 above.</p>	
38.	<p>As we mentioned as part of our response at question 36 above, the concept of taking account of specific security mechanisms (such as the "value" of the Pension Protection Fund) is wholly disproportionate. The majority of IORPs are small and were established by small businesses to provide pensions for a small workforce. The level of complexity envisaged in requiring each IORP to take such mechanisms into account on a prescribed footing is unworkable at a practical level.</p>	

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	Ultimately, limited funds are available to sponsors to fund pension commitments, and any additional regulatory burden will inevitably reduce funds available to secure members' benefits.	
39.	Subject to our comment above, assessing technical provisions on a three year cycle with annual (approximate) updates for larger schemes seems sensible.	
40.	An additional mandatory triggering level would be excessive and disproportionate in the case of many IORPs.	
41.	It is correctly observed that "valuation of security mechanisms is a complex issue". Introducing such complexity into the funding regime of IORPs is likely to be very burdensome. Inclusion of the value of the Pension Protection Fund to a given IORP as a standalone asset on anything other than a wholly simplistic basis would be hugely time-consuming. Inclusion as a reduction to insolvency risk presupposes that the insolvency risk is readily quantifiable (which it is not for many IORPs). Overall, we do not see an implicit or explicit valuation of such assets as a proportionate and workable element of a prudential supervision regime.	
42.	As regards DC schemes, the calculation and maintenance of a reserve to cover operational risk adds significantly to frictional costs. In the UK, the logical consequence is for the sponsor may be to move to a contract basis where this reserve is "implicit" and is in fact paid for by members by way of lower returns, thus losing all the advantages of trustee oversight.	
43.	<p>We agree that monitoring the financial position is as important for IORPs as it is for insurance companies; however, the objective is different, as is the recourse to additional finance, the appropriate timescales for rectification and the motivation for providing the pension in the first instance.</p> <p>For UK IORPs this monitoring objective is in practice met at present via proper internal controls and governance mechanisms, and more formally as a result of the required actuarial valuation reporting cycle. If such a monitoring process were also to be more formal and continuous, it would indeed potentially be an extra administrative burden on IORPs and supervisors.</p> <p>Having potentially thousands of IORPs reporting to the supervisor on market downturns would serve</p>	

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	<p>no purpose.</p> <p>It is therefore optimal to have supervision defined at Member State level, on a risk-based approach as appropriate to the size and nature of the IORPs within that Member State. This relates not only to triggers and ongoing monitoring requirements, but also timescales and appropriate lengths and contents of recovery plans (having regard to the need to protect jobs within the sponsor).</p>	
44.	<p>It is vital given the number and diversity of IORPs and sponsors, given also the potential impact on jobs and the economy, that flexibility (including that related to length of recovery period) is retained. Inflexibility could result in an avoidable insolvency and loss of employment. A risk-based approach needs to be taken, on a case by case basis, bearing in mind the sheer numbers of IORPs under discussion.</p>	
45.		
46.	<p>Proportionality should apply. Specifying that all IORPs must produce recovery plans including revenue accounts and a forecast balance sheet as well as the resources which are intended to meet the technical provisions is unnecessarily inflexible. Such plans are subject to actuarial oversight as well as supervisory oversight at Member State level. Such calculations may well form a part of the underlying actuarial calculations, but prescribing that they appear on the face of the recovery plan itself adds no value.</p>	
47.	<p>In our view the existing prudent person principle is sufficient. However it is essential that the regulations make clear that it is permissible for an IORP to delegate some of the risk measurement and controls to third parties. If additional requirements were imposed this would likely create the adverse consequence of plans below €1bn having insufficient internal resource to invest in more complex asset classes and this is likely to result in higher levels of risk taking and/or lower levels of investment return, due to inability to access the full range of investments.</p>	
48.	<p>In general we would be of the view that a single set of investment restrictions should exist at a European level. This reflects that any restrictions at Member State level, particularly for host Member States, will certainly be a considerable barrier to the widespread creation and adoption of cross-border schemes.</p>	
49.	<p>In a DC context it is important that regulations differentiate between schemes where plan members bear all of the investment risk, and those where some risks are borne by the sponsor. We observe</p>	

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	that best practice provision within the DC marketplace has evolved significantly in the past few years and it would seem to us that well intentioned regulations to encourage adoption of current best practices for default funds and lifestyling approaches within multifund IORPs could have unintended consequences should newer techniques and methods emerge.	
50.	<p>Broadly speaking we agree with the analysis presented by EIOPA in its advice. We draw your attention to the following additional comments and views on the options presented:</p> <p>7.1- in relation to Article 132(2) - Our strong preference is for Option 3 to be adopted, given that an IORP is typically likely to be smaller in size than an insurer and therefore would often delegate some of the risk measurement and control processes to third parties. Additionally, the regulations should apply to DC schemes only where relevant.</p> <p>7.2 – in relation to Article 18(1)(f) - Our view is that a form of Option 2 would be desirable. A possible approach might be to introduce the clarification that for multi-sponsor DB schemes sponsor-related investment should be limited to 5% of total assets per sponsor and 10% of total assets across all sponsors.</p> <p>7.3 – in relation to Article 18(5) - Our strong preference is for Option 2 to be adopted. This would create a level playing field cross-border for sponsors. Also, whilst Option 3 might appear appealing from a member protection perspective we consider that it will ultimately limit the creation and adoption of cross-border DC pension schemes.</p> <p>7.4 – in relation to Article 18(5)(b) -We favour Option 2. From an investment perspective, a further reason for permitting overseas assets to be held, and which is not mentioned in the consultation paper, is that assets denominated in overseas currencies can provide a valuable hedge against domestic market stresses, in circumstances where holding domestic assets could expose an investor to losses (e.g. very high inflation or fiscal concerns leading to devaluation relative to external currencies, etc). In our view this argument is also a valid reason to reject Option 3 as compulsion in hedging currency risks would remove a key “tail risk” mitigation device for pension scheme investors.</p>	

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7.5 – in relation to Article 18(5)(c)- We favour Option 2. We agree that the current provision is unclear, but furthermore, the current provision if interpreted literally would discourage or prohibit pension schemes from investing directly in unlisted assets that enable them to participate in the wider economy, such as infrastructure or real estate. This would likely lead to greater inefficiencies in capital allocation in the wider economy as pension schemes are well placed to invest in such assets, subject to suitable diversification, due to their long time horizons and low requirement for liquidity.

7.6 – in relation to Article 18(6) – No response.

7.7 – in relation to Article 18(7) - We favour Option 2, to reduce impediments to the widespread creation and adoption of cross-border schemes. In our view the additional member protections achieved by Option 1 are likely to be minimal.

7.8.1 – in relation to Article 132(3) - Option 3 is to be favoured on the grounds of ensuring consistency (whilst maintaining subsidiarity principles), however, if adopted there would be significant disincentives to the creation of hybrid schemes. Therefore if the creation and promotion of hybrid schemes is considered desirable EIOPA should favour Option 1, however if consistency is paramount then Option 3 would be more appropriate.

7.8.2 We favour Options 1 and 4 from a consistency perspective, and, to reduce impediments to the widespread creation and adoption of cross-border schemes. However, Option 4 seems to have the unintended effect of incentivising DC schemes and sponsors not to offer a default fund or lifestyling, which seems contrary to member interests. We also note that the DC marketplace is constantly evolving and it would seem counter-productive to us to try and inhibit adoption of new superior practices by putting additional restrictions on default funds and lifestyling approaches within multifund IORPs that are based on historic considerations of what best practice constituted at the time of drafting the regulations.

7.8.3 and 7.9 - We agree with EIOPA that no further regulation in these areas is desirable at the present time.

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	7.10 We favour Option 1 as regards valuation of derivatives on the grounds that the prudent person principle provides meaningful protection to scheme members. Furthermore, the principle is robust to changing perceptions of what constitutes best practice, whereas more prescriptive regulation may have the unintended negative consequence of limiting portfolio flexibility.	
51.	We agree with EIOPA that the current prohibition on borrowing is on balance desirable, provided clarity is provided that only direct borrowings are covered by the scope of the prohibition. One counterargument to this view is that an IORP may wish to make use of short-term overdraft facilities for reasons of efficient portfolio management, for example in anticipation of an incoming cashflow, or to avoid selling securities and incurring transaction costs, and a restriction on borrowings would restrict an IORP's flexibility with regard to liquidity management.	
52.		
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55.	We agree that the above recommendations are sensible, as long as additional burdens on IORPs are avoided/minimised in the normal course of events.	
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57.		
58.	No. The home state is the supervisor of the IORP and should be responsible for enforcing its regulation and to require "double" regulation will act as a substantial barrier to the development of cross-border plans.	
59.	<p>We agree that Member States should have a supervisory review process which is proportionate and spans to the diverse nature of IORPs within that Member State. There is clear public interest in (the existence and effectiveness of) such a process.</p> <p>We believe that prescribing the supervisory review process at European level could result in significant inefficiency. Member States should be capable of developing a satisfactory, robust supervisor, which can specify solvency, governance, reporting and internal control mechanisms on a risk based and proportionate basis. The sheer number of IORPs and the diversity of the social</p>	

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	legislative frameworks within which the IORPs provide pensions merely reinforces this argument.	
60.	<p>We agree that the supervisor ought to have capital add-on powers. However, we do not agree that the regime for insurers should be imported onto the IORPs' supervisors. The insurers' supervisor deals with a (relatively) small number of (relatively) large commercial organisations. It is not unreasonable for the insurance supervisor to retain teams of actuaries and other experts to provide a high degree of challenge to each and every insurer, particularly in the extreme case of capital add ons. If this regime were directly imported or translated onto the tens of thousands of IORPs it would be practically unworkable and counter-productive.</p> <p>It is essential that any capital add-on regime for IORPs is proportionate both to the scale of the problem, and to the desired scale of the supervisor itself. The mechanism should be determined at Member State level.</p>	
61.	We would be strongly opposed to the rules for IORPs on outsourcing for pension funds being the same as those for insurers on the grounds of proportionality and increased cost/inefficiency. The proposed requirements would add very significant additional cost to the administration of pension funds. Furthermore, the lack of any clear definition of "outsourced services" makes the provision unworkable (does the provision of say, communication consultancy services to a pension fund constitute outsourced services, if yes, what of the printing of a booklet?) These would need to be more tightly defined and any rules restricted to core identified areas.	
62.	We would be strongly opposed to such rules on the grounds that it would effectively preclude IORPs from choosing to purchase their outsourced services in the most cost-effective way within the common constraints and protections of civil and criminal law. This would make IORPs unable to compete with insurers with their larger buying power to meet the costs of compliance. Once again by effectively precluding the provision of say, actuarial or computing services from a non-EEA state such a provision would simply add to costs without in any way improving the security of members or aiding effective governance.	
63.	We agree with the general recommendation that IORPs should adopt the material elements of Solvency II for governance subject to proportionality. What is proportional must be clearly spelt out in level 2 text. The average IORP is significantly smaller than the average insurer. For example, a significant number will have no individual employed full-time in running the IORP. It will be better	

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	<p>for an IORP to undertake a limited number of carefully chosen focussed governance activities than to have a long list covering issues that have little relevance for the specific IORP, documented in boilerplate language and with little substantive governance activity underpinning the list.</p> <p>Remuneration policy is a case in point. In the UK, for example, it is common for trustees of the IORP either to be unremunerated, or for remuneration to be paid directly by the sponsoring employer at no cost to the IORP. In these circumstances a remuneration policy has no relevance, and the time spent producing this piece of paper could be much more usefully spent elsewhere.</p>	
64.	We agree that member participation and remuneration policy are examples of areas where IORPs and insurers differ. A full list of these areas needs to be developed as part of the impact assessment of the proposed new arrangements.	
65.	This response also addresses the issues raised in question 66. We agree that fit and proper requirements should be adopted for IORPs. However, the text of the EIOPA commentary appears to envisage the supervisor taking significant direct responsibility for monitoring the status of all those with significant functions within an IORP, perhaps maintaining a database of individuals. This sounds like a highly bureaucratic process, with significant cost issues given the large number of IORPs compared with insurers. We think that risk-based monitoring by the supervisor coupled with a clear statement by the supervisor of the fit and proper requirements that must be met, to be monitored by the IORP, would be a far better use of resources.	
66.	We agree that fit and proper requirements should apply at all times. Our response to question 66(b) is included in our response to question 65.	
67.	<p>We agree that the supervisor should have appropriate powers to take action to enforce the fit and proper requirements. The most important of these is the power to remove and replace individuals who are not fit and proper. Other sanctions may be appropriate if, for example, an individual has lied about significant issues to obtain their appointment.</p> <p>Any system that is put in place must be proportionate, must be capable of being appealed, and must not having the same organisation acting as "judge, jury and executioner".</p>	
68.	We agree with the overall purpose of the proposal to have a risk-management system that addresses all risks. However, some small alterations must be made to the list for insurers to make them	

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	<p>relevant to IORPs. For example, many IORPs will be obliged to accept all employees of the sponsoring employer as members, regardless of their state of health. For that reason, underwriting is a far less relevant issue than it is for insurers. If the main headings are not changed, there is a risk that management time will be wasted addressing issues that are of marginal relevance.</p> <p>We suggest the following revised list could act as a basis:</p> <p>(a) evaluation of technical provisions (b) asset–liability management; (c) investment, including derivatives and similar commitments, liquidity and concentration risk management; (e) operational risk management (including data management); (f) insurance and other risk-mitigation techniques, including underwriting if relevant</p> <p>During the impact assessment phase of this project, we strongly recommend an assessment of the requirement to manage risk “on a continuous basis”. As pointed out earlier, many IORPs do not have any full-time employees or other individuals who are capable of managing all aspects of risk on a continuous basis. In practice, a risk management plan might include some or all of:</p> <ul style="list-style-type: none"> • Reporting to trustees or a management board on key activities at their regular meetings • Whistle-blowing responsibility for individuals involved in the management of some scheme activities who discover significant issues at any time • If considered relevant by the trustees or board, the breach of pre-set triggers that have been set by the board or trustees, for example in relation to significant movement in investment markets, or significant events in relation to the sponsor (eg M&A activity, insolvency). <p>Finally, although proportionality is a difficult concept within the topic of risk management we would ask that the impact on smaller schemes be particularly studied and would note that there be a need for supervisors to assist and guide schemes in this area (for instance by supplying standard documentation).</p>	
69.	It is difficult to object to the underlying principles behind ORSA. Those responsible for running an IORP should be aware of the risks that would have a significant effect on the IORP, avoid risks in	

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	<p>areas which would have a serious detrimental effect on the IORP, monitor and react to risks which cannot be avoided or are necessarily incurred as part of a risk-taking strategy that is expected to be beneficial to the IORP (e.g. equity investment).</p> <p>The problem with ORSA as laid out for Solvency II relates to the scale of typical IORPs. Many defined benefit IORPs, with assets that may be under Euro or GBP 100 million, simply do not have the resources to operate ORSA with continuous monitoring that Solvency II requires.</p> <p>For employer-sponsored IORPs, the risks may be small when compared to the size of the sponsoring employer. This is not intended as a rejection of the principles of ORSA in all circumstances. There are IORPs sponsored by a weak employer, where risk-taking by the IORP is not affordable. But our concern is that a blanket requirement to perform ORSA in all circumstances is inappropriate, will become a box-ticking exercise and a wasteful use of IORP resources for many.</p> <p>Our strong preference is for risk assessment to be a scheme-specific exercise, where the IORP, overseen by its national supervisor, undertakes risk assessment activity that is appropriate for the risks that the IORP faces. We certainly think it appropriate for supervisory bodies to give guidance on the scope of assessment, but a standard approach for all would be unnecessary.</p> <p>This may seem an odd comment coming from the Association of Consulting Actuaries, whose members stand to gain additional work in supporting ORSA. However, we believe that it is in the long-term interests of the pensions industry and, frankly, ourselves that IORPs should not be saddled with additional costs and take up management time and resources on activities that will be inappropriate for many.</p>	
70.	<p>There are a number of risks, other than operational risks, that are specific to IORPs where members bear all the risks. We suspect that ORSA will not give these the prominence that they deserve.</p> <p>For defined contribution schemes, on top of operational risks such as delivering the investment returns intended, these include:</p> <ul style="list-style-type: none"> Benefits being inadequate for the member's objectives, either because of inadequate contributions or inappropriate investment Members being unaware of investment risks and making inappropriate investment choices Members making inappropriate decisions when converting their fund to a retirement pension, typically via an annuity purchase 	

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	Other scheme designs will have other risks specific to their design. For example, the managers of Collective Defined Contribution schemes in the Netherlands, which share pension risks between different generations of members, are likely to want to set a limit on the extent to which risks are transferred in this way. Any risk assessment needs to focus on these kinds of risks that are relevant to the members of the IORP.	
71.		
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76.	<p>EIOPA rightly recognises that that it is the board or trustees of the IORP who are ultimately responsible for making decisions relating to the funding of a pension scheme. It is therefore essential that any amendments to the IORP directive in respect of the actuarial function recognise that the role of the actuary is limited to providing calculations and advice to the board/trustees.</p> <p>We also agree with EIOPA's conclusion that there should be no requirement for pure DC schemes to have an actuarial function. However, actuarial skills are relevant to the projection of future events under such pure DC schemes, notably in relation to the projection of assets, risks and expected outcomes.</p> <p>It should be noted that the role and duties of the actuarial function may currently arise from a number of different sources, both technical and professional. For example, in the UK, actuaries must abide by:</p> <ul style="list-style-type: none"> • UK legislation which requires certain work to be carried out by actuaries (including the valuation of pension schemes in a number of different contexts and the calculation of the debt incurred by an exiting employer) and which requires actuaries to blow the whistle in certain situations; • Codes of practice and guidance from the Pensions Regulator as to the carrying out of the roles prescribed in legislation; • Technical standards prescribed by the Board for Actuarial Standards; • Professional conduct standards ('The Actuaries' Code') prescribed by the Actuarial Profession (the 	

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	<p>Institute and Faculty of Actuaries) and other guidance on professionalism issues, such as whistle-blowing;</p> <ul style="list-style-type: none"> Any requirements specified in the deed and rules governing the specific IORP: for example, some scheme rules require certain activities (such as calculating transfer values) to be carried out by actuaries where there is no legislative requirement for this. <p>Although all of these items cover aspects of the role and duties of the actuarial function, we do not believe that the revised text of the IORP directive should cover all these requirements. In particular, it is not necessary that the professional responsibilities of the actuarial function should fall within the scope of the IORP directive.</p>	
77.	<p>The role of the actuary in insurance undertakings and IORPS are very different and we question the extent to which it is practical to use Solvency II as a starting point. If it is so used, we believe further amendment is required to that proposed in EIOPA's draft advice.</p> <p>As noted below, the text of Solvency II incorporates some elements which are currently prescribed through Technical Actuarial Standards rather than by legislation, and would therefore be redundant in the UK at least. We note, however, that other Member States may not currently have a framework equivalent to our Technical Actuarial Standards and therefore that the specification in a revised IORP directive may have greater impact on other jurisdictions.</p> <p>In particular, looking at the paragraphs in Article 48 of the Solvency II Framework Directive:</p> <ul style="list-style-type: none"> (a) we have no objection to this wording per se, although we do not see what is wrong with the wording 'computed and certified by an actuary' in Article 9 of the current IORP directive; (b) we agree that the change from 'ensure' to 'assess' is required to reflect the fact that actuaries are not responsible for setting the assumptions for calculating technical provisions; however, should there also be a requirement for them to 'advise the IORP' on the appropriateness of the method and assumptions? (unless that is intended to be covered under (e)); (c) we agree that assessing the sufficiency and quality of the data used is a key actuarial duty; we note, however, that in the UK this is achieved by means of the Technical Actuarial Standards governing actuarial work rather than by prescribed legislative requirements; (d) we have no objection to the principle of comparing the assumptions used at previous valuations with experience; however, we note that that the precise wording of this sub- 	

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	<p>paragraph would depend on the decisions taken about valuations and best estimates elsewhere in the revised IORP directive;</p> <p>(e) we are not sure whether this sub-paragraph is intended solely to cover whistle-blowing to the supervisor (or also to cover reporting to the board/trustees of the IORP); further redrafting may therefore be required;</p> <p>(f) this sub-paragraph (on overseeing the calculation of technical provisions in the event that approximations have to be made) seems unobjectionable;</p> <p>(g) this seems irrelevant in an IORP context (at least in the UK), and it is not clear why it should be retained; however, the wording 'where applicable' is adequate;</p> <p>(h) seems appropriate;</p> <p>(i) in the event that such a risk-management system is applied to IORPs (which we discuss elsewhere in our response), we believe that this does fall within the specification of the actuarial function. However, the actuary is unlikely to have any direct role in the 'effective implementation' of the risk management system and so we would expect that some amendment of this sub-paragraph may be necessary.</p>	
78.	<p>We agree in the independence of the actuarial function from the IORP, although noted that this should not preclude the actuary being an employee of the IORP or its sponsoring employer. We note however that this is often achieved by means of actuaries being required to adhere to professional conduct standards, which may prescribe rules in respect of conflicts of interest, and therefore question whether any further requirement is needed under the IORP directive.</p>	
79.	<p>We do not see that any evidence has been put forward to suggest that standardising the actuarial function will 'alleviate cross-border activity'.</p> <p>As noted above, in some Member States, such as the UK, there are already sufficient regulatory requirements applying to the actuarial function such that the negative impacts identified from the 'no change' option are not applicable.</p> <p>We agree that the proposals would have little practical impact in terms of the overall scope of the actuarial function in the UK. This does not mean, however, that the change would be cost-free; actuaries would need to review all aspects of their work to be comfortable that what they had done previously will still comply under the amended regime, and might need, for example, to update their</p>	

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	reports to the new definition of actuarial function, replacing references to Technical Actuarial Standards to the relevant legislation.	
80.	Yes (subject to comments above as regards CfA 12)	
81.		
82.		
83.	We favour Option 1 under 26.4.1(i) in that this option would recognise the distinction between a sponsor-supported pension scheme and a regulated insurance undertaking, subject to Member State regulation. In particular we feel it is important to recognise that in trust-based schemes the trustees already carry out the oversight function and the appointment of a depositary would result in duplication and unnecessary costs being imposed on such schemes. Additionally we are not in favour of providing Member States with the ability to prohibit free disposal of assets, and would consider this to be an impediment to the functioning of cross-border schemes.	
84.	We broadly agree with EIOPA's assessment of the impacts of the proposals, although have concerns in relation to the costs of compliance, particularly for schemes below €500m in assets. We also note that the custody / depositary market has high barriers to entry due to the required investment in IT infrastructure to enable successful provision of these services.	
85.	We note that for smaller schemes below €500m, some of the costs of compliance with the depositary requirements could be significant and discourage provision of pension schemes by sponsors. This is both in terms of a) safe-keeping of assets and b) oversight functions. This may suggest alternative approaches be sought on proportionality grounds.	
86.	The list of requirements appears reasonable, although we have concerns in relation to compliance costs for schemes below €500m in assets.	
87.		
88.		
89.	This response addresses questions 89 and 90. With the variation of different IORPs that exist in the European Union, with different models prevailing in different Member States, we do not believe that a single detailed list of information is appropriate. It is appropriate for the IORP Directive to describe themes and issues that could be covered by provision of information requirements, but to leave the detail around this to the	

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	supervisors in the Member States.	
90.	See Question 89	
91.	No – current DB disclosure minimum standards are appropriate and do not need to be extended	
92.	We would concur with EIOPA in the rejection of the replication of the KIID approach for the same reasons as stated. We would welcome the introduction of standardised minimum information contents within a KID for DC schemes to ensure clear participants throughout the EU. However, we do not believe that the introduction of any standard KID document would be appropriate in that if there is a “standard” document this may essentially become the common approach and would stifle creativity in the way in which good employers and IORPs seek to communicate to their employees/members. This is consistent with our belief that the most important issue is to communicate members’ choices and entitlements, rather as is the case with UCITS , to aid comparisons between entities.	
93.	We do not believe that these items should be specified within any EU-wide legislation or regulation. However, we believe it essential that IORPs should always be allowed the ability to allow for longer-term differences in return and volatility in relation to asset classes when communicating to members.	
94.	Yes as regards a requirement for annual statements for DC (or similar) plans (only for DC, since DB entitlements often do not change significantly from year to year – for example for deferred pensioners) and that those “DC” statements should contain information on charges/costs. The detailed format of such statements and the treatment of ante and actual costs should, we believe, be left to local regulators to decide on the principle of subsidiarity and given national differences in the regimes concerned (e.g. the degree to which choice is given, the state of development of existing local IORP disclosure regulation and local preferences for type of communication). For instance, it would not be appropriate to apply a UK-style SMPPI document structure to a Spanish Qualified Pension Plan where employees have no choice of funds.	
95.		
96.	No – we believe that there will be considerable costs associated with any KID implementation. Even the best run IORPs may not include all the information set out in EIOPA’s draft response on page 505 in that particular document. Some may use websites, scheme booklets rather than a KID-type document, or split the information between this and a KID. A much more rigorous impact assessment would need to undertaken to determine the costs to IORPs of such implementation.	

