	Comments Template on **Discussion Paper on Sponsor Support Technical Specifications**	**Deadline** **31 October 2013** **18:00 CET**
Name of Company:	Dexia Asset Management	
Disclosure of comments:	Please indicate if your comments should be treated as confidential:	Public
	Please follow the following instructions for filling in the template: ⇨ Do **not** change the numbering in the column "reference"; if you change numbering, your comment cannot be processed by our IT tool ⇨ Leave the last column empty. ⇨ Please fill in your comment in the relevant row. If you have no comment on a question, keep the row empty. ⇨ Our IT tool does not allow processing of comments which do not refer to the specific numbers below. **Please send the completed template, in Word Format, to DP-13-001@eiopa.europa.eu** **Our IT tool does not allow processing of any other formats.** The numbering of the questions refers to Discussion Paper on Sponsor Support.	
Reference	**Comment**	
General Comment	Dexia Asset Management welcomes the opportunity to comment the discussion paper on sponsor support technical specifications. We would like to express again that prudential regulation cannot be treated in isolation from national Social and Labour Laws. A prudential regulation not fit to the actual pension environment would make IORPs costly and inefficient. Employer could be further deterred from providing occupational pensions.	

	On the political context, the review of the IORP directive is at a standstill. The Quantitative Impact Survey also shown important biases and limitations in the Holistic Balance Sheet (HBS) framework. Moreover, most of the HBS is based on the Solvency II principles, a directive which content is still discussed and implementation date is again postponed. As long as no political agreement is reached, we believe the project should come to a halt in order to avoid the costly regulatory uncertainty we are witnessing on the Solvency II directive. In general, the case for using Solvency II principles for IORPs still has to be made, with regard to the HBS design. Firstly, the focus on market valuation of IORPs balance sheets raises lots of issues. The relevance of such valuations for IORPs balance sheet is debated in the Netherlands. Though it is aimed at increasing transparency and reducing reliance on arbitrary and risky estimates, we firmly believe that - It is impossible to have reliable market data for long term maturities instruments - Market valuation can be distorted by supply and demand imbalances and foster pro-cyclical behaviour - Deviation from market valuation could be undertaken on a reasonable basis in a transparent manner without using unreliable assumptions Secondly, the possible supervisory responses are ill-defined. The measures of shortfall are numerous - Financial assets vs. level B technical provisions - Financial assets + security mechanisms vs. level B technical provisions	

	- Financial assets vs. level A technical provisions - Financial assets + security mechanisms vs. level A technical provisions - Financial assets vs. level A technical provisions + minimum capital requirement - Financial assets + security mechanisms vs. level A technical provisions+ minimum capital requirement - Financial assets vs. level A technical provisions + solvency capital requirement - Financial assets + security mechanisms vs. level A technical provisions+ solvency capital requirement. A too strong complexity of the balance sheet can only give rise to confusion and go against the purpose of transparency and enlightened decision processes. We do not believe it is possible and necessary to express the value of sponsor support in monetary units. A qualitative assessment would be more useful than a figure in order to estimate whether or not the IORP is at risk on the sponsor support. Breaking down security mechanisms into various different components is difficult and artificial since they are all included in collective arrangements with a broad range of stakeholders - Risk and cost sharing, with for instance increase in employee contributions - Pension Protection Schemes - Benefits reduction mechanisms - Last-Man Standing principle in some multiemployer schemes. The discussion paper on sponsor support technical specifications provides interesting ways to cope with issues related with credit ratings. However the proposed ways to handle industry wide schemes and sponsors of several IORPs are not clear. Within the proposed framework, the reliance on accounting data is now very strong. It raises the	

	issues of - confidentiality (especially in the case of multiemployer schemes, sponsors of several IORPs, pension schemes with state support) - backward looking assessment - availability of data - comparability between economic sectors and countries. In this context we welcome EIOPA states IORPs should use their judgement and come with their own estimate of sponsor strength when possible and useful. The proposed approach could be simplified. For example, for sake of simplicity, EIOPA could assume that a medium strong sponsor covers 100% of the shortfall instead of 98.8%. It looks clear from the table of sponsor support value in function of its strength that the only cases that matter are the weak and very weak sponsors, and, to a much smaller extent, medium sponsors. A possible simplification of the alternative approach would be to set only two levels of sponsor support - weak sponsors with a value of 50% of shortfall - strong sponsors with a value of 100% of shortfall. Further simplification would be reached by setting sponsor support equal to 100% of shortfall for every IORP but monitoring more closely the IORPs with both a significant shortfall of financial assets and a sponsor who appears to be weak after a quantitative and qualitative analysis, possibly based on credit ratios among other indicators.	

Q01.	**Q1: Should IORPs be provided with additional guidance for conducting a stochastic valuation of sponsor support?** The principles provided in the QIS for running a stochastic market valuation are sound, but we fear it does not suit practical purposes. We think stochastic valuation can sometimes provide useful information, but market valuation is neither possible nor adapted to IORP environment. In general, there is no deep, liquid and transparent market for pension obligations so market consistency is anyhow hard to reach. Stochastic valuation only adds information with regards to deterministic valuation to give a price for options and guarantees. IORPs have time horizons of decades and there is no deep, liquid and transparent option market for such time horizons. Moreover, there are supply and demand mismatches which possibly weigh down on prices on very long maturities on interest rates and inflation curve. Therefore, the less reliable information impacts the most assumption-sensitive part of the valuation: long maturities. Lastly, if all IORPs are sensitive to and react in function of the same market changes, some overreaction should be feared. Too much guidance should be avoided, stochastic valuation should be flexible and reflect expert judgement in order to allow each IORP to model its own situation and apply its own strategy, while it remains a sensible one. Stochastic models imply huge costs, therefore they should not be imposed as the only accepted valuation method.	

	In conclusion, we think stochastic valuation - Should be focused on expert judgement rather than on market information - Should not be constrained by a too strong guidance - Should not be the compulsory way for every IORP to value its balance sheet.	
Q02.	**Q2: Should IORPs be provided with additional guidance for conducting valuations of sponsor support using either Simplification 1 or 2? Should either of these simplifications be removed or should any other simplification be developed?** We do not believe lack of guidance is the major issue with these simplifications. Further guidance cannot remedy to complexity (real or perceived). However, we believe more guidance should have been provided during the QIS for the use of spreadsheets. We reassert that Simplification 1 and 2 - can only be used in a limited number of pension arrangements (one rated sponsor for one IORP) - rely strongly on questionable or unavailable parameters: credit ratings, accounting data which vary between economic sectors and countries… - therefore yield result which are questionable or unavailable, not comparable and of limited use in many cases. A possible simplification would be to set two levels of sponsor support - weak sponsors with a value of 50% of shortfall	

	- strong sponsors with a value of 100% of shortfall. The assessment of the sponsor strength would be based on qualitative and quantitative analysis. Further simplification would be reached by setting sponsor support equal to 100% of shortfall for every IORP but monitoring more closely the IORPs with both a significant shortfall of financial assets and a sponsor who appears to be weak after a quantitative and qualitative analysis, possibly based on credit ratios among other indicators.	
Q03.	**Q3: In the stakeholders' view what role should the concept of maximum sponsor support play in the general valuation principles for sponsor support?** We understand maximum sponsor support defines an upper bound for the deviation of pension liability the sponsor is able to take on. This could be in theory a very important measure of sponsor support, all the more as long as the link between sponsor cash contributions and sponsor support value in the HBS is not clarified. However it is not necessary to produce a value of the maximum sponsor support, the IORP is only interested in the ability of the sponsor to cover the shortfall. For instance it does not matter if the maximum sponsor support is 4, 5 or 12 times the shortfall plus capital charge. Anyway, we doubt calculating maximum sponsor support is possible and reliable. We do not know a method that will in general give a reliable estimate of the maximum liability a corporation is capable to finance (a pension liability or any other one). Moreover the	

	valuation method proposed in the QIS only apply to a very specific type of arrangement: 1 single IORP ⇔ 1 single parent sponsor company. The proposed formula is questionable because - sponsor current accounting data can be treated as confidential, sponsor business plan for future years is certainly confidential - sponsor accounting data can be published with several months lag with respect to the IORP prudential valuation - some parameters seem to be arbitrarily chosen (why "1/3" of future cash-flows ?) - accounting rules vary between countries - independently to the capacity to finance the pension promise, the economic sector impacts accounting values	
Q04.	**Q4: Is wage an appropriate additional measure for estimating the maximum amount of sponsor support? If so, please explain why? Are there any other measures which could be used to assess the maximum sponsor support?** Total wage can in some specific situation give a good estimation of maximum sponsor support, for example, for a multiemployer plan or industry-wide scheme. But in general it is not true: labour intensiveness does not relates with capacity of and involvement in financing pensions. We do not know a method that will in general give a reliable estimate of the maximum liability a corporation is capable to finance (a pension liability or any other one).	

Q05.	**Q5: Are stakeholders comfortable with the concept of linking default probabilities, credit ratios and sponsor strength?** Credit ratios are a good alternative to credit rating. However, though we can understand sponsor strength is an important information, it is very unclear how it could be used in the HBS framework. Issues related to accounting data remains - sponsor current accounting data are backward looking and can be treated as confidential - sponsor business plan for future years is certainly confidential - sponsor accounting data can be published with several months lag with respect to the IORP prudential valuation - accounting rules vary between countries - independently to the capacity to finance the pension promise, the economic sector impacts accounting values - assets cover ratio rely on the assumption that the IORP is the most junior creditor of its sponsor. Moreover the case of multiemployer schemes or sponsors with several IORPs still raise issues.	
Q06.	**Q6: Do stakeholders agree with exploring the possibility of including a standard table in the technical specifications that links credit ratios with default probabilities?**	

	In the framework of the HBS, a standard table of correspondence between default probabilities and credit ratios could be included as a general guidance. More directly, it could also be a table of correspondence between credit ratios and sponsor support as a percentage of shortfall.	
Q07.		
Q08.	**Q8: Do stakeholders agree that timing of sponsor support reflecting the affordability of making additional payments could be an improvement to the general principles for valuing sponsor support?** Affordability of timing is a very important issue for the design of a recovery plan, in which case national legislation should also be considered, but we believe this issue is secondary on the issue of sponsor support valuation in the HBS. Sponsor support valuation in general is aimed at reflecting ability of making additional payments. It is not necessary to break down affordability into timing and default probability. In particular, in the proposed methodology - sponsor strength directly determines sponsor value as a percentage of shortfall - the only important assessment to make is to know if the sponsor strength is weak or not. The impact of credit ratios is composed, since it impacts both the default probability and the timing of sponsor support. Should the information given by credit ratios be irrelevant in some cases, it would have a dramatic impact.	

Q09.		
Q10.	**Q10: Should more detailed guidance be provided in future technical specifications to value sponsor support that is subject to discretionary decision-making processes? If yes, please explain in what way. Could the suggested detailed guidance also be applied to benefit adjustment mechanisms that contain discretionary elements?** Guidance should only remain at the level of general principles because decision-making processes can only be dealt with properly on a case by case basis.	
Q11.	**Q11: Please provide your general comments on the alternative approach.** This alternative approach is welcome as it avoid too strong reliance on credit rating, which is necessary for non-rated sponsors (the most general case). The general presentation of the alternative approach looks also more transparent since it explicitly links the sponsor strength to a fixed coverage of shortfall. Nevertheless we doubt the valuation of sponsor support (in monetary unit) is necessary. A qualitative assessment would be more useful to estimate whether or not the IORP is at risk on the sponsor support. The proposed approach can work in the model of one single sponsor for one single IORP. The proposed ways to handle industry wide schemes and sponsors of several IORPs are	

	not clear and don't seem to be properly addressed. In particular, the "Last Man Standing" principle for industry wide IORPs cannot be handled in this approach. The choice of market consistent valuation follows the sound principle of transparency, but a too strong focus on market valuation of liabilities is indeed flawed since there is no market for pension liabilities. No option market is enough deep, liquid and transparent for IORPs on very long maturities. There are also supply and demand mismatches on interest rates and inflation markets for very long maturities. We also fear market valuation will entail more pro-cyclical behaviour and will deter IORPs to take risks, which could harm the long term financing of European economy and increase the costs of pension funding. The reliance on accounting data is now very strong and raise the issues of - confidentiality (especially in the case of multiemployer schemes, sponsors of several IORPs, pension schemes with state support) - backward looking assessment - availability of data - comparability between economic sectors and countries. Some parameters, such as the contributions duration, could be justified. Therefore we welcome EIOPA states IORPs should use their judgement and come with their own estimate of sponsor strength when possible and useful. The proposed approach could be simplified. For example, for sake of simplicity, EIOPA could assume that a medium strong sponsor covers 100% of the shortfall instead of	

	98.8%. It looks clear from the table of sponsor support value in function of its strength that the only cases that matter are the weak and very weak sponsors, and, to a much smaller extent, medium sponsors. A possible simplification of the alternative approach would be to set only two levels of sponsor support - weak sponsors with a value of 50% of shortfall - strong sponsors with a value of 100% of shortfall. An other simplification would be setting sponsor support equal to 100% of shortfall for every IORP but monitoring more closely the IORPs with both a significant shortfall of financial assets and a sponsor who appears to be weak after a quantitative and qualitative analysis, possibly based on credit ratios.	
Q12.	**Q12: Does the alternative approach address the concerns raised during the previous consultation on the technical specifications?** The alternative approach addresses the concerns about overreliance on credit ratings. It does not address the more general issues of the relevance of the HBS and how sponsor support would be used for supervisory response and recovery plan design. The approach fit the model of one single sponsor for one single IORP and fit less complex IORP-sponsor relations (multiemployer schemes, sponsors of several IORPs and complex structures of sponsoring of the IORP). Moreover, the proposed methodology strongly rely on accounting data, which can also raise some concern	

	- confidentiality (especially in the case of multiemployer schemes, sponsors of several IORPs, pension schemes with state support) - backward looking assessment - availability of data - comparability between economic sectors and countries.	
Q13.	**Q13: Are there any areas that have not been addressed adequately enough?** The case of multiemployer IORPs, sponsors of several IORPs and complex sponsoring structure (the sponsor of the IORP being the subsidiary of a larger parent company) should be further developed. More generally, breaking down security mechanisms is quite difficult since they all function altogether, included in collective bargaining of IORPs with their sponsor and other stakeholders - Risk and cost sharing: increase in employee / employer contributions - Pension Protection Schemes - Benefits reduction mechanisms - Last-Man Standing principle in some multiemployer arrangements	
Q14.	**Q14: Are IORPs still likely to want to calculate a maximum value of sponsor support (even if not required under the alternative approach)? If so, for what purpose?**	

	We believe it is a positive move that no maximum sponsor has to be calculated. - We do not believe a maximum liability a company can take on can be reliably calculated - What is important to assess is the ability for the sponsor to cover existing liabilities.	
Q15.		
Q16.		
Q17.		
Q18.	**Q18: Are Income Cover and Asset Cover suitable credit ratios to use for Stage 1?** Income Cover and asset cover are useful to estimate sponsor strength, but these indicators raise some concerns - confidentiality (especially in the case of multiemployer schemes, sponsors of several IORPs, pension schemes with state support) - backward looking assessment - availability of data - comparability between economic sectors and countries. For complex structures of sponsoring (multiemployer schemes, sponsors of multiple IORPs, sponsors subsidiaries of a larger group) - the issues of confidentiality and availability are even more important - the ratios are complex or impossible to calculate. Finally, asset cover ratio rely on the assumption that the IORP is the most junior creditor	

	of a sponsor who goes bankrupt, which is a questionable assumption.	
Q19.		
Q20.		
Q21.		
Q22.		
Q23.		
Q24.		
Q25.		
Q26.	**Q26: Is it reasonable to not allow for any recoveries from sponsor defaults? Please provide examples where this could increase the calculated value of sponsor support.** It would be reasonable to allow for recoveries in a sponsor quantitative valuation. Any recovery on sponsor default should be considered as an additional security. An historical study of the impact of European companies going into default on the pension schemes they support would be an interesting basis for this discussion.	
Q27.		
Q28.		
Q29.		
Q30.	**Q30: Is the approach to determining the loss-absorbing capacity appropriate?** The calculation method of loss-absorbing capacity seems much clearer than the method	

	proposed in the Quantitative Impact Survey. However the exact purpose of solvency capital requirement for IORPs should be clarified, since as long as there is not enough assets to cover level A technical provisions, a shortfall at least equal to sponsor default risk will remain. This does not add much information with respect to a qualitative appreciation of sponsors default risk, and the relation with cash funding requirements is still unclear.	
Q31.		
Q32.		
Q33.	**Q33: What additional work should be carried out if this methodology was to be used for determining sponsor support in a regulatory or supervisory environment?** The following studies would be both very useful and interesting - a comprehensive study of security mechanisms for European IORPs with a some detailed examples • Pension protection schemes • Cost and risk sharing (increase in employer and employees contributions) • Management of pensions indexation, benefits or accruals reductions • Last-Man Standing principle in some multiemployer schemes - an historical study of the impact of European companies going into default on the pension schemes they support, with a few representative detailed examples - an analysis of market based valuation on the IORPs investment strategies - a study on how recovery plans could be designed in the HBS framework and how they could evolve dynamically • Possibly with *simplified assumptions*	

	1. TP average maturity of 15 years 2. level B / level A TP in percentage of invested assets of 80%/100%, 80%/150% and 120%/200% 3. sponsor support value of 0%, 50% and 100% of the shortfall 4. Net SCR of 0% and 20% of invested assets (reflecting the riskiness of the investment strategy) • On a *dynamic* perspective: how an HBS and recovery plans would change after 1. A cash contribution of +10% of assets 2. A decrease in the assets value of -10%	
Q34.		
Q35.	**Q35: Are there any aspects of the suggested approach which are unclear?** The treatment of multiemployer / industry-wide schemes and sponsors with multiple IORPs are not workable, so are the link between sponsor support and other security mechanisms such as - Pension Protection Schemes - Benefits reduction mechanisms - Increase in employee contributions - Last-Man Standing principle in some multiemployer arrangements	
Q36.		