



Society of Actuaries in Ireland

Department of Social Protection Consultation on IORPS II Directive

5 September 2014



SECTION 1: GENERAL OBSERVATIONS/OTHER REMARKS

The Society welcomes the opportunity to respond to the Department's consultation on the proposal for a revision to the IORP Directive.

The two main areas in which the proposal would lead to significant change are governance (Section 2, Title 2) and information to members (Section 2, Title IV). The Society welcomes the increased emphasis on risk management for IORPs and the introduction in Article 28 (for DB schemes) of a formal actuarial function within the governance structure. The Directive envisages that the actuarial function would contribute to the effective implementation of the risk management system and we would expect that the actuary would play a key role in risk management for IORPs, and in the development of the Risk Evaluation for Pensions introduced in Article 29. The Society set up a working party on risk management for pensions earlier this year and the group has produced some excellent material. This is due to be finalised shortly and we will share it with you when it is available.

We would encourage the Department and the Pensions Authority to retain the existing requirement that the calculation of technical provisions under (proposed) Article 14 be undertaken by an actuary who holds a Scheme Actuary Certificate issued by the Society and that a similar requirement is introduced for the actuarial function holder under the new proposal.

Whilst the Society welcomes the proposed enhanced governance structure, we would urge the Department to ensure that a proportionate approach is taken for smaller schemes, and not just to retain existing de minimis exemption for schemes with fewer than 100 members. In our view, a key to enhancing the governance of Irish pension schemes is for trustees to have a better understanding of the issues and of their responsibilities under trust and pensions law, and we would support an enhanced training requirement for those who are or wish to become trustees. We do, however, question whether it is appropriate to require trustees to have a "professional qualification" as set out in Article 23.

The importance of effective member communication and engagement cannot be overstated, especially for DC Schemes, and we welcome the increased emphasis on disclosure in the draft Directive. However, we are strongly of the view that the proposed harmonised Pensions Benefit Statement is not the optimum approach to achieving better understanding by members of their pension rights, and we would recommend that the detail of benefit statements should be left to member states, so that they can fit in with national social and labour law, social security, tax and culture.



SECTION 2: KEY PROPOSALS IN IORPS II DIRECTIVE

TITLE 1: GENERAL PROVISIONS

Q) *What is your view in relation to the logic and potential impact of proposals to facilitate cross border IORPs activity including the transfer of pension schemes across Member States?*

We welcome the amendments to the Directive to facilitate increased cross border activity. The clarification of the cross border status of an IORP and specifying that the host Member State cannot impose additional investment restrictions or information requirements should lead to an increase in cross border activity, particularly in relation to DC schemes. While we believe the detail should be left to member states, the Directive could provide an outline of the information required in the benefit statement.

The inclusion of specific provisions in relation to the transfer of pension schemes across Member States should make scheme transfer more feasible. It is worth noting that a few IORPs have been set up since 2003 which have involved Irish pension schemes.

We welcome the fact that the European Commission has decided to take more time to consider solvency requirements for IORPs. The QIS exercise undertaken in 2012 highlighted that there was a significant shortfall in the funding of Irish pension schemes and if sponsors were required to address these shortfalls over a short time frame, it could lead to more wind-ups with members not receiving the full value of their benefits. However, it may be possible for schemes to provide and fund benefits over a longer time period. Given the diversity of funding regulations for defined benefit schemes across Member States our view is that funding regulations for DB schemes should be set by each Member State.

The retention of the requirement that cross border IORPs be fully funded is consistent with each Member State setting their own funding regulations. The increased prominence of DC schemes makes the fully funded requirement for cross border DB schemes less of an issue in facilitating cross border activity.

TITLE 2: QUANTITATIVE REQUIREMENTS

As the Department has noted, Articles 14 to 20 are largely unchanged. In particular, Article 14, which is almost identical to the previous Article 15, continues to provide for technical provisions to be certified by an actuary (or other specialist) according to national legislation, on the basis of actuarial methods recognised by the member state. This confirms that the possible change to a holistic balance sheet/Solvency II approach as proposed by the Commission and tested in the QIS last year, will not be introduced as part of this proposed revision of the Directive.



As noted above, the Society welcomes the decision by the Commission to take more time to consider possible changes to quantitative measures in view of the many issues that need further detailed analysis and the significant impact that changes such as those proposed would have on pension systems in some Members States, including Ireland.

TITLE 3: CONDITIONS GOVERNING ACTIVITIES

Q) What are your views in relation to the proposals which would require ‘those who effectively run schemes’ to have professional qualifications? (The current Directive offers the option of placing this requirement on those running the scheme OR the scheme’s advisers.)

The key question in this proposal is what would constitute a sufficient “professional qualification”. In this regard, we would raise the following points:

1. The word “professional” implies a qualification to a level comparable to that required of other professionals, such as doctors, accountants, actuaries, etc. We would argue that qualification to this high level would certainly not be necessary for Trustees. Moreover, to impose such a high level would seriously limit the potential range of Trustees that Schemes can appoint, probably cutting out all but professional Trustees, which is not desirable.
2. There is a balance to be achieved between encouraging member participation of pension schemes through appointing Member Trustees, and ensuring that Trustees spend enough time and effort improving and maintaining their knowledge to an adequate level for them to fulfil their roles. To achieve this, any “qualification” would need to be focussed exclusively on what is required knowledge for a Trustee.
3. We believe there is a minimum level of competency that must be achieved and maintained by all individual Trustees in order to fulfil their role. We are strongly of the opinion that the current Trustee training requirements set out by the Pensions Authority are not adequate in this respect. We believe a “qualification” or approval requirements for Trustees should be brought in and administered by the Pensions Authority. We would suggest it has the following characteristics:
 - a. Trustees would be required to be qualified *before* becoming a Trustee (rather than during a certain period of time after being appointed). For example, potential Trustees with no previous experience could be required to sit on the Trustee Board as observers for a certain period before fully joining. This would give them experience of what is involved, and to reduce the chance of a Trustee being appointed who does not appreciate the commitment required.



- b. A more thorough formal assessment than that currently in place. For example, an online exam that, if failed, cannot be immediately retaken.
 - c. A requirement to keep the Trustee's knowledge up to date.
 4. It is not necessary for every individual Trustee on a Trustee Board to have extensive knowledge of every field – a Trustee Board could be assessed in aggregate for necessary expertise. Therefore, it may be desirable to have optional additional modules as part of the Trustees' qualification with a requirement being that, at any one time, each of the additional modules are held by at least one Trustee (and preferably two) on the Board.
 5. Careful consideration is needed in regards to the principle of proportionality. We do not believe that, just because a scheme has less than 100 members, this makes it sufficient for Trustees to be less knowledgeable and experienced. Indeed, a small scheme would usually have a smaller budget for hiring external advice and lower ability to absorb volatile experience, which would effectively put more responsibility on the Trustees to ensure the scheme is run well.

Article 23 introduces a requirement for Trustees to be proper. We welcome this addition, and note that one way of doing this could be consistent with the requirements for an individual to be a company director. The requirements should also be considered in the context of the Fitness and Probity Regime operated by the Central Bank of Ireland.

Q) What are your views in relation to the proposed new governance requirements on risk management, outsourcing and internal audit? This would include the requirement for schemes to compile a 'Risk Evaluation for Pensions' report.

We welcome the risk management requirements and requirement to produce a Risk Evaluation for Pensions, subject to it being relevant and proportional. If implemented correctly, we believe these will add value to Irish pension schemes. Actuaries are well-placed to advise on the process, for example, the SAI are already looking into this through our Risk Management Working Party.

We also approve of the internal audit function in principle, but note that, as many schemes do not have such a formal structure already in place, it would be beneficial to phase in its introduction. There are also a number of questions raised, such as the definition of an "independent" person, and potential overlap with the current external audit requirement for schemes' annual report and accounts (especially if the independent person is external to the sponsor / scheme). We would hope that the detailed implementation would guard against excessive requirements for schemes.

We have no objections to the proposed Directive's requirements on outsourcing.



Throughout this response, we would be wary of imposing unnecessarily burdensome requirements on small schemes, and we would expect the principle of proportionality to apply at this point. We also note that there is explicit remit for the Commission to make delegated acts, so we would expect more detail to follow.

Q) What are your views in relation to the proposals which would require that schemes have a remuneration policy? This would include disclosing the pay of those who run the scheme.

As Trustees are not paid for carrying out their duties as Trustees (other than professional Trustees), we do not believe this would affect Irish schemes in this respect. In regards to professional Trustees, we believe it is entirely reasonable for their costs to be disclosed.

The term “remuneration policy” suggests the possibility of performance-related bonuses or other variable remuneration, which we do not see as applicable in this context. However, notwithstanding the terminology used, we welcome the measures that encourage greater transparency of costs incurred by schemes so the monitoring of these can aid the decision making of Trustees, sponsors and other stakeholders. We previously advocated this in our submission to the Pension Authority’s Consultation on the future of DC pensions¹, and, where relevant, this should apply equally to other schemes.

Q) What are your views in relation to the proposals which would preclude restrictions on long-term investments?

We have no objections to this proposal.

Q) What are your views regarding the logic and impact of proposals which may require DC schemes to appoint a depository, with responsibility for safe-keeping of assets and oversight?

In this response, we assume there is no difference between a “depository” and “custodian”.

For DC (and defined benefit) schemes that are fully insured (as are the vast majority) we believe the requirement for the scheme to appoint a depository is unnecessary and onerous. In these cases, the investment manager will employ a custodian to hold the official documents for the assets (e.g. share certificates, etc.). We understand that the safe keeping of insured assets in this way is dealt with in independent legislation.

¹ Under section “Value for Money”, pages 16-17. The full paper is available on the Society’s website here: <https://web.actuaries.ie/sites/default/files/story/2013/10/131030%20Pensions%20Board%20DC%20Consultation%20-%20FINAL.pdf>



For self-administered DC schemes (and defined benefit schemes also), we would also expect the investment manager(s) to employ custodian(s).

If it is proposed that investment managers' custodians can be counted as the scheme's depository for the purpose of the Directive, we would suggest that the wording be changed to allow for multiple depositories for a single scheme (as it currently only allows one per scheme).

Any Further Comments Regarding Proposed Title III Provisions?

We welcome the introduction in Article 28 of a formal actuarial function (for DB schemes) in the proposed Directive, including the list of tasks to be undertaken, although the list needs some amendment as it is based on the corresponding tasks for insurance undertakings under Solvency II (e.g. express an opinion on the overall underwriting policy in the event of the institution having such a policy). We recommend that the Directive require the actuarial function be fulfilled by an actuary, as actuaries are best equipped to advise by virtue of their training and experience in long term financial management. In addition, we recommend that the existing Irish Scheme Actuary Certificate system be retained and extended to cover the actuarial function.

The Directive envisages that the actuarial function would contribute to the effective implementation of the risk management system and we would expect that the actuary would play a key role in risk management for IORPs, and in the development of the Risk Evaluation for Pensions introduced in Article 29. As noted earlier, the Society has established a working party on risk management for pensions and will share their output when it is available.

TITLE IV: INFORMATION TO MEMBERS

Q What are your views in relation to the proposals regarding information requirements regarding members, prospective members and beneficiaries?

Article 38 sets out the principles and while these are desirable, some specific observations are as follows:

- Technical terms are inevitable in some documents such as the rules setting out the conditions of a pension scheme. Suggest amending the language to 'avoiding technical terms where possible'
- The requirement to use colours that will not diminish if photocopied to black and white does not make sense. If the provider is willing to issue a document to a member in colour, then there is no need to be concerned about a photocopy of the document. This could also limit the extent to which the document engages the member.



Article 39 sets out new requirements for schemes where members bear investment risk and these appear sensible. The requirement to publish the conditions of a pension scheme on a website appears unnecessary. The conditions are typically a legal document or a set of legal documents and are used by the advisors and managers of pension schemes. However, they should be readily available for members.

In relation to Article 56, while it is timely to interact with members two years before retirement in relation to members' options at retirement, this would be too late for members to take action and have a meaningful impact on their retirement outcome. Consideration should be given to providing additional information 5 to 10 years before retirement, which would better enable members to take action if the projected outcomes were deemed to be sub-optimal.

Indeed, one of the main issues that companies and Trustees are grappling with in relation to DC schemes in particular is getting the members to engage properly in relation to their pension savings. Perhaps the third objective of the proposal could reflect this and be changed to 'providing clear and relevant information to members and beneficiaries that seeks to enhance their level of engagement with the IORP'.

It is also important to differentiate between information and communication. The Society's reply to the Pensions Board consultation on defined contribution in 2013 identified a number of key principles on communication that could be followed:

- As with communication in any field, the more simple and uncluttered the message can be made, the more likely it is to be understood by members.
- Personalised messages reflecting the member's own circumstances will generally have a higher impact than generic messages. A number of opportunities arise to produce personalized messages in the DC area, for example significant birthdays or career events.
- The stage of retirement saving journey is relevant – the messages that resonate with younger members starting off their DC saving are very different to those that are important to members approaching retirement.
- Well-designed graphics can be very helpful in conveying complex messages.

To encourage access electronically, one option would be to provide members with access to a website which would layer access to the information.

While providers can and should continually strive to improve the quality of member communications, there is also a responsibility and challenge on behalf of members to commit sufficient focus to ensure they understand the issues they face in planning successfully for retirement.



Q What are your views in relation to the proposals for a prescribed mandatory, EU wide harmonized Pension Benefit Statement, to be sent at least annually to every scheme member?

We would question the desirability of having a standard statement when the majority of members will have a pension in only one State.

Article 40(2) provides that a pension benefit statement should be sent to each member (which includes active and deferred members) at least annually. This reflects the current requirements of Irish legislation for active members, but deferred members of Irish pension schemes are currently only entitled to a statement on request.

We agree that every member (active and deferred) should be sent a statement annually, notwithstanding that this would increase the costs of administration of both DB and DC schemes.

Bearing in mind that one of the objectives of the proposal is to provide clear and relevant information to members and beneficiaries, we believe that the proposal sets out too much information to be included in the statement. Furthermore, setting out the information in a maximum of two pages as is proposed would either prove difficult or would result in a document that would be unlikely to engage the recipient.

It would be better to have concise information and not to prescribe the format and content in detail. For instance, an alternative approach may be to have a simplified annual benefit statement that gives clear information about opening and closing benefits / balances for the year, with the changes in the benefits / balances broken down between contributions, investment performance, tax, charges and benefit payments for DC plans, and between accrual of service and salary increases for DB plans. Such a format may also be more appropriate given the trend towards allowing members avail of flexible drawdown post-retirement, as such a format would continue to be appropriate for members who are in receipt of benefit.

Given the low level of member engagement experienced to date in DC schemes, and by extension the likelihood that the annual benefit statement may be the only document read by the member in relation to the IORP, there should be an emphasis on ensuring it is easy for the member to understand and encourages the member to engage appropriately in their retirement provision.

Different schemes will require different items to be emphasized so perhaps basic content should be prescribed and the remaining information included as appropriate to the scheme.

While a common format facilitates comparison of information and should help ensure consistency of content across member states, most people will have a pension from one State.



Some specific observations are as follows:

- If the objective is to set out specific information on the statement, then the presentation of such a statement should not be limited to two pages. The information might be better presented on three or more pages.
- If the objective is to have a two page benefit statement, then consideration must be given to removing some items from the list.
- Referencing other information that is available would also be helpful if content is limited to two pages and members could be directed to a contact person or other source for such information.
- Some of the material on pension projections, investments, past performance and supplementary information might be better provided in accompanying/reference documents which would effectively layer the information for members e.g. if a member wanted to find out more about projections, then the member could be directed to a website or projection tool.

TITLE IV(2): PRUDENTIAL SUPERVISION

We support the stated objective of prudential supervision as the protection of members and beneficiaries of IORPs. Article 61 requires that prudential supervision is based on a risk-based and prospective approach, and that supervisory powers be applied in a timely and proportionate manner, and we are strongly supportive of these principles.

We have no comments at this stage on the detail of the supervisory powers and duties as outlined in the draft proposal.

TITLE VI: FINAL PROVISIONS

We consider the proposed implementation date to be extremely challenging, given that the new Commission has not yet been appointed, and the European Parliament has not yet considered the proposal. Even if there were agreement on the Directive by end 2015, there would be a need for significant change to the Pensions Act (and related statutory and regulatory provisions) to transpose the Directive into Irish legislation, taking into account proportionality and any Member State options.



SECTION 3: ESTIMATED COSTINGS

We have not reviewed in detail the Impact Assessment undertaken by the Commission but note that

- The Impact Assessment Board of the Commission was unable to issue a positive opinion on the assessment
- The additional costs for IORPs appear to be based on a qualitative survey, subsequently adjusted to reflect changes in the scope of the proposal, and we are unable to find any indication that Ireland was covered by this assessment.

This suggests that the figures provided may not give a reliable guide to the additional costs which would arise for Irish IORPs, which would be passed on to employers and/or members.

For small schemes, the additional cost per member of the proposed governance requirements could be matenless they are applied proportionately. Significant one-off costs could arise if it became necessary to revise completely the content of benefit statements for DC Schemes. In addition, if additional trustee training were required, this would have cost implications.

We are not in a position at this time to comment on the figures shown, or to provide our own figures for the likely impact on Irish IORPs of the proposed changes, particularly as the extent to which proportionality will be applied is not known. We would be pleased to discuss with the Department in due course how we could assist with an assessment of the cost to enable informed decisions to be made about the implementation of the Directive in the event it becomes law.

Please direct any questions on this response to Yvonne Lynch, Director of Professional Affairs, Society of Actuaries in Ireland, at the contact details overleaf or Yvonne.Lynch@actuaries.ie.



Society of Actuaries in Ireland, Clanwilliam House, Clanwilliam Place, Dublin 2

tel: +353 1 634 0020 | fax: +353 1 634 0039 | web: www.actuaries.ie

Registered in Dublin as a Company Limited by Guarantee No.146024. Registered Office: Clanwilliam House, Clanwilliam Place, Dublin 2, Ireland