
EU Pensions Directive

Submission to Pensions Board
re: Implementation

Introduction

IAPF welcomes the implementation of Directive 2003/41/EC and the important step it represents. We are fortunate in Ireland to have a system that is both well structured and efficient in the way it functions and look forward to the added cohesion that the enabling legislation will bring.

Our submission has the following format:

- 1) The main body of the submission identifies those aspects of the Directive where we have comments or views regarding implementation
- 2) In the appendix, we set out a possible pro-forma structure for one of the most significant implementation impacts, arising out of Article 12.

We appreciate the complexity of the process and would be glad to meet with representatives from the Board to provide any necessary clarifications.

We may have further comments to make in the future on the provisions of the Directive as we continue to assess its impact.

Irish Association of Pension Funds

September 2004

Article 2 : Scope

Comment

- This fits comfortably with the existing Irish view of what constitutes occupational pension schemes.

Article 4 : Optional application to Institutions covered by Directive 2002/83/EC
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Comment

- IAPF welcomes any measures that provide security to pension fund members. However Irish legislation currently has strict controls on insurance companies who are regulated by IFSRA and the Department of Enterprise & Employment. Any further regulation may result in extra costs, which would ultimately be borne by pension funds, without any real increase in the level of security.
- One way or the other, significant changes in this area cannot take place without extensive consultation and deliberation by the current regulators within the industry.

Article 5 : Small Pension Institutions & Statutory Schemes
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Comment

- IAPF believe that all schemes should be subject to a prudent level of regulation and supervision but this must not create a situation where the resultant costs have the impact of:
 - discouraging the creation of new schemes (which by definition are small at inception)
 - putting the ongoing survival of existing schemes into question
- IAPF's view is that small schemes in Ireland are subject to an effective regulatory regime by the Pensions Board and would feel that some of the additional provisions of the Directive would place an unacceptable burden on small schemes, such as the cost of producing and auditing annual accounts (Article 10).

Implementation

- **We therefore recommend that the derogation in Article 5 should be utilised for schemes with less than 100 members in respect of those provisions of the Directive not already applying under local legislation.**
- For the purposes of the directive, "members" include both deferred and active members. This means that schemes who may have marginally greater more than 100 members by virtue of an increase in the number of "deferreds" will fall under the full terms of the directive with the resultant costs. This is likely to be most prevalent in Defined Contribution Schemes. Linking back to our own agenda for simplification, IAPF believes that there is a need for a legislative amendment to allow trustees of defined contribution schemes to secure deferred members benefits by personal retirement bond purchase or PRSA without member consent. We also

believe that for defined benefit schemes the current value regarding transfers without members' consent should be increased to a value of at least €15,000 (subject to annual indexation) and a time limit, post leaving, of nine months.

- The Directive also extends the potential derogation to institutions (schemes) established under statute, pursuant to legislation and guaranteed by a public authority. Provided the nature of the pension promise is underwritten then using the derogation appears sensible. This is a specific area where further discussion with the Board may be useful.

Article 6 : Definitions

Comment

- In general, the definitions contained in the Directive are broadly compatible with existing terms in Irish legislation.

Implementation

- IAPF would understand the definition of an IORP to include Group based personal pension schemes. It is arguable that Personal Retirement Savings Accounts, which are individually based, fall outside the definition of an IORP but we would be interested in any views the Board has on this.

Article 7 : Activities of an Institution

Comment

- This does not appear to be an issue.

Article 8 : Legal separation between sponsoring undertakings & IORPS

Comment

- IAPF is in agreement with the principle of legal separation between the sponsoring undertakings and IORP's, safeguarding members and beneficiaries interests.

Article 9 : Conditions of Operation
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Comment

- IAPF welcomes any measures that provide protection for scheme members and beneficiaries by requiring appropriate registration, governance and provision of information.
- In general, the provisions contained in this article are broadly compatible with existing terms in Irish legislation, save for the requirement that an IORP "...is effectively run by persons of good repute with appropriate professional qualifications and experience, or who employ advisers

with such qualifications.”

- Notwithstanding the relatively non-specific language used here in terms of qualifications and experience, IAPF believes that Trustee Training and Qualification will take on a higher profile in the coming years and is already firmly part of our agenda on behalf of members.

Implementation

- Generally, we would like to see a normal registration (Art 9(1) procedure for commencement of IORPs (ie current domestic schemes). The prior authorisation requirement for cross-border activity (Art9(5)) should be seen as a one-off formality for individual IORPs which intend to carry out cross border activity. Please see further comments under Article 20 for cross border activities.
- IAPF would be glad to discuss ways in which standards of Trustee experience and qualification could be established in respect of Irish Schemes.
- Para 1(f) - says that each member state shall ensure that “members are sufficiently informed of the conditions of the pension scheme” – the specific points covered in sub points i) through iii) seem to place significant additional burdens on schemes.
- IAPF would suggest that there are risks applying to members of DC schemes that require different communication than defined benefit schemes. While there is no requirement to establish this distinction in legislation, it is worth note for the ongoing formulation of strategy for the Board.

Article 10 : Annual Accounts & Annual Reports
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Comment

- IAPF is supportive of the principle and practice of strong scheme governance, which includes the maintenance of proper records and accounts.
- At present, full annual accounts and reports are required only for Defined Benefit (DB) schemes with more than 50 members. The collective “ownership” of the assets of a defined benefit scheme supports the need for independent verification that audited accounts provide.
- This article, as written, extends the requirements to Defined Contribution (DC) schemes (over 100 members when the derogation is taken into account). It should be acknowledged that, other than representing the aggregation of the members’ individual interests, a specific member has no call or rights in respect of the entirety of the scheme’s assets. This distinguishes them from DB schemes.

Implementation

- IAPF believes that discretion should be utilised to strike a balance between proper dissemination of information to members and creating excessive time and cost burdens that may push sponsors away from formalised retirement provision.
- We would suggest a separation of the requirements for DB and DC schemes, reflecting the differing fundamentals they exhibit and the range and complexity of investment arrangements typically employed.
- IAPF supports the retention of the requirement for Defined Benefit Schemes with more than 50 members to produce annual accounts and reports. This maintains the existing level of

oversight and protection for members but will not result in an additional cost burden for these schemes.

- The requirement for DC schemes to produce annual accounts needs to be approached with care. Statements of members' individual entitlements are the primary records to show assets, and activity levels pertaining to their own retirement provision. To maintain proper oversight (which is consistent with the spirit of the Directive), while avoiding unnecessary cost, IAPF recommends that consideration be given to defining the requirements for DC Schemes in terms of an abbreviated annual report and accountants report (rather than audited financial statements) for DC schemes.
- Again, in the context of the above, our comments (under Article 5) with regard to the efficiencies of enabling the purchase of deferred benefits in DC schemes without member consent apply and accordingly we recommend the introduction of enabling legislation to allow Trustees to proceed in this regard. Please also note our comment under Article 5 in relation to DB schemes (transfers up to €15,000).

Article 11 : Information to be given to Members & Beneficiaries
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Comment

- Transparency is vital in both protecting members' interests and encouraging them to engage in retirement provision. This transparency can be achieved by the existence of appropriate information, structured in a simple to understand fashion.
- Providing information to members on the range of options is standard practice, though the method of dissemination and format should be left to the discretion of the trustees.
- Many of the schemes where members bear the investment risk are DC schemes and most of these invest through some form of pooling arrangement (unit trusts or unit-linked funds). Indeed, members can have their assets invested across a range of unit funds. Therefore, providing the "actual investment portfolio" and "risk exposures" may prove extremely unwieldy, at least on a consolidated basis.
- Where funds are with profits in nature or whose eventual investment outturn is dependent on undeclared bonus rates specific provisions may be included in the empowering legislation.

Implementation

- At the start of this article, the following phrase is used; "Depending on the nature of the pension scheme established...". IAPF believes that this discretion should be utilised to strike a balance between proper dissemination of information to members and creating excessive time and cost burdens that may push sponsors away from formalised retirement provision.
- We would suggest a separation of the requirements for DB and DC schemes, reflecting the differing fundamentals they exhibit and the range and complexity of investment arrangements typically employed.
- The points raised in implementation with respect to para. 4 c) suggest that it may be sensible to define the actual investment portfolio as the percentage invested in each of the primary asset classes for each unit fund or pooled vehicle in use.
- Rather than place the onus on trustees of DC Schemes to produce this information themselves it may be more appropriate to suggest that where investment is outsourced that "Fact sheets" are made available by the service provider(s) at regular intervals.

- Finally, we appreciate that the Draft Disclosure Regulations are likely to link in with the implementation of this aspect of the Directive. We would be glad to offer comment or review of these whenever they are available.

Article 12 : Statement of investment policy principles

Comment

- During the course of the last two years, many of our own publications have been on the topic of Governance in relation to both running the scheme itself and overseeing the assets. IAPF welcomes the introduction of a requirement to produce a Statement of Investment Policy Principles (SoIPP).
- At present (and by way of background), Section 2 of the IFSRA Code of Conduct (imposed on Investment Intermediaries via the Investment Intermediaries Act, 1995) details the need for an investment management agreement which contains, amongst other things, details of the clients investment restrictions and the discretion available to the manager(s). This is not the same thing as the statement referred to in Article 12 of the Directive. We envisage that the Statement required here is at a scheme level and (while linked) is independent of the ultimate investment structure(s)/provider(s) used.
- The nature of the scheme (and who bears the investment risk) means that any requirements in relation to this Statement need to be high level.

Implementation

- On first reading, the language here does not confer the same level of discretion (in terms of differentiating requirements depending on the nature of the scheme) as pertains to Article 11.
- However IAPF is of the view that:
 - “Principles” by their nature should be pre-determined but allow freedom of implementation, especially given the variability of conditions that exist in providing for retirement.
 - Given that the directive underpins the “prudent person” approach, this strongly suggests that implementing an overly mechanistic approach would be ill advised. Further, we believe that it could constrain trustees and stifle innovation, which may be required to protect and/or enhance retirement provision.
 - The language is broad enough to allow local legislation to specify the requirements in a way that implements the Directive in spirit and practice while making it workable from a trustee perspective.
- The phrases “investment risk measurement methods” and “risk management processes” do not have fixed meaning. In addition, they suggest a predominantly quantitative (and possibly overly prescriptive) approach – this could result in a “rules based” rather “principles based” approach.
- **We suggest, in Appendix 1, some possible pro-formas that can be used by schemes to comply with this provision. There is ample scope for individual schemes to make them as specific as required but do not place an unrealistic burden on the entire spectrum of IORP’s. We would be glad to discuss this in more detail with the Board.**

Article 13 : Information to be provided to competent authorities

Comment

- The Board has pre-established reporting requirements with respect to the information to be provided by individual IORP's. IAPF is supportive of the Board's oversight function including the ability to compel specific information to be disseminated.

Implementation

- It is important that to ensure that pension schemes are run in an effective way. However, to comply with the all of the above requirements is onerous and, depending on the nature and content of the enacting legislation, could add an increased administrative burden (and by extension costs) on pension schemes and their members. This will be particularly so for DB schemes.
- We suggest that some mechanism be agreed which allows, insofar as possible, automatic transmission or collection of the information.
- One way of reading of Article 13.b suggests that the Pensions Board may overlap into territory currently occupied by IFSRA and this needs to be co-ordinated.

Article 14 : Powers of intervention & duties of competent authorities
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Comment

- Paragraph 14.1 points to the need for sound administrative and accounting procedures. As mentioned in relation to a number of previous areas, the nature and complexity of the scheme organisation has a material bearing on what should be required. This falls into the overall governance of scheme's – something IAPF supports.

Implementation

- From an implementation perspective, the transfer of powers mentioned in paragraph 14.3 highlights the need for co-ordination with other agencies such as IFSRA in respect of any overlap in roles or responsibilities.

Article 15 : Technical Provisions
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Implementation

- This article should be implemented in a fashion which strikes an appropriate balance between the reasonable costs of maintaining our existing system and ensuring adequate oversight.
- We support the use of triennial calculations of provisions, augmented by certification of a lesser magnitude in the intervening years.

- Obviously, the nature of the scheme and the promise associated with it should drive the extent to which these calculations are required.
- IAPF does not believe that the home Member State should lay down additional requirements as per Article 15(5).

Article 16 : Funding of technical provisions

Comment

- Maintenance of sufficient and appropriate assets is central to protecting members' interests – IAPF supports this.
- IAPF is also of the view that in situations where a sponsoring entity is underwriting the promise there needs to be some recognition of their role in funding to preserve the level of technical provisions. This should not serve to undermine member's interests, instead supporting the idea of partnership that exists in reality.

Implementation

- We believe that Paragraph 16.1 must be read as setting down the principal standard for full funding, i.e. an institution is fully-funded for the purposes of the Directive if it has "sufficient and appropriate assets" to cover the technical provisions.
- We believe that notwithstanding what follows on, if the legislators had intended the Directive to impose a standard other than "sufficient and appropriate assets" they could have quite easily used an alternative form of words in Article 16(1) by, for example, expressly demanding that institutions always have assets to cover fully their technical provisions. Although this would have still left open what is meant by 'full cover', it would have been stricter than the actual wording "sufficient and appropriate".
- It is worth bearing in mind that the actual choice of wording in Article 16(1) and the reference in Article 16(2) to the need to re-establish the requirements of Article 16(1) indicate that IORPs are fully funded if they have "sufficient and appropriate" assets. There is, therefore, no requirement that full-funding amount to 100% cover of technical provisions for every second of the day.
- We are aware that the concept of "sufficient and appropriate assets" introduces a certain degree of vagueness, but latitude in determining how this level is to be decided is consistent with the principle of subsidiarity. Presumably, the review of the funding standard will deal with this in a substantive fashion.
- The word "appropriate" implies that the amount of assets could vary in different circumstances – we subscribe to this notion.
- Such a 'qualitative' approach is fully in line with the philosophy of the Directive, in particular, with the concept of prudence that is so important in relation to the investment rules. If the Directive can operate with qualitative terms such as prudent person, there should be no objection in principle to "sufficient and appropriate" being a similar and equally dynamic standard.

Article 17 : Regulatory own funds
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Comment

- IAPF does not believe that this provision should have a significant impact on Irish schemes.

Article 18 : Investment Rules

Comment

- The “prudent person” rule is well established in Ireland. We agree with the existence of a qualitative approach as it respects the individual nature of specific IORP’s.
- Based on our interpretation, the specifics mentioned in the paragraphs contained in the article appear non-contentious.

Implementation

- Paragraph 2 – the prohibition on borrowing detailed here may conflict with the provisions of the recent Finance Act which give occupational schemes the ability to borrow.
- IAPF do not believe that Irish legislation needs to include more detailed rules and quantitative limits. The prudent man principle has operated well in Ireland without prescriptive quantitative requirements. This point is particularly reinforced in Recital 31 of the Directive. “In order to protect adequately the rights of members, institutions should be able to opt for an asset allocation that suits the precise nature and duration of their liabilities. These aspects call for efficient supervision and an approach towards investment rules allowing institutions sufficient flexibility to decide on the most secure and efficient investment policy and obliging them to act prudently.”
- We have a question over the meaning of that part of Paragraph 7. Specifically, there seems to be a suggestion that investment in non-EU assets can be restricted by the host state (30% limit mentioned). This potentially goes against a “prudent-person” approach, which is qualitative in nature. Given the presence of a large number of US multi-nationals as sponsoring undertakings this may be viewed as contentious. We would appreciate any clarity the Board can provide on this point.
- Given the specific nature of the proposed investment restrictions, care needs to be taken that consistency in implementation is applied across all Member States.

Article 19 : Management & Custody
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Comment

- This does not appear to be an issue.

<p>Article 20 : Cross-border Activities</p>
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Comment

- IAPF are very supportive of the cross border opportunities of this article.
- We believe that it is important that this Article is implemented across the Member States in a consistent manner so as not to restrict the ability of pension schemes to avail of cross border activities.

Implementation

- Cross Border – Full Funding A significant issue is the requirement for full funding at all times in respect of cross-border activity (16.3). The Directive does not make provision for recovery periods in the case of cross-border activity, but no scheme can guarantee full funding at all times. It also talks of “fully funded in respect of *the total range of pension schemes operated*”. This would appear to suggest that the domestic part of the IORP would have to operate to a higher standard than is allowed in article 16.2. We believe that it should be possible to separate these two areas. With regard to our fuller views on the funding of cross border activity, please note our views under Article 16.
- Notification Procedures Generally, we would like to see a normal registration (Art 9(1) procedure for commencement of IORPs (ie current domestic schemes). The prior authorisation requirement for cross-border activity (Art9(5)) should be seen as a one-off formality for individual IORPs which intend to carry out cross border activity. However, the notification procedure (Art 20(3) and following) may be triggered each time a new cross-border sponsor is sought. The precise method suggested in the Directive is somewhat vague. It is IAPF’s view that national implementation rules should make it clear that:
 - Authorisation for cross border activities is a once off
 - Authorisation should be kept distinct from the notification procedure
 - The notification procedure should be designed to allow a streamlined arrangement, i.e. full procedure for the first one and a more streamlined after that. This is when an IORP would be adding additional sponsors to the current group.
- Social & Labour Law IAPF believe that a relatively narrow view of social and labour law should be taken. Care should be taken to ensure that only social and labour law relevant to occupational pensions should be applied. IAPF believe it would be in the best interests of all if each Member State (to satisfy article 20(5)) would publish in advance their social and labour law applicable to occupation pension provision. This would remove the need for the time period in Art 20(5).
- Information & Language Requirements Article 20(7) (cross border activities) says that a host state may impose its own rules on the information requirements in Article 11 on an EIORP located in another Member State in respect of members located in the host state. This could potentially result in a Member State enforcing onerous requirements. The information requirements as regards cross-border members are only sketchily dealt with by the Directive. We hope that when dealing with the information issue, a proportionate approach will be taken. This is particularly the case if language requirements fall to be dealt with as information requirements and questions arise as to which documentation needs to be translated. We also would wish the option that the Members and sponsors can agree on a language other than the host State language.

Appendix 1

- Pro-Forma Statements of Investment-Policy Principles

Defined Benefit Plans

Scheme Name: ABC Ireland Pension Scheme

Date of Issue: 30/7/04

1. Characteristics of the Scheme

- The scheme is a salary related defined benefit scheme
- It's liabilities are not affected by the investment returns on assets
- Employer and Employee (if any) contributions are dependent on the Scheme's experience
- Members have a direct interest in the sufficiency of the assets of the Scheme (i.e. the extent to which the assets are sufficient to meet the benefits promised) but, apart from that, have no direct interest in the investment returns on the Scheme Assets
- The term of the liabilities are long due to the age profile of the workforce, therefore the scheme can tolerate short term volatility in the value of the assets, if in the long term, the strategy being pursued would maximise return.

2. Investment Objectives

- The long term objectives of the scheme are:
 - To meet the liabilities as they fall due, and
 - To minimise the cost of providing the benefits

3. Investment Policy Principles

- It is the present policy of the Trustees to:
 - Delegate the investment management of the Scheme assets to recognised experts
 - To set investment guidelines and constraints which reflect the trustees wishes and exclude asset exposures that are unacceptable to the trustees
 - To set specific performance objectives which have regard to the investment guidelines/constraints set by the trustees and the level of risk acceptable to them.
 - Review the performance of the scheme's selected investment managers on a regular basis to ensure:
 - That the allocation of the scheme's assets are consistent with the nature and duration of the scheme's liabilities, notwithstanding the existence of temporal imbalances brought about by changes in asset markets or the cost of funding liabilities.
 - That the investment risks being taken on behalf of the scheme are appropriate and that adequate diversification is being achieved.
 - That compliance is maintained with investment restrictions given and/or that they are working within the parameters agreed.
- Review (in line with statutory provisions) the relationship between the assets and the liabilities of the scheme so as to inform their decision-making.

Defined Contribution Plans

Scheme Name: ABC Ireland Pension Scheme

Date of Issue: 30/7/04

1. Characteristics of the Scheme

- The Scheme is a defined contribution pension scheme.
- The employer and employee (if any) contributions are not dependent on the Scheme Assets experience, including the investment returns on assets.
- Members have a direct interest in the option(s) (if any) provided for investment and in the returns and volatility that such funds provide. This is due to the retirement benefit being dependent on the final asset value of the member's account at retirement.

2. Investment Objective

- The principal investment objective of the Scheme Assets is to allow members to maximise their final employee benefit subject to a suitable level of risk.

3. Investment Policy Principles

- It is the present policy of the Trustees to:
 - Delegate the investment management of the Scheme assets to recognised experts
 - Provide access for members to such investment vehicles as provide an exposure to investments which reasonably reflect the memberships term to retirement and risk appetites
 - Set specific performance objectives for any investment options available to members
 - Review the performance of the scheme's selected investment managers on a regular basis to ensure:
 - The nature and characteristics of any investment option(s) utilised adequately reflect the needs of the broad membership of the scheme.
 - That the investment risks being taken on behalf of members are appropriate
 - That compliance is maintained with investment restrictions given and/or that they are working within the parameters agreed.
 - Make available, either directly or via the appointed experts, such information as will enable members to make informed decisions.
- Having selected an investment vehicle(s), the Trustees recognise that they by themselves cannot control the specifics of that vehicle's overall investment activity. Subject to the provisions of the relevant trust deeds and / or policy documents, investments shall for the most part be limited to widely held securities traded on recognised markets, and adequate diversification is required.