An Roinn Coimirce Sóisialaí
Department of Social Protection
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# DEPARTMENT OF SOCIAL PROTECTION CONSULTATION AND INVITATION FOR SUBMISSIONS

# IORPS II Directive 2003/41/EC of the European Parliament on the Activities and Supervision of Institutions for Occupational Retirement Provision

**Issued Friday 18th July 2014**
**(Closing date for Receipt of Submissions Friday September 5th 2014)**

## 1) BACKGROUND - IORPS 2003/41/EC

The first Directive (2003/41/EC[1]) on the activities and supervision of Institutions for Occupational Retirement Provision (IORP) was published in 2003 and was transposed into Irish law in September 2005. This Directive established the basic EU requirements for occupational pension funds and their supervision, including rules obliging schemes to invest their assets prudently. The key goals of the Directive were to:

- provide security for scheme members through a minimum common standard of governance;
- facilitate cross-border pension schemes.

In Ireland, IORP refers to occupational pension schemes. The present directive applies to all Irish occupational pension schemes. However, many of its articles mainly relate to defined benefit schemes. There are over 800 defined benefit schemes with some 180,000 scheme members. The proposed amendments to the IORP directive extend the scope and will significantly impact defined contribution schemes. There are some 60,000 active defined contribution pension schemes with 240,000 scheme members.

Currently IORPs operating within the EU hold assets worth €2.5 trillion on behalf of around 75 million people, which represents 20% of the EU's working-age population.

## 2) BACKGROUND - IORPS II Proposals

The financial crisis had a significant impact on pension schemes. Many schemes lost significant amounts during the crisis. There was also a decline in the number of defined benefit schemes and an increase in defined contribution schemes. This focussed attention on the need for improved governance of pension schemes and also on the need to focus on issues relating to DC schemes, which do not feature strongly in the current IORPS Directive.

Specific problems the IORPS II Directive intends to address includes:

i) The number of Europeans relying on defined contribution schemes, has increased. With defined benefit schemes, assets are pooled and the risk is shared by all scheme members. With defined contribution schemes the responsibility and risks shifts from IORPs and employers to individuals. There is a low level of awareness of what this entails among defined contribution scheme members.

ii) Recent financial and economic crises, which resulted in pension funds losing significant amounts, have shown that current minimum levels of protection for scheme members and beneficiaries needs improving.

iii) Individuals do not receive essential information about their pension in a comprehensible manner, which prevents them from making informed decisions about their retirement financing.

[1] See http://ec.europa.eu/internal_market/pensions/directive/index_en.htm

iv) Supervisory powers are insufficient to ensure that IORPs comply with governance and transparency requirements.

(v) Prudential barriers make it more expensive for employers to join an IORP in other Member States. The experience of employers, IORPs and supervisors over the past years has clearly shown that important prudential barriers restricting cross-border operations of IORPs remain.

### 3) IORPS II

The EU Commission has now proposed that the 2003 IORP Directive be revised to address these issues. The key objectives of the revised IORP II Directive are to;

(i) Give greater protection to scheme members and beneficiaries by introducing:
- new governance requirements for pension schemes e.g. risk management function, internal audit function and effective internal controls;
- Improved risk management and remuneration policies (which refer to the cost of running the scheme);
- new requirements to ensure IORPS are managed professionally;
- a requirement to use a depository for the safekeeping of assets and oversight duties.

(ii) Require IORPS to provide members with clear and relevant information about their pension entitlements by;
- improving information delivered to scheme members and beneficiaries to allow for informed decision making;
- require a simple statement to be provided to all members with the essential information about benefits on a yearly basis (The proposed Directive contains detailed requirements regarding the format and content of these statements).

(iii) Remove obstacles for cross-border provision of services by;
- clarifying the cross-border status of an IORP. A cross border scheme is where the scheme is in one Member State but the members are in another Member State;
- specifying that the host State cannot impose additional investment restrictions and information requirement on an IORP;
- maintaining the requirement for the cross border IORPs to be fully funded.

(iv) Encourage long-term investment in growth-environment and employment enhancing economic activities;
- this would modernise investment rules to allow for investments in assets with a long term profile such as infrastructure etc.

(v) Ensure that the supervisors have the necessary tools to enable them to effectively supervise IORPS by;
- granting new powers in relation to the outsourcing of key functions of a pension scheme and stress testing the financial position of a scheme.
- granting sufficient powers to verify compliance.

Prior to the publication of the revised Directive, there was some discussion around the possibility of introducing stringent solvency requirements for IORPS, which would have had a significant impact on defined benefit schemes. However, this has not been included in the proposed IORPS II.

### 4) Timeframe

The IORPS II proposal will now be considered by the European Parliament and the Council of the EU. This includes participation at EU Member State Working Group level on which Ireland is represented by officials from the Department of Social Protection supported by the Pensions Authority (who in turn engage with officials from other Government Departments where appropriate).

The proposed Directive may be amended as a result of Member State/EU discussions but the underlying import of the Directive is unlikely to change significantly. The proposed deadline for implementation by Member States is 31 December 2016 (but again this is subject to discussion/agreement).

### 6) Consequences for national legislation

As an EU Directive, this will require implementation into Irish domestic law. This may require significant changes to the Pensions Act and relevant regulations.

If passed, this Directive will give the EU Commission the powers to make delegated EU acts in relation to the following three areas:

- Remuneration policies applying to those parties performing the key functions of the scheme (Art. 24)
- Risk evaluations of pension administration (Art. 30). This evaluation forms part of the risk management system
- Pension Benefit Statements (Art 54)

The Lisbon Treaty introduced a new system for delegating to the Commission limited powers to make minor changes to laws, provided these do not affect the "core" legislation decided by Parliament and the Council. The European Parliament and the Council of the EU can revoke these delegations at any time. The EU Commission must report any delegated legislation it makes to the European Parliament and the Council of the EU, who have the power to object to it.

The delegated acts could be passed into law as, for example, an EU regulation, which would be directly applicable; i.e. there would be no requirement on Ireland to implement it into domestic law.

# QUESTIONNAIRE/CONSULTATION DOCUMENT[2]

## SECTION 1 GENERAL OBSERVATIONS/OTHER REMARKS[3]

***Q)*** *You are invited to detail the views of your Organisation in relation to the proposals contained in the revised IORPS II Directive. This may include overarching views or a particular position in relation to the European Commission's Impact Assessment or specific proposals contained with IORPS II.*

The IAPF represents pension savers and works to ensure that those savers can have pensions that are secure, fair and simple. We welcome the opportunity to submit comments and observations on the IORPS II Directive.

We particularly welcome the fact that the proposals do not contain new solvency capital requirements for pension schemes. These requirements would have been particularly detrimental to defined benefit pension schemes in Ireland. We believe that pension schemes require strong governance and that the communication to members of pension schemes can be improved. However we are not convinced that the Directive approaches this is the most effective way.

In the Background to the IORPS II Proposals set out in the Department's Invitation for Submissions there are a number of statements that we would question.

Firstly, the reference to pension funds losing significant amounts as a result of the recent financial and economic crises. As large investors, pension funds suffered as a result of the financial crisis. However pension funds are also long-term investors and returns over the long term remain positive. Unlike may other victims of the crisis, pension funds did not receive any bail-out of public funds to cover their losses. This highlights the ability of pension funds to take a longer term view, and also to adjust benefits payable in order to secure the long-term sustainability of those benefits.

The document states that individuals do not receive essential information about their pension in a comprehensible manner which prevents them from making informed decisions. We have highlighted this issue for some time and the information members receive is prescribed in Irish legislation and can, and should, be simplified without the need for a European Directive.

Similarly, if supervisory powers are deemed to be insufficient to ensure IORPs comply with governance and transparency requirements, these can be amended in national legislation.

It is not clear to us that prudential barriers are the biggest restriction to cross-border operations of IORPs. The vastly different pension systems across the EU and, particularly, the differing tax treatment and regulation of contributions, investments and benefits are much bigger issues that restrict the effective operation of cross-border schemes.

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[2] Please note – Submissions made to the Department of Protection may be made publicly available following the consultation process.

[3] The revised IORP II Directive together with support documents including the Impact Assessment which provides an EU Commission rationale/background to the proposals can be found at. http://ec.europa.eu/internal_market/pensions/directive/index_en.htm

Overall the Directive has many good intentions but the level of detail set out is far too prescriptive. Pension schemes, as they operate in Ireland, are established by employers for the benefit of their employees. They are not financial institutions and involve more of a social partnership element with trade unions often involved in negotiating their establishment and the benefits provided. Members of the schemes are often trustees involved in the governance of the scheme. This needs to be reflected in the type of regulation and supervision that is appropriate and proportionate.

The focus of the Commission should be on improving the situation of the majority of Europeans who do not have access to workplace pensions.

Pension systems across the EU differ greatly and it is extremely ambitious to have a harmonised system of supervision. It would be more appropriate to set out general principles that should apply and allow national regulators and legislators to put the detail around these and put them into practice.

It is also notable that the Impact Assessment published by the European Commission is not sufficiently reliable and fails to satisfy the requirements set out in the Commission's own Impact Assessment Guidelines.

Finally, the issue of proportionality is important. Many of the proposals seem to stem from regulation of financial institutions. The current proposals do not apply to schemes of less than 100 members. It is not clear that this is the correct cut-off point and it may be more appropriate to look at the level of assets under management.

## SECTION 2 KEY PROPOSALS IN IORPS II DIRECTIVE

**TITLE 1: GENERAL PROVISIONS (**Articles 1 to 13)

***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 see the main obstacles to cross-border activity being the differences in social and labour law and the differing tax treatment of pension schemes. Furthermore the requirement to be fully funded at all times is a restriction of defined benefit schemes operating cross-border. The proposed Directive does provide some improvement on the current situation but it fails to address those fundamental issues.

**Any Further Comments Regarding Proposed Title 1 Provisions?**
**Response: {add response here}**

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**TITLE 2: QUANTITATIVE REQUIREMENTS** (Articles 14 to 20 are largely already part of existing IORP Provisions)
**Response: {add any observations here}**

No comments

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**TITLE 3: CONDITIONS GOVERNING ACTIVITIES** (Articles 21 to 37)

***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.)*
**Response: {add any response here}**

We would be concerned that this would exclude member trustees. While we strongly believe that trustees should have certain minimum standards and appropriate training and experience, we are not convinced that this should mean that each individual is professionally qualified. The requirement should apply to the trustee body as a whole. It is also unclear as to what professional qualifications would be appropriate.

***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.*
**Response: {add any response here}**

We believe that the governance requirements are too prescriptive and that general principles should be set out and Member States then decide on implementation. The issue of proportionality is very important as there are very differing requirements for schemes with hundreds of billions in assets and most Irish schemes.

***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.*
**Response: {add any response here}**

We do not see the need for a remuneration policy in the context in which Irish schemes are run and governed. Most of the functions are outsourced. For the small number of schemes that do have internal resource, this resource is usually provided and paid for by the employer rather than the scheme. In these cases, the conflicts that a remuneration policy seems to be trying to avoid do not arise. Furthermore, lay trustees are generally not paid for their roles so any remuneration policy should not require disclosure of their salaries, which are not in any way connected to their role as a trustee.

***Q)*** *What are your views in relation to the proposals which would preclude restrictions on long-term investments?*
**Response: {add any response here}**

We welcome these proposals.

***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?*
**Response: {add any response here}**

We do not see any logic behind this proposal. All DC schemes outsource the investment of assets to investment managers, who are already required under the AIFMD Directive to appoint a depository. This proposal is therefore unnecessary and is only likely to add costs with no benefit to members.

**Any Further Comments Regarding Proposed Title III Provisions?**
**Response: {add any response here}**

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**TITLE IV INFORMATION TO MEMBERS** (Articles 38 to 58)
***Q)*** *What are your views in relation to the proposals regarding information requirements regarding members, prospective members and beneficiaries?*
**Response: {add any response here}**

We agree with the requirements to provide good quality information to members and many of our members put a significant amount of effort into this. However, overly prescriptive requirements hinder this. We would suggest the Commission follows the principles set out in the EIOPA document "Good practices for information provision for DC Schemes". The format in which information is provided should also be considered and should allow for electronic provision.

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

**Response: {add any response here}**

We do not see how this can work in practice. Pension systems are too different across Europe to try and harmonise the requirements. It is also difficult to see how the information, that requires six pages in the Directive, can be condensed into a two page statement. If this proposal were to proceed it is likely that members of Irish schemes will just receive different information, rather than better information.

**Any Further Comments Regarding Proposed Title IV Provisions?**
**Response: {add any response here}**

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**TITLE IV – PRUDENTIAL SUPERVISION** (Articles 59-71)
***Q)*** *What are your views in relation to the proposals regarding general rules for prudential supervision including chain outsourcing and the possibility to require stress tests?*
**Response: {add any response here}**

We believe that the objectives set out in the Directive should be widened, not only to include the protection of members, but to also facilitate the establishment and continuation of pension schemes. Unnecessary regulation, that results in fewer employers willing to establish schemes and greater costs for members, is not in the long-term interest of members.

**Any Further Comments Regarding Proposed Title IV Provisions?**
**Response: {add any response here}**

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**TITLE VI – FINAL PROVISIONS (Transposition)**
***Q)*** *What are your views in relation to the proposed implementation timeframe in the Directive which under the existing proposal would require that Member States bring the new Directive into force by 31 December 2016?*

**Response: {add any response here}**

The timescale would appear to be ambitious.

**Any Further Comments Regarding Proposed Title VI Provisions?**
**Response: {add any response here}**

## SECTION 3 ESTIMATED COSTINGS

***Q) In the Impact Assessment attached to IORPS II, potential cost estimations are provided, in the form of initial once-off costs as well as annual recurring costs, in regards to implementation of various proposals contained in the Directive. You are invited to detail the views of your organisation in relation to the robustness or otherwise of these estimations and/or to provide any alternative estimation of costs (with reasoning) you believe would likely arise in relation to some or all of the proposals.***

**Response: {add any response here}**

It is extremely difficult to evaluate the cost implications as many of the proposals are vague. However we do note that the Impact Assessment does not meet the Commission's own guidelines.