LCP Radar Update

IORP II has finally landed!

Broad ranging legislative changes to pension schemes have been enacted

The Minister for Social Protection formally announced new pension regulations on 27 April 2021. The regulations ('European Union (Occupational Pension Schemes) Regulations 2021') transpose the requirements of the EU IORP II Directive into Irish law.

So what has changed?

Quite a lot as it happens. The regulations are very broad ranging and will require immediate action for many schemes. The ultimate aim of the IORP II directive is to introduce an effective system of governance for the operation of pension schemes across the EU. The requirements range from the qualifications of trustees, appointment of new risk and internal audit function holders, right through to the enforcement powers of the Pensions Authority. We have highlighted some of the key changes below.

LCP Comment: Following a delay of over two years, we very much welcome the transposition of IORP II into Irish law. However, there is a lot for pension schemes to digest and we recommend that sufficient lead in time be provided to allow for full implementation.

Fit and Proper requirements

Trustees will need to demonstrate that they are of good repute and have the qualifications, knowledge and experience which, together with the qualifications, knowledge and experience of the other trustees, are collectively adequate to ensure the sound and prudent management of the pension scheme.

LCP Comment: LCP welcome the fact that the qualification and experience requirements will be a collective requirement as there was some doubt in relation to this point.

Effective System of Governance

The trustees are required to put in place an effective system of governance which provides for sound and prudent management of the activities of the scheme. Written policies on risk management, internal audit, actuarial, remuneration and outsourced activities are required. Key functions must be put in place for (a) a risk management function; (b) an internal audit function; (c) where applicable, an actuarial function.

The risk management function must be structured to facilitate the functioning of a risk management system with procedures in place to ensure key risks can be identified, measured, monitored, managed and be regularly reported on.

The internal audit function must be fully independent of the risk management and actuarial functions. In addition, the legislation provides that, except for exceptional cases where potential conflicts are managed, all key functions in the scheme should be independent of the same functions in the employer.

LCP Comment: While much of what has been legislated for in the area of governance is along expected lines, the amount of work required for many schemes to achieve full compliance is considerable. It is notable that (except for a five year derogation for one member schemes previously established) there is no derogation for small schemes in relation to these requirements and the related administrative burden will be very onerous for smaller schemes.

Investment regulations

There have also been significant new requirements on investment inserted into the Pensions Act. While much of the content is along the same lines as previously covered under the Occupational Pension Schemes (Investment) Regulations, including the requirement to invest the resources of a pension scheme, in such a manner as to ensure the security, quality, liquidity and profitability of the portfolio as a whole, it is notable that derogations in previously for one member arrangements have been removed.

In particular, one member schemes can no longer borrow (existing arrangements may continue) and must make new investments so as to ensure the resources are held predominantly in regulated markets.

LCP Comment: While there has been a five year derogation for existing one member schemes for many of the new governance requirements, the investment regulations apply with immediate effect for all new one member schemes and for all new investments for existing schemes. This, combined with a number of other regulations (eg the requirement for all new one member arrangements to appoint a Registered Administrator), will put this whole area under considerable pressure as providers seek to adapt to higher administration costs and members adjust to the limitations on investment options.

A new system of regulation

The Pensions Act has been amended to reflect the fact that the Pensions Authority shall carry out prudential supervision of pension schemes **on a forward-looking and risk-based approach**, and in a manner that comprises an appropriate combination of off-site activities and on-site inspections. This is likely to result in a move away from a reliance on backward looking snapshots of solvency to an oversight that includes a much higher risk focus.

The Pensions Authority powers have been enhanced with explicit provisions made for a supervisory review process whereby the regulator will review the strategies, processes and reporting procedures established by the trustees of a scheme. The Pensions Authority may also require trustees to carry out stress tests or an external report with the scope and timetable set by the regulator. A new Advisory Notice process has also been put in place to enable the Pensions Authority to formally notify pension scheme trustees of any areas of concern.

An annual compliance statement will be required to be completed, the first of which will be due no later than 31 January 2022, in respect of the calendar year 2021.

Finally, the provisions in relation to whistle blowing have been considerably expanded. The responsibility to whistle blow now extends beyond material misappropriation and fraud to any material breach of the Pensions Act that could have a significant impact on the interests of the members (and have not been remedied within 21 days). Key Function Holders have been added to the list of relevant persons with whistle blowing responsibilities.

LCP Comment: The move to a forward looking risk based approach to regulation is welcome and is ultimately in members' best interests. The timeline for completion of a compliance statement is quite short – particularly if full compliance with all aspects of the regulations is expected to be part of the certification for 2021. All relevant persons covered by the new whistle blowing regulations should set out appropriate procedures for dealing with actual or potential breaches given the significant responsibilities being imposed.

Disclosure of Information

A Pensions Benefit Statement, with new, additional disclosures is required to be prepared once annually for all members with the first such statement to be issued in 2022. While the derogation in relation to preparation of audited accounts has been maintained for small schemes, there is now a requirement to prepare a Statement of Investment Principles.

LCP Comment: The enhanced disclosure requirements will further increase the administrative burden for pension schemes.

Timelines

Most of the new governance provisions have immediate effect for all pension schemes (there are some provisions with deferred implementation for one member schemes). There is quite a lot of detail where clarification would be very useful in the form of guidance from the Pensions Authority. The Pensions Authority in turn have indicated that they are *"reviewing the detail of transposition and will provide further information and guidance over the coming weeks and months"* with a series of guidance notes to be published over the period May to December 2021.

LCP Comment: While we welcome the additional clarification and guidance from the Pensions Authority, it is likely to be somewhat frustrating for trustees and pension scheme sponsors that the publication of the guidance will come some time after the legislation is in force.

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