

Summary

- The IORP II Directive comes into effect on 13 January. It includes provisions regarding an effective system of governance for trustees, transparency, ESG practices, amendments to the cross-border regulatory framework, encouragement of risk-based regulation and the transparency and protection of data.
- While the new regulations should still mean ‘business as usual’ for UK schemes, one major change is a requirement to send an annual benefit statement. However, the upcoming pensions dashboard may cover this requirement.
- The most significant part of the directive is expected to be its focus on enhanced governance.
- If the UK gets a withdrawal agreement on Brexit, the IORP II Directive will still apply for pensions. However, this is more uncertain in the event of a no deal Brexit.
- Implementing IORP II has been in the shadow of GDPR and GMP equalization in 2018 but is likely to come to the fore in 2019.

About 15 years ago, the initiative to stimulate cross-border pension funds growth was implemented. The original directive on the activities and supervision of Institutions for Occupational Retirement Provision, or so-called IORPs, was meant to grow together with the European single market. But parallel to the UK’s reconsideration to its EU membership, the IORP Directive is having its own revision – IORP II.

The IORP II Directive, which comes into effect on 13 January, includes provisions regarding effective system of governance for trustees, transparency and disclosure of information to scheme members, ESG practices, amendments to the cross-border regulatory framework, encouragement of risk-based regulation and transparency and protection of data and information held and used by TPR.

The regulations, confirmed by the UK parliament on 23 October 2018, do not apply to master trusts and public service pension schemes that fall under the 2017 and 2013 Act definitions, but do apply to all other occupational pension schemes like defined benefit and defined contribution.

The Pensions and Lifetime Savings Association (PLSA) has worked closely with the government on the IORP II Directive for several years, seeing

it go through the European Union’s legislative process to discussing it with the Department for Work and Pensions and becoming law, PLSA policy lead, engagement and EU, James Walsh, explains.

He highlights that while the deadline might be this January, this is very much only for the government. “We have been keen to avoid a scenario where the IORP II Directive leads to substantial new administrative requirements on schemes and although we await to see the details, it looks like that’s the direction the government is heading in.”

Business as usual

“Schemes will only have to act when the government, or rather The Pensions Regulator (TPR) is telling them to do so. And that won’t be anytime very soon,” Walsh says.

TPR interim executive director of regulatory policy, Anthony Raymond, said in a recent speech that the regulator will make clear what is expected of schemes in sufficient time, to make any changes with minimum cost and disruption.

“From our point of view, for those schemes that continue to operate poor systems, we will be able to take more targeted and timely action against them as there will be clear and enforceable legal requirements in place,” Raymond

New rules

Sunniva Kolostyak explores the upcoming implementation of the IORP II Directive, how the UK will implement this European regulation in the shadow of Brexit, and the extent of the impact the directive will have on pension schemes

said, anticipating a consultation on the implementation around late spring 2019.

Walsh says the PLSA expects changes to be quite modest. “The government is really stressing that it wants to implement IORP II by pointing to existing practice, things that schemes already do, rather than introducing many new requirements.”

An unavoidable change is the annual benefits statement, which pension funds will be required to send all its members, something which UK defined benefit schemes are not required to at the moment.

This is a major new requirement, Walsh says. However, he notes that the government aims to have this covered by another disputed initiative with its own timetabling issues – the pensions dashboard.

“The government is saying that once the dashboard is in place, that will provide members of DB and DC schemes alike, including deferred members of DB, with sufficient information to satisfy requirements in the IORP II Directive.”

Enhanced governance

However, the most significant part of the directive is perhaps the focus on enhanced governance. Sackers associate director Ferdinand Lovett says it will be a case of codifying policy directions that have been on the agenda for UK pensions

for a while, in terms of systematizing and creating a structure around governance.

“I think it is fair to say that we will not know the full detail until the code has come out but I think it is a question of communicating to clients that it is business as usual in terms of good governance,” Lovett says.

“It will be a question of checking what they are doing is in line with the new requirements. What the new regulations do is for those schemes that could do better, it puts a structure in place and gives some direction in terms of what good governance looks like.”

In his view, IORP II provides a structural backbone off which the changes to the Pensions Act 2004 and the codes of practice will hang off. In addition, it will align with TPR’s 21st Century Trusteeship programme.

The directive also brings in the own risk assessment (ORA) for outlining key risks. According to TPR, schemes will need to perform an own-risk evaluation at least once in every three years and immediately following any significant change in the scheme’s risk profile, considering integration in different processes, funding, operations and ESG.

Brexit

With most questions relating to politics, the uncertainty caused by Brexit affects the IORP II Directive too. The elephant in the room, as Walsh describes it, will however not act as an immediate obstacle.

“Obviously there is a huge amount of uncertainty, but what the government has always said is that as long as the UK is a

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member of the EU, then we will meet our obligations in full.” This would of course include the 13 January deadline, which arrives before the start of a transitional period, so the United Kingdom will still be an EU member state.

However, if the Prime Minister’s withdrawal agreement gets passed through the House of Commons, “and that’s entirely uncertain”, Walsh points out, “then that really maintains things pretty much until the end of December 2020. So we would then expect the process of going ahead with implementing IORP II to continue.”

“If we don’t get a transitional phase, perhaps because we leave on a no deal, then that’s a different situation and the government then has to decide what it wants to do about implementing IORP II. That would be influenced, I’m sure, by other factors such as what contingency arrangements we put in place, and what continuing relationship there might be between TPR and EIOPA,” Walsh speculates.

“Despite Brexit, the directive does apply to us,” Raymond said in his speech at Pensions Research Accountants Group. “The good news is that because the UK was influential in drafting IORP II, and so it aligns with the direction of UK policy, DWP were able to transpose IORP II without lots of new legislation,” he said, pointing out that the new legislations cover effective governance systems and the cross border regulatory framework.

The two Gs

DLA Piper partner Matthew Swynnerton explains that in 2018, Brexit has not been the biggest matter up for discussion for schemes. He says that on the trustee side, it is the introduction of the GDPR, and addressing issues in relation to GMP equalisation in light of the Lloyds judgment earlier this year, that has ruled the conversation.

“Due to the fact that the publication of TPR’s codes of practice on IORP II regulations are not expected until 2019, and the government stating its intention

to give schemes sufficient time for familiarisation with and planning for the implementation of IORP II, this isn’t high on many trustee meeting agendas at the moment, especially given that there are more pressing matters,” Swynnerton says.

Lovett agrees that IORP has ended up in the shadow. “To be brutally honest, I think clients have been grappling with the two Gs, GDPR and GMP equalisation. I suspect it is going to be more on business plans for 2019.”

However, Lovett points out the new regulations will be an opportunity for schemes who are not entirely sure that their governance is fit for purpose to review policies internally.

The cross-border side of IORPs has faced long-standing issues as the original directive required cross border schemes to be fully funded at all times – “that’s possibly one of the reasons there are very few cross-border pension schemes”, Walsh says, as the regulatory requirements are demanding.

Spurring the development of cross-border pension schemes was the main point of the original 2003 IORP Directive, as part of the development of the European single market. This has, however, not happened.

The PLSA has been keen to see the funding requirements relaxed in IORP II and indeed it has been, Walsh says. The language, however, has the “classic euro touch” where it in one sentence says schemes need to be fully funded, while in the next one it says it does not. However, the PLSA takes this as a relaxation of the rules.

“I think that’s sensible, it will make it a little easier to set up an operative cross-border scheme,” Walsh says, however barriers such as different tax regimes must still be taken into consideration.

While the consensus seems to be similar across the industry, that the expected changes will be mellow, Walsh says elements are still uncertain. “We await to see what that means in practice.”

➤ **Written by Sunniva Kolostyak**