

IORP II PENSIONS AUTHORITY INFORMATION FOR TRUSTEES

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Pensions Authority issues draft Code of Practice for trustees

Following the transition of the IORP II Directive into law on 22 April 2021 the Pensions Authority have published a draft code of practice for trustees of occupational pension schemes. The document contains details of the Pension Authority's minimum expectation of trustees under six headings, Governance, Administration, Internal Control Systems, Investment, Defined Benefit Financial Management and Fit & Proper Requirements.

The code is subject to a consultation process; however, it provides trustees and scheme sponsors with a basis for reviewing their current governance plan and identifying any gaps.

This update summarises the pension Authority's expectations for the conduct and practice of trustees, it is likely to replace the DC Codes of Governance issued in 2016 as many of the areas covered in those codes are incorporated into the draft code of practice.

Many of the items covered in the draft codes were well flagged, however there are some new requirements not previously mentioned, for example: -

- **Trustee Meetings**
 - Trustees must appoint a secretary to the board of trustees who will be responsible for circulating the agenda and other paperwork in advance of meetings and will record the minutes of each meeting.
 - Trustees must appoint a Chairperson to lead meetings and who will be responsible for ensuring that all items stated on the agenda have been completed.
 - Where trustees have an appointment to more than one scheme each meeting must be scheme specific.
- **Written Policies**
 - Trustees must have written procedures for the appointment of service providers, member engagement, trustees skills knowledge & experience, on selecting Key Function Holders, and must retain documented evidence of compliance with these procedures.
- **General contract terms for outsourced activities**
 - Detailed specifications to be included in contracts with service providers
- **DB Financial Management**
 - For DB schemes, the trustees will need to verify the contributions to the scheme will be adequate to meet the cost of ongoing benefit accrual and must consider whether there are any threats to the current contributions.

The draft code covers all the areas trustees will need to consider in managing their scheme in a complaint manner, including: -

- **Chapter 1 General governance requirements**

Trustees must ensure that the scheme has an effective system of governance that provides for its sound and prudent management. This chapter sets out the actions that the Authority expects trustees to take to ensure satisfactory governance of their scheme, this includes details on the following: -

 - General Scheme Management
 - Trustee Meetings
 - Documentation of decisions reviews and actions taken by trustees
 - Written policy on Data Strategy
 - Written policy for conflicts of interest for trustees and Key Function Holders
 - Written contracts that are legally enforceable for all outsourced activities
 - Written procedures for the appointment and review of service providers
 - Remuneration policy
 - Member engagement, trustees must prepare a written policy regarding the ways in which they will engage with members

- **Chapter 2 Administration**

The trustees must create and maintain a written administration policy which must cover the following: -

 - The purpose of the policy should be defined in terms of its specific goals
 - The scope of the policy should be defined
 - The role and responsibilities of all stakeholders involved in the administration of the scheme needs to be identified
 - Data management
 - Reporting of information that must be provided by the administrator to the trustees, to KFHS, to the Authority and to any other service provider
 - Written policy and procedures identifying the employer's role and obligations in the administration process
 - Written administration contract with service provider
 - Quarterly review by trustees of the administrator's performance followed by an annual written assessment

- **Chapter 3 Internal control system**
 - Trustees must put in place an effective internal control system that provides reasonable assurance that a scheme is compliant, properly administered and managed and has appropriate reporting systems
 - Trustees must have clear and robust accounting procedures that define how the scheme will record, classify, and summarise financial transactions
 - Trustees must put in place an effective internal control framework that includes well functioning risk management and internal audit functions. The main elements of this internal control framework are risk management, the establishment of well-identified internal controls that monitor risks, and an ongoing process that monitors and reviews the internal controls
 - Risk Management Function – The policies governing the risk management function must be structured in such a way as to facilitate operation of the trustees' risk management system

The risk management function must be well integrated into the decision-making processes of the scheme. The risk management function is to be overseen and executed by a risk management KFH

- Risk Management Policy - Trustees must have a documented risk management policy that provides a framework for the management of risk
 - Own Risk Assessment - Trustees must have a documented ORA process to identify and assess risks that threaten achievement of the scheme's objectives
 - Internal Controls - Trustees must put in place internal controls that are sufficient to ensure that the scheme is managed well and in accordance with the scheme rules, the Act, and other relevant legislation:
 - These internal controls must consist of policies and procedures that ensure that any risks identified by the trustees' risk management system are prevented or reduced to an acceptable level.
 - Monitoring and review of internal controls - Trustees must have processes and procedures in place for examining and assessing whether the scheme's internal controls are functioning properly.
 - Internal Audit Function - To assist the trustees with the monitoring and review of internal controls, they must establish and maintain an effective internal audit function that is overseen and executed by an internal audit Key Function Holder.
 - Internal Audit Policy - Trustees must have a documented internal audit policy that provides a framework within which internal audit is able to provide objective and independent assessments and advice to the trustees. Minimum scope of the internal Audit Policy are set out in the codes
- Chapter 4 Investment
 - Statement of investment process
 - Setting the investment objectives and strategy
 - Implementation of investment objectives and strategy
 - Investment Contracts
 - Overseeing investment performance
 - Safekeeping and administration of scheme assets
 - Chapter 5 Defined benefit financial management

This chapter specifies the kinds of studies and evaluations that trustees must commission and consider in their management of DB schemes. In line with the trustees' governance, financial management, and risk-management responsibilities, they must:

 - ensure that they have access to the necessary financial and actuarial data to meet their responsibilities, and
 - have a proper understanding of the issues related to the funding of the scheme.
 - Solvency - At appropriate intervals, trustees must review the solvency of the scheme, using a range of bases of calculation
 - Sustainability - At appropriate intervals, trustees must confirm that the contributions to the scheme will be adequate to meet the cost of ongoing benefit accrual and must consider whether there are any threats to the current contribution rate
 - Financial Risk - At appropriate intervals, trustees must commission and consider quantitative estimates of the likelihood that the scheme will develop funding shortfalls relative both to the funding standard and to the trustees' own funding objectives

- Support from sponsoring employer - Trustees must form a comprehensive view of the scheme's ability to absorb financial risks through the quantitative assessment described above and through regular discussions with the sponsoring employer
- Chapter 6 Fit and proper requirements
The Act requires that trustees and KFHS must be fit and proper, chapter 6 of the code sets out in detail the fit and proper requirements for trustees and Key function holders and the ongoing compliance required

What happens next?

Following the consultation process a final code of practice will be published in the week commencing 15 November 2021.

We strongly recommend that employers and trustees examine the draft code to be familiar with the new requirements. The first Annual Compliance Return is due to be submitted by trustees by the 31st January 2022. This does not provide trustees or employers much time to consider the final code of practice and implement the necessary policies and procedures to ensure compliance.

For some schemes the new regulations may be too onerous, and they may look to an alternative solution such as the APT Master Trust which undertakes all of the governance and fiduciary responsibilities on behalf of the sponsoring employer.

If you have any questions on this update, please contact either.

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