Regulatory Impact Assessment

This is in two parts. Part 1 deals with the Regulatory Impact Assessment in relation to the Defined Benefit pension provision changes. Part 2 is a Regulatory Impact Assessment dealing with the changes to the Funding Standard.

Part 1: Regulatory Impact Assessment in relation to Defined Benefit Changes

STEP 1: Summary of Regulatory Impact Assessment

The changes to the defined benefit model as announced are as follows:

I. *Agree for the drafting of legislation for the following changes to the defined benefit model to allow for :*

   a. *the introduction of a risk reserve into the funding standard, with a long lead in time;*
   b. *changes to the revaluation of scheme benefits to ensure greater equity between deferred and active scheme members;*
   c. *The introduction of a statutory mechanism that requires a scheme to wind up where it is clear that even following benefit reductions a scheme will not be sustainable.*

II. *Agree for the drafting of legislation to change the current priority given to existing pensioners on the wind-up of a DB pension scheme by introducing a benefit threshold on the amount and percentage of payment that will be provided in the initial distribution of scheme assets.*

The Regulatory Impact Assessment focuses on point Ia. above and the potential cost and benefits of the proposal to require DB pension schemes to hold risk reserves. Items Ib and Ic are more straightforward and item II is being currently given further consideration.

In terms of policy, the changes form the final part of a suite of measures introduced to assist DB schemes. The proposal to introduce a risk reserve is intended to change how DB schemes are structured. The primary policy objective is to bring increased stability to DB pension provision and lessen their exposure to risks.

In terms of increased costs, the requirement for increased funding could lead to additional funds of the order of 10% being required, but this is mitigated by the fact that it is intended that the Funding Standard will give credit to schemes that reduce their equity risk and where enforceable employer guarantees are in place. Scheme liabilities can also be reduced through the purchase of Sovereign Annuities which were provided for in legislation in 2010. Schemes that take this route may not in fact have to increase their funding and this makes the proposal potentially cost neutral. Changing trustee behaviour is an additional and important benefit of the proposal.

A consultation with the pension industry was undertaken on the measure and there was broad support for the proposal subject to the caveat that a long lead in time would be required. The final proposal has taken into consideration the outcomes from the consultation.

STEP 2: Description of Policy Context and Objectives

Policy Context

This Regulatory Impact Assessment (RIA) deals with the proposal in the draft Memorandum for Government to introduce changes to defined benefit (DB) pension provision.

The background to the proposal is that DB schemes have been under pressure since 2000 because of the volatility in stock markets and poor investment decisions. These shocks to the funding position of schemes have been combined with structural and demographic changes affecting schemes. Increasing longevity has added to the number of pensioners on pension schemes, and also the length of time for which pensions need to be paid.

Between 1980 and 1999, the DB pension environment was healthy with average pension schemes managing fund returns of the order of 20% per annum. Periods of poor performance were unusual and relatively short lived. Until 2000, few schemes had any difficulty meeting the Funding Standard.

However, DB pension schemes have suffered a series of shocks over the last number of years. Many DB schemes had funding difficulties since the downturn in financial markets in 2001 and 2002 and the structural drop in interest rates. Subsequently, 80% of DB pension schemes restored their required funding levels. However, the 2008 downturn in the financial markets put in excess of 90% of schemes into an underfunded position, and while there has been some recovery since in the markets, the situation is still volatile and many schemes remain in a difficult funding position. The precise position of DB schemes will not emerge until the Funding Standard is re-introduced. However, following a survey of DB schemes undertaken by the Pensions Board in 2010, an estimate of the funding position of DB schemes is set out in Table 1.

Table 1. Estimated funding position of DB schemes – 2010.

Funding Level	DB schemes
<50%	2%
50% - 60%	20%
60% - 70%	31%
70% - 80%	17%
100%	30%

The number of DB schemes has been reducing over many years: at the end of 2010 there were just over 1,000 DB pension schemes with 222,000 active members, down from 1,200 schemes with 254,000 members in 2009, 1,500 in 2003 and just over 2,500 schemes in 1991.

The continuous and persistent nature of the difficulties being experienced by DB schemes has led to the conclusion that there are significant structural problems with the current design for funded DB schemes. The National Pensions Framework contained proposals for the development of a new DB model to address these difficulties. The development of these proposals was put forward as a final response by the previous Government and the last part of the suite of measures introduced over the past few years.

Immediate Policy Objectives

These were already outlined earlier at Step but are as follows :

I. *Agree for the drafting of legislation for the following changes to the defined benefit model to allow for :*

   d. *the introduction of a risk reserve into the funding standard, with a long lead in time;*
   e. *changes to the revaluation of scheme benefits to ensure greater equity between deferred and active scheme members;*
   f. *The introduction of a statutory mechanism that requires a scheme to wind up where it is clear that even following benefit reductions a scheme will not be sustainable.*

II. *Agree for the drafting of legislation to change the current priority given to existing pensioners on the wind-up of a DB pensions scheme by introducing a benefit threshold on the amount and percentage of payment that will be provided in the initial distribution of scheme assets.*

Ultimate Policy Objectives

The primary aim of the proposed changes to the DB pension provision model are the same as apply to DB provision generally ; to provide a secure pension for its members into the future and also to help ensure the sustainability of DB schemes.

The proposed immediate changes will:

- Assist schemes manage shocks such as downturns in the financial markets ,
- Provide more flexibility in its design and give schemes trustees more management options,
- Minimise the need for widespread Section 50 type reductions/restructuring (which is explained further below),
- Provide a stable solution so there should be no requirement for the continuous legislative and regulatory interventions that have taken place over the last number of years.

STEP 3: Identification and Description of Options

The ad hoc group established to develop the DB model concluded that if current defined benefit model is not changed, it is inevitable that in all but the most optimistic outcomes every DB scheme will sooner or later accumulate a deficit that requires a reduction of benefits under Section 50[1].

[1] Section 50 of the Pensions Act allows the Pensions Board under certain conditions to grant permission to schemes to reduce pension benefits. Any reduction in benefits under a Section 50 notice can apply to the pension rights of active and deferred scheme members and to post retirement increase in benefits for all scheme members.

The conditions under which the Pensions Board can allow schemes to restructure scheme benefits relate to the scheme's failure to satisfy the Funding Standard.

An initial consultation took place with relevant stakeholders in the pensions industry in October/November 2010. The ad hoc group then developed a consultation document which:

- proposed 3 main options (and some sub options) for defined benefit
- asked a series of questions to gauge views on the key difficulties facing schemes and the way forward;

The options proposed are:

Option	Outline
Option A	This is essentially a minimalist option; it involves the re-imposition of the funding standard modified only to take account of sovereign annuities/bonds and legislative change to facilitate adoption of the new DB model as a form of scheme design. While this option is included for the purposes of the consultation process, the retention of the status quo would not address the problems facing the current DB system as set out above.
Option B	This can be characterised as a further strengthening of the current solvency regime for DB schemes including new requirements aimed at encouraging improved risk management on the part of schemes. It also incorporates legislative change to facilitate the adoption of the new DB model as a form of scheme design. Under this option, the new solvency regime would be introduced after a lead in time of a number of years.
Option B1	This is identical to Option B but the changes to the solvency regime would be introduced in the short-term, i.e., from the beginning of 2012.
Option C	This involves the adoption of a new funding standard (to apply to past accrued and future benefits) as well as legislative change to facilitate the adoption of the new DB model as a form of scheme design.
Option C1	This is a variant of Option C; the proposed new funding standard would only apply in respect of future service.

2. The following are the 10 questions contained in the consultation document

    1. *Is the analysis accepted that DB schemes, as currently organised, are too exposed to economic shocks?*

2. *Is it accepted that under the current DB structure most schemes are not in a position to provide a "promise" to their members that is reasonably predictable and enjoys a high level of security?*

3. *A revised approach to DB provision should be one that provides a "promise" to scheme members that is reasonably predictable and that enjoys a high level of guarantee. Which of the options best advances this objective?*
4. *Any new approach to DB provision should be one that is robust in the face of economic difficulty and downturns in financial markets:*

   a) Would the introduction of risk reserves and the new stipulations around recovery periods under Option B offer a sufficient protection for schemes in future? Or

   b) Is it necessary to adopt Option C if schemes are to further enhance their security in the future?

5. *A desirable feature of new DB system would be that of design flexibility meaning that scheme trustees could employ adjustment options other than reliance on employer contributions.*

   a) Under all options, a legislative change to allow trustees greater discretion as regards the revaluation of deferred members' benefits is envisaged. Would this change significantly enhance flexibility in scheme management?
   b) Under both Options C, the revised funding standard would only apply to core benefits; other benefits would be discretionary. As the level of core benefits would be a matter for scheme-level determination, is it accepted that this option would significantly enhance flexibility?

6. *Once the existing funding standard or a revised one is re-introduced/introduced respectively, a significant number of DB scheme restructurings including benefit reductions through the Section 50 process can be expected. However, following this period, it would be expected that future DB benefit reductions would be less common. Accepting that significant scheme restructuring in the near term is likely to be inevitable under any scenario, is there a view as to which of the options would reduce the need for benefit reductions in the future?*

7. *It is intended to bring a degree of policy and regulatory stability to the DB sector after the period of uncertainty of the last few crisis years.*
   a) How likely is it that further major regulatory changes could be avoided over a medium-term timeframe if Option A, or either of Options B, which could be characterised as minimalist or incremental in nature, were to be adopted?

   b) *Given the stated intention of the European Commission to examine the existing EU solvency framework as part of its review of the IORPS Directive, what is your view as to which of the options presented here is likely to conform best to any new EU standards?*
   c) *Would the adoption of Option C1, which would result in a dual funding standard regime in operation, of itself create a degree of uncertainty and instability?*

8. *Government policy aims to minimise the degree of regulatory and administrative burdens associated with new policy initiatives. Against this backdrop, views on the degree of additional regulatory and administrative burden associated with the options under consideration would be of interest. In particular, what would be the implications for schemes of the dual funding standard regime inherent in Option C1?*

9. *Taking account of your responses to the above, which of these options presented in this paper would your organisation prefer to see adopted?*

10. *Does your organisation wish to propose another option or variant of the options presented above that would meet the objectives articulated for a new DB system?*

Step 4 Consultation (Responses)

The consultation paper on "Proposed Approach to Defined Benefit Provision" with the options as outlined in Step 4, was issued in April 2011 to the following;

- Society of Actuaries in Ireland (SAI)
- Irish Association of Pension Fund Managers (IAPF)
- Irish Business and Employers confederation (IBEC)
- Irish Congress of Trade Unions (ICTU)
- Association of Pension Lawyers in Ireland (APLI)

In addition, the following organisations also contributed to the consultation: UNITE, Irish Life, PWC, AON-Hewitt, Mercer, KPMG, Tower Watson, INVESCO, Musgrave, McElvaney Consultants and IBA.

All groups were offered the opportunity to meet with officials to present and discuss their response to the consultation paper. The Minister for Social Protection was present at the meeting attended by SAI, IAPF, IBEC, ICTU and APLI. The consultation process was concluded in June 2011.

A summary of the responses to the options proposed in the consultation paper are in Appendix 1.

Key Messages from the Consultation

All groups agreed that DB schemes as currently organised are too exposed to shocks. No clear view emerged as to whether schemes are in a position to provide a "promise" to their members that is reasonably predictable and enjoys a high level of security.

Many of the participants favoured option A but many also supported option B. On the basis of the feedback from the submissions and the discussion during the consultation in the context of widespread agreement on the fact that DB schemes are too exposed to shocks, the original proposal was revisited to form the final proposal.

Additional points which emerged from the consultation:

- The priority order provided to pensioner benefits in windup needs to be addressed.
- There is strong support for the concept of moving to a risk reserve approach (option B). However, the transition to this approach would require an appropriate timeframe and transition measures to ensure all viable schemes were secured.
- The use of a voluntary "enforceable employer guarantee" should form part of the funding standard. (This is being considered by the Pension Board who have no difficulty with the proposals as long as the employer guarantee is, in fact, enforceable.)
- The current administrative procedures related to the funding standard should be overhauled;
- Less stringent funding criteria should apply to funding proposals which requires the Pension Board to issue a Section 50 notice to reduce scheme benefits.

STEP 5: Analysis of Costs, Benefits and Impacts of the Options

Introduction

The cost benefit analysis aspect of this exercise was undertaken within the policy development process by the ad hoc group during a series of meetings and before, during and after the consultation process.

Option A and Option B as outlined in the DB Consultation document are dealt with below. Option C in the consultation document is not analysed in detail here. It is based on the current Dutch defined benefit pension model, and while representing the best practice in DB scheme

design, it is accepted that it would, if implemented, require considerable additional costs to schemes as well as a significant increase in administration. At the consultation, there was consensus that this option should not be pursued and this was agreed by the ad hoc group.

Cost and Benefits of Option A

This option is minimalist in nature incorporating a number of changes to the existing model, including (i) legislative changes to the revaluation of scheme benefits to ensure greater equity between deferred and active scheme members and (ii) changes to enhance the powers of the Pensions Board including requiring a scheme to wind up.

The implementation of the legislative changes involves no costs to the schemes and the proposed technical change to revaluation provides increased equity in the annual revaluation of scheme benefits. However, this option does not address the fundamental deficiencies in the current DB model. It would mean that schemes would continue to be exposed to the volatility of the markets with the consequent impact on member's benefits and resulting costs. Neither does it do anything to influence trustee behaviour by encouraging some move away from equity investment.

Costs and Benefits of Option B

Option B incorporates the attributes of option A but the proposal went further in that it:

(i) introduced a mechanism to facilitate the operation of a discretionary revaluation system,

(ii) included a requirement for schemes to build up a risk reserve.

Core/Discretionary Benefits: In relation to (i) the new DB model aimed to provide for a mix of core and discretionary soft benefits, with the core benefits, the level of which can be determined within each individual scheme, providing a greater level of certainty than is the case under the current DB system. The view was that the mix of core and discretionary soft benefits would give schemes more flexibility to absorb losses and deal with volatility in an environment where increases in employer contributions are unlikely. This meant that in years of negative investment returns, scheme trustees would have the flexibility to grant little or no revaluation (soft benefits), while in years of positive returns, trustees would seek to provide the revaluation that had not been paid in previous years. However, the outcome of this would be that at a given level of contribution, the new DB model would provide a lower level of guaranteed benefit, and would maintain a significant level of ongoing reserves.

During the consultation process, this option was examined in-depth and it was decided not to proceed with this aspect of it (there is a lessor technical issue in relation to the impact of negative CPI on revaluation which also needs to be addressed). The view was that there was a

risk that schemes would move to provide only a core benefit resulting in a reduction in benefits. Also, significant difficulties emerged during discussions on transitioning schemes to a new regime, in particular in relation to benefits already accumulated. This option would have resulted in a two tier system with two Funding Standards and a resultant significant increase in regulation and administrative costs.

Risk Reserve: With regard to (ii) the benefits of the risk reserve are that: it gives schemes a "buffer" - when shocks occur, it puts in place a structural mechanism to give some protection to schemes against the persistent volatility they have encountered since 2000; also the design of the proposal encourages more prudent investment by trustees - it has a built in incentive (outlined below) to encourage trustees to move away from an over reliance on equity holdings. Therefore, it fulfills the purpose of the original exercise.

In relation to costs, the introduction of a risk reserve will add to scheme liabilities. The actual impact on a scheme's funding position of implementing the risk reserve aspect of this option will vary depending on two key factors: (i) the scheme's pensioner liabilities, (ii) the scheme's planned holdings of assets that require a risk reserve (the size of the risk reserve is within the power of the trustees to increase or reduce by changing the scheme's asset allocation). Neither of these effects is definitely quantifiable but it can be estimated that the overall effect would be to increase the level of the funding standard in the order of 10%. This 10% assumes that most of the scheme's assets remain in equities attracting a risk reserve, but this could be offset by a move to bonds/annuities[2] with a resultant credit under the funding standard. Therefore, 10% represents the maximum increase in additional scheme costs and may not, in fact, need to be met. Therefore, while potentially adding to scheme costs, if trustees avail of the credit in the Funding Standard the proposal has the potential to be cost neutral. This proposal would also be facilitated by the introduction of the sovereign annuity – due to be introduced shortly. The costs of the proposals also need to take into consideration that some schemes (it is not possible to accurately predict how many) are still underfunded and may perceive a risk reserve as an additional further cost. However, the overriding consideration is the need for longer term stability in this important sector, and the introduction of a "buffer" over a long period to absorb risk is intended to do that.

The potential for the proposal to be cost neutral is also important in the context of the recent introduction of the pension levy (which was announced during the consultation process), which adds to scheme liabilities. The timeline required to increase funds for the risk reserve is significantly longer than the duration of the levy.

[2] (While it is apparent that there are many fluctuations in the bond market at present, over the longer term bond markets have traditionally been more stable than equity markets).

With regard to impacts on scheme members, the proposal aims to improve the security of the promise to members and give stability to schemes for the future.

A further option in relation to meeting the additional reserves emerged during the consultation with instruments such as employer covenants/enforceable employer guarantees providing the potential to meet the need for additional funding requirement without actually requiring employers to provide the funding. This option has been examined in a positive way by the Pensions Board and it is intended to give effect to it, subject to conditionality around ensuing that any such guarantee would be enforceable.

A further benefit is that the step towards a risk reserve is likely to reflect the emerging thinking from the EU on the direction to be taken on DB schemes.[3]

Conclusion

It was decided not to proceed with the original Option B as proposed in the consultation document. A less significant change to DB design was proposed. This can be summarised as Option A plus the proposal of a risk reserve from Option B.

Administrative Costs to schemes of the introduction of a risk reserve

The extended time period of approximately 11 years allows schemes to build up their funds for a risk reserve and should not cause any significant additional administrative burden as the changes proposed are taking place within existing procedures. Under current procedures, the Pensions Board gives 3 years to a pension scheme to make up a deficit but this timeline can be extended for a further period, depending on the funding position of the scheme. The timeline allowed to a scheme is at the discretion of the Pensions Board.

However one of the concerns raised at the consultation related to the administrative burden associated with the existing Funding Standard. As a separate exercise, the Pensions Board have since had a number of meetings on introducing changes to reduce the administrative burden (and therefore administrative costs).

[3] The EU is reviewing the IORPS Directive. Incorporated within the review is a potential move to a Solvency II type approach which would potentially require schemes to have substantial additional funds.

STEP 6: Enforcement and Compliance

The Pensions Board has responsibility for enforcement of the Funding Standard. Any issues in relation to compliance for adherence to the submission of proposals will be dealt with under existing legislation under the Pensions Act.

A further proposal in the Memorandum relates to enforcement by giving the Pension Regulator powers to wind up pension schemes. It is envisaged that this would only be used rarely, but would deal with very particular situations where a scheme is unsustainable and/or where there is no engagement by the employer or trustees.

STEP 7: Review

Any policy change will be kept under review. By nature, DB pension schemes are under constant review. There is ongoing consultation and feedback with the pensions industry and the need to submit funding proposals etc means that this environment is constantly being monitored.

Part 2: Regulatory Impact Assessment on the Re-Introduction of the Funding Standard

STEP 1: Summary of the Regulatory Impact Assessment on the re-introduction of the Funding Standard

The Funding Standard is a regulatory tool and while there were pragmatic reasons for its suspension in 2008, to allow schemes times to assess their funding position and also allow the Department to introduce measures to ease the pressures on schemes, it is now considered timely to re-introduce the Funding Standard. The Pensions Regulator is responsible for the operation of the Funding Standard and has indicated that he wishes to re-introduce it.

There are costs/benefits in relation to the re-introduction of the Funding Standard but it is considered that the overriding factor is the need for the regulation of pension schemes.

STEP 2: Description of Policy Context and Objectives

The Funding Standard is in existence to provide a standard to which schemes must adhere to demonstrate that they are funded to a particular level to provide secure benefits to members. The provision of a “promise” in relation to a pension brings with it a need to provide security and some certainty that the promise can be met. The ultimate objective of the Funding Standard is to ensure that a scheme can meet this promise.

The Funding Standard as set out in the Act is a wind up standard, which means that it obliges schemes to hold assets that would be sufficient if the scheme were wound up on the date of calculation. The current Funding Standard does not reflect the actual cost of a DB scheme. This cost is determined by the benefits provided by the scheme, the investment returns earned and the experience of the scheme. Even where a scheme meets the current Funding Standard, it may not have enough assets to meet its obligations without further contributions. The Funding Standard provides a benchmark against which the “health” of the scheme can be tested. The existence of the Funding Standard itself is not the central issue in relation to whether a scheme is properly funded. Rather the responsibility rests with the employer (whose role is voluntary) and the trustee for ensuring that the scheme is properly funded and managed. However, the Funding Standard does provide the regulatory mechanism for ensuring that a scheme can live up to its promise.

Context for the original suspension of the Funding Standard

The Funding Standard was suspended for sound administrative reasons in 2008, i.e. to give pension schemes who had suffered losses an opportunity to assess and respond to the financial crisis and also to allow time for proposals to be introduced to assist schemes. It is likely that a significant number of schemes would have failed or closed if the Funding Standard had been in operation, with potential negative consequences for scheme members. This view would also have been reflected in the representations made by the industry, trade unions and employers at the time. The deadline for the phased submission of recovery plans to the Pensions Board was extended by 6 months initially and then further extended on a number of occasions. On each occasion, a suspension was justified as the then Government had announced and subsequently enacted significant legislative proposals.

In the time since the Funding Standard has been in abeyance, many schemes have restructured and have taken action to reduce their deficits and future liabilities.

Measures introduced during its suspension

The following measures have been introduced to ease the funding pressures on DB pension schemes:

- Significant legislative changes in the Social Welfare and Pensions Act in 2009 allowed for the restructuring of underfunded schemes by removing the priority given to post-retirement increases for pensioners to ensure a more equitable distribution of assets in the event of the wind-up of a DB scheme;

- The powers of the Pensions Board were strengthened to ensure that pension contributions are remitted by employers to scheme trustees.

- The Pensions Insolvency Payments Scheme was established to reduce the cost of purchasing pensions for trustees where the employer has become insolvent. This scheme came into effect in February 2010 and ensures a more equitable distribution of assets following the wind up of underfunded pension schemes where both the pension scheme and the employer are insolvent.

- The most recent measure taken to assist the funding position of schemes is the introduction of the Sovereign Annuity initiative. This initiative was proposed by the Irish Association of Pension Funds and the Society of Actuaries in early 2010 and following consideration, was announced in December 2010. Legislation has now been introduced which will facilitate schemes trustees on a voluntary basis purchase the sovereign annuities for the scheme or for pensioners. Guidelines have been published by the Pensions Board. The NTMA can issue bonds on which the annuity products will be based.

The last time the Funding Standard was suspended (in October 2010) it was done on the basis that proposals would be brought forward on changes to the DB model.

STEP 3: Description of Options

The options in relation to the Funding Standard were either:

(a) To continue with its suspension

(b) To re-introduce it

With regard to (a) the context for its last suspension in October 2010 was to allow for the completion of the review of the defined benefit changes. This review (which is outlined in detail in the previous regulatory impact assessment) was concluded and given this fact and the suite of measures that were introduced in the last few years to ease pressure on DB schemes, the view of the Department is that there is no further reason to continue to suspend the Funding Standard.

The Pensions Regulator has indicated that he plans to reintroduce the Funding Standard. Many representatives of the pensions industry during the consultation also expressed the view that it is time to reintroduce the Funding Standard. Therefore, while there were sound reasons for its suspension at the time, the collective view is now that it should be reinstated.

STEP 4: Consultation

Given the nature of the Funding Standard as a regulatory tool, there was no specific consultation on its re-introduction. However, as outlined above it was generally discussed as part of the consultation on DB and there was a widespread view that it should be re-introduced.

STEP 5: Analysis of Costs, Benefits and Impacts of the Options in relation to the Reintroduction of the Funding Standard

Continued Suspension of the Funding Standard

It is difficult to identify the costs and benefits of this as one of the consequences of a continuing suspension means that less knowledge is available in relation to the funding position of pension schemes. However, without the operation of a standard, some pension schemes will continue to behave responsibly and continue to fund their schemes. However, others will not, and could for example view the lack of regulation as a reason for not contributing to their pension scheme. While this could reduce costs to the employer the ultimate result is a failure to provide benefits to members as promised. From the Department's perspective, its continued suspension without good cause is not tenable.

Reintroduction of the Funding Standard

Again, it is difficult to predict how the re-introduction of the Funding Standard will be perceived. Feedback received from the industry is that some responsible employers and trustees have obtained advice and negotiated with their members with a result that many DB schemes have restructured and are waiting to submit proposals on the reintroduction of the Funding Standard. Others, principally the trade unions, have expressed the view that the re-introduction of the Funding Standard may have the effect of closing schemes as employers will take the view that the DB scheme is no longer sustainable. It is also very likely that there are still some schemes which have taken no action or have been unable to agree any action and these will emerge when the Funding Standard is re-introduced and the funding position of these schemes comes to light. These schemes may not welcome the re-introduction of the Funding Standard. However, given that considerable time has been given to schemes to restructure and make some efforts to recover their funding position, the Department view is that schemes have had every opportunity to address their position and the regulatory status quo needs to be re-established. Ultimately any concerns relating to the reintroduction of the Funding Standard need to be balanced with the need to ensure that members benefits can be secured, which is the ultimate objective of the Funding Standard.

STEP 6: Enforcement and Compliance

The re-introduction of the Funding Standard will ensure that the regulatory system for DB schemes is back in place. Schemes will be given a period of time in which to develop a submit proposals to the Pensions Board.

STEP 7: Review

The operation of the Funding Standard is kept under constant review, in terms of its existence and operation**.**

Appendix 1

Summary of issues raised in response to consultation document on Defined Benefit provisions

The consultation paper on "Proposed Approach to Defined Benefit Provision" was issued in April 2011 to the following;

- Society of Actuaries in Ireland (SAI)
- Irish Association of Pension Fund Managers (IAPF)
- Irish Business and Employers confederation (IBEC)
- Irish Congress of Trade Unions (ICTU)
- Association of Pension Lawyers in Ireland (APLI)

In addition, the following organisations also contributed to the consultation.
UNITE, Irish Life, PWC, AON-Hewitt, Mercer, KPMG, Tower Watson, INVESCO, Musgrave, McElvaney Consultants and IBA.

All groups were offered the opportunity to meet with officials to present and discuss their response to the consultation paper. The consultation process was concluded in June 2011.

A brief summary of the main issues raised by the organisations who submitted a response to the consultation document are outlined below.

SAI

- All of the proposals suffer from the fundamental flaw that they do not address the inequities and distortions caused by the pensioner priority rule. These inequities and distortions will increase over time in most schemes, as the proportion of retired members grows.
- Option B with an appropriate lead-in time and transition measures is the Society's preferred approach.
- The SAI supports the concept of risk reserves, however, unless any new requirement to hold additional risk reserves is introduced over an extended period, it will force otherwise viable schemes into premature benefit reductions.
- Unilaterally increasing technical reserves is likely to negatively impact on the security of members' benefits.

- Greater thought and recognition should be given to other forms of employer guarantees, which may represent a more efficient way of achieving security for pension scheme benefits than paying contributions into the fund and potentially creating trapped surplus.
- The existing funding regime is over-engineered, too costly to implement and significantly risks alienating employers
- Guidelines on sovereign annuities are required.

IAPF

- Option B modified is the only option that can be considered
- The priority rule applying to pensioners should be changed
- No changes should be made that would threaten the provision of benefits and would trigger the wind-up of schemes which are currently viable.
- The existing funding system is not fit for purpose and should be overhauled.
- Simple practical measures could be introduced to cut down on the work involved in submitting Funding Proposals, applying for Section 49 extension periods and Section 50 orders.
- A full and detailed Impact Analysis is carried out before any changes are introduced also many elements of the existing system were not considered.
- The requirement to reserve using annuity pricing for pensioners should be removed
- Rules should be changed to allow ARFs to be bought for existing pensioners.

IBEC

- IBEC is of the opinion that none of the options outlined will adequately address the crises which exists for DB schemes.
- The funding standard is already too strict and should be re-accessed prior to the re-instatement of any deadline. Any proposal which would require increases in the level of the funding standard would not be realistic.
- The crisis is compounded by disintegration of pension and tax policy also the proposals do nothing to deal with current scheme deficits
- The impact of factors, such as tax relief, the effects of the pensions levy, the minimum funding standard, the priority order and sovereign bonds, cannot be separated from the proposals at hand.
- Consideration should be given to the problems of the present, particularly in respects of past service liabilities, in advance of, or at least concurrently with, any design modelling for the future.

- Any benefit which is described as core benefit is likely to become the only benefit paid, any benefit described as 'discretionary' are likely to be considered aspirational and are unlikely to be paid.

ICTU

- ICTU believe that changes are best achieved by agreement within the industrial relations area and each scheme should be dealt with separately.
- The views of scheme members regarding the level of risk they are prepared to accept should inform the decision making process.
- The approach to s50 applications to date has been over cautious and is damaging the survival chances of many schemes.
- Option A provides the best hope of achieving the right balance however they could live with Option B
- Remodelling DB is a job for employers, workers and trustees

UNITE

- Option B will improve the security of pension promises if introduced over a sufficiently long period. Any sudden requirements to increase contributions at present, without a requirement from employers to commit to their pension promises, will be detrimental to private sector pension provisions.
- A higher funding standard would need to be introduced over a period of at least 10 years with no increase at all in the funding requirement over the next five years given the state of the economy.
- Employers should be required to commit to the promises made in the past

Irish Life:

- Option A is the least detrimental to those existing DB schemes which can have a reasonable likelihood of surviving and providing meaningful benefits into the future.
- The administration and regulatory burden associated with the current funding regime is already too great which none of the options address.
- A minimum of 6 – 12 months should be allowed if the current regime is to be re-imposed, with the lead-in time increasing rapidly, the more the new regime departs from the current model.
- Irish Life have outlined features of what they believe to be a more reasonable funding regime which they believe could allow a significant number of meaningful DB schemes to

survive, based on the existing Funding Standard Regime plus numerous additions and simplifications including: Clarity on Sovereign Annuities or extend PIPs to all schemes/pensioners; ARF facility for pensioners on wind-up; Discretionary revaluation of deferred benefits; Removal of investment test in s49(3); Simplification of s50 process; Flexibility for annual certification of funding.

PWC

- Option B would be their preferred option within the limits of how the question is phrased.
- Any attempt to enforce a higher degree of certainty on DB promises would likely lead to a reduction in certainty for members
- The shorter recovery period envisaged in the consultation document are likely to reduce rather than increase robustness
- Some of the solutions developed in the UK would likely add value if implemented here

Aon –Hewitt

- Option B with some transitional arrangements, would be the preferred approach in the current economic climate.
- The current position is unsatisfactory, in that the funding standard requires schemes to hold reserves for pensioners based on market annuity prices and these pensioners have priority on wind-up, which means that other members have poor security.

Mercer

- Option A is their preferred option.
- Any additional reserving requirements, if deemed necessary, must be phased in on a basis that does not adversely affect schemes that have invested a lot of time and effort and incurred significant costs in putting in place recovery plans under the current regulatory regime
- More security is not necessarily better, if the benefits enjoying the additional security are significantly diminished as a result.

KPMG

- The proposed more stringent funding standard comes at a time when few companies can afford additional contributions to pension schemes and while the aim is to improve security of members' benefits, the reality is that

- Companies will either need to significantly increase contributions to DB schemes or apply for reductions to benefits in order to maintain current contribution levels.
- Companies with strong employer covenants committed to addressing deficits in their schemes will lose the flexibility to fund according to their own timelines, reflecting the needs of their business.
- Priority order continues to be an issue for many schemes and should be included in any discussion on the future of DB provision.

Tower Watson

- Tower Watson believes the current funding standard is onerous and are not in favour of proposals to strengthen the funding standard at this time which they believe will herald the demise of DB schemes.
- Risk re Option B applied to future service benefits only with a two year lead in is the approach likely to do the least damage is their preferred option if changes have to be made at all.
- reserves being proposed in line with S.50 are unduly conservative for schemes that have a strong employer covenant.
- The necessary regulations governing sovereign annuities should be introduced immediately and the obligation to fund for post retirement increases in line with price inflation under the 'new model' be removed.
- The impact of the pension levy should also be considered.

INVESCO

- Option A with some modifications offers the best solution for the majority of members
- If it is deemed that some level of risk reserves are necessary, the proposals set out in Option B would in our view be more than sufficient. In addition, the inclusion of any risk reserves should be done over an extended period.
- INVECO would support a system which incorporates a discretionary element in both revaluation of deferred benefits and, where currently provided pension increases.
- A better and more viable long term basis of funding would be to move to a scheme specific standard such as exists in the UK.

Musgrave

- The Musgrave Group is supportive of a regulatory system which protects the security of benefits for members.
- They believe that the current funding standard is sufficient and feel that any further strengthening of the funding standard will do nothing to assist existing schemes.

- The Group are of the view that the current S.50 mechanism is an appropriate mechanism to reduce members past service entitlements in certain circumstances and It also provides the Pensions Board with a process to ensure that any proposed benefit reductions are accompanied by appropriate risk reduction measures.

McElvaney Consultants

- Option B for pensioners and Option A for other members would then be adequate.
- The provision of a high degree of security should only be necessary for pensioners. Other members should be made aware that, while they're in a DB scheme, the DB benefit only crystallises when they reach retirement.

IBA

- Option A is the preferred option with improved communication and more flexibility on asset shares/distribution in a wind-up event are required
- The current Funding Standard delivers an overall asset level that provides good protection but there are issues with priorities and distribution in a wind up event.
- If DB schemes are forced to reserve at too high a level, then continued DB provision will be at risk.
- The MFS should be maintained in line with current format but with some flexibility introduced.