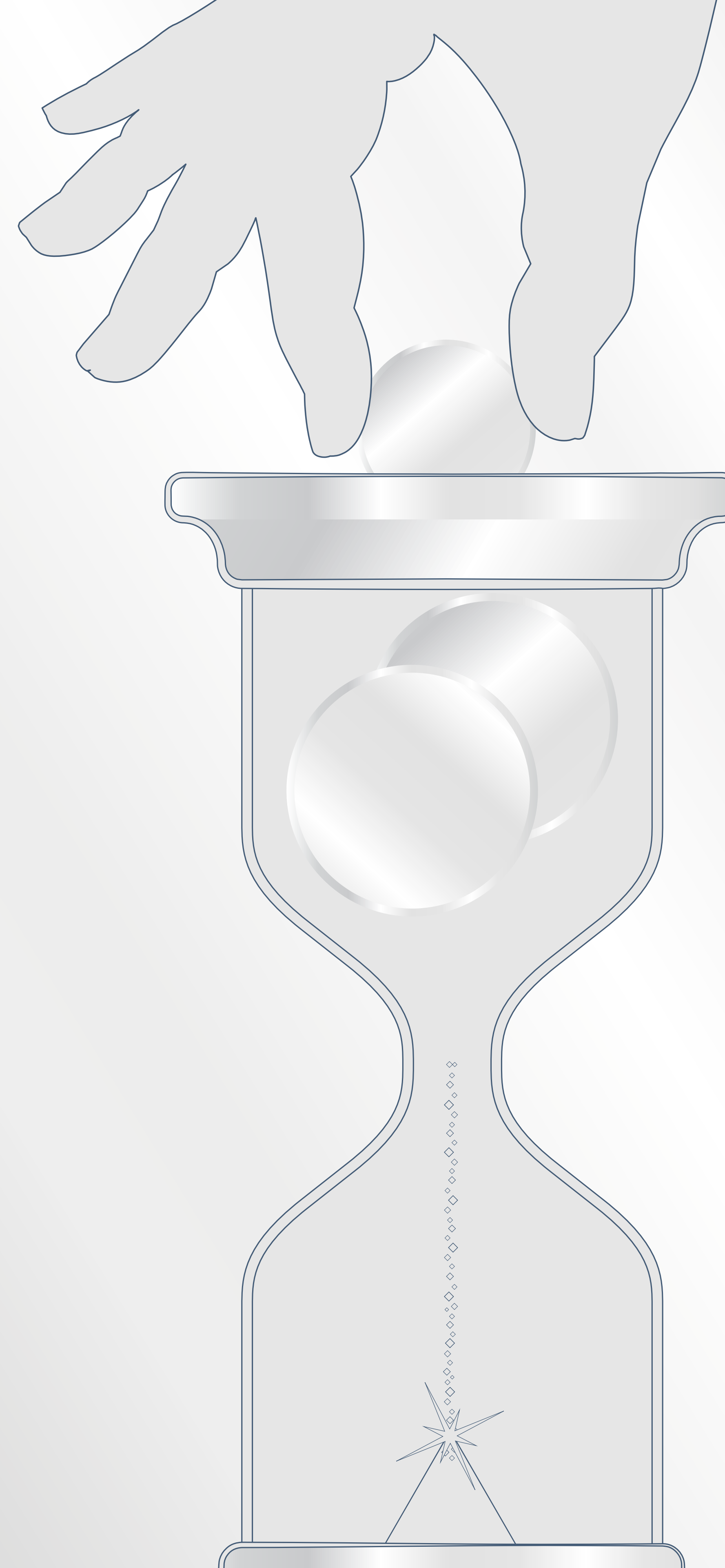
IRELAND PENSIONS UPDATE 2022



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WELCOME TO OUR PENSIONS UPDATE 2022

2022 was a landmark year of change for Irish pensions. 2022 saw the Irish Government introduce a number of simplifications to the pensions tax regime, approve Ireland's first auto-enrolment plan and announce significant structural reforms to the State Pension.

In conjunction with these systemic changes, 2022 has seen the continued evolution of master trusts in Ireland. wwThe regulatory changes introduced by IORP II, the cessation of new one member arrangements and the introduction of the auto-enrolment are all expected to contribute to a significant growth in the master trust industry.

In this edition, we examine some of these significant pension developments in 2022.

PENSION REFORM: IRELAND MOVES CLOSER TO AUTO-ENROLMENT

After many twists and turns and lengthy delays, the Cabinet has now approved the General Scheme of the Automatic Enrolment (AE) Retirement Savings Bill. This General Scheme marks significant progress on the delivery of a new auto-enrolment scheme in Ireland which will see potentially hundreds of thousands private sector workers automatically enrolled into a pension scheme.

BACKGROUND

On 10 October 2022, Social Protection Minister, Heather Humphreys, announced that the Government had approved draft heads of new legislation which will underpin the long-awaited pension system that will see as many as 750,000 private sector workers automatically enrolled into a pension scheme. The General Scheme of the Bill will now be examined by the Oireachtas Joint Committee on Social Protection before the final wording of a law introducing the new regime is published.

Over the years a number of attempts have been made to introduce some form of pension auto-enrolment system in Ireland but none have reached the stage of draft legislation. Minister Humphreys noted that the scheme represents a "historic milestone" which will enable private sector workers who do not currently have pension schemes to save for their retirement. After almost two decades of discussion about auto-enrolment, it appears that the introduction of auto-enrolment is firmly on track. It is expected that the Bill will be introduced to the Oireachtas in early 2023, with the scheme up and running in early 2024.

Auto-enrolment is aimed at the combating the problem of people who do not enrol in a pension scheme because they 'haven't got around to it'. Minister Humphreys stated that auto-enrolment would be a "*generational reform in the Irish pensions landscape*" and would turn the current system on its head by creating a scenario where workers will have to consciously 'opt out' of supplementary pension coverage rather than 'opting in'.

FEATURES OF THE SCHEME

The following elements of the new pension auto-enrolment pension scheme have been settled in principle by Government:

Eligibility/Ability to opt-out

All private sector workers aged between 23 and 60 years of age, who earn more than €20,000 per year will be automatically enrolled into the new scheme unless they are existing member of a pension scheme.

Those outside the eligibility criteria (for example, those earning below €20,000 or those aged under 23 or over 60 years of age) will be able to 'opt-in' to the scheme if they so wish.

Membership of the new scheme will be compulsory for the first six months. Thereafter, members can choose to 'opt-out'. Members who choose to opt-out will receive a refund of their own contributions paid up to the point of opt-out. Members will be automatically re-enrolled after two years but will have the ability to opt-out again under the same circumstances as outlined above. The option to opt-out will only exist in the first ten years of membership and thereafter members will be able to suspend payment of contributions but they will not be entitled to a refund of their contributions - instead the contributions will remain in the pot.

Contribution Levels

The new scheme will see contributions paid by employees being matched by their employers and the State will also add a top-up to the money paid into the scheme.

Contributions to the scheme will be introduced on the following a phased basis:

Years	Employee	Employer	State
	(as % of salary[1])		
Years 1-3	1.5%	1.5%	0.5%
Years 4–6	3%	3%	1%
Years 7–9	4.5%	4.5%	1.5%
Year 10+	6%	6%	2%

The scheme will be capped at €80,000 of an employee's gross salary but people earning above that amount can still make additional contributions to the scheme. However, employers will not be required to match the amount.

Accessing funds

It is proposed that there will be a limited ability for members to access their accumulated retirement savings with only serious illness being considered as grounds to do so.

Administration and Investment

A Central Processing Authority (CPA) will be established to administer the scheme. This body will do much of the administrative work and act in a custodianship capacity for participants.

The pension contributions will be invested by four registered providers, and there will also be four different investment portfolios available for members, depending on their risk appetite. It is envisaged that there will be an online portal where members will be able to review the size of their pension pot.

Drawdown

It is expected that drawdown of pension benefits will be aligned with the State Pension age.

Penalties for Employers failing to implement

Employers who fail to implement auto-enrolment scheme for its employees or fail to deduct and remit contributions will face administrative penalties initially, and ultimately risk prosecution as a criminal offence.

IS AUTO-ENROLMENT THE SOLUTION TO IRELAND'S PENSIONS TIME BOMB?

It is estimated that just 35% of private sector workers have an occupational pension scheme. With so few private sector workers making any provision for their retirement, the fiscal implications of the hundreds of thousands of retired private sector workers relying on the state pension as the main source of their income is deeply worrying. The introduction of this auto-enrolment system is aimed at reducing strain on the already unsustainable state pension system.

However, there some issues and criticisms in respect of the proposed new scheme. Chief among these is the effect the new scheme is likely to have on employers. With a backdrop of businesses recovering from the pandemic and the ongoing energy crisis, employers will understandably be concerned about the costs of this new scheme. A connected fear is that, in order to control costs, employers who currently offer more generous pension schemes may be tempted to treat the auto-enrolment scheme as a cost saving opportunity and phase out their existing schemes.

However, the proposed scheme is a significant step towards dealing with Ireland's ticking pensions time bomb and increasing pension coverage for private sector workers. In the UK, pension coverage jumped from 47% to 80% in the decade after the introduction of auto-enrolment. Given the UK's experience, it would appear that auto-enrolment could go a long way towards securing the financial futures of hundreds of thousands of private sector workers who at present have made no provision for their retirement.

[1] Up to a maximum gross salary of €80,000.

REGULATORY UPDATE – PENSIONS

FINANCE ACT 2021

The Finance Act 2021, enacted on 21 December 2021, introduced several notable changes to tax provisions relating to pensions in Ireland. The relevant changes, which became effective from 1 January 2022, are highlighted below.

Death-in-Service Benefits – ARF Option

Previously, where an employee died in service before normal retirement age (and prior to drawing down his/her pension), Revenue rules permitted the payment of the following benefits:

- a lump sum not exceeding the greater of €6,350 or four times salary; and
- after the payment of the lump sum, any additional funds could only be used to provide a pension for a spouse or dependent(s).

In practice, this meant that, after the payment of the lump sum, the trustees would be required to purchase an annuity for the employee's spouse or dependents. Given the cost of annuities, the purchase of annuities can be an unattractive option.

Section 12 of the Finance Act 2021[1] has now introduced an option for trustees to transfer the surplus funds into an Approved Retirement Fund (ARF) for the benefits of the deceased's spouse or dependents. This now aligns with the options available to pension scheme members who draw down their pension at normal retirement age.

This change is of particular relevance to trustees who may need to update their trust deeds to allow for this new flexibility to use an ARF for death-in service benefits.

Chapter 10 of the Revenue Pensions Manual has been amended to reflect the above-mentioned change.

PRSAs - Removal of 15-Year Rule Requirement

Courtesy of Section 13 of the Finance Act 2021[2], scheme members are now permitted to transfer their benefits under their occupational pension scheme to a Personal Retirement Savings Account (PRSA) irrespective of that member's period of service. Previously, members of occupational pension schemes were not allowed to transfer their benefits under the scheme to a PRSA if such members had more than 15 years of service.

The '15-Year Rule' was long considered to be an anomaly in the Taxes Consolidation Act 1997, one which has been happily rectified, and the removal of this requirement will give members more choice when leaving service or changing employer.

Chapters 13 and 24 of the Revenue Pensions Manual have been amended to reflect the above-mentioned changes.

Removal of Approved Minimum Retirement Fund (AMRF) Requirements

The Finance Act 2021 has abolished the Approved Minimum Retirement Fund (AMRF) requirements. Previously, before an individual could avail of an Approved Retirement Fund (ARF), the individual was required to have:

- a guaranteed retirement income of over €12,700 per annum; or
- have €63,500 invested in an AMRF.

The purpose of the AMRF requirements was to protect pensioners without a minimum level of retirement income from drawing too much income from their pension funds.

The removal of the AMRF requirements is intended to simplify post retirement options and provide individuals with more flexibility in accessing their pension funds.

Chapter 7 of the Revenue Pensions Manual has been amended to reflect the above-mentioned change.

FINANCE BILL 2022

The Finance Bill 2022, which is expected to be signed into law on or before 25 December 2022, includes a number of changes to the tax provisions relating to pensions in Ireland. A summary of the proposed changes is set out below:

Changes to tax treatment of pension contributions to PRSAs

Under the current tax rules, employer contributions to Personal Retirement Savings Accounts (PRSAs) are treated as a Benefit in Kind (BIK) for the purposes of employee income tax. The Finance Bill proposes to alter the current position by abolishing the BIK charge for employer related PRSA contributions.

If passed into law, this change will bring the tax relief available for employer contributions to a PRSA in line with the tax relief available for employer contributions to an occupational pension scheme. The change may increase the popularity of PRSAs as a genuine alternative to executive pension plans.

Pan-European Personal Pension Product (PEPP)

PEPPs are EU-wide voluntary pension products designed to facilitate cross-border pension savings with the EU. The Finance Bill proposes to introduce a new provision in the Taxes Consolidation Act 1997 which will provide tax relief on contributions to a PEPP, similar to the tax treatment on contributions to PRSAs.

Tax treatment of lump sums from foreign pension scheme

From 1 January 2023, the tax treatment of lump sums from foreign pension schemes are to be treated in the same way as lump sums from an Irish occupational pension scheme, for an Irish resident individual (i.e. a tax-free exemption of up to €200,000 on the lump sum).

[1] Amending Section 772(3) of the Taxes Consolidation Act 1997 (as amended).
[2] Amending Section 772(3D) of the Taxes Consolidation Act 1997 (as amended).

MASTER TRUSTS – WHAT DO YOU NEED TO KNOW?

The transposition into Irish law of the IORP II Directive[1] (IORP II) has resulted in a period of significant change for the Irish occupational pension schemes landscape. IORP II is a wide-ranging suite of legal requirements that seek to enhance pension scheme governance and strengthen management standards of pension schemes. IORP II introduced a number of new requirements for Irish occupational pension plans, in particular in relation to governance and risk management, plan management and member communications.

The task, and associated costs, of complying with increased obligations and responsibilities as a result of the transposition of IORP II new regime is leading many employers to examine master trusts as an alternative vehicle for providing pension benefits to employees.

WHAT IS A MASTER TRUST?

A Master Trust is essentially a type of trust based occupational pension scheme in which multiple employers (who do not have to be related) can participate. Typically, each participating employer has its own ring-fenced section within the Master Trust which is then managed by a single corporate trustee who is independent of each of the participating employers. The administration, governance, investment and communications will all be controlled by the Master Trust provider.

Similar to other occupational pension schemes, Master Trusts require Revenue approval in order to obtain exempt approved status and they must be registered with the Pensions Authority. Currently, Master Trusts are subject to the general occupational pensions regulatory framework, including IORP II. However, it is expected that, over time, the regulatory framework applicable to Master Trusts will expand and become more specific to Master Trusts.

WHAT ARE THE KEY BENEFITS EMPLOYERS SHOULD CONSIDER?

Outsourcing Regulatory Requirements

The regulation of pension scheme has increased significantly in recent years, particularly with the transposition of IORP II. As Master Trusts are provided by established pension providers or financial institutions, they often have significant in-house pension scheme expertise as well as an accomplished and professional corporate trustee. Moving to a Master Trust essentially removes the substantial regulatory responsibility from the employer's shoulders, to be managed and overseen by the Master Trust and its trustee(s).

Potential Cost Savings/Economies of Scale

Larger Master Trusts should be able to exploit economies of scale and thereby reducing financial and regulatory costs and enhancing their efficiency and effectiveness. For example, by utilising the scale of multiple companies' pensions, Master Trusts may be able to negotiate better terms and fees in the marketplace from investment managers.

Engagement Advantages for Members

All functions of a pension scheme including member communication will be dealt with by the Master Trust provider. Master Trusts can potentially enable members to have access to resources which may not be available or affordable in other pension vehicles including interactive tools and apps, online platforms and other innovative communication methods.

WHAT ARE THE KEY ISSUES THAT EMPLOYERS SHOULD CONSIDER?

Pensions Authority Guidance for Employers

The Pensions Authority has published guidance (**Guidance**) for employers when considering a Master Trust for pension provision. The Guidance recommends that employers consider the following:

- Confirm whether the Master Trust trustees are qualified to carry out their trustee duties and obligation and that they meet the Pensions Authority's Code of Practise for Trustees.

- Ensure you are aware of and understand the Master Trust charges and consider how the charges compare to other Master Trust providers.
- Review the investment and default investment options that are offered to members and ensure that such options are appropriate and that such investment options are clearly explained to members.
- Review example of members communications and ensure that such communications are clear and easy to understand and confirm how member enquiries will be dealt with.
- Confirm that the Master Trust provider meets the capitalisation expectations of the Pensions Authority.
- Confirm that the Master Trust trustees have an adequate conflicts of interest policies in place which meets the Pensions Authority's Code of Practise for Trustees.

Indemnities in favour of Master Trust trustees

Under the terms of the governing documentation of the Master Trust, participating employers will generally be required to provide extensive and broad indemnities in favour of the Master Trust provider and the trustees. Employers should be aware of such indemnities and consider whether this level of legal risk is acceptable.

Issues with changing Master Trust providers in the future

Employers should be aware of the complexity involved with changing Master Trust providers in the future. An employer's right to cease to participate in the Master Trust may be subject to a notice period and the ability to transfer members' benefits to new Master Trust may be subject to the consent of the existing Master Trust provider or trustee.

Conclusion

It is imperative that employers considering the move to a Master Trust take their time to fully understand the advantages and disadvantages associated with Master Trusts. While Master Trusts will address some of the task, and associated costs, of complying with IORP II, employers should take the time to consider whether a move to a Master Trust is the right choice for their business.

Further, employers should be aware that not all Master Trusts are created equal, and the terms offered by each Master Trust will vary from provider to provider. The Pensions Authority's Guidance will assist employers when it comes to assessing providers. It is also crucial that a legal review of the Master Trust documentation is completed so that employers are aware of the legal risks before moving to a Master Trust.

[1] Directive (EU) 2016/2341

A NEW ERA FOR THE STATE PENSION

On 20 September 2022, Minister for Social Protection, Heather Humphreys, announced what she described as the *"biggest ever structural reform of the Irish State Pension System".* The measures, which were initially recommended by the Irish Pensions Commission[1], included, the introduction of a flexible State Pension age and the planned introduction of measures that will allow an employee to stay in employment until the State Pension age.

The need for the changes to the State Pension system were highlighted by the Pension Commission's report which highlighted that the current system is not sustainable into the future. The Pension Commission therefore set forward a suite of recommendations to be considered by Government.

The approval by the Cabinet of some of these measures heralds a new era for the State Pensions system. A review of the key measures announced is carried out below:

FLEXIBLE STATE PENSION AGE

Changes to the State Pension age in Ireland have been fraught with controversy over recent years. The last change to the State Pension age took effect on 1 January 2014, whereby the State Pension age was increased from 65 to 66. The State Pension age was then set to be further increased from 66 to 67 in 2021 and 68 in 2028.

However, due to the public backlash expressed during the 2020 General Election, the Government deferred such increases and instead established the Pension Commission to consider the sustainability of the State Pension system.

The Government has now announced that, with effect from January 2024, people will have the option to continue working up until the age of 70 in return for a higher State Pension. Minister Humphreys stated that this flexible approach is an acknowledgment that a 'one size fits all' approach is not suitable since *"everybody's job and circumstances are different"*. She contended that these measures aim to give people more choice as to when they will retire and to put the *"power in people's hand*".

The flexible approach will operate by allowing people to continue to draw their State Pension at the age of 66, however it will introduce the ability for people to continue working beyond the age of 66 until 70, in return for a higher pension. Under the proposed flexible model, and based on current payment rates, the five weekly payment rates are as follows:

- Age 66 – €253 (current weekly rate)
- Age 67 – €266
- Age 68 – €281
- Age 69 – €297
- Age 70 – €315

This translates to a combined increase in the State Pension of 24% if a person was to remain in employment until age 70.

MEASURES TO ALLOW AN EMPLOYEE TO STAY UNTIL STATE PENSION AGE.

Although the Minister Heath Humphrey's has provided limited detail on what 'measures' are likely to be introduced, the recommendations of the Pensions Commission may be indicative of what may be coming down the line.

The Pensions Commission recommended aligning retirement ages in employment contracts with State Pension age, by introducing legislation which will allow an employee to stay in employment until State Pension age. The proposed objectives of this legislation would be that an employer would not be permitted to set a mandatory retirement age below the State Pension age and such legislation would also apply to existing employment contracts overriding any provision which sets a mandatory retirement age below the State Pension age.

EMPLOYERS TO WATCH OUT

It is important for employers to stay alert to potential changes to employees' rights when it comes to retirement. Employers will need to prepare and assess the potential effects on their business.

As it currently stands, mandatory retirement ages are generally provided in either employment contracts, company policies and/or by way of custom and practice.

To date, employers are permitted to fix a mandatory retirement age where it is objectively and reasonably justified by a legitimate aim and the means of achieving that aim are appropriate and necessary.

However, Minister Humphrey's announcement implies that this position is about to change and employers may soon be prohibited from setting mandatory retirement ages below the State Pension age.

While no draft legislation has yet been proposed, employers should be alert to these potential changes which are proposed to be introduced in January 2024.

[1] Report of the Commission on Pensions published on 7 October 2021

2021 ANNUAL PENSION AUTHORITY REPORT

In the Pension Authority's recently published annual report and accounts (Report)[1], Chairman Mr David Begg emphasised the significance of transposition of the IORP II Directive (IORP II) into Irish law in April 2021 and the effect that IORP II has had on the supervisory activities of the Pensions Authority (Authority).

INCREASED SUPERVISORY RESPONSIBILITIES

According to the Report, the Authority's supervisory functions have increased significantly in 2021. The transposition of IORP II resulted in a significant change for the Irish pensions industry generally and for the Authority. The increased obligations and responsibilities on pension trustees as a result of IORP II has also resulted in the increase of the supervisory responsibilities of the Authority. The Report states that the transposition of IORP II requires a new and *"more comprehensive, challenging, judgement-based, and intrusive oversight"* by the Authority.

The Report also highlighted that, following the transposition of IORP II, the Authority has issued several important information updated and guidance including:

- a Code of Practice for trustees of occupational pension schemes and trust RAC;
- an employer guide to defined contribution Master Trusts;
- FAQs on investment and borrowing for one-member arrangements; and
- Information on:
  - the annual compliance statement;
  - trustees' outsourcing notification obligations and how to advise the Authority of the appointment of key function holders;
  - the timing of the own-risk assessment;
  - the DB financial risk measure; and
  - the courses that meet the Authority's requirements for trustee qualifications.

In addition to the IORP II related supervisory work, the Authority has also continued its normal supervisory activities, including oversight of PRSAs, monitoring of defined benefit (DB) solvency obligations and investigating instances of non-compliance with the Pensions Act.

Mr Begg highlighted that the increased supervisory responsibilities have led to considerable increase in the Authority's costs (mainly because of increased staffing and IT costs). The Report acknowledged that Minister for Social Protection approved an increase in the Authority's fees for occupational pension scheme with effect from 1 January 2022[2] .

PENSIONS REGULATOR'S STATEMENT[3]

Much of the statement from the Pensions Regulator, Mr Brendan Kennedy, concerned the challenges faced by scheme trustees in ensuring that their standards of management and governance meet that required by IORPS II. The Regulator also noted that schemes (other than newly established one-member schemes) are expected to be compliant by the beginning of 2023.

The Regulator states that significant consolidation of Irish pension schemes is the only practical means of achieving high standards of management, good value for money and effective supervision. Further, the Regulator said trustees of all pension schemes should be assessing whether to continue their current pensions arrangements or to take steps to transfer members' benefits to compliant pension arrangements (such as master trusts).

PROSECUTIONS

In 2021, six cases were concluded and secured three convictions. Two convictions related to the failure of an employer to the deduct pension contributions from employees' wages and remit them to the pension scheme trustees and one conviction related to the failure of an employer to remit the employer contributions to the pension scheme trustees.

ON-SITE INSPECTIONS

The Authority carried out 7 on-site inspections, all of which were on PRSA providers to establish if they were using third party / parallel contracts which are prohibited by the Pensions Act.

INVESTIGATIONS

In 2021, the Authority commenced 15 new investigations of alleged breaches of the Pensions Act. The alleged breaches ranged from issues surrounding the non-remittance of pension contributions to failures to reply to statutory requests for information. During 2021, 24 investigations were finalised and closed by the Authority.

ENGAGEMENT MEETINGS

20 engagement meetings took place between the Authority and the trustee boards of master trusts, defined contribution and defined benefit schemes. The focus of these meetings was to examine how well-equipped schemes are to meet the enhanced governance and risk management requirements under IORP II.

DEFINED BENEFIT SCHEMES

The Report states that, at the end of 2021, there were 553 DB schemes subject to the funding standard and almost 90% of these DB schemes met the funding standard. Only four of the remaining schemes did not have a funding proposal in place or are in the process of submitting a funding proposal. The Authority approved five funding proposals from DB schemes in 2021.

CONCLUSION

Both the Report and the Regulator's Statement highlighted the significant change for Irish pensions as a result of the transposition into Irish law of IORP II and the resultant increased obligations on pension scheme trustees. The Authority has set a deadline for trustees of all relevant schemes to be complaint with their new obligations by the end of 2022.

Trustee boards should be well underway in ensuring that their schemes are compliant. The Regulator emphasised that compliance is not just a matter of putting in place new processes and governance practices but rather the objective is to make sure that the management of the scheme is informed, thoughtful and thorough.

[1] Copy of the Pensions Authority Annual Report and Accounts 2021 is available here
[2] Details of the increased occupation pension scheme fee rates are available here
[3] Copy of the Statement from the Pensions Regulator is available here

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