EXPLANATORY MEMORANDUM TO

THE OCCUPATIONAL PENSION SCHEMES (INVESTMENT) (AMENDMENT) REGULATIONS (NORTHERN IRELAND) 2010

S.R. 2010 No. 287

1. Introduction

1.1 This Explanatory Memorandum has been prepared by the Department for Social Development to accompany the Statutory Rule (details above) which is laid before the Northern Ireland Assembly.

1.2 The Statutory Rule is made under Articles 40(1) and (2)(e) and 166(1) to (3) of the Pensions (Northern Ireland) Order 1995 and is subject to the negative resolution procedure.

2. Purpose

2.1 These Regulations amend the Occupational Pension Schemes (Investment) Regulations (Northern Ireland) 2005 ("the Investment Regulations") to ensure those Regulations reflect the limits on investments by occupational pension schemes in the sponsoring employer which are required by Article 18(1)(f) of European Union Directive 2003/41/EC on the activities and supervision of institutions for occupational retirement provision ("the IORP Directive"). They also make a consequential amendment and revocations.

3. Background

3.1 Article 18(1)(f) of the IORP Directive imposes restrictions on the proportion of an occupational scheme's resources which may be invested in the sponsoring employer ("employer-related investments").

3.2 The Investment Regulations already limit employer-related investments to a maximum of 5 per cent, but include transitional provisions which disapply the restrictions to schemes which had such investments in excess of 5 per cent before 6th April 1997. They also contain exemptions in respect of employer-related investments by collective investment schemes. Those exemptions, which rely on the discretion available under Article 22(4) of the IORP Directive to postpone transposition of Article 18(1)(f), cannot continue beyond 23rd September 2010.

3.3 These Regulations partially transpose the requirements of Article 18(1)(f) of the IORP Directive which requires that employer-related investments are limited to 5 per cent of the market value of a scheme's investment portfolio. Article 18(1)(f) was transposed in all other respects by regulation 17 of the Occupational and Personal Pension Schemes (Miscellaneous Amendments) Regulations (Northern Ireland) 2009 (S.R. 2009 No. 115).

3.4 These Regulations also remove transitional protection for schemes which retained certain investments in their sponsoring employer on 6th April 1997, in excess of the 5 per cent limit required by the IORP Directive.

4. Consultation

4.1 There is no requirement to consult on these Regulations as they make in relation to Northern Ireland only provision corresponding to provision contained in regulations made by the Secretary of State for Work and Pensions in relation to Great Britain.

5. Equality Impact

5.1 In accordance with its duty under section 75 of the Northern Ireland Act 1998, the Department has conducted a screening exercise on the legislative proposals for these Regulations. As the amendments are technical in nature or consequential, the proposals would have little implication for any of the section 75 categories. In light of this, the Department has concluded that the proposals would not have significant implications for equality of opportunity and considers that an Equality Impact Assessment is not necessary.

6. Regulatory Impact

6.1 The provisions may impose some new costs on business, charities and voluntary bodies which sponsor occupational pension schemes. This will happen where the scheme holds investments in the sponsoring employer in excess of the 5% limit on such investments, either directly, or through a collective investment scheme. A copy of the Regulatory Impact Assessment is attached as Annex A to this Explanatory Memorandum.

7. Financial Implications

7.1 None for the Department.

8. Section 24 of the Northern Ireland Act 1998

8.1 The Department has considered section 24 of the Northern Ireland Act 1998 and is satisfied that these Regulations –

(a) are not incompatible with any of the Convention rights,

(b) are not incompatible with Community law,

(c) do not discriminate against a person or class of person on the ground of religious belief or political opinion, and

(d) do not modify an enactment in breach of section 7 of the Northern Ireland Act 1998.

9. EU Implications

9.1 A copy of the Transposition Note detailing the extent to which Article 18 of the Directive is transposed by these Regulations is attached as Annex B to this Explanatory Memorandum.

10. Parity or Replicatory Measure

10.1 The corresponding Great Britain Regulations are the Occupational Pension Schemes (Investment) (Amendment) Regulations 2010 (S.I. 2010/2161) which come into force on 23rd September 2010. Parity of timing and substance is an integral part of the maintenance of single systems of social security, child support and pensions provided for in section 87 of the Northern Ireland Act 1998.

Annex A

REGULATORY IMPACT ASSESSMENT

The costs outlined in this Regulatory Impact Assessment are calculated on a United Kingdom-wide basis.

Introduction

1. This impact assessment considers the effect on schemes of removing the transitional provisions in regulation 14 of the Occupational Pension Schemes (Investment) Regulations (Northern Ireland) 2005 ("the Investment Regulations").

Issue under consideration

2. Where certain employer-related investments exceeded 5 per cent. of the market value of the assets of the scheme immediately before 6 April 1997, the transitional provisions set out in regulation 14 of the Investment Regulations permit those investments to be retained until disinvestment can be effected.

3. The Government consulted on amendments relating to the transposition of provisions in the European Union Directive 2003/41/EC on the activities and supervision of institutions for occupational retirement provision[1] ("the IORP Directive") during the final quarter of 2003 and again in March 2005. The 2005 consultation proposed to remove some of the existing transitional arrangements in the Investment Regulations but, in light of the issues raised by respondents (in particular that it may lead to a 'forced sale' of assets which could be detrimental to the members' interests), the Government decided they would permit the current transitional provisions for pre-owned investments to continue.

Rationale for Government intervention

4. The transitional provisions cannot continue beyond 23 September 2010, when the discretion available under Article 22(4) of the IORP Directive to postpone the transposition of Article 18(1) and (2) of that Directive is withdrawn.

Objectives

5. To remove the risk of UK pensions law being in breach of the IORP Directive, which may lead to infraction proceedings being taken against the UK Government.

---

1 (OJ No. L 235, 23.9.03, p.10)

Intended effect

6. The intended effect is to ensure that those elements of Article 18(1) and (2) of the IORP Directive, which are not currently found in domestic legislation, are incorporated through regulations. This will also protect the Pension Protection Fund from additional costs due to schemes which are heavily invested in the sponsoring employer.

Main affected groups

7. The main groups affected by the proposals are as follows:

- **Pension schemes with employer-related investments in excess of 5 per cent. immediately before 6 April 1997:** These Regulations withdraw transitional provisions in regulation 14 of the Investment Regulations. From the date the changes come into operation, (with very few exceptions) pension scheme investment in a sponsoring employer will be restricted to no more than 5 per cent. of the scheme's portfolio.

- **Pension schemes which invest in collective investment schemes (CISs):** These Regulations withdraw transitional provisions exempting CISs from the calculation of the level of employer-related investment. Schemes will be required to ensure that there is 'look through' into the CIS to allow them to monitor the level of employer-related investment they are making through the CIS.

- **Government:** The Government and the taxpayer stand behind private pension provision by providing tax relief on contributions to schemes. It is important, therefore, to have a regulatory regime that supports and encourages prudent investment.

- **The Pensions Regulator:** The Pensions Regulator will enforce these Regulations, based on its usual risk-based approach.

- **The Pension Protection Fund:** The Pension Protection Fund provides pension compensation to members of eligible defined benefit schemes in the UK. These Regulations make a small reduction in the likelihood of the Pension Protection Fund being called upon to provide compensation.

Implementation

8. These Regulations will be laid before the Assembly on 1 September 2010 (coming fully into operation on 23 September 2010).

Alternative options

9. The only alternative to removing the current transitional provision would be to do nothing. However, this would result in UK pensions law being in breach of the

IORP Directive which could, in turn, lead to infraction proceedings being taken against the UK Government.

Numbers affected

10. Given that the transitional provisions are intended to give schemes with employer-related investments in excess of 5 per cent. immediately before 6 April 1997 time to divest, it is expected that most schemes will be within the permitted limit by the time the changes come into operation. For the same reasons, it is anticipated that schemes with employer-related loans will have effected repayment. Consequently, it is expected that the number of schemes affected by the removal of the provisions will be low.

SCHEMES: One-off and annual costs

11. Where schemes have employer-related investments in excess of the 5 per cent. limit, the trustees or managers of those schemes will have to instruct their investment managers to liquidate the excess employer stock and use the proceeds to purchase alternative assets. The scheme will bear the transaction costs of this process. The aggregate cost would be the sum of the per-scheme transaction cost across all the affected schemes. This is a one-off cost – there are no on-going costs. The Government has no evidence available about the size of these costs. However, since the number of schemes affected is expected to be low, we also expect the overall cost is also expected to be small.

12. Schemes investing in collective investment schemes (CISs) would bear a one-off cost in setting up systems to monitor the level of investment in the sponsoring employer through the CIS. There will be an on-going cost of monitoring the level of employer-related investment in the CIS to ensure that the total level of employer-related investment in the scheme remains below the 5 per cent. limit. Alternatively, schemes could comply by investing in CISs which commit not to invest more than 5 per cent. in any one company. The Government has no evidence available about the likely size of these costs or the number of schemes who are invested in CISs. It is believed that a relatively small proportion of schemes make use of CISs, therefore these costs are expected to be negligible.

SCHEMES: Non-monetised benefits

13. Reducing the dependence of scheme assets on the sponsoring employer's stock is intended to provide increased financial security for schemes in the event of the sponsor suffering from adverse business conditions.

GOVERNMENT: Annual costs

14. Negligible (smaller than the costs described above). The Pensions Regulator will enforce these Regulations applying their usual risk-based approach.

Pension Protection Fund: Non-monetised benefits

15. Increased financial security for trust-based defined benefit schemes reduces the risk of such schemes looking to the Pension Protection Fund to provide compensation. Reducing the reliance of employer-related investment will make a small improvement in the funding position of some schemes entering the Pension Protection Fund.

KEY ASSUMPTIONS/SENSITIVITIES/RISKS

Key assumptions

16. Since these transitional provisions have given schemes the opportunity to reduce their employer-related investments over a number of years, it is assumed that the majority of schemes will, by 2010, have reduced their employer-related investments to 5 per cent. or less. It is assumed that the transaction costs of disinvesting the sponsoring employer's stock will be small, and that the cost of setting up monitoring systems and carrying out on-going monitoring is also small.

Sensitivities/Risks

17. That the number of schemes affected by these Regulations and the costs incurred by these schemes will be greater than that envisaged in the 'Key assumptions'.

IMPACT TESTS

Competition

18. These Regulations apply to trust-based pension schemes. Schemes are employer specific and do not compete to serve a market. Therefore these Regulations do not directly or indirectly affect the number or range of suppliers in a market, or alter their ability or incentives to compete.

Small firms

19. These Regulations are less likely to impact on small firms than on other types of firms. This is because they are much less likely than other firms to sponsor occupational pension schemes. A small firm is very unlikely to make up a significant part of the value of a collective investment scheme. Small schemes (those with fewer than 12 members, all of whom are trustees) are already exempted from the restrictions on loans and employer-related investments. There is no scope within the IORP Directive for the exemption of small firms.

I have read the Regulatory Impact Assessment and I am satisfied that the benefits justify the costs.

Signed for the Department for Social Development



Anne McCleary
1 September 2010

Contact points: Joanne Nesbitt, Social Security Policy and Legislation Division
Level 1, James House, 2 – 4 Cromac Avenue, Gasworks Business Park,
Ormeau Road, BELFAST BT7 2JA

Tel: 02890819135
E-mail: Joanne.Nesbitt@dsdni.gov.uk

Annex B

TRANSPOSITION NOTE

Transposing that part of the European Union Directive 2003/41/EC on the activities and supervision of institutions for occupational retirement provision[2] (IORP Directive) which concern the investments of private sector occupational pension schemes

Article	Requirements	Implementation
18(1)(f)	Investment by schemes in the sponsoring undertaking shall be no more than 5% of the portfolio as a whole.	This requirement is already satisfied in part by Article 40 of the Pensions (Northern Ireland) Order 1995 and regulations 10 to 16 of the Occupational Pension Schemes (Investment) Regulations (Northern Ireland) 2005 ("the Investment Regulations"), which restrict the proportion of the market value of a scheme's resources that may be invested in the sponsoring employer. Such investments are called employer-related investments. Regulation 2 of the Occupational Pension Schemes (Investment) (Amendment) Regulations (Northern Ireland) 2010 amends regulations 13 and 14 of the Investment Regulations with effect from 23 September 2010 to bring additional employer-related investments within the limits required by Article 18(1)(f) of the IORP Directive.

2 (O.J. No. L235, 23.9.03, p.10)