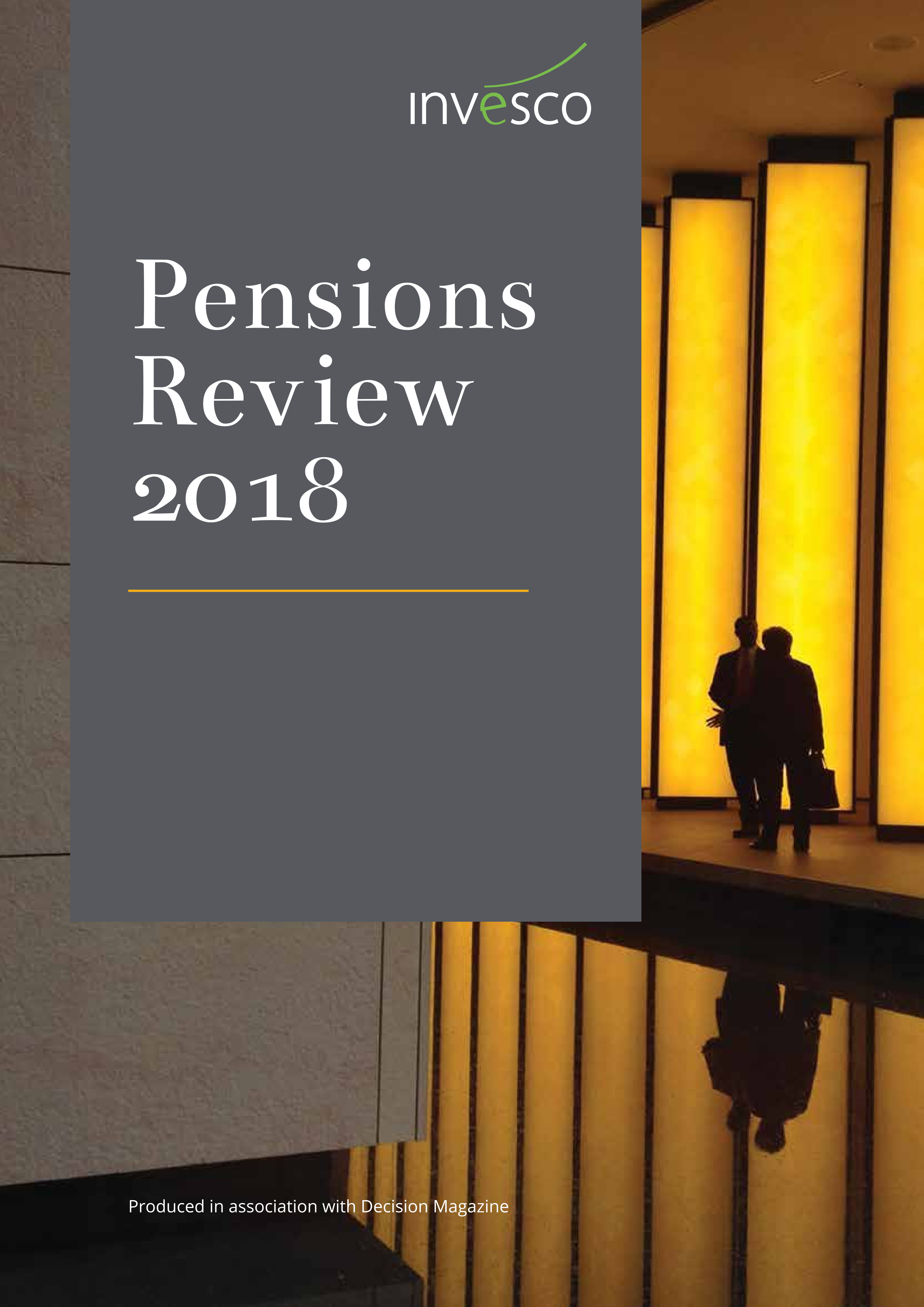

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Pensions Review 2018

Produced in association with Decision Magazine

Contents

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A PRIME TIME TO INVEST IN BUSINESSES, PEOPLE AND PENSIONS

Des McGarry
Managing Director

The outlook for pensions remains strongly positive for the coming year. Investment markets have been remarkably strong for some considerable period of time with most of the world's major economies expected to have excellent growth rates. The inflation environment also remains benign.

Closer to home, the performance and recovery of the Irish economy has been nothing short of exceptional. Ireland is once again Europe's fastest growing economy and this is reflected in corporate profits. The improved economic environment and profit outlook has allowed companies to invest in their businesses and people and to review their pension arrangements.

In the downturn many business owners were forced to reduce or even suspend their own pension contributions. Contributions to staff schemes were also scaled back in many instances. The recovery has allowed for a reversal of those measures and we are seeing many companies increasing contributions to their pension schemes which is a welcome development.

We should not waste the current positive economic environment to address the bigger issue of pension coverage. In theory the proposed introduction of an auto-enrolment pension scheme will go some way to addressing this but it seems we may have to wait until 2021 at the earliest for the introduction of this scheme.

The quality of pension provision is also an issue. Our own research shows that the level of benefits that are likely to emerge in the typical defined contribution scheme will be well short of many people's target retirement income, particularly in the current low interest rate environment.

While it is true that pension coverage in the private sector is in general low, the problem is by no means intractable. Coverage rates are far from uniform and in some sectors, such as financial services and pharmaceuticals, coverage is actually very high. These sectors have traditionally offered very attractive benefits packages to employees and good pension schemes are the norm rather than the exception. This should be the benchmark for all sectors both in terms of coverage and levels of contributions.

But it would be wrong to place the responsibility for this state of affairs entirely on the shoulders of the sponsoring employers. There is little doubt that if employees placed pensions higher on their list of preferred benefits employers would respond. The State also needs to play its part by easing the regulatory burden on pension schemes, restoring USC and PRSI relief on employee contributions and increasing pension fund limits and the earnings cap on pension contributions.

The value of a workplace pension scheme may not be fully understood or appreciated. Communication and engagement are vital to address this issue and all involved, employers, the State and the pensions industry must tackle this together.

With the recovery firmly established there is now a real opportunity to address pensions coverage in terms of quality and quantity. We shouldn't let the opportunity pass.

Des McGarry

Frank Downey
Director

EUROPE IS NOW SETTING THE PENSION SCHEME RULES

Frank Downey looks at the impact of the EU Directive IORP II.

The EU Directive on the activities and supervision of institutions for occupational retirement provision or IORPs (IORP II) came into force on 12 January 2017 and must be transposed into national law by 13 January 2019.

The main provisions in IORP II relate to governance, investment, risk management, cross-border schemes and member communication as well as strengthening supervisory powers.

Notably, the Directive did not include provisions for a new harmonised solvency standard for defined benefit schemes. These had been a long-standing and controversial part of earlier deliberations but were ultimately dropped from IORP II. This means that the current funding standard requirements under the Pensions Act will remain in force.

Governance

The Directive requires that all pension schemes should have an "effective system of governance which provides for sound and prudent management of their activities". This includes the following key functions:

- risk management
- internal audit
- actuarial (for defined benefit schemes)

Schemes will have to formally appoint individuals or firms to undertake these roles. The actuarial function will be similar to the scheme actuary role but risk management and internal audit are new requirements.

The Directive sets out "fit and proper" requirements which must be fulfilled by persons involved in the running of pension schemes. For trustees their qualifications, knowledge and experience should be collectively adequate to enable prudent management of the scheme. For persons who carry out key functions their qualifications, knowledge and experience must be adequate to properly carry out their roles.

Risk management and responsible investment

Schemes will be required to carry out and document their own risk assessment at least every three years. This is a material requirement and similar to the requirements applicable to insurance companies under the Solvency II Directive.

The required system of governance states that trustees will have to include consideration of environmental, social and governance (ESG) factors related to investment assets in investment decisions. In addition, the statement of investment principles must include a statement on how the investment policy takes ESG factors into account.

Cross-border schemes

Promoting and facilitating cross-border schemes is one of the key objectives of IORP II. The rules in this regard have been relaxed a little as the Directive allows for periods of underfunding provided the trustees ensure that member benefits are "adequately protected". Cross-border schemes may therefore become a more feasible and attractive option for certain multinational employers.

Member communications

The Directive includes significant member disclosure requirements. Key changes include a requirement to provide an annual statement to all members, including deferred and pensioner members and, for DC schemes, the provision of investment performance information over the previous five years.

Conclusion

IORP II is set to shape the governance of pension schemes from 2019 onwards. The extent of the impact of the Directive will depend on how the government interprets and seeks to implement its principles into Irish law – it is stated that the application of the Directive should be "proportionate to the nature, scale and complexity of the activities" of schemes.

It is hoped that IORP II doesn't become another (expensive) regulatory burden on employers and pension scheme members and that it might go some way to achieving its objective of protecting members and supporting retirement provision.

To find out more about how Invesco can help your scheme in dealing with the impact of IORP II contact **Frank Downey** fdowney@invesco.ie.

Gerry Winters
Director

A QUESTION OF ENGAGEMENT

Pension scheme member engagement requires a multi-channel, multimedia, multi-disciplinary approach according to Gerry Winters.

There is no one size fits all approach to pension scheme member engagement. Every member is different. They are at different life and career stages, have different family circumstances and have varying ambitions for their retirement. Their financial priorities also change over time.

Personalised engagement based on your member needs "3 Personas"

What is required is a means of engagement that flexes to meet the needs of different members within a cost-effective structure. Invesco has devised such an approach with our new Easy Steps Engagement process.

The personalised engagement process focuses on three broad member "personas" – new hires, current members and pending retirees. The communications are designed to be directly relevant to each persona.

For example, there is little point in explaining approved retirement funds (ARFs) in depth to a new hire. In most cases retirement will be far too distant to feature in their thoughts. The most important thing at that stage is to point out the reasons for joining the scheme and explain very clearly how it works. Relevance is critically important at each stage.

The adequacy of the state pension varies according to people's earnings and employees at the lower end of the salary scale are not going to be particularly engaged by a conversation around retirement income targets. They are, however, very likely to be interested in the potential of retiring with a significant lump sum at very little cost to themselves.

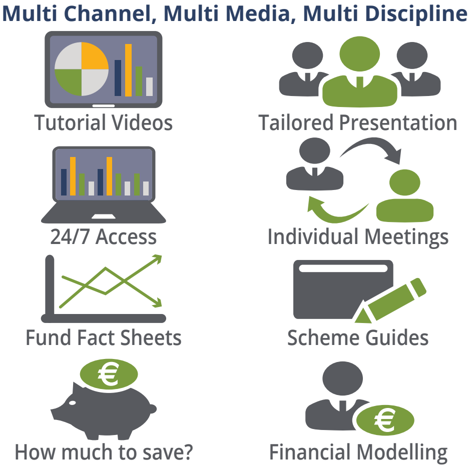
The discussion with members who are approaching retirement will be very different. First of all, there is a need to explore investment strategies. Are they aligned to the needs and ambitions of the member in question? This is the time to start talking about ARFs and how they can be constructed.

The needs of current members who are perhaps more than 20 years from retirement will be different again.
As people move through life stages their financial priorities alter. Their ability to contribute to their pension changes as their commitments move up and down.

The nature of the engagement is also very important. There is a greater emphasis on face to face meetings for members approaching retirement while other tools such as tutorial videos, tailored presentations, online access to scheme information and scheme guides are also available and are used in a blend which suits each individual member.

The Easy Steps Engagement process has proven enormously successful since it's introduction. The number of new recruits joining non-mandatory schemes has increased markedly. We have also seen members become much more active in terms of their engagement with schemes and all the evidence points to a much greater level of appreciation of the benefit being provided by the employer.

Multi Channel, Multi Media, Multi Discipline



For further information on the Easy Steps Engagement process contact **Gerry Winters** gwinters@invesco.ie.

Finian O'Driscoll
Director

HOW RESPONSIBLE ARE YOUR INVESTMENTS?

Finian O'Driscoll considers ESG investing for pension schemes.

ESG refers to the environmental, social and governance factors that pension schemes may take into account when selecting investments and is something which trustees now need to consider. In practice, it can be thought of as being akin to "responsible investing" or "sustainable investing" or even "ethical investing".

The focus on ESG considerations continues to grow and a number of pension schemes now have an ESG policy in operation. More investment products with ESG selection mechanisms are being brought to the market, together with products aimed at helping trustees monitor ESG practices.

ESG is already standard practice for Continental European pension schemes. It forms part of the investment policy of the Ireland Strategic Investment Fund (formerly the National Pensions Reserve Fund) operated by the NTMA, and is included in the IORP II Directive to become effective in 2019.

The rationale for ESG from an investment point of view is that there is growing evidence to suggest that ESG factors, when integrated into investment analysis and decision making, may offer investors potential long-term performance advantages.

ESG analysis involves looking at companies from the following perspectives:

- **Environmental** stewardship, e.g. carbon emissions or energy consumption
- **Social** practices, e.g. relations with staff or suppliers, or health and safety considerations
- Corporate **governance,** e.g. structure or compensation packages

It is normally a risk assessment of long-term sustainability. The aim being to understand how business practices might affect investment return.

A regulatory requirement to consider ESG for pension schemes will come into effect from January 2019 under the IORP II Directive, the extent of which will depend on how the Irish government choose to enshrine its provisions into national laws. IORP II includes the following specific requirements:

- Within the "prudent person rule" pension schemes can take account of ESG factors when assessing the long-term impact of investment decisions
- The system of governance should include consideration of ESG factors related to investment assets in investment decisions
- The risk management system should cover ESG risks relating to the investment portfolio
- How investment policy takes ESG factors into account must be included in the Statement of Investment Policy Principles
- Whether and how ESG factors are considered in the investment approach should be included in the information provided to prospective or automatically enrolled members

It is an option under the Directive, however, to determine that ESG factors are not considered or that the costs of monitoring the relevance and materiality of ESG factors are disproportionate to the scheme.

So, is ESG an appropriate consideration for trustees of pension schemes? The primary investment duty of trustees is seen as balancing returns against risks. ESG factors can properly be considered by the trustees to the extent that they believe they are relevant to the investment *as a financial proposition.*

Apart from the new regulatory requirements, it is to be expected that scheme members themselves will be looking for sustainable investment options. Sponsoring employers may also wish that their own ESG policies be reflected in their pension schemes.

All of this means that ESG will now need to be considered by trustees as part of the governance of their pension schemes.

To find out more about how Invesco can help your scheme introduce an ESG policy contact

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Brian Sexton
Client Services Director

ARE WE THERE YET?

Brian Sexton looks at the slow progress being made towards a national auto-enrolment pension scheme.

In a welcome development towards the end of 2017 the Department of Social Protection announced that the government will roll out a five-year pension reform plan in the near future. The key measure in the plan will be the introduction of an auto-enrolment supplementary retirement savings system for all employees who are not already members of a pension scheme.

In September 2017, the Taoiseach also confirmed the objective to have the auto-enrolment scheme up and running by 2021. While this commitment is positive it should be noted that as far back as 2010 the National Pensions Framework indicated that such a scheme was necessary to address the poor level of supplementary pension coverage in this country and envisaged the introduction of auto-enrolment by 2014.

The necessity for urgent action was further highlighted by a 2012 report from TILDA (The Irish Longitudinal Study on Ageing) which forecast that the pensioner support ratio in Ireland would decrease from 5.4 to 1 in 2010 to 2.3 to 1 in 2055. At the same time, the country faces a further challenge in the form of mounting pension costs which the TILDA report predicted will rise from 7.5% of GDP in 2010 to 11.4% in 2050.

Earnings	State pension as approx % of gross wage	State pension + occupational pension as % of gross wage*
€35,592 (avg earnings)	34.1% (€12,123)	72.1% (€25,661)
€53,338 (1.5 times avg earnings)	22.7% (€12,123)	60.7% (€32,406)

**Occupational pension based on contributions totalling 10% of salary from the age of 20.*

Source: OECD

Pension coverage also remains stubbornly low at below 50% of the working population with only one third of all private sector employees contributing to a pension. As can been seen in the table above, for those on the average industrial wage of €35,000 the state pension will deliver 34% of their pre-retirement income. However, somebody on 1.5 times that income will only get 22% from the state pension. That would see the "squeezed middle" suffering even further pressure in retirement.

In these circumstances, it is clear that urgent action is required before the situation deteriorates even further. While there is no magic bullet solution it is also clear that auto-enrolment has a positive impact on coverage levels if the experiences of our nearest neighbour are anything to go by.

The UK faced many of the same problems as Ireland before it decided to establish a national auto-enrolment pension scheme. When the scheme was introduced in 2012 coverage stood at just 47% – about the same level as Ireland's at present. By the end of 2015 it had risen to 59%. This quite dramatic improvement was achieved against the background of national austerity policies and stagnant wage growth. Meanwhile Ireland's coverage was going in the opposite direction in much the same circumstances.

The OECD has estimated a contribution level of 15% of salary would be required to deliver an adequate level of income in retirement. If an auto-enrolment pension were pitched at that level it would likely meet with very high opt-out rates. A recent policy paper published by the Economic and Social Review, having examined a number of scenarios, indicated that a rate as low as 8% could be sufficient.

Recent speculation from Government sources indicate that the rate will be pitched at around 5% for employers and employees respectively, with the employee share being effectively lowered as a result of tax relief. Details such as this will be clarified during the consultation process which will lead up to the establishment of the new scheme.

We can only hope that the consultation process is concluded speedily and that we have certainty around an auto-enrolment scheme sooner rather than later.

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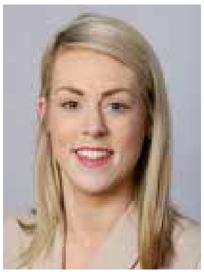

Bronagh Traynor
Investment Consultant

Gerald Fitzgerald
Investment Consultant

SIMPLE STEPS TO INVESTMENT SUCCESS

Bronagh Traynor and Gerald Fitzgerald outline three key questions to ask when deciding on an investment strategy.

Investment is an easy process. Generating consistent positive returns on the other hand is a challenge. Investors throughout time have been exposed to many risks, some widely known and accepted and others which have emerged catching investors unawares.

Over the last decade investors have had to deal with new vulnerabilities threatening their investment strategies. These have manifested themselves as two principal risks, geopolitical risk and central bank influence. Thanks to globalization, these risks have resulted in the economics and political stability in one country either purposely or unintentionally having overarching consequences for other countries, which in turn affects investors.

Given the prevalence of these risks, some investors have sought alternatives. In following the craze to invest in cryptocurrencies such as Bitcoin you would have to wonder whether investors have really evaluated the opportunity set or are merely participating for fear of missing out on "the next big thing".

Whilst some have hailed this market as the future, scepticism has remained, with many referencing the children's fairy tale of the Emperors' New Clothes. Throw fake news into the mix and the challenge for investors becomes all the more complex.

At a fundamental level, the objective of any investment is simple in nature, to deliver a positive return while taking as little risk as possible in achieving this. Easier said than done, however.

Investors' experience of markets in recent years has been a pleasant one, with markets trending upwards in similar fashion to an escalator in a shopping mall with its consistent almost mundane propulsion forward.

Whilst we constantly strive to move forward, it is as important to be cognisant of our surroundings, and to understand the risks to which we are exposed. In particular, unless appropriate infrastructure is in place to safeguard your interests, the faster you want to get to your destination the more inherent risk involved.

If we are to take any normal life event, be it travelling in a car or enjoying the sunshine outdoors, there are a host of safeguards in place to help mitigate risks. When travelling in a car, the vehicle has been designed to perform efficiently and protect the health of the occupants upon impact. The car will have been rigorously tested before being approved for sale. Speed limits and safety cameras are in place to mitigate human error.

The latter probably presents an annoyance for some, but they do serve a vital purpose of helping reduce the probability of negative outcomes. Knowing a journey takes an hour within the speed limit means that if you want to reach your destination in 50 minutes you have knowingly increased the probability of a negative outcome be that a speeding fine or worse.

When it comes to sunshine we rely on the expertise of others who have studied the effect of UV rays, and designed sun protection that mitigates the risk of sunburn or skin cancer. Unlike driving a car there are fewer regulations on our ability to tan but constant media campaigns, common sense and hopefully not too many previous bad experiences have taught us to take heed of the sun's power.

Whilst the above somewhat digresses from the task at hand, it does serve to highlight the ongoing risks to which a person is exposed, some of which we manage well and others not so well. Unless the risks are acknowledged and managed, the potential loss can be significant.

In the case of the above, the risks include a speeding fine or sunburn (at best). This compares to investing where risks include everything from losing your investment to not participating in markets, which ultimately impacts on your reasonable expectations at the point of cashing in and calling it a day.

We look to investing as a means of getting richer, securing our future be it in retirement or saving for that big capital expenditure down the line.

Questions in identifying an investment strategy
A misplaced question that is often put to people is the extent of the investment return that they are looking to achieve; misplaced in the sense that the question has validity and purpose, but it should not be the first question an investor asks themselves. Rather, an investor firstly needs to look at the negative side of investment (the risk) and ascertain what is a tolerable loss.

The second question that needs to be answered is the time period the individual is looking to invest these assets for. There is a strong overlap between the first and second question. Only when these questions have been answered will an investor truly be able to move onto the next matter of identifying a particular return target on their portfolio.

If we look at the returns on a range of global markets over various time periods, the potential for a sizeable range of returns is significant at shorter periods.

Investors need to appreciate the time horizon to which they are looking to target.

A misalignment of an investors' time horizon may result in unintended consequences. For instance, if an investor was a year from retirement and decided to invest their portfolio in global equities their portfolio could have fallen (and did for some unfortunately) by 38% over a 1-year period. If, however, the same individual had a time horizon of 15 years the individual would have generated a return on their equity portfolio of at least 2% per annum.

A common approach utilised in analysing markets is to refer to the past, seeking reason or understanding to apply to our current position based on previous achievements. Like any piece of financial analysis, however, we need to be acutely aware that just because something happened once previously – or even several times – doesn't mean it is necessarily going to happen again. The past is, however, a useful guide which helps to feed into the decision-making process.

Whilst investors have to be prepared for market volatility as seen recently, a review of the three key investment questions highlighted above can provide focus for the road ahead. This will ensure that alterations can be made in a timely manner or indeed allow investors the opportunity to reaffirm their existing positions accepting any short-term volatility in pursuit of long term returns.

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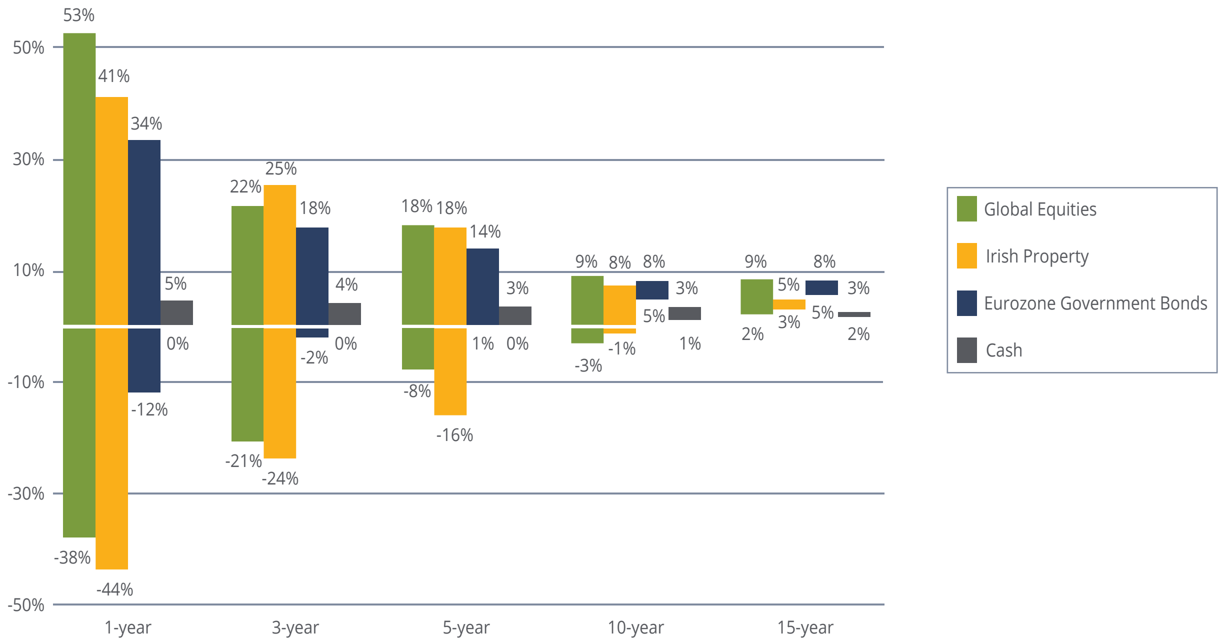
Gerald Fitzgerald gfitzgerald@invesco.ie

Rolling Annualised Returns on Asset Classes since 1999



Declan Keena
Director
Head of Actuarial

MANAGING LIABILITIES AND ENHANCING VALUES

Declan Keena considers the benefits of enhancing transfer values to reduce scheme liabilities.

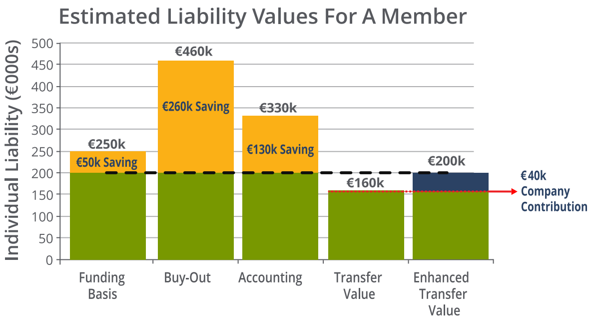
Various factors have contributed to the ongoing decline in the number of active defined benefit (DB) schemes in recent years. Chief among these has been affordability for both sponsoring employers and scheme members. Improved longevity coupled with historically low bond yields have driven costs higher for all DB pension schemes. Even in cases where schemes are well funded, employers are increasingly moving to remove the risk associated with DB schemes from their balance sheets.

The uncertainty around future funding costs was further increased by the current Taoiseach's comments during his brief tenure at the Department of Social Protection. Mr Varadkar stated that he believed there was merit to legislation which prevents the immediate closure of DB pension schemes where a deficit exists. The introduction of such legislation could have a major financial impact for companies with schemes which fail to meet the funding standard. Indeed, the prospect of such legislation may in itself represent another reason to close a scheme, regardless of its funding position.

The question is how to approach the closure? To date, employers have taken a variety of steps. In some cases, schemes have been wound-up with a top up contribution from the employer, while others have wound-up without a discretionary employer contribution.

We have seen the vast majority of active schemes being closed to new entrants. Many schemes are also closed to the accrual of future service benefits. Those benefits are instead provided through a separate defined contribution plan.

Where the aim is to eventually wind-up a scheme some employers are seeking to accelerate this process by offering members incentives to leave, principally by offering enhanced transfer values. This offers members amounts in excess of the minimum transfer value to move their benefit out of the DB plan, thereby removing the liability for providing the future benefit. The basis and amount of the enhancement varies from company to company. An enhanced transfer value exercise can be very attractive from an employer perspective as it can often reduce liabilities at a cost lower than the accounting liability. Therefore, there will be a gain on the profit and loss side for the employer as a result of the member's transfer.



From a member perspective, each case must be taken on its own merits. For example, if a scheme is only 50% funded and the employer's ability to make good the deficit or even to continue trading as a going concern in the long term is in some doubt, the option of taking an enhanced transfer value might be very attractive.

On the other hand, deferred members of a blue-chip employer sponsored fully-funded scheme, who wish to take their benefits in the form of an income, may opt not to take a transfer value regardless of the enhancement offered. However, even the most stable blue-chip companies can have rapid changes in strategy and this may cause them to wind-up a scheme or reduce benefits with little notice. In this case the enhanced value may turn out to have been the better option after all.

There is no hard and fast rule regarding enhanced transfer values, either in relation to how much to offer or what represents an attractive offer to members. This makes it absolutely critical that members receive professional financial advice when considering any offer. This financial advice will need to consider each member's individual circumstances and in particular their attitude to risk and their future income requirements.

To discuss enhanced transfer values contact:

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Gary Morrissey
Head of Business Development

MASTER TRUSTS QUALITY AT LOWER COST

Gary Morrissey outlines some of the advantages offered by the Invesco Master Trust.

A stated aim of the Pensions Authority is to reduce the number of occupational pension schemes in Ireland. One means of achieving this is the use of master trusts which group a number of defined contribution (DC) pension schemes within one single trust structure.

Master trusts offer benefits such as cost efficiencies through economies of scale. They allow DC schemes to benefit from the expertise of a professional trustee at a far lower cost than would otherwise be the case. Grouping a number of schemes within a single master trust structure removes the requirement to have a trustee for each scheme.

Invesco has established its own master trust to meet the needs of its clients. It offers companies all the flexibility of a trust based pension scheme at a lower cost than running their own trustee structure. Furthermore, by delegating fiduciary oversight to independent, professional trustees the Invesco Master Trust allows employers to offer a defined contribution pension plan with best-in-class governance and member communications.

The Invesco Master Trust has been certified by the Irish Association of Pension Funds as meeting its Pension Quality Standard (PQS). The PQS recognises high quality defined contribution pension schemes. It is designed to raise confidence in workplace pensions, help employers demonstrate the value of their scheme to current and future employees and help employees recognise that their scheme is of a high quality.

The Invesco Master Trust has already been used in a range of different situations. Some employers have used it to continue to provide retirement benefits to their employees following the winding up of a defined benefit scheme. Others have consolidated a number of existing DC schemes into a single new scheme in the Invesco Master Trust in order to achieve efficiencies and realise cost savings. In addition, companies setting up in Ireland for the first time have used the Invesco Master Trust to establish new DC schemes from scratch.

Among the key advantages of the Invesco Master Trust is that it removes the need for an employer to establish its own scheme, appoint administrators and investment managers or liaise with the Pension Authority or Revenue. Instead, all they have to do is join the Invesco Master Trust by completing a deed of participation. The costs and management time associated with running an occupational scheme are further reduced by the removal of the requirement to appoint trustees or auditors. Administration and investment costs are paid from members' funds and all compliance and governance costs are shared across participating employers, lowering the total cost for all.

The Invesco Master Trust structure does not limit investment options. Invesco's investment consulting team have evaluated and selected a wide range of funds to suit all employee investment and pension needs. We endeavour to provide best in class funds across the main asset classes (cash, bonds, equities, multi-asset and alternatives). These include both passive and active funds. Risk profiling tools are provided to assist employees in selecting the investment strategy best suited to their risk appetite.

Employers have choices as well. They are free to decide the benefit structure that will apply to their employees within the scheme. This encompasses eligibility to join, contribution levels and retirement age to name just a few variables.

Employee satisfaction and retention is a top priority for all employers. A good quality pension scheme helps to make employees feel more valued. The Invesco Master Trust offers employees a comprehensive range of communication supports including a welcome pack with member booklet and investment guide, an industry-leading web portal, telephone and email support and the opportunity for face to face contact with our pensions experts.

To learn more about the Invesco Master Trust contact:

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Orla Ormsby
Head of Legal

Brid McDonnell
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GDPR – WHAT IT MEANS FOR PENSION SCHEMES

Orla Ormsby and Brid McDonnell look at the implications of GDPR on pension schemes.

Introduction
The General Data Protection Regulation ("GDPR") will govern the processing of personal data in all Member States with effect from 25 May 2018. GDPR will replace the existing data protection legislation (the Data Protection Acts 1988 and 2003) and provide a single set of data protection rules throughout the EU. Trustees, sponsoring employers, administrators and service providers should be aware of the implications that GDPR will have for the handling of personal data.

Trustees of pension schemes are data controllers who are legally responsible for personal data. Personal data means any information relating to an identified or identifiable living person, for example members and other beneficiaries of a pension scheme. The role of data controller carries with it serious legal responsibilities.

The processing of scheme members' personal data is often outsourced to Registered Administrators who will be data processors if they are given any personal data. A data processor holds or processes personal data, but does not exercise responsibility for or control over the personal data. Invesco, as Registered Administrator, is the data processor of scheme member data.

While the Registered Administrator is usually the main data processor, legal advisers, the scheme sponsor, the actuary, medical advisers and insurance companies may also be data processors.

Key changes under GDPR
While GDPR enhances many of the current data protection principles that apply under the Data Protection Acts 1988 and 2003, it also introduces some significant changes. GDPR introduces a new idea, "privacy by design" which is intended to be the framework on which to demonstrate transparency and accountability for data protection obligations.

The principal changes that arise under GDPR are:

Privacy Notice
Under the Data Protection Acts 1988 and 2003, there is a requirement for data controllers to notify data subjects in relation to the processing of their personal data. Currently, when personal data is being collected, data controllers are required to provide certain information to the data subjects, including the identity of the data controller, the reason the data is being collected, the uses it will be put to and to whom it will be disclosed. GDPR increases the level of information to be notified to data subjects including:

- details of the legal basis under which data is being processed
- details of the length of time data will be retained
- information in relation to the individual's right of complaint where they are not satisfied with how their data has been processed

The wording of privacy notices should be sufficiently wide to cover all processing activities that may be carried out on personal data. Communications in relation to data protection should be made in a transparent manner and must be in concise, clear and plain language.

Data Subject Consent
GDPR clarifies and extends the conditions to be met where consent is relied on as a condition for processing. To demonstrate a data subject's consent, data controllers will no longer be permitted to rely on pro-forma terms and conditions unless consent is "clearly distinguishable" from other matters and is "in an intelligible and easily accessible form, using clear and plain language".

Data subjects have the right to withdraw consent at any time. It may not therefore be practical for trustees to rely on consent as a basis for processing and it may instead be prudent to rely on a different legal basis for processing, such as for the purposes of legitimate interests being pursued by the data controller; if it is necessary for the performance of a contract; if it is necessary to comply with a legal obligation and/or if it is in the public interest; or to protect the vital interests of an individual. Importantly, where special categories of data are being processed such as data relating to health, sexual orientation, racial or ethnic origin etc., explicit consent of the data subject is required.

New and enhanced data subject rights
GDPR introduces strengthened data subject rights. These new rights represent significant changes to the current position under Irish law and include the right to be forgotten (the "right of erasure") and a right to data portability, which is intended to facilitate the return of data to a data subject and to have data sent to another processor.

Data subjects can make a claim against a data controller or a data processor if they have suffered a data protection breach. Although the trustees, as data controller will ultimately be responsible for GDPR compliance, data processors will also be liable to data subjects where they have failed to comply with their obligations. Data subjects can also sue for compensation in certain circumstances.

Data subjects must be told the period for which his or her data will be retained or, if this is not possible, the criteria for deciding the retention period. Data subjects must also be told about their right to have their data corrected, deleted or to restrict the processing of their data.

Mechanisms will have to be put in place to respond to the exercise of data access rights within the statutory 30 day timeframe and any information requested by a data subject must be provided free of charge.

Reporting a Data Breach
In most cases, where there has been a data breach, trustees are obliged to notify the Office of the Data Protection Commissioner ("ODPC") without undue delay and where possible within 72 hours of becoming aware of the breach. Reasons for a delay must be provided to the ODPC if the breach is not notified within 72 hours. There are fines for failure to notify and for the breach itself. In certain circumstances, for example where the breach carries a high risk to the rights and freedoms of individuals, the relevant data subjects must also be notified.

Data Protection Agreements ("DPA")
Arrangements must be made before 25 May 2018 to ensure appropriate measures and procedures are in place to meet GDPR requirements and to ensure the rights of data subjects are protected.

A data controller can do business with a data processor only on the basis of a written contract or a contract in equivalent form which includes appropriate security and other data protection safeguards.

Key points for inclusion in a DPA are:

- that the data controller is responsible for the duty of care owed to personal data and accordingly when drawing up the contract the data controller should be very specific in the instructions given as to what the data processor can do with the personal data provided.
- that the data processor will process personal data only on the basis of the authorisation and instructions received from the data controller. This provision ensures that personal data passed on to a data processor may not be retained or used by the data processor for its own purposes.
- that the data processor will commit to apply appropriate security measures to the personal data to protect it from unauthorised access or disclosure.
- that data must be returned or deleted upon termination of the contract.
- that the data controller or their agents have a right to inspect the premises of the data processor to ensure compliance with the provisions of the contract.

Trustees will need to carefully review existing processing and service level agreements to ensure that GDPR provisions are incorporated. In addition, under GDPR, liability is apportioned between data controllers and data processors and data controllers in particular will need to ensure that the liability provisions in the DPAs are appropriate.

Data Protection Impact Statements (DPIA)
Where processing may involve a high risk to members or beneficiaries, trustees will have to carry out an assessment (a "Privacy Impact Assessment") of the risks to members or beneficiaries before carrying out that processing and assess the appropriateness of any proposed measures to mitigate those risks.

Enforcement and Penalties
There will be a harmonised sanctions regime under GDPR. In particular, GDPR grants the ODPC the ability to impose extensive financial and non-financial sanctions on data controllers and data processors. These sanctions may include fines of up to €20 million or 4% of annual worldwide turnover (whichever is higher) depending on the severity of the breach.

It is evident that working towards compliance with GDPR will involve a significant amount of forward planning and it is advisable to take action now to consider what steps are needed in advance of 25 May 2018.

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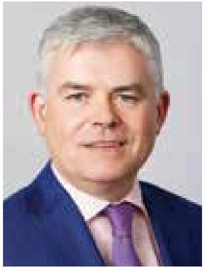

Brian McGarry
Director

MEETING THE NEEDS OF MEMBERS

A good quality pension scheme can be a key employee retention tool writes Brian McGarry.

The pace of the Irish economic recovery has been quite startling. From a position just five years ago where commentators were talking bleakly about a recession which could last a generation we have now arrived at a situation where Ireland has once again become the fastest growing economy in the Eurozone.

This changed environment is having an impact both on labour costs and mobility. There are shortages in some critical areas and it is becoming harder for employers to retain staff. Enhanced benefit packages have proven to be effective in improving retention rates. They tend to work better than headline increases not only because of the tax efficiency of certain benefits but also because they demonstrate the value an employer places on their employees.

A key element of benefits package is a well-designed pension scheme and it is vitally important to ensure that the scheme is structured to meet the needs of members throughout their working lives.

A well-designed scheme should include the following elements:

- An **appropriate and flexible contribution structure.** Contributions should be at a level that fund for meaningful benefits at retirement, but flexible enough not to discourage employees from joining. Typically, employees might be required to contribute something in the range of 2% to 8% of salary with the employer at least matching these amounts.
- **Investment options** that give members sufficient choice to enable them to maximise the need to generate returns within their own risk profile. There should also be a range of default investment strategies which are appropriate for the needs of members. Members also need to be given the tools to help them make the best investment decision for their pension contributions.
- **Good communications.** Pension scheme documentation has too often been full of jargon and seen as alien to many members. This should not be the case. Booklets, explanatory materials and benefit statements should be clear, readable and written in plain English.
- **Strong member engagement** is vital. Members need to feel part of and engage with their pension scheme. This can be achieved through workshops, group presentations and one-to-one advisory sessions to ensure that scheme members receive the support they need to make informed decisions in relation to their pensions.
- **Excellent administration** including online and mobile portals which give members access to their pension information anytime and anywhere they wish.
- **Life assurance.** This is a very valuable benefit that can be provided at a reasonable cost.
- A strong **governance framework.** Members need to be assured that their scheme is run to the highest professional standards.
- **Value for money** both in terms of administration charges and fund management fees.

An employer who is seen to look after the pension needs of all of their employees throughout their careers is likely to be far more attractive than one who does not and a well-designed pension scheme will go a long way to achieving this.

To learn more about this or any other aspect of DC pension scheme design contact:

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THE HUMAN CAPITAL FACTOR

Conor Murray and Padhraic Kelly explain the importance of striking the right balance between our human and financial capital.

Conor Murray
Personal Financial Advisor

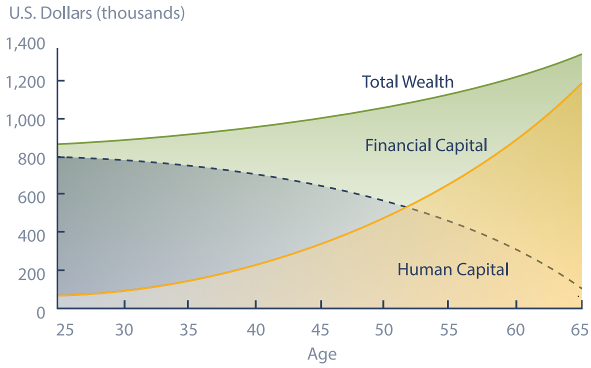
Padhraic Kelly
Personal Financial Advisor

Most people measure their wealth in terms of physical and financial assets. They consider the value of their property, savings, investments and pension. Many will also consider their debts and borrowings to give an indication of what they believe is their net worth. This is known as financial capital. But it doesn't tell the full story. In order to get an accurate picture of an individual's total wealth we must also consider human capital.

Human capital is the present value of an individual's expected lifetime earnings. This may be dictated by age and profession, but an individual can also improve their human capital by investing in themselves through education and work experience.

Over the course of a career, we would expect earnings to increase, pensions to accrue and assets to accumulate. We would also expect debts such as loans and mortgages to reduce. In other words, financial capital is expected to increase throughout our working life. Conversely, our ability to earn future income diminishes as we approach retirement. As a result, human and financial capital should have an inverse relationship as seen below:

Expected Financial Capital, Human Capital, and Total Wealth over Life Cycle with Optimal Asset Allocation



Source: "Lifetime Financial Advice: Human Capital, Asset Allocation and Insurance"

The relationship between human capital and financial capital is a relatively straightforward one. However, it is important that one protects human capital in the event of being unable to work due to illness or disability or premature death. To ensure there is no material impact on your family's lifestyle, it is imperative that you incorporate both income protection as well as life insurance to hedge this risk.

All income protection should increase over time in order to keep pace with anticipated wage growth and average inflation. This ensures that the protection remains fit for purpose. The opposite is true for life insurance, which when analysed is a protection for our families against the loss of our future earnings due to death. As a result, the life insurance we put in place should mirror our human capital, with the greatest level required when we are young, diminishing over time as this need is replaced by financial capital.

This can be achieved by calculating an individual's current human capital (estimated future after-tax earnings), deducting any fixed expenditure that would be covered by other protection (such as mortgage protection and Death in Service benefits through employment) and finally, deducting an individual's personal spending need. This will give a good indication of the impact on loss of future potential earnings to the household in the event of death.

If we were to take a 30-year-old on a salary of €40,000 paying a mortgage of €700 per month on the family home, we would estimate that the need for life insurance would be circa €1,000,000 set up on a decreasing basis to age 65. While this seems a very large number, given the age of the client and the decreasing nature of cover, this plan could cost less than €50 per month.

We will spend much of our working lives converting our human capital into financial capital, and while this is hugely important, investing in our human capital is also essential. Further education, travel and gaining new experience through changing job or roles within the same company can enhance our human capital. This in turn improves our ability to build financial capital over the course of our careers. With so much personal investment and sacrifice, it is vital that we protect what may be our greatest asset.

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SMALL IS BEAUTIFUL

Richard White & Paddy Swan consider whether smaller companies offer a long term investment opportunity.

Richard White
Senior Investment Consultant

Paddy Swan
Director

Over the longer term, smaller company returns have outstripped those of their large cap peers. This is known as the 'smaller companies effect'. Traditional academic theory suggests that abnormal returns are fleeting, arbitraged away by investors seeking to exploit the anomaly. However, various factors suggest that this asset class could continue to generate premium risk-adjusted returns over the long term. Here, we examine the reasons for these outsized returns and outline why the factors behind this small cap effect are likely to persist for a considerable time.

The smaller companies effect
The first 10 years of the millennium were frequently described as a 'lost decade' for equities. Global stock markets have since strengthened substantially, however, long term returns from large cap and small cap equities have diverged starkly. Indeed, between 1 January 2000 and 1 September 2017, global large cap equities delivered a 75.5% total return. By contrast, total returns from global smaller companies have been dramatically stronger at 187.2%.

In most cases, smaller companies deliver a premium return over their larger counterparts. Rolf Banz in his University of Chicago doctoral thesis, later published in the Journal of Financial Economics, first identified and computed the 'size effect' for US stocks. In analysing US common stocks listed on the New York Stock Exchange, he discovered that on average smaller companies enjoyed higher risk-adjusted returns than larger peers and that the 'size effect' was long term, persisting for over 40 years.

An underappreciated sector
There are two key factors that suggest smaller companies will remain underappreciated in the longer term.

- **Institutional investor behaviour**
Traditionally, institutional investors' world view has tended not to separate smaller companies from the wider 'equity' category as an asset class, thus overlooking an area with strong excess return potential.

- **The rise of passive investments**
According to Thomson Reuters Lipper data, passive investments constituted only 5% of total European mutual fund assets under management in 2004. By 2011, this figure had increased to 8% and by 2016 to 12%. Due to the sheer number of stocks involved and much lower levels of dealing activity, smaller companies markets offer investors opportunities to exploit inefficiencies and generate enhanced returns.

An under-researched sector
It makes economic sense for some analysts and banks to restrict themselves to covering a small number of very large companies. It is not unknown for the analysts at 'bulge bracket' investment banks to work full time on only two or three companies. Many hundreds of pages of research about these companies are published on a regular basis.

There is undoubtedly less research available on smaller companies and the small cap research that is available is often much shallower. This information gap opens up opportunities to find compelling investment ideas that others have yet to discover.

Risk and risk-adjusted returns
Since the millennium, some of the largest and most stable companies in the world have either imploded or declined precipitously in value. Scale, size and international reach do not necessarily equate to low risk, as investors in RBS, BP or Nokia know only too well. Consequently, the risk differential between the largest and smallest companies may not be as great as one might assume. While lower risk smaller companies have been shown to outperform higher risk small caps, the asset class as a whole also outperforms on a risk-adjusted basis. In other words, small caps generate higher returns per unit of risk assumed.

To conclude, concern on the part of some investors regarding apparent risk is unlikely to dissipate soon. However, over the long term, research shows that investing in smaller companies has resulted in premium returns compared with those achieved by large caps. Ultimately, the small cap effect should continue to provide those investors deploying a robust and consistent stock selection process with attractive long term returns.

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Andy Kelly
Director

MAKING UP FOR LOST TIME

It is not too late to make up for lost years in pension contributions Andy Kelly advises.

With the recovery now firmly established many business owners and senior directors are once again looking at their pension arrangements. In many cases they will be looking at making up for a decade of missed contributions.

When the financial crisis hit in 2008 those businesses which weren't swept away altogether only survived through the imposition of severe cuts. SME's were particularly badly affected. There were job losses across the economy and salary reductions at all levels of companies. Every cost deemed not absolutely necessary was eliminated and very often this started with executive pension contributions.

Facilities from banks were scarce and any spare cash held by companies had to be retained for contingencies. At the outset a reduction in contributions appeared sufficient but as time went on very many were left with no option but to cease pension funding altogether.

The effect of these measures was amplified by the impact of the pension levy which depressed the growth in value of pension funds over the period. In addition, quite a few shareholder directors were forced to exercise the option to draw down up to 30% of their AVC value in order to reinvest in the company or pay off personal or business debt.

In these circumstances it would be all too easy for an individual to assume that it is already too late to make up for the lost years, but they would be wrong. Not only is it never too late but there are considerable advantages to resuming contributions to the maximum extent possible regardless of how near you are to retirement.

The first step is to estimate what income will be required in retirement. This will involve an analysis of the lifestyle required in retirement and the minimum annual income needed to support this. Lifestyle analysis will include where the individual is going to live, what they want to drive, healthcare requirements, leisure activities, holidays, helping children out with life events such as weddings, paying off debts and so on.

Items of expenditure will also have to be taken into account. Whilst mortgages may be paid off by the time an individual retires there are other costs such as motoring and health insurance which tend to be borne by companies that will have to be paid from retirement income.

This will help determine the contribution rates necessary over the coming years to fund a reasonably comfortable retirement. After that, it's a question of looking forward to when the individual wishes to retire. From there it is a reasonably straightforward exercise to calculate the gap between what's in the pension fund at present and what it needs to be at retirement.

It is then a question of planning to bridge that gap. While the gap may seem large at the moment prompt action can mean it is addressed relatively painlessly. For example, an individual in their early 50s wishing to fund for a maximum tax-efficient pension fund of €2.15M can have their company make very significant contributions annually in order to achieve this goal even if they have not yet established a pension scheme.

This is a very tax efficient way of distributing profits from a business. It is also a very attractive alternative to using after-tax income to pay down personal debt which may have been accumulated during the downturn. An individual with a €2 million pension fund can take a lump sum of €440,000 net from their pension fund at age 60 and use this to pay off debt. This is certainly not reason enough in itself to catch up on lost pension time but it is one of the many options which are available for those that do.

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John Lucey
Director

TAKING THE STRESS OUT OF RETIREMENT

John Lucey looks at the need to plan for both financial and lifestyle adjustments in retirement.

Retirement isn't what it used to be. It is no longer just an event, it is a continuum. It is a significant period of most people's lives and it is getting longer. Indeed, an Irish man reaching age 65 in 2018 can expect to live on average until 86 and a woman until almost 89. This means that an individual retiring at 60 may find their retirement lasting at least 25 years.

When we consider how many hours we spend on work and at work every day, that's a lot of time to fill in. Most people will spend more than 50 hours on work between actual time on the job and commuting. Many business owners and senior executives will spend a lot more than that, particularly when social events linked to work are taken into account.

That leaves a lot of available hours when we retire – 3,000 a year for many of us. That's where the whole concept of active retirement comes in. People have to think long and hard about what they are actually going to do in retirement if they are to lead happy and fulfilled lives.

All the research shows that people who are active in their retirement remain fitter and healthier for longer. Further education, travel, sporting activities, personal development and community activity may all be on the agenda. While mortgages may be paid and children may be financially independent lowering outgoings considerably, other costs might increase. Even hobbies like painting can end up costing quite a lot when classes, materials and field trips are taken into account.

This makes it critically important to have a financial plan for retirement that not only meets your basic income requirements but your lifestyle requirements as well. Not only will this help us decide on our life goals and ambitions in retirement it will also act as a decision support tool when it comes to pension and retirement income planning. The two can come together in some quite surprising ways.

When looking forward to our lifestyle plan we might find that we don't really want to retire completely, that we want to continue working part-time or flexibly in a consultancy role. This option might be available with our current employer or there may be other avenues through which we can apply our skills and experience. This will have the dual effect of helping us lead a happier, more fulfilled life when we move into retirement as well as offering an additional source of income to help support our overall lifestyle.

Alternatively, we might find that by taking out an ARF and supplementing our lump sum by downsizing our home there is ample funding to support our lifestyle without any need to even consider continuing working if we don't want to.

Whatever the outcome of the planning process, having enough money in retirement takes away a huge worry and allows you to focus on important lifestyle factors.

To find out more about funding your retirement lifestyle goals contact **John Lucey** at:

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