

# The Supervisory Review Process for Institutions of Occupational Retirement Provision (IORPs)



Insurance and Pensions Supervision

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## **1. The Functions of the MFSA**

The Malta Financial Services Authority (“Authority”) is the competent authority established by the Malta Financial Services Authority Act (Cap. 330) to act as the single regulator for financial services in Malta. Article 4 of the said Act lists the functions of the Authority. For the better performance of its functions, the Authority collaborates with other local and foreign bodies, Government departments, international organisations, with the European Securities and Markets Authority (ESMA), the European Banking Authority (EBA) and colleges of supervisors, the European Insurance and Occupational Pensions Authority (EIOPA), the European Systemic Risk Board (ESRB), the European Central Bank (ECB), the Single Resolution Board (SRB) and other entities which exercise regulatory, supervisory or licensing powers under any law in Malta or abroad or which are otherwise engaged in overseeing or monitoring areas or activities in the financial services sector and the registration of commercial partnerships, and to make arrangements for the mutual exchange of information and for other forms of assistance in regulatory and supervisory matters.

## **2. General Supervisory Powers**

The Authority is responsible for the prudential supervision of a retirement scheme. The Authority conducts its supervision on a retirement scheme on a forward-looking and risk-based approach. Supervision by the Authority of a retirement scheme is carried out in a timely and proportionate manner and comprises of an appropriate combination of desk-based reviews and on-site supervision. The Authority has all the necessary powers to be able to obtain information from a retirement scheme.

## **3. The Objectives of Insurance and Pensions Supervision ‘IPS’ in relation to the Supervision of IORPs**

With regards to pensions, the main objective of supervision of the Authority is namely to protect the rights of members and beneficiaries and to ensure the stability and soundness of retirement schemes. The Authority, in carrying out its duties is to duly consider the potential impact of its decisions on the stability of the financial system in the European Union, in particular in emergency situations.

## **4. The Maltese Legal Framework**

The Retirement Pensions Act Cap. 514 (‘the Act’), together with Regulations and Pension Rules issued thereunder, provide a statutory basis for the regulation of Retirement Schemes, Retirement Funds, and related Service Providers in Malta.

The following Legal Notices supplement the Retirement Pensions Act:

- L.N. 6 of 2015 – Retirement Pensions Act (Exemption) Regulations
- L.N. 7 of 2015 – Retirement Pensions (Control of Assets) Regulations
- L.N. 8 of 2015 – Retirement Pensions (Technical Provisions) Regulations
- L.N. 10 of 2015 – Retirement Pensions (Fees) Regulations
- L.N. 48 of 2020 – Retirement Pensions (Cross-Border Activities and Cross-Border Transfers) Regulations
- L.N. 50 of 2020 – Retirement Pensions (General Provisions of Supervision) Regulations

The Pension Rules issued under the Retirement Pensions Act (Cap.514) which supplement the Retirement Pensions Act are the following:

- Pension Rules for Occupational Retirement Schemes
- Pension Rules for Personal Retirement Schemes
- Pension Rules for Retirement Funds
- Pension Rules for Service Providers.

In accordance with the Act (Cap. 514), the MFSA may, from time to time, issue, amend, or revoke Pension Rules which shall be binding on licence holders and, or recognised persons under the said Act. Such Pension Rules may lay down additional requirements and conditions in relation to activities of that licence holder. Moreover, the Act grants supervisory powers to the MFSA to be able to effectively carry out its supervision on these licence holders.

Following the publication of Directive (EU) 2016/2341 (“IORP II Directive”), IPS embarked on a transposition process of the said Directive. The IORP II Directive introduced a new regulatory framework for occupational retirement schemes, its main objective being to provide for adequate protection of members and beneficiaries of occupational retirement schemes. It aims to ensure higher standards of governance and a modern risk-based governance system to improve risk management and transparency of institutions for occupational retirement provision.

In order to transpose the IORP II Directive, the Retirement Pensions Act was amended by Act No. V of 2020 published on the 3 March 2020 in the Government Gazette of Malta No. 20,357. Furthermore, the following Legal Notices were amended and published on the 13 March 2020 in the Government Gazette of Malta No. 20,366 in order to transpose provisions from the IORP II Directive:

- Legal Notice 48 of 2020 - Retirement Pensions (Cross-Border Activities and Cross-Border Transfers) Regulations, 2020;
- Legal Notice 50 of 2020 - Retirement Pensions (General Provisions of Supervision) Regulations, 2020;
- Legal Notice 46 of 2020 - Retirement Pensions (Transitional Provisions on Back-Office Administrators) Regulations, 2020;

- Legal Notice 47 of 2020 - Retirement Pensions (Control of Assets) (Amendment) Regulations, 2020;
- Legal Notice 49 of 2020 - Retirement Pensions (Exemption) (Amendment) Regulations, 2020;
- Legal Notice 45 of 2020 - Retirement Pensions (Defined Benefit Retirement Schemes) (Amendment) Regulations, 2020;
- Legal Notice 51 of 2020 - Retirement Pensions (Transitional Provisions) (Revocation) Regulations, 2020.

The main reason for the publication of the amendments to the Pension Rules is to transpose the remaining provisions of the IORP II Directive, which had not been included in the Act and regulations issued thereunder. The amendments also aligned the Pensions Rules for Occupational Retirement Schemes with some of the requirements that have been introduced in the Pension Rules for Personal Retirement Schemes.

Following the publication of the amendments to the Act, the Legal Notices, and the Pension Rules on the 23 March 2020, IPS finalised the transposition of the IORP II Directive by publishing a Circular to inform the market on the publication of the new Pension Rules for Occupational Retirement Schemes.

The MFSA issued further clarifications on the IORP II Directive by means of a publication of a Circular on the Implementation of the IORP II Directive on the 11 May 2020. The guidance in this Circular was based on four Opinions published by EIOPA on the 10th July 2019 entitled: Opinion on the supervision of the management of environmental, social and governance risks faced by IORPs, Opinion on the use of governance and risk assessment documents in the supervision of IORPs, Opinion on the supervision of the management of operational risks faced by IORPs and Opinion on the practical implementation of the common framework for risk assessment and transparency of IORPs. It should be noted that the information of this Circular is not exhaustive and as such, IORPs are required to review the opinions in detail.

## **5. General Principles of the Supervisory Review Process**

Supervision carried out by IPS is based on a forward-looking, proactive and risk-based approach. IPS conducts its supervisory activities in a proportionate manner commensurate to the nature, scale and complexity of the risks inherent in the business of the licence holder. IPS is committed to carry on its supervisory duties in a transparent and accountable manner taking into account the protection of confidential information. The main areas of supervisory activity carried out by IPS contribute towards ensuring that an IORP ensures that:

- a. its directors, senior management and key function holders are fit and proper at all times;

- b. it has a culture that supports prudent management and take into consideration environmental, social and governance factors;
- c. it has in place sufficient controls to minimise incentives for excessive risk-taking by management and risk-taking staff;
- d. it deals with the MFSA in an open and co-operative manner;
- e. any significant decisions involve at least two persons who effectively run the IORP before the decision is implemented;
- f. the Board's size and composition is suitable for the IORP and the board members collectively possess appropriate qualification, experience and knowledge;
- g. it builds an effective system of governance in accordance with the IORP II Directive which provides for sound and prudent management;
- h. it has in place clear structures of accountability and delegation of responsibilities for individuals and committees, including checks and balances to prevent dominance by an individual. Senior individuals should remain accountable for the actions of those to whom they delegate responsibilities, including where third parties are utilised with respect of outsourced functions;
- i. it invests its assets in accordance with the prudent person rule taking into consideration environmental, social and governance factors related to investment assets in investment decisions;
- j. it maintains at all times an adequate level and quality of capital, taking into account the risks to which it is exposed. Capital should be sufficient to absorb unexpected losses, based on a wide range of internal and external stresses;
- k. there is no significant risk that it cannot meet its liabilities as they fall due, and to have appropriate risk management strategies and systems in place for managing its liquidity;
- l. it implements an effective Own Risk Assessment (ORA) process which ensures an effective link between an IORP's business plan, risk appetite, and capital management plans;
- m. it identifies all material risks to be addressed by contingency plans covering the areas where it considers itself to be vulnerable.

## **6. The Supervisory Review Process**

In terms of Article 41A of the Retirement Pensions Act CAP. 514), the MFSA reviews the strategies, processes and reporting procedures which are established by a Retirement Scheme Administrator or an occupational retirement scheme to comply with the provisions of this Act and any regulations and Pension Rules issued thereunder taking into account the size, nature, scale and complexity of the activities of the scheme.

The review also considers the business environment and market in which the IORPs are operating, including third party services providers which provide for outsourced key functions or any other tasks or activities for such IORPs. The review encompasses an assessment of the following:

- (a) qualitative requirements relating to the system of governance;
- (b) the risks the IORP faces; and
- (c) the ability of the IORP to assess and manage those risks.

The MFSA has implemented monitoring tools commensurate to the size of the market. This enables the MFSA to identify deteriorating financial conditions in an IORP and to monitor how a deterioration is remedied.

The MFSA conducts reviews, evaluations and assessments on a regular basis. The frequency and intensity of supervision is determined by the risk posed by the IORP having regard to the size, nature, scale and complexity of the activities of the IORP concerned.

The Supervisory Review Process consist of the following steps:

1. **Analysis of Inbound Information** – the consideration of qualitative and quantitative data available from different sources including but not limited to regular reporting requirement as well as other information that is available to the MFSA from other supervisory interactions.
2. **Risk Assessment** - the identification and assessment of current and future risks that IORPS are or may become exposed to including the IORPs capacity to identify, measure, monitor, manage and report on risks. This assists the MFSA to determine the likelihood and severity of risks affecting IORPs as well as the intensity and frequency of supervision which are determined in the supervisory plan.
3. **Detailed Review** - determination of whether a desk-based review or thematic reviews, supervisory meetings, an on-site inspection or a combination of these is to be carried out by the MFSA, based on the supervisory plan, taking into account all relevant information and focusing primarily on the areas of risk.
4. **Supervisory Measures** - identification and monitoring of supervisory measures based on the conclusions of the Detailed Review. The measures are commensurate to the weaknesses, deficiencies and/or breaches detected. The MFSA requests IORPs to remedy such weaknesses or deficiencies or breaches within such period and in such a manner as it may deem necessary or appropriate in the circumstances in terms of the powers given to it by the Retirement Pensions Act.

The MFSA will notify the IORPs in writing about the specific measures that it should implement. Where appropriate this will include a specification of the appropriate timeframe in which the IORP is to implement the actions necessary to comply with the measures. Once the measures are implemented, the MFSA will update the supervisory plan to reflect the degree of effectiveness of the supervisory measures as implemented by the IORP.

## **7. Co-operation and Exchange of Information**

In terms of the IORP II Directive, articles 52, 55, 58 and 60, which have been transposed in articles 52, 52A, 52B, 52C, 52D and 52E of the Retirement Pensions Act, the Authority has the power to co-operate and exchange of information.

## **8. Information to be provided for Supervisory Purposes**

In terms of article 41B of the Retirement Pensions Act, an occupational retirement scheme shall submit to IPS the information, which is necessary for the purposes of supervision, as may be specified by means of regulations or Pension Rules which shall also specify the period within which such information is to be submitted.

## **9. Will IPS Prevent Failures of Authorised IORPs?**

The MFSA accepts that risk-based supervision does not eliminate risks but mitigates risks and in the event of a failure of an IORP, IPS will ensure that the IORP winds up in an orderly manner.

## **10. Conclusion**

By adopting a risk-based, forward-looking, proactive and proportionate approach to supervision, IPS believes that it shall be creating incentives for IORPs to keep raising their standards and maximising their success whilst keeping within the parameters of the regulatory framework.