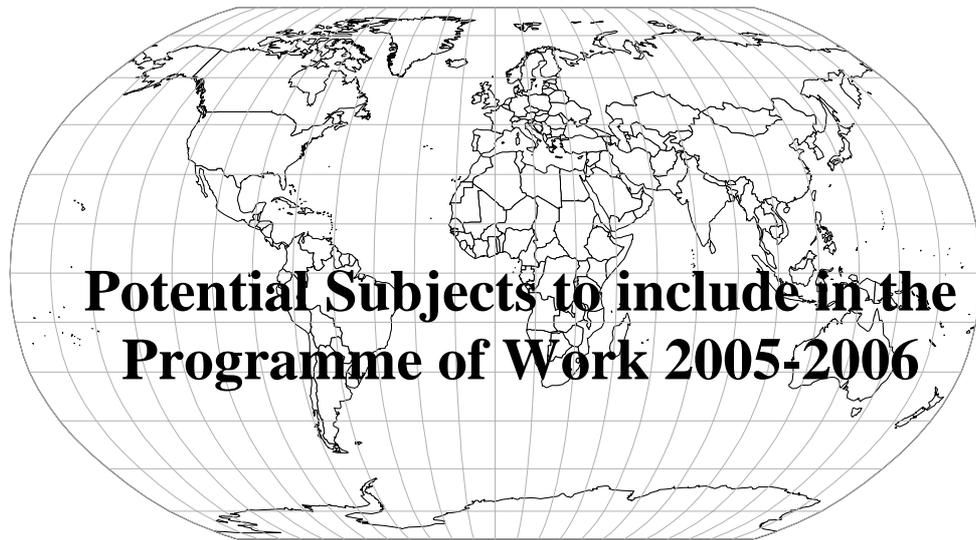


THE INTERNATIONAL ORGANISATION OF PENSION SUPERVISORS (IOPS)



REVISED VERSION

INTERNATIONAL ORGANISATION OF PENSION SUPERVISORS (IOPS)

The following Programme of work was approved by the Technical and Executive Committees of the IOPS during their meetings on the 13th and 14th of December 2004. The decision was taken to prioritize the following projects, and for them to be led by the delegates listed:

1. *Guidelines for good practices in pension supervision*—OECD*, Croatia, Italy, Jordan, Mauritius and possibly the Netherlands
2. *Core elements of a risk-based approach to pension supervision and strategic planning*—World Bank*, Australia, Germany, Netherlands, Pakistan, United Kingdom.

The following projects will be started during 2005, including through a discussion in the Technical committee of a detailed project outline:

3. *Supervisory education, outreach and communication, including training of trustees*—Kenya*, Ireland, South Africa, United Kingdom, World Bank
4. *Guidelines for compliance with the licensing of pension funds*—Australia*
5. *The documentation of methods for pension supervision*—Australia*
6. *Analysis of supervisory structures*—Mexico*, Italy
7. *Cross-border pension supervision*—Spain*
8. *Utilization of IT technology in off-site supervision*—Turkey*

Potential subjects to include in the Programme of work to be started in 2005-06

This paper has been prepared to inform decisions to be taken on the first programme of work of the International Organization of Pension Supervisors (IOPS) following the founding of the organization on 12th July, 2004. It is intended that topics to be included in the programme of work will be drawn from this paper and should be capable of being started during 2005 and 2006, with at least two of them being completed during this period. The paper should also provide a useful starting point for the IOPS when it considers future programmes of work.

The programme of work for 2005/06 will be selected from this paper by the IOPS Technical Committee bearing in mind the priorities for the IOPS and pension supervisors generally and what is practically and financially feasible viable given budgetary constraints and other commitments by the IOPS members. As the bulk of the work will be completed by IOPS members themselves, it is very important that the priority ranking between the activities to be considered in the programme of work reflect actual commitments by those members to participate actively to the work.

The programme of work is consistent with the IOPS purpose to serve as the standard-setting body on pension supervisory issues and on regulatory issues related to pension supervision, through the development and promotion of the implementation of international principles, standards, and good practices in pension supervision, the provision of a world-wide forum for policy dialogue and the exchange of information on pension supervisory issues and on regulatory issues related to pension supervision. The activities of the IOPS aim to improve the quality and effectiveness of the supervision of private pension

systems throughout the world with the objective to enhance the development, operational efficiency and effectiveness of these to provide a secure source of retirement income in as many countries as possible. Throughout its work, the IOPS will place the highest priority on the enhancement of international cooperation, the coordination of standards and practices across borders.

The work programme of the IOPS is focused on issues directly related to the organization, operation and evaluation of private pension supervisory programs. It will cover the pension supervisory issues and regulatory issues related to pension supervision as defined in the IOPS by-laws –i.e. mainly issues related to the organisation, structure and functions of the supervisory body, the development of proper supervisory techniques and the implementation of enforceable regulations by supervisory bodies.

The work should seek to distinguish and separate the IOPS from other related entities that are concerned with broader questions of retirement income policy, public management, the insurance industry or the regulation of pension systems. The IOPS should seek to limit its involvement in issues related to the establishment of legislation and regulation (rule making), broader retirement income, macro-economic or development policy to those with a direct nexus with the management and operation of supervisory programs.

The activities from which the programme of work will be selected fall into the following areas:

- Standards and good practices in pensions supervision
- Information gathering and analytical projects
- International co-operation

I. Standards and Good practices in pension supervision

1. The core goal of the IOPS is to identify good practice in the field of pension supervision. The initial project of the organization could therefore be to draw up a set of pension supervision guidelines. These guidelines could be generalised to private pension plans (both occupational and personal). The standard-setting activity of the IOPS will be conducted in close co-operation with the OECD, which is the standard-setting body for regulation of private pensions, following the modalities developed in the Co-operative agreement between the two bodies (see annex 1 –to be provided later on).¹ These guidelines would expand on previous work carried out by the INPRS and OECD², and could for instance build on observations of good practice on the organization of pension supervisors identified by both bodies, such as the OECD's recent survey of supervisory methods³. The following conclusions from the survey could be used as a basis for the guidelines:

- *Mission statements and division of responsibilities: Supervisory authorities should have well defined mission statements specifying their responsibilities and focusing on the protection of the participants' interests. Different financial supervisory agencies should cooperate, coordinate actions and share information.*

¹ This agreement, which also organises the transfer to IOPS of the leading role on supervisory issues, mentions in this respect that the standard-setting work on and related to pension supervision will first be initiated by the IOPS Technical Committee or one of its sub-groups and then shared with the OECD WPPP. The regulatory standard-setting work will be initiated by the OECD WPPP or one of its sub-groups and then shared with the IOPS Technical Committee. The co-operation may also include joint meetings.

² In this respect, one of the first decisions by the IOPS may be to seek to endorse the existing OECD core Principles in order to develop new standards in a compatible way with existing ones.

³ The work would also be expected to develop guidelines detailing the sixth OECD principle on supervision of private occupational pension plans

- *Political and institutional independence: Supervisory agencies should have institutional and political independence to perform their activities. IOPS recognises that supervisors from different nations will be subject to varying levels of autonomy, because of national differences which might be, for example, institutional, legal, cultural, historical, or political, in nature. For the purposes of its work IOPS understands political and institutional independence to mean that at the day to day operational and decision making level the supervisory agency has autonomous management of its activities. IOPS recognises that at a higher, more policy oriented level, supervisory agencies may be subject to national Governmental and political influences which may be outside of their control.*
- *Funding: Supervisory institutions should have stability at the top directorial level.*
- *Staffing: Supervisory institutions should have flexibility in human resources management and the capacity to offer good employment conditions compared with the private sector*
- *Governance of supervisory bodies and conflicts of interest: Principal-agent problems and conflicts of interest should be addressed. Well designed governing or consultative boards with external participation and the adoption of a conflicts of interest code may be a solution.*
- *Enforcement capacities: Supervisory agencies should be endowed with adequate power and the revision of their acts should only be via a judicial decision or some other equitable and fair appeals process.*
- *Accountability, reporting and disclosure: Supervisors should be supervised (variety of options: parliament, ministries, National Audit Office, pensions industry, general public).*

2. As well as these organizational issues, guidelines relating to the various supervisory tools or methods could also be developed. The development of additional guidelines, however, would probably require additional analytical work, as described in Section II. Previous INPRS work has already identified the following questions which could be addressed in order to develop guidelines in these areas:

- *Authorisation: how should the supervisory authority structure the process of assessing the compliance of pension plans and pension funds with minimum conditions for licensing or registration? What kinds of information should be provided to the supervisory authority in order for approval to be evaluated? What kinds of measures may be taken by the supervisors depending on the result of the examination (e.g. to give the licence, to refuse, to ask for modification)?*
- *Reporting / off-site supervision: what type of information should be provided to the supervisor, how frequently and in what manner (primary data of the reporting system)? What are the suitable data-processing methods to enable the supervisor to monitor the operation of pension funds and plans (secondary data of the monitoring system)? What are the main indicators and their limit values to be used in a warning system (that require automatically the supervisor to act)?*
- *On-site inspection: what type of inspections do the supervisory authorities carry out? What are the frequency and contents of a general (full-scale) audit? How are the topics of the issue examinations selected? What are the methods and consequences of the issue examinations? What are the reasons of the case inspections (indicators from the warning system, complaints of participants)? What are the process and consequences of the issue examinations?*
- *Sanctions, intervention, and other remedial actions: what type of sanctions should the supervisory authorities use for different infractions? Is there a need for standards to make the sanctioning system consistent? How should it be set up? What is the process of termination of the operation of pension plans and pension funds and what is the role of the supervisory authority? How thorough should be*

examinations carried out by the supervisory authority for the termination of pension plans and pension funds?

3. The IOPS Technical Committee will also be expected to co-operate closely⁴ with the OECD Working Party on private pensions (which is the standard-setting body for the regulation of private pensions) on the development of regulatory standards, principles, guidelines and good practices (this may for instance include funding, investment, governance, risk management, financial education).

4. To avoid duplication IOPS should look to the work of other international supervisory bodies, in particular the International Association of Insurance Supervisors (IAIS), where IOPS considers the work of the other supervisory bodies is relevant to the work of IOPS.

5. IOPS should focus its early work on essential first principles to create a common understanding of how its members approach their supervision role, the kinds of pension scheme/institution for occupational retirement provision they supervise, and what IOPS' goals and objectives should be. Once that common understanding has been established its later work can move into more technical areas.

6. IOPS should, in the process of standard setting for pension supervision, take account of the diversity of national pension systems and the different national traditions and cultures involved with pension regulation and supervision. Having regard to the different national traditions and cultures, IOPS should strive to ensure good practice is achieved and maintained with pension regulation and supervision. To this end IOPS might find it helpful to reach agreement about some general principles which might form the basis of good practice.

II. Information Gathering and Analytical Projects

A broad range of topics have been identified for information gathering and analysis by the IOPS. They would provide a demanding programme for some years to come. Initial topics could be selected from the following:

1. *Components of a risk-based approach to supervision:* The principle of risk-based supervision has been developed and considerably advanced in bank supervision over the past two decades. In this context it is primarily oriented toward the establishment of methods to assign coefficients to the financial risk associated with individual institutions primarily for purposes of adjusting capital and reserve requirements. The concepts are gradually being adapted to other types of financial intermediaries and extended to address operational as well as financial risks. In private pension supervision the principle of risk assessment has long been used to address the problem of making decision about how best to direct and deploy scarce resources because many pension supervisors, unlike those in other financial areas, oversee thousands of individual entities with a relatively small level of staffing and resources. The World Bank has initiated a study on these methods among several countries, and an IOPS project in this area could work in partnership with and extend this project, collecting specific information about risk-based methods from a broad sample of members. Initially, the focus of this project could be on the risk-based supervision of pension funding and investment (procedures for assessing compliance with rules related to funding, asset-liability matching, use of derivatives, investment mandates, and other investment regulations). It would also be useful to contrast the approach to risk-based supervision in a concentrated market structure versus a dispersed one. This project should be closely

⁴ See also the co-operative agreement between the IOPS and the OECD.

combined with project number 3, given that a risk based approach will identify key areas where supervisory resources should be directed.

2. *The development of outcome or results based measures of the effectiveness of supervision:* To the extent there has been prior work on pension supervision it has primarily been descriptive in nature, attempting to catalogue and categorize the programs and methods of supervisors. Although this can provide the foundation for some transfer of knowledge it does not fully support the development of good practices because it does not incorporate any objective or outcome based methods for evaluating the consequences of relative effectiveness of different supervisory programs or methods. The measures that are typically used are process or input based. They simply assess the number of actions taken, cases worked or sanction applied rather than the degree to which these contribute to the ultimate purpose of supervision, is to increase the security of private pensions. In addition very few of these measures lend themselves to consideration of the cost effectiveness of the supervisory programs which is a major issue in market oriented private pension systems. Many public institutions are explicitly moving toward results based measures for program evaluation and resource allocation. This work would assist supervisors in staying out in front of this trend. This project would attempt to formulate some outcome-oriented measures, drawing on existing experience where available, that could be used by supervisors to consider their programs and practices in a broader but ultimately more meaningful context, how effective they are at improving private pension security. This would support better consideration of cost effectiveness and ultimately the identification of good practices on a more object manner.
3. *Strategic Planning among Pension Supervisors:* Closely related to the issues above many supervisors have explicit requirements to engage in an annual strategic planning process in which they consider their goals and objectives for the period and how best to deploy the resources at their disposal to achieve these. Sound management would dictate that this sort of strategic evaluation and planning be undertaken at periodic intervals regardless of legal requirements to ensure that supervisors remain focused on their mission and are explicitly considering how effective their programs have been. This project would seek to identify a generic framework for strategic thinking and the issues specific to pension supervision to advance the development of the thinking in this area and to assist members in addressing what is typically a very difficult problem. A common framework developed through such an international body would provide a much stronger and more defensible foundation for individual members faced with the requirement to justify their programs, resource levels and management decisions. This project should be closely combined with project number 1, given that a risk based approach will identify key areas where supervisory resources should be directed.
4. *Documentation of Supervisory Methods:* Most supervisors now use manuals and procedures to develop and document their techniques and to ensure operational and policy consistency in the conduct of their activities. New supervisory agencies often engage in the time consuming process of developing these from scratch. Although every system is specific to the legal and cultural environment in which it operates as well as specific constraints such as staffing and resources the supervisor must face there are some common structure and elements to these types of manuals. This project would seek to utilize the expertise and experience of the staff of supervisors to develop a generic framework and perhaps some content for a set of operational manuals. This project could facilitate both cross border cooperation and commonality of approaches as well as be of immeasurable value to any newly established supervisors trying to establish their programs and procedures. This project may also be combined closely with project number 10, conducting a cross-country analysis of supervisory methods.
5. *Effective Use of Third Party Oversight:* Many private pension systems, due to both resource constraints but also to reduce compliance burdens, rely to a considerable degree on private third party methods of oversight. The most common of these is the requirement for an independent audit of the financial books and records. Others have begun to extend this into the conduct of compliance audits or

requirements for various forms of compliance committees and officers to have an active role in fund management. This item of a work program would seek to collect information about the manner and extent to which these third party based methods are in use and to undertake some initial assessment of whether any approaches can be deemed to have been more or less cost effective. Cross country experience and comparison, if properly interpreted, can provide very useful insights into the potential and pitfalls of this approach to monitoring and compliance enforcement.

6. *Approaches to securing compliance without imposing legal sanctions:* supervisors can often find it cheaper, quicker and more effective to secure compliance through dialogue and consultation with the entities they supervise, leaving legal sanctions as a last resort or to be applied only to the most serious forms of non-compliance such as those involving criminal intent. They may even allow entities to come forward voluntarily where there has been inadvertent failure to comply with rules or standards, with a promise that sanctions will not apply so long as compliance is secured in a timely manner. This approach does, however, expose supervisors to the risk of criticism if its application is not perceived to be even-handed or a compliance failure subsequently causes a serious problem. And it may reduce the incentive to comply. The underlying policy design therefore requires considerable care and thought and a balance between expedience and incentives. The project would examine how different supervisors formulate such approaches and the safeguards they deploy so as to identify and share good practice, while recognising that different supervisory approaches are appropriate to different circumstances. Given the sensitivity of the subject matter, some information might need to be collected confidentially and some findings anonymised.
7. *Education, Outreach and Communication by Supervisors:* Pension supervisors are increasingly being called on to not only perform compliance enforcement function but also to serve as the focal point for educating practitioners in the field about the requirements of the law. This represents perhaps the most important type of program result because it conceivably prevents any deviation from the requirement of the law from occurring in the first place, presuming that ignorance rather than intent is often the cause of compliance issues. This type of project would collect information about the purposes, structure and operation of these types of programs with the goal of developing some principles of good practices in this area. This project would also be developed in close co-operation with the World Bank distance learning programme. This too is a program which has an element of mutual recognition. Not all supervisors see it as part of their function to educate and inform, but some do. This should present an opportunity for IOPS to understand how those supervisors who do see education and information as part of their role carry out that role. Supervisors should be able to consider the relative costs and benefits of an educative and informative approach to supervision, without feeling under any pressure to adopt those working methods if they consider they are inappropriate for their own country.
8. *Training of Trustees and Fiduciary/Prudential standards education:* A distinctive subset of outreach and education program are those very specifically directed to the training of practitioners in the role and responsibilities of the Trustees/ Directors, Fiduciaries or other formal designations that are the individuals formally responsible for the administration of the private pension funds. The IOPS could undertake a narrowly focused version of this type of project.
9. *Analysis of supervisory structures:* The OECD's survey of good practice in pension supervision (DAFFE/AS/PESN/WD (2002)26) identified the following structures of supervision: integrated; partial; specialized. One suggested topic of future work suggested by this survey, for which IOPS would be the most appropriate vehicle, was an analysis of these different models, highlighting the potential up and downsides of each. For example the following were suggested as possible advantages of the integrated approach: efficiency (especially as financial conglomerates become more important); overlapping products driving need for comprehensive approach; the elimination of loopholes between sectors; improved information flows; economies of scale; transparency, accountability, increased power. Meanwhile, specialized agencies were seen as offering the following benefits: pensions still

specialized area with unique risks; political (too much power in the hands of one agency not advantageous); efficiency, flexibility (integrated agencies too bureaucratic and slow to respond); public has more confidence in specialist; good coordination can achieve flows of information just as successfully.

10. *Analysis of supervisory methods*: This project would conduct a cross-country analysis of supervisory methods, expanding the current database. This comparative analysis would provide the background for the development of documentation of supervisory methods mentioned in item 7. The project may also be combined closely with project number 4, documenting supervisory methods.
11. *Cross-border supervision*: The IOPS could analyse the role of supervisors in the context of multinational pensions and international pension entitlement and to suggest good practices in this field. This project would play an important role in the development of the international co-operation on pensions supervision. This project will draw on recent work in the EU.
12. *Role of supervisors in participation and individual choice*: A project on this subject could evaluate the role of supervisors in easing members' decisions in private pension systems. In addition to case studies, highlighting the experience of individual IOPS members, the project would aim at developing good practices on the supervisors' role. This could include functions such as provision of comparable fee and performance tables, making available basic information about financial issues through brochures and the internet, etc.
13. *Utilization of IT technology in off-site supervision*: In accordance with the pervasive utilization of the IT technology within the financial sector, some countries have established daily e-monitoring and e-supervision mechanism for the effective and efficient supervision of pension funds and pension fund managing companies. Such technology can be very effective at detecting problems and assisting supervisors in providing solutions regarding the functioning of the private pension system.
14. *Supervisory issues specific to personal pension plans*: In some countries pension funds and pension fund managing companies are the main financing vehicles and providers, respectively, of personal pension plans. This project would focus on the special features of supervision that are required to ensure a successful development of this system.

III. International Cooperation

Though establishing its own programme of work, the IOPS will continue its close collaboration with the OECD's Working Party on Private Pensions (WPPP), consistent with the IOPS's cooperation agreement with the OECD (which involves cooperation on standard setting activities and the two bodies consulting with each other, informing and sharing of work projects, questionnaires, surveys, meetings etc.). This co-operation will include the OECD outreach activities organised on pensions issues. Both bodies will also have to discuss the future of some INPRS activities which have not been transferred yet to the IOPS. The IOPS will also work very closely with the World Bank especially for issues related to technical assistance. IOPS will also seek as many opportunities as possible to coordinate its work with other international organizations such as AIOS, CEIOPS, ISSA, IAIS and IOSCO. Further more the organization places a high priority on constructive interaction and engagement with private sector entities of all types (financial, administrative, legal and others) that are engaged in the business of private pensions to provide a forum for communication, cooperation and coordination between the public and private sectors.

The co-ordination agreement between the OECD and the IOPS highlights the following outstanding OECD projects to which the IOPS will contribute:

- *The Parties will co-ordinate in the field of database building. The institutions agree to update, modify and expand a comparative survey on private pension regulation and supervision in both OECD and IOPS countries.*
- *The parties will also endeavour to further develop the OECD Global Pension Statistics Project which currently includes the following elements; revision and extension of the OECD taxonomy and glossary; development of a common survey instrument for OECD countries; collection and analysis of statistical data on private pensions for the OECD countries; building of related databases and the development of methodologies for distributing the data and other work product from the project.*

In addition, the IOPS should undertake to expand the OECD's survey of pension supervisory structures (via the questionnaire DAFPE/AS/PEN/WD (2002)26). This survey currently incorporates the supervisory structures of 19 countries (Australia, Canada, Czech Republic, Denmark, Germany, Hungary, Iceland, Ireland, Italy, Japan, Mexico, the Netherlands, New Zealand, Poland, Portugal, Spain, Sweden, Turkey and the United Kingdom). An analysis of supervisory methods, however, extends to only 5 countries (Australia, Ireland, Hungary, Mexico and the United States). The international members of the IOPS can clearly expand the coverage and analysis of this survey further.

The IOPS will seek develop further co-operation with the World Bank on technical assistance programmes

The IOPS can play a central role in assisting the World Bank and the International Monetary Fund in assessing the implementation of the 15 principles as part of the Financial Sector Assessment Programme (<http://www.imf.org/external/np/fsap/fsap.asp>).

The IOPS may in future develop an electronic database of pension supervision, to compliment to comparative survey of private pension regulation and supervision produced by the OECD/ ISSA / INPRS.

The IOPS should also seek to make public the results of its analysis through its website (initially, this can be hosted at www.inprs.org), meetings, and publications. The preparation of some documents may also require consultations with private sector representatives.

IV. Provisions of training and technical assistance

The IOPS intends to be engaged in the provision of training and technical assistance to countries in an early stage of private pension development. The organization intends to serve as a source of accumulated knowledge and expertise and to make such information available to organizations establishing new pensions supervision arrangements. This work will be undertaken where possible with other international bodies working in a similar field. To initiate this project during 2005, IOPS will elaborate a framework and policy procedure for peer contacts and other means of facilitating such a cross transfer of knowledge.