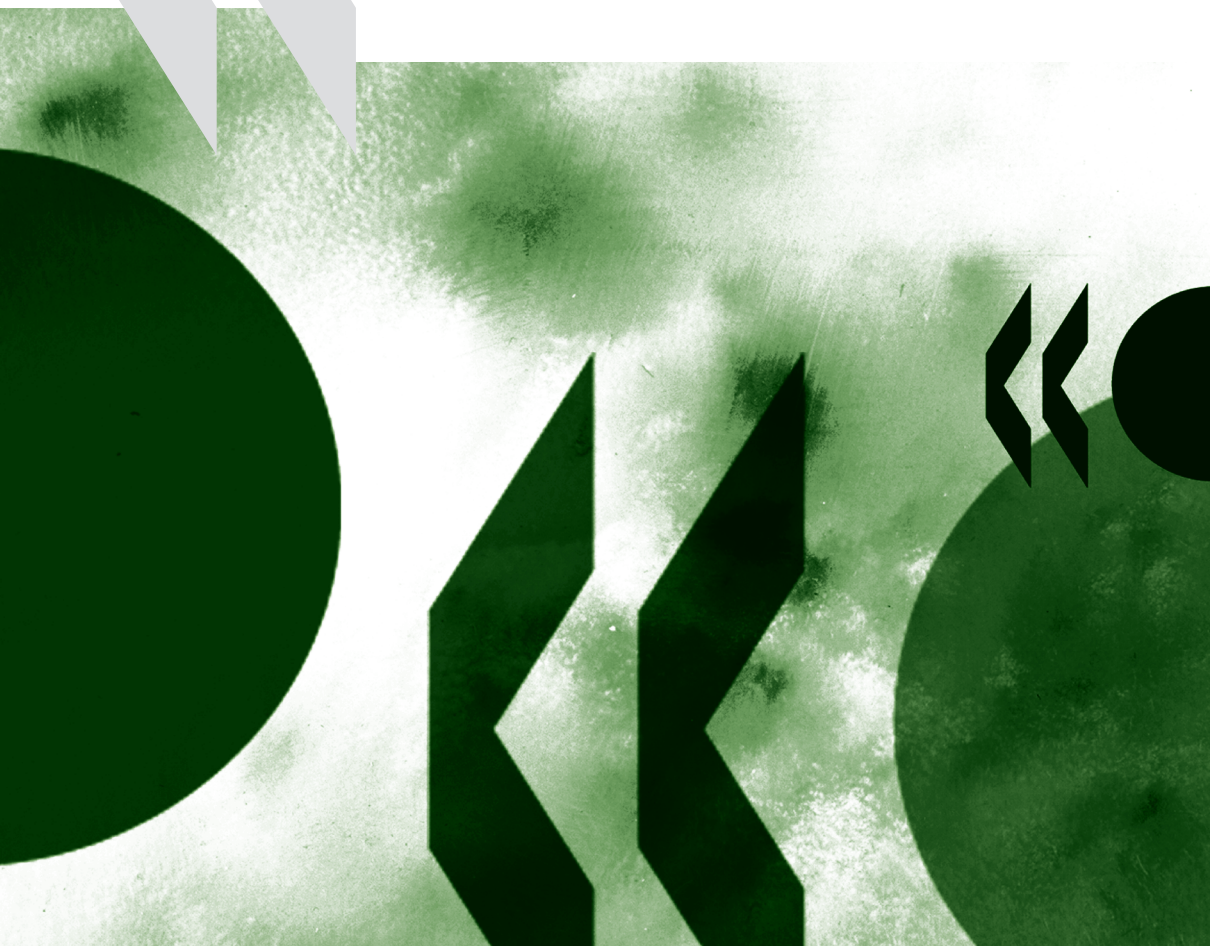
OECD Principles of Occupational Pension Regulation

METHODOLOGY FOR ASSESSMENT AND IMPLEMENTATION



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Foreword

Occupational pensions play a major role in OECD countries and worldwide, complementing retirement income from state sources. At the end of 2009, private pension savings reached USD 25 trillion. Population ageing has led many OECD countries to undertake a wide range of pension reforms – the overall effect of which has been to reduce public pension promises and, in turn, to increase the importance of private pension savings for retirement.

Efficient regulation, strong governance and oversight of pension schemes are needed to ensure that today's employees will enjoy secure and adequate retirement pensions tomorrow. OECD governments have agreed on seven Core Principles of Occupational Pension Regulation to assist in meeting this objective. The Core Principles were originally developed by the OECD's Working Party on Private Pensions and were approved by the OECD Council in June 2009.

The Methodology for Assessment and Implementation provides a structured approach for evaluating a jurisdiction's regulatory system for private pensions in relation to the Core Principles. The purpose of the Methodology is to provide guidance in the development of future policy. It was originally designed in 2008 as the primary tool for the examination of the private pension systems of candidate countries for Accession to the OECD as well as a tool for regulators, government officials and stakeholders to help in other assessment processes.

The Core Principles cover seven key areas:

- Conditions for effective regulation and supervision;
- Establishment of pension plans, pension funds, and pension fund managing companies;
- Pension plan liabilities, funding rules, winding up, and insurance;
- Asset management;
- Rights of members and beneficiaries and adequacy of benefits;

- Governance; and
- Supervision (developed in cooperation with the Internal Organisation of Pension Supervisors).

The ultimate goal of the Core Principles is to promote the sound operation of private pension plans, pension funds, and pension entities. The Methodology is intended to help identify specific strengths and weaknesses of countries' private pensions systems in relation to the Core Principles, to identify reform priorities and to ultimately improve the performance of private pensions in delivering income and security to pensioners. The Methodology is a tool to help regulators, government officials and stakeholders make practical decisions in order to implement the Core Principles in day-to-day practice.

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Executive Summary

The OECD Consolidated Core Principles of Occupational Pension Regulation (the "Core Principles") present the key principles and recommendations that should guide the regulation of privately managed occupational pension systems. The ultimate goal of the Core Principles is to promote the sound operation of private pension plans, pension funds, and pension entities as a means of providing income in retirement to plan members and to promote the security of pension benefits.

The Methodology presented in this paper is intended to provide a structured approach for evaluating a jurisdiction's occupational pension regulatory system in relation to the Core Principles. The Methodology may also be used for evaluating personal pension plans that are secured via pension funds. All Core Principles, with the exception of most of Core Principle #3, can be applied to such arrangements.

The Core Principles of Private Pension Supervision as published by the International Organisation of Pension Supervisors (IOPS) are presented in Section 7 of this Methodology and are intended to be used to evaluate the supervision of a jurisdictions private pensions.

This Methodology is intended as the primary tool for the examination of the private pension systems of the candidate countries for Accession to the OECD. This Methodology is also intended as a tool for regulators, government representatives and OECD officials to help in other assessment processes. Assessments can be complemented with a review of a jurisdiction's supervisory framework, following the International Organisation for Pension Supervisors' "IOPS Principles of Private Pension Supervision".

This Methodology is intended to provide guidance in the development of future policy in the arena of private pensions.

The structure of this methodology

The Methodology that is presented in this report is structured into the following main sections:

- I. Introduction
- II. Country Background and National Regulatory Framework
- III. Core Principles
- IV. Overall Assessment
- Appendix I and II

Section I titled *I. Introduction* describes the purpose of the Methodology, the general approach and grading system to be used in performing an evaluation of a jurisdiction's private pension system, and the suggested reporting format for the outcome of such an evaluation.

Section II titled *II. Country Background and National Regulatory Framework* deals with the various regulations, practices and structural information that is necessary for putting the assessment into a national/jurisdictional context.

Section III titled *III. Core Principles* deals with each of the OECD Principles (one chapter for each Core Principle). The treatment of each chapter of the Core Principles follows a common pattern and comprises of two main sections: an *Introduction* and an *Implementing Guidelines and Commentary* section.

The *Introduction* portion of Section III discusses the general understanding of the overarching principle that opens each chapter of this section. Building on the annotations to the Core Principle under consideration, the introduction also discusses special concerns and aspects that are intended to be taken into account when considering implementation of the respective principle.

The *Implementing Guidelines and Commentary* portion of Section III states the Implementing Guidelines associated with each Core Principle. To clarify how a jurisdiction's practices can be assessed against the Core Principles and their associated Implementing Guidelines, there is additional commentary which describes the purpose and meaning of the respective principle and guidelines in more detail.

Section IV titled *IV. Overall Assessment* deals with how all the Principles and associated assessments should be drawn together in a final assessment, including a discussion of policy priorities and specific measures

that might be considered. The assessment would cover not just the assessed strengths and weaknesses of individual principles but also indicate how they serve to determine the operation and efficiency of the overall regulatory system of private pensions. In discussing policy priorities, the assessment also needs to consider the presence of interrelationships whereby some policy measures might be ineffective until accompanied by other initiatives, either by pension entities or by the authorities.

Appendix I contains a list of questions to aid the reviewer in the assessment process. The purpose of the questions is to gather relevant information and background material in order to be able to form a comprehensive understanding of the pension system in the jurisdiction to be assessed.

Appendix II contains a list of questions specifically designed to aid the reviewer in the assessment of a jurisdiction's supervision of its private pension system. This questionnaire has been designed by the IOPS.

I. Introduction

The Core Principles provide the fundamental framework and guidance for the regulation of privately managed occupational pension systems. The purpose of the Methodology presented in this paper is to provide a structured approach to the assessment of a jurisdiction's private pension system in relation to the Core Principles.

Originally, the Core Principles were primarily designed for occupational pension arrangements. However, the Core Principles – with the exception of most Core Principle #3 - are also applicable to personal pension plans secured via pension funds. Therefore, references in the Core Principles or the Methodology to "occupational pensions" may also be considered in the context of personal pension plans should they be relevant in the jurisdiction under assessment.

The use and scope of this methodology

The Methodology is intended to underpin an assessment of the implementation of the Core Principles in a jurisdiction and to provide a framework for policy discussions. The ultimate purpose of an assessment is to identify the nature and extent of specific strengths and weaknesses in private pensions systems, and thereby, underpin policy dialogue that will identify reform priorities leading to the improvement of private pensions governance, regulation and supervision.

This Methodology emphasises "functional equivalence". Functional equivalence means that there are many different ways, institutions, laws, etc, for achieving the outcomes that are advocated by the Core Principles and, as such, implementation of the Core Principles needs to be adapted to national circumstances. It is important to note that the criteria to judge whether a principle has been implemented that are presented in this Methodology are intended to evaluate the effectiveness and efficiency of current arrangements in terms of achieving desirable outcomes, rather than solely to evaluate the laws that may be in place.

The approach of the Methodology to making an assessment is principally qualitative. As such, the assessment cannot be reduced to a quantitative score or set of quantitative scores; however certain quantitative measures may be taken into account. The Methodology does not make use of indicators based on the number of "yes" and "no" answers for the reason that the importance of some responses will be quite different across countries.

The Methodology calls for an approach where a qualitative assessment of the private pensions system in a jurisdiction is first evaluated in relation to each of the Core Principles in isolation based on a rating system which is described in the section below. After the individual Core Principles evaluations have been made, a final holistic evaluation should be presented that takes into account the private pensions system as a whole in relation to all the Core Principles.

The grading structure

The Core Principles have associated Implementing Guidelines which go into deeper detail than the overarching Core Principle. The Methodology focuses on the Implementing Guidelines since they better reflect the operational outcomes that are regarded as important for the overarching Core Principle. Where the reviewer considers it important to form a judgement about a specific Core Principle as a whole, in the absence of good arguments to the contrary, the overall judgement should reflect the weakest Implementing Guideline.

As an aid to the assessor in their evaluation, the Core Principles and their Implementing Guidelines are accompanied by commentary. The purpose of the commentary is to provide clarification. They are also intended to make the evaluation of a jurisdiction's private pension system more specific and easier to verify by a reviewer for effective evaluation of implementation, while preserving functional equivalence. The commentary also provides important guidance for detailed fact finding questions and how responses can be used to form a judgement. However, the commentary is an aid to making an assessment and is not a substitute for the Core Principles, the Implementing Guidelines or for a careful judgement about actual outcomes.

To aid the process of assessment, the Methodology follows an assessment scale similar to that used by the other international standard setters, which classify according to the following:

- Fully implemented
- Broadly implemented
- Party implemented
- Not implemented
- Not applicable

Table 1. **Summary of Assessment Scheme**

Assessment Scheme	Summary
Fully Implemented	The OECD Principle is fully implemented in all material respects with respect to all of the applicable Implementing Guidelines. Where the Implementing Guidelines refer to standards (i.e. practices that should be required, encouraged or, conversely, prohibited or discouraged), all material aspects of the standards are present. Where the Implementing Guidelines refer to practices, the relevant practices are widespread. Where the Implementing Guidelines refer to enforcement mechanisms, there are adequate, effective enforcement mechanisms. Where the Implementing Guidelines refer to remedies, there are adequate, effective and accessible remedies.
Broadly Implemented	A Broadly Implemented assessment is likely appropriate where one or more of the applicable Implementing Guidelines are less than fully implemented in all material respects, but, at a minimum: • All of the applicable Implementing Guidelines are implemented to some extent; • The core elements of the standards are present (*e.g.* general standards may be in place although some of the specific details may be missing); and • Incentives and/or disciplinary forces are operating with some effect to encourage at least a majority of market participants, including significant enterprises, to adopt the recommended practices.

Partly Implemented	A Partly Implemented assessment is likely appropriate in the following situations: • One or more core elements of the standards described in a minority of the applicable Implementing Guidelines are missing, but the other applicable Implementing Guidelines are fully or broadly implemented in all material respects (including those aspects of the Implementing Guidelines relating to governance practices, enforcement mechanisms and remedies); • The core elements of the standards described in all of the applicable Implementing Guidelines are present, but incentives and/or disciplinary forces are not operating effectively to encourage at least a significant minority of market participants to adopt the recommended practices; or, • The core elements of the standards described in all of the applicable Implementing Guidelines are present, but implementation levels are low because some or all of the standards are new, it is too early to expect high levels of implementation and it appears that the reason for low implementation levels is the newness of the standards (rather than other factors, such as low incentives to adopt the standards).
Not Implemented	A Not Implemented assessment is likely appropriate where there are major shortcomings, for instance, where: • The core elements of the standards described in a majority of the applicable Implementing Guidelines are not present; and/or, • Incentives and/or disciplinary forces are not operating effectively to encourage at least a significant minority of market participants to adopt the recommended practices.
Not Applicable	This assessment is appropriate where an OECD Principle (or one of the Implementing Guidelines) does not apply due to structural, legal or institutional features (*e.g.* defined benefit plans may not exist in a particular jurisdiction).

The reviewer and the assessment process

The process of assessing each of the Core Principles requires a judgemental weighting of numerous elements that only qualified assessors with practical experience can provide. Many reviewers of standards seek to ensure both this and inter-jurisdictional consistency by including in their teams members with broad international experience. Under all circumstances, in-depth consultations with individuals and constituencies having first-hand experience of the assessed jurisdiction is an absolute necessity and may, in addition to relevant authorities, include auditors, trustees, employers, actuaries, researchers, *etc.*

The reporting format for an assessment using this methodology

A formal assessment of a jurisdiction's private pensions system may be most appropriately served by a written report. However, depending on the intended use of the assessment, the format is open to the choice of the user of the Methodology. Note that any formal assessment in the form of a written report should, at a minimum, include a short executive summary followed by a summary of key findings and recommendations. The main body of the accompanying documentation should also include a table summarising the assessments of each Core Principle and Implementing Guideline. The report should also include a holistic evaluation of the private pensions system taking into account all the Core Principles.

It is important to note that specific formats may be required if the assessment is for certain specific purposes.

Limitations of an assessment

Even if a jurisdiction might be implementing the individual principles or the Core Principles as a whole, there may be considerable room for improvement. The Core Principles are not intended to substitute for government, quasi-governmental or private initiatives to develop more detailed "best practices" in the regulation and supervision of private pensions, but are meant to provide guidance and a framework around which pensions legislation can be structured. Government, quasi-governmental or private initiatives might be especially important in those jurisdictions there is significant variation in pension practices and where focusing this distribution could improve overall performance and security. These issues are not covered explicitly by the Methodology although they should form an important component of policy dialogue.

II. Country Background and National Regulatory Framework

This section outlines the type of information that a reviewer will need to form an assessment about the importance of individual principles for the private pensions regulatory framework in a jurisdiction and in forming questions relevant for a judgement about the associated Implementing Guidelines.

Appendix I to this paper presents a list of questions to be asked in order to gather relevant information and background material in order to be able to form a comprehensive understanding of the pension system in light of an evaluation. The questions cover the following 4 main topics:

- *The Structure and Operation of the Pension System:* It is important for the reviewer to have an understanding of the overall structure and operation of the pensions in the jurisdiction under question. It is essential to have an understanding of both private pensions and state-provided pensions in a jurisdiction and their relative importance as income during retirement. The reviewer must not only understand what is "market practice" in the jurisdiction under question, but also the historical and national context under which market practice and the regulatory environment with respect to pensions has developed. This includes an understanding of past crises and scandals that have helped shape the pensions environment in the jurisdiction.

- *The Regulatory and Supervisory Framework:* The reviewer must have an understanding of the jurisdiction's current regulatory and supervisory framework in order to make a judgement on where the jurisdiction's private pensions regulation currently stands in relation to the Core Principles.

- *Pensions Statistics:* Statistical information as to the prevalence of different types of private pension plans and coverage will prove helpful to the reviewer. The reviewer should also know the prevalence of different types of pensions plans (for example, the percentage of pension plans that are defined contribution in nature) and the prevalence and size of various forms of pension plan financing.

- *Additional Information:* Other information that could be helpful to the reviewer would be copies similar reviews that may have been performed in the past by, for instance, the World Bank, the International Monetary Fund, the International Association of Insurance Supervisors and the International Organisation for Pension Supervisors.

III. Core Principles

This section presents the Core Principles, Implementing Guidelines and commentary against which a jurisdiction's private pension system will be assessed. [1]

Section III of this Methodology is structured into chapters – one for each of the Core Principles. Each of the chapters is divided into an introductory section and a section devoted to the Implementing Guidelines and the commentary.

The *Introduction* portion of each chapter discusses the general understanding of the overarching Core Principle that opens each chapter. The introduction discusses the special concerns and aspects that are intended to be taken into account when considering implementation of the principle.

The main section of each chapter is the *Implementing Guidelines and Commentary*. This section lists the Implementing Guidelines associated with each Core Principle. Under the Implementing Guidelines, there is brief commentary to provide clarification. The commentary is intended to provide deeper explanation and, in some cases, briefly discusses the actual situations and practices that might confront a reviewer in relation to the principle under consideration. Guidance is given as to how actual situations might be assessed against the outcome recommended by the Core Principle or Implementing Guideline under question.

1. In EU countries, Core Principles 2 to 7 may not apply to those occupational private pension plans, pension funds and pension entities that fall outside the scope of the Directive 2003/41/EC of the European Parliament and of the Council of 3 June 2003 on the Activities and Supervision of Institutions for Occupational Retirement Provision. The Core Principles also do not cover insurance contracts as such (although they may be used in both occupational and personal pension plans). The International Association of Insurance Supervisors has developed principles for the supervision of insurance *('Insurance Core Principles and Methodology').*

Core Principle 1:
Conditions for effective regulation and supervision

An adequate regulatory framework for private pensions should be enforced in a comprehensive, dynamic and flexible way (taking into account the complexity of the schemes) in order to ensure the protection of pensions plan members and beneficiaries, the soundness of pensions plans and funds and the stability of the economy as a whole. This framework should however not provide excessive burden on pensions markets, institutions, or employers.

A productive, diversified investment of retirement savings which spreads risk requires well-functioning capital markets and financial institutions. The development of advance-funded pension systems should go hand-in-hand with a strengthening of the financial market infrastructure and regulatory framework (including the development of new financial instruments and new markets such as inflation-indexed markets and the improved functioning of retirement annuity markets).

Regulation should promote a level playing field between the different operators and take account of the usefulness of a functional approach. The fair competition should benefit to the consumers and allow for the development of adequate private pensions markets.

1.1. Introduction

Successful implementation of the Core Principles depends upon the existence of an institutional framework that ensures the adequacy of the legal provisions in a changing environment of occupational pension provision. The legal provisions need to take into account external factors, such as the tax treatment of occupational pensions, the role of public pension plans, and labour market regulations. These aspects of the first Core Principle focuses on an overall assessment of the pensions system and should be given primary weight in the holistic review described in Section IV of this Methodology.

The ultimate goal of pension regulation and supervision is to protect the rights of plan members and beneficiaries. The regulation pertaining to occupational pensions should be flexible enough to allow their efficient operation. Also, they should not place an excessive administrative burden on pension plan sponsors nor require pension sponsors to bear undue costs and risks.

1.2. Implementing guidelines of Core Principle 1 and commentary

1.1	Occupational pensions are subject to a set of legal provisions that regulate the main aspects of the operation of those plans.
	Additional Comments on Implementing Guidelines The legal provisions should be assessed in their overall effectiveness and practicality in promoting sound, effective and well-run pension plans. The body of legal provisions includes laws, regulations, decrees and other requirements and guidance issued by regulatory and supervisory authorities. This official framework is usually complemented with a set of industry best practices and other forms of self-regulation by the industry.
1.2	The legal provisions promote the protection of pensions plan members and beneficiaries and the soundness of pension funds.
	Additional Comments on Implementing Guidelines The twin goals of protecting the rights of plan members and the soundness of pension funds should be reflected in the relevant law. The implementation of these goals is carried out through regulations consistent with the rest of the Core Principles.
1.3	The legal provisions provide the necessary flexibility in order to permit the efficient operation of occupational pension plans.
	Additional Comments on Implementing Guidelines The principle advocates that the authorities consider the costs and benefits of proposed and current legal and regulatory measures. An assessment of the individual Core Principles needs to consider the efficiency of the regulatory and legal requirements and their impact on incentives for plan sponsors and plan members.
1.4	The legal system allows the enforcement of financial contracts pertaining to occupational pensions. In particular, there is a body of ethical, professional and trained lawyers and judges, and a court system, whose decisions are enforceable. Comparable standards apply in cases where alternative dispute mechanisms exist.
	Additional Comments on Implementing Guidelines The legal system should be instrumental in protecting the integrity of pension plan promises. Individual members should have legal redress and protection from the breach of fiduciary obligations or pension fund misappropriation (See Core Principle #5). Such rights need to be enshrined in relevant legislation. Mechanisms for the exercise of such rights may vary across countries. In some countries, the supervisory authority may play the role of arbitrator in any disputes between members and plan sponsors or providers. In other countries, litigation via the courts may be more commonly used.

1.5	Accounting standards for plan sponsors of occupational pensions are comprehensive, documented, transparent and consistent with international standards.
	Additional Comments on Implementing Guidelines Examples of internationally used pension accounting standards are International Accounting Standard No. 19 (IAS 19), the United States' Financial Accounting Standard No. 158 (FAS 158) and the United Kingdom's Financial Reporting Standard No. 17 (FRS 17).
1.6	The legal provisions take into account the state of development of financial markets.
	Additional Comments on Implementing Guidelines The implementation of the occupational pension core principles assumes the existence of a properly functioning financial sector. Occupational pension provision relies on a variety of financial institutions and other service providers. It may involve the management of investment and actuarial risks through funding vehicles that operate in the financial system. Hence, well-regulated and supervised financial systems are an essential complement to pension-related legal provisions. Pension regulators and supervisors also rely on other financial sector regulators and supervisors to perform their functions and meet their objectives effectively. The operation of occupational pension plans also assumes the existence of liquid financial markets that offer securities suitable for long-term investment.
1.7	The legal provisions encourage efficiency in pension provision.
	Additional Comments on Implementing Guidelines Implementation of the occupational pension core principles also requires policies aimed at ensuring a level playing field between different private pension providers. Competition policy can play a key role in ensuring that plan sponsors and members have adequate choice in a robustly competitive environment that engenders price and product competition. The goal of competition needs to be carefully applied to mandatory and collectively bargained systems as such systems rely on mandatory membership or automatic enrolment to a particular pension arrangement in order to achieve efficient forms of risk sharing and cost management. Regulations should seek to promote an efficient scale of operation of pension funds and a competitive market of service providers via a transparent disclosure of fund's costs and investment performance.

Core Principle 2:
Establishment of pension plans, pension funds, and pension fund managing companies.

An institutional and functional system of adequate legal, accounting, technical, financial, and managerial criteria should apply to pension funds and plans, jointly or separately, but without excessive administrative burden. The pension fund must be legally separated from the sponsor (or at least such separation must be irrevocably guaranteed through appropriate mechanisms).

2.1. Introduction

The establishment of pension plans, funds, and entities is normally carried out in the context of pension tax, or other legislation that stipulates certain features that plans, funds and entities must have. While basic standards for the establishment of occupational pension plans can be identified, countries vary in the type of funding vehicles permitted, the type of autonomous pension fund, and the legal form of the pension entity.

The choice of funding vehicle depends on the legal framework of the country as well as the objectives of the pension plan and the role and responsibilities of the plan sponsor. If the plan sponsor decides or is required to establish an autonomous pension fund as an independent legal entity with legal capacity (that is, as a pension entity) to segregate the pension assets, the function of these entities needs to be defined. The pension entity is normally responsible for the management of the pension fund and other aspects of the administration of a pension plan. In such cases, legal provisions are required to encourage the investment of the pension fund in a prudent way and that the pension entity has governance mechanisms in place to ensure an effective control of decision-making processes. Legal provisions are also needed to define the type of legal form of pension entities that should be permitted. Plan members may have either a legal or a beneficial ownership right over the pension fund, or a contractual claim against the pension entity with respect to their rights to the pension assets.

The main alternative to setting up the pension fund as a pension entity is to deposit the contributions in a legally separate account or pool of assets of a financial institution or a dedicated provider (pension fund managing

companies) where they are invested with the objective of funding the retirement benefits of the plan members and beneficiaries. The pension provider would then be considered the pension entity.

The licensing of pension entities should be an integral part of principles-based regulation of the provision and management of private pension systems. An effective licensing process contributes to the establishment of appropriate governance structures and mechanisms for pension plans. It also strengthens confidence in the pension system and its supervisory system, and promotes the development of a pension market, while avoiding the creation of inappropriate barriers to market access. Licensing requires applicant pension entities to demonstrate they have in place the policies and procedures that are consistent with a system that seeks to ensure that benefits are delivered to plan members as provided under the terms of the plan and consistent with the pension laws of the country.

In some countries, where a full licensing regime as described in these guidelines is not applied to the start of operation of a pension entity, licensing may be restricted only to the authorisation given for purposes of beneficial tax treatment. Other than that, the establishment of a pension entity may require only the submission of certain documents to the relevant authority and the registration of the pension entity and/or pension pln. As such, the registration of pension entities and/or plans does not require the supervisor to conduct an approval process with respect to the guidelines. This alternative to a full licensing process as defined in these guidelines may be deemed appropriate given the country's general legal system, the existing oversight of financial institutions involved in pension plan/fund management and the goal of facilitating the establishment of pension plans in the country. In countries applying this approach, it is critical that a well-developed and effective ongoing legal regime be in place (including remedies for wrongdoing by pension entities) in order to promote a similar level of protection of pension funds and/or plans as the one that can be achieved through the implementation of the advance approval standards in these guidelines.

Similarly, the requirements for good governance that are required as conditions of licensing need to be established in these alternative licensing approaches by means of legislation and guidance that place duties on those charged with running the pension entities. In particular, the legislation should require pension entities to have similar controls and documentation in place as would be required for licensing purposes in a licensing regime, albeit that registration need to be contingent on the provision of such information by the pension entity. The legislation should also permit affected members to inquire and/or complain about actions or decisions that adversely affect them, and the supervisory authority to investigate breaches

of those requirements that would apply in a licensing regime. A critical foundation to this is that the legal system be sufficiently developed so that imposition of those requirements by legislation is reasonably expected to be effective at producing general compliance.

To the extent that financial institutions are capacitated to perform the functions of pension fund administration and management, the licensing process should be limited to the verification of those requirements that have not already been covered by the financial institution's other supervisor(s). Examples of matters that may only apply to the extent that they have not already been covered by a financial institution's other supervisor(s) might be those relating to capital, governance and governing documents, and business planning.

To the extent that an applicant for a license has not yet commenced operating, some specific requirements may not be in place at the point of application for a license. Examples may include risk control and internal reporting and audit mechanisms, and statements of investment policy. In such cases, preparations to establish the relevant procedures or policies should be evidenced and capable of review by the licensing authority.

2.2. Implementing guidelines of Core Principle 2 and commentary[2]

Legal provisions on licensing

2.1	Legal provisions are in place requiring the licensing of pension entities (and where relevant, pension plans) by the relevant authorities.
	Additional Comments on Implementing Guidelines The legal provisions in place for the licensing of pension entities should call for an orderly, documented and supervised process. Pension entities that apply for licensing should have to present evidence as to their readiness for legal compliance, provide evidence of initial capital where appropriate, resources, and expertise. The pension entity should also demonstrate that the appropriate governance structure is in place and that their administrative systems are functional and established. The authorities that regulate the licensing process should be an independent body that has the legal authority to inspect the pension entities at the time of licensing, as well as the ability to conduct meaningful follow-up reviews. The licensing authorities should have the authority to suspend or revoke a pension entities license in the case of serious irregularities, if any licensing requirements are not met, or in the case of serious infringement of the law.

2. These Guidelines were developed jointly by the OECD and the IOPS.

2.2	Legal provisions are in place regarding the type of pension plans and/or pension funds that can be established and the legal form of pension entities.
	Additional Comments on Implementing Guidelines Legal provisions indicate the type of pension plans or funds that can be established (for example defined benefit (DB), mixed, hybrid or defined contribution (DC) plans) and the legal form of pension entities (for example trustee, foundation, non-profit association, joint-stock corporation, limited liability company). The legal, ownership and organizational structure of pension entities should be clearly laid out by the law. The question as to what type of organization can be a pension entity should be addressed: Can a pension entity be formed by individual corporations, trade unions, industry-wide groups, financial service providers? Should pension entities be exclusively dedicated to pension funds or may they provide other services?

Governing documents

2.3	Pension plans or/and pension entities should have formal, written charters or documents describing the plan's/entity's objectives and the plan's parameters (such as types of contributions and benefits), its governance structure and outsourcing or third party service provisions, and the rights of members and other beneficiaries.
	Additional Comments on Implementing Guidelines The plan document should describe at least the following aspects: • The pension plan's objectives and parameters (*e.g.* contributions, benefits, guarantees, accrual rules, benefits upon leaving service, *etc.*); • The identification of the plan sponsor and its main responsibilities; • The identification of the governing body and its main responsibilities, where relevant; • The type of funding vehicle (a pension fund, insurance policy, *etc.*), the type of pension fund (autonomous or non-autonomous, and if autonomous, whether it is a pension entity or a pool of assets or separate account managed by a financial institution); • The conditions for membership in the plan; and • Dispute resolution procedures for members and beneficiaries. The plan document should be available to all plan members. The pension entity's or pension plan's governing documents can be the charter, articles of incorporation, articles of association, trust deed, the entity's statutes or the plan rules, depending on the relevant legal provisions and the legal form of the pension entity.

	The governing document should specify that the main objective of the pension entity and the pension plan is to be a secure source of retirement income. They should also state whether or not any return or benefit guarantees or promises are conditional on the performance of the fund or plan. Where there are unconditional promises, it is essential that the governing documents specify whether the sponsoring employer and/or the plan members may be required to increase their contributions in order to restore the financial balance of the fund or plan. It is important that the governing documents also set out the (i) legal form of the pension entity, its capital structure and purpose; (ii) the contributions and benefits (iii) the vehicles to be used to ensure the legal separation of the pension plan/fund assets from the pension fund management company as well as the other plans and /or funds managed by it; (iv) the organisational structure; (v) the governance structure and the roles and responsibilities of the governing body or bodies; and (vi) any affiliation contracts through which the pension entity subjects itself to the management of another company.

Risk control, reporting and auditing mechanisms

2.4	Pension entities should have adequate risk control mechanisms in place to address investment, operational and governance risks, as well as internal reporting and auditing mechanisms.
	Additional Comments on Implementing Guidelines Risk management procedures contribute to sound corporate practice and help to establish adequate risk measurement and management systems. These procedures include mechanisms to identify and address conflicts of interest and operational risks, such as those linked to technological failure. Specific tools are also required for the assessment and management of investment and other risks related to the pension fund or, where applicable, pension plan. It is essential for adequate supervision, transparency and sound corporate conduct that arrangements for a periodic audit and reporting duties for the auditor, actuary (defined benefit plans) and the governing bodies are in place. Internal reporting rules increase the transparency of the actions of the governing bodies, as does the establishment of organisational and administrative procedures.
2.5	If they manage more than one pension plan or fund, pension entities should be required to maintain separate accounts and records for each of the pension funds, or where relevant, each of the pension plans that they manage.
	Additional Comments on Implementing Guidelines In the interest of transparency and accountability, pension entities should be required to maintain separate records for each fund or plan that they manage. This is particularly important when different plan sponsors are involved.

Funding policy

2.6	Pension entities that offer defined benefit (DB) and hybrid/mixed plans should have a funding policy that specifies the sources of funding, the actuarial method to be used, and the mechanisms for fulfilling legal funding requirements.
	Additional Comments on Implementing Guidelines The funding policy sets out in detail the strategy that the pension entity follows to comply with the required funding levels set by the regulator (see Core Principle 3). In the case of DB plans and hybrid/mixed plans, the funding policy is based on approved actuarial methods and techniques.
2.7	Where a pension entity manages assets for different pension funds or plans, separate funding policies and methods should be prepared for each pension fund or, where relevant, each pension plan.
	Additional Comments on Implementing Guidelines In the interest of transparency, it is essential that there be identified funding policies and methods for each pension fund, or where relevant, each pension plan administered by the pension entity.

Investment policy

2.8	Pension entities should prepare a statement of investment policy.
	Additional Comments on Implementing Guidelines The investment policy establishes the financial objectives of the fund or the plan. It also sets out the investment principles, the strategic asset allocation, the performance and risk objectives, the process for selecting asset managers as well as the mechanisms for monitoring and reviewing performance and changing the asset allocation and asset managers. (see Core Principle 4) Submission of the investment policy as part of the licence application permits the licensing authority to assess whether the investment policy is adequate and whether it is in line with the fund's objectives and liabilities and the relevant legislative requirements, and facilitates effective post-licensing supervision of the pension entity's investment activities. It is particularly important that the investment policy is consistent with the financial liabilities of the pension plan or fund.
2.9	Where a pension entity manages different pension plans or funds, separate statements of investment policy should be prepared for each pension fund or, where relevant, each pension plan.
	Additional Comments on Implementing Guidelines In the interest of transparency, it is essential that there be identified investment policies for each pension fund, or where relevant, each pension plan administered by the pension entity.

Capital requirements

2.10	At least where directly exposed to financial and demographic risks, pension entities should be required to hold a minimum amount of free, uncommitted starting capital or otherwise have access to adequate financial resources. The amount should be dependent on the risks to be covered. The required minimum capital should not be used to cover set-up costs. In order to ensure the guarantee function of the minimum capital, legislation could require the setting aside of appropriate assets. In some jurisdictions, capital requirements may also be satisfied by the purchase of insurance providing the same level of protection to the plan members and plan beneficiaries.
	Additional Comments on Implementing Guidelines In certain jurisdictions, the pension entity must have a minimum amount of basic capital in order to be licensed. Where this is the case, the minimum amount of starting capital that is required depends on the types of risks managed, the extent to which the pension entity bears any liability for any return/benefit guarantees or for mismanagement, and the size of the funds managed. In those jurisdictions, the licensing authority must receive proof that the capital requirements have been fulfilled (to the extent not addressed by the financial institution's other supervisor(s)).

Governance

2.11	Pension entities should have a governing body that is ultimately responsible for the entity and a code of conduct for the members of its governing bodies and staff. The code of conduct may be laid out in specific legislation applying to pension entities.
	Additional Comments on Implementing Guidelines Pension entities are normally required to submit information setting out the pension entity's governance structure, such as the names, CVs and contact details of the members of the governing body. This information may also include copies of professional certificates and a declaration confirming that they have not been convicted of a financial or property-related crime and that no criminal proceedings are pending against them. The requested information may be contained in any of the following documents, which the pension entity will usually be asked to submit: • the entity's or, where relevant, the plan's charters or documents; • a code of conduct for the members of the governing body and other supporting staff that, among other issues, addresses conflicts of interest and prohibited appointments; • any outsourcing (third party) service contract; • information regarding risk management, internal reporting and auditing mechanisms. For supervisory purposes and in the interest of transparency, the pension entity may also be required to submit one or more of the following: the contact details of the plan sponsor(s), the plan/fund actuary, the independent auditor and the custodian.

	In some jurisdictions, corporate governance requirements may take the form of formal restrictions under which the manager of the pension plan or fund is prohibited from exercising its power over the plan or fund to direct investments towards related parties. More generally these requirements can be reflected in prohibitions against a person who is in any manner related to the pension entity from being involved in any transaction involving assets of the plan or fund. Where outsourcing arrangements are made clear during the licensing procedure, it will be clear to all parties involved who carries out what activity. Information on the outsourcing arrangements permits the authority to assess whether the applicant does not overstep the limits to outsourcing, does not breach its duty to monitor and oversee the external service providers and does not absolve itself of its responsibility for the outsourced activities.
2.12	Member of the governing bodies of the pension entity should be subject to fit and proper requirements.
	Additional Comments on Implementing Guidelines "Fit and proper" criteria should call for appropriate experience , knowledge and skills, integrity of the governing body and the management staff. (see Core Principle 6)
2.13	Pension entities should be required to keep a functional separation between those staff responsible for investments and those responsible for settlement and bookkeeping.
	Additional Comments on Implementing Guidelines A separation between the staff responsible for investments and those responsible for settlement and bookkeeping is desirable in order to avoid conflict of interest, to enhance transparency and to protect the interests of the pension entity members and beneficiaries. This separation could be reflected in the pension entity's organizational structure.

Business plan

2.14	Pension entities should create a business plan which should at least include (i) a list of the plans/funds that the pension entity will manage; (ii) the types of obligations that the pension entity proposes to incur (*e.g.* return or benefit guarantees), if any; (iii) the estimated setting-up costs and the financial means to be used for this purpose; (iv) the projected development of the fund/plan; (v) where relevant, the means for fulfilling any capital requirements; and (vi) details regarding the adequate risk control reporting and auditing mechanisms, and a sound investment policy that are in place or to be established at start-up.
	Additional Comments on Implementing Guidelines The business plan describes the proposed activity of the pension entity in the first years after its establishment. The projected development of activities includes information on the contributions levels, assets under management, benefit payments, and operational expenses for each of the funds or plans that it will manage. Information on parameters such as the expected number of plan members, information about the target group (type of income group, type of occupation, *etc.*) and the projected pay-back period of set-up costs could also be included in the documents regarding the projected development of the plan/fund.

License withdrawal

2.15	The legal provisions require the withdrawal of a licence from a pension entity in certain circumstances.
	Additional Comments on Implementing Guidelines It is in the interest of legal certainty that the law sets out the circumstances under which a licence can be or is considered withdrawn. This is, for example, the case in any of the following situations: (i) whenever the entity no longer meets the licensing requirements; (ii) whenever it seriously infringes the law in force; (iii) when the pension entity expressly renounces the licence; (iv) if the pension entity does not make use of the licence within a certain period of time; (v) when the pension entity ceases to operate; or (vi) when the licence was obtained by providing false or incorrect information. In jurisdictions where a licence can be withdrawn if the pension fund does not make use of the licence within a certain period, the law must clearly indicate that period.
2.16	Legal provisions grant the pension entity whose licence has involuntarily been withdrawn the possibility to appeal the decision and have it reviewed.
	Additional Comments on Implementing Guidelines Justice requires that statutory redress mechanisms be available to those pension entities whose licence has involuntarily been withdrawn.

Role of the licensing authority in supervisory matters

2.17	The legal provisions should endorse the role of the licensing authority in the wider supervisory and regulatory system and, where there are separate licensing and supervisory authorities, allow for the supervisor to be consulted on each specific licence application.
	Additional Comments on Implementing Guidelines This guideline underlines the importance of the link between the licensing of pension entities and their continuous supervision, as both are essential to achieving the objectives set out in the introduction to these guidelines. In most cases, the licensing authority and the supervisor are one and the same entity, and consistency between the licensing requirements and the rules and aims of continuous supervision is ensured. Where there are two or more separate entities however, consultation of the supervisor on licence applications contributes to consistency between licensing practices and continuous supervision.

Clarity of licensing application procedure

2.18	The legal provisions should promote the clear setting out of the application process, including: • information about the obligations on the licensing authority, for example the timeframe in which it must decide an application*;* • procedures for the licensing authority to seek further information from the applicant; • the actions that the licensing authority will take to confirm the information received as part of the licence application; • requirements that the staff of the licensing authority observe the appropriate standards of confidentiality with regard to the information gathered as part of the licensing application process (with the exception of information which may have to be provided to other public authorities). • rules ensuring that the licensing authority does not unduly delay the licence application process and avoids affecting the viability of the applicant's planned activities.
	Additional Comments on Implementing Guidelines In the interest of legal certainty for applicants and licensing authorities, and in order to ensure an expedient licensing procedure, it is important that the law clearly sets out the different steps in the licensing procedure and the powers of the licensing authority. These powers could include a review of the documents and on-site inspection either before or after licensing. Equally, the duties and responsibilities of the licensing authority and the applicant must be described. The steps during the application process that should clearly be described are, first of all, the information and documents which the licensing authority requests from the applicant. Other steps that should be set out are whether and when the licensing authority can request additional information or request rectification of deficient applications and the timeframes within which the applicant can do so. It is also important for the applicant to know what types of decisions the licensing authority can take, which documents will be reviewed, whether on-site inspection will take place, whether and to what extent the licensing authority can carry out checks at other public authorities for the purpose of the licence application. Finally, the applicant must be aware how the decision of the licensing authority will be notified and understand the process for appealing the decision if the applicant feels aggrieved by it.

Submission of documents

2.19	The licensing authority should have the power to require the submission of the governing documents and other documents necessary for assessing the entity's compliance with the licensing requirements.
	Additional Comments on Implementing Guidelines In order for the authority to assess whether the pension entity meets the licensing

	requirements and in order to facilitate on-going supervision, the pension entity may be asked to submit written information. This information includes the governing documents, documents proving that the pension entity meets the capital requirements (if any), the governance structure, risk control mechanisms and reporting and auditing mechanisms. Auditing mechanisms, if not required before obtaining approval to operate, must be developed afterwards. Other material to be submitted includes documents setting out the funding policy, the investment policy, capital requirements and the business plan.

Assessment of the licence application

2.20	The licensing authority should have the power to: • examine the proposed legal, managerial and ownership structures of the applicant and its wider group (if any); • evaluate proposed directors and other members of the governing bodies as to their expertise and integrity, their skills and experience and their judicial records; • review the proposed strategic and operating plans of the applicant, including: – determining that an appropriate system of corporate governance, risk management and internal controls and a code of conduct will be in place, and – considering whether the operational structure of the applicant reflects the scope and degree of sophistication of the proposed activities of the applicant; • review the policies and procedures that the applicant has/intends to put in place to ensure ongoing compliance with its obligations under relevant legislation and the conditions of the licence and the risk management control framework established by the applicant. • review financial projections for the applicant and assess its financial strength and other resources; • where applicable, identify and determine the suitability of major shareholders, including the ultimate beneficial owners, and others that may exert significant influence on the applicant, as well as assess the transparency of the ownership structure and the sources of initial capital (if required).
	Additional Comments on Implementing Guidelines As the scope of licensing assessments varies, it is important that the licensing authority has the power to assess various aspects of the pension entity. Those powers should be clearly set out in legislation. The intensity of the licence assessment may vary according to the size and complexity of the pension entity's operations and the scope of any such powers should not only be clearly delineated in relevant legislation, but any such power should be required to be exercised treating all parties the same way and consistent with the rule of law, and which thus not only follow processes which are transparent, but also follow substantive practices which are pre-established and transparent.

	The licensing authority may need to assess the expertise and integrity of the pension entity's directors and senior management by means of a fit and proper test, including the potential for conflicts of interest, assessing the skills and experience in relevant financial operations commensurate with the intended activities of the applicant, and seeking confirmation that there is no record of relevant criminal activities or adverse regulatory judgments that make a person unfit to uphold important positions in the applicant pension entity. The licensing authority may, where applicable, need to assess the suitability of the pension entity's shareholders in similar fashion to the way it assesses the pension entity's directors and senior management. The licensing authority will normally also have the power to carry out an assessment of the financial strength of the applicant (including whether any mandatory capital requirements are met), the adequacy of the funding policy and actuarial techniques and methods, its operation structure and governance, to support the proposed strategic plan. The assessment may also involve an examination of mechanisms related to the detection and prevention of criminal activities by anyone within the pension entity, as well as the oversight of proposed outsourced functions.
2.21	The licensing authority should, under specific circumstances, have flexibility in applying legislative requirements so that the type, scale and complexity of an applicant's activities may be taken into account in the assessment as to whether and how licensing criteria are met. The circumstances in which the licensing authority may apply legislative requirements flexibly must be clearly stated in legislation and protection against arbitrary action on the part of the licensing authority must be guaranteed.
	Additional Comments on Implementing Guidelines The licensing authority should have some degree of discretion, clearly bounded by the legal provisions in application of the licensing process. In particular, the need for assessing an application may vary depending on the type, scale and complexity of the pension entity.
2.22	The licensing authority may have the power to impose conditions on the licence of the applicant, and to subsequently vary or withdraw those conditions. The circumstances in which conditions can be imposed, withdrawn or modified must be clearly stated in legislation.
	Additional Comments on Implementing Guidelines In the jurisdictions where the licensing entity may impose conditions on the licence of the applicant, the powers and limitations to impose these conditions must be clearly stated in legislation in order to ensure transparent licensing procedures, fairness and legal certainty. Conditions can be imposed, modified or withdrawn either following a request by the licensee or unilaterally by the licensing authority (if necessary in conjunction with the supervisory authority where there is a separate supervisor).

Guidance materials

2.23	The licensing and/or supervisory authority/ies may provide guidance to applicants regarding their expectations as to how they may meet licensing criteria, so that better internal systems (such as risk management systems) result for the applicant.
	Additional Comments on Implementing Guidelines The licensing process can be made easier for the applicant if there are guidance materials available to applicants. Useful materials would include a checklist of all requirements that the applicant has to meet, application forms and explanation guides accompanying the application forms, as well as explanations on how applicants will satisfy the licensing criteria.
2.24	The licensing authority should provide appropriate guidance to officers carrying out the licensing assessment.
	Additional Comments on Implementing Guidelines The licensing application process in many countries involves the submission and analysis of complex information. It is therefore beneficial to make guidance materials available to both the licence assessors working for the licensing authority and to the applicants. They reduce the amount of time that is required to assess a licence application and facilitate the assessors' tasks. Useful guidance materials for assessors are checklists and manuals, or a set of procedures for off-site or on-site inspections.

Power to reject, modify or withdraw a licence

2.25	The licensing authority should have the power to reject an application if the criteria are not fulfilled or if the information provided is inadequate, so that the assessment process supports the objectives of the licensing regime. Any rejection should include identification of the specific criteria on which the rejection is based.
	Additional Comments on Implementing Guidelines A licensing system is only effective if the licensing authority has the power to reject the licence application when the applicant does not satisfy the licensing requirements. It is important that the licensing authority does not have unchecked discretion when making the decision, but be required to rely on whether the legislative requirements have been fulfilled. The power to reject licence applications needs to be exercised pursuant to transparent practices, which are disclosed in advance to the entity seeking licensing. Transparency is also required in the rejection decision and practices need to be consistent with the rule of law. The scope of discretion that may be exercised by the licensing authority should be precluded or limited to the extent possible. In order to ensure a transparent and fair process, it is also essential that the licensing authority informs the applicant of the precise reasons that led to the decision to reject the licence application.

2.26	The licensing authority should have the power to make adjustments to a licence already granted and to withdraw a licence when the conditions for the licence are no longer fulfilled. These powers must be clearly stated in legislation.
	Additional Comments on Implementing Guidelines In licensing systems where the licensing authority has the power to impose conditions on the operating licence, it normally has the power to modify those conditions should the situation require this. The licensing authority also has the power to withdraw the licence, but only in specific circumstances to be clearly identified in the legislative requirements. The licensing authority also needs to inform the pension entity in a clear and timely manner of the precise reasons that led to the decision to withdraw the licence.
2.27	The licensing authority should have a review mechanism in place to examine the demands of entities whose licence has been modified or withdrawn.
	Additional Comments on Implementing Guidelines Pension entities whose licence has been withdrawn or modified should be able to have the withdrawal or modification decision reconsidered (administrative appeal) or examined by a court of law (judicial appeal). The review mechanism should be transparent and include due process protections in modification and especially in withdrawal of authorisation or loss of tax benefits. Care should be taken that such withdrawal or loss does not occur prior to the completion of the review mechanism, except in cases in which delay would result in irremedial harm, particularly to plan members. The review mechanisms should avoid unnecessarily costly or burdensome requirements or procedures (again, conditional on adequate protections for plan members).
2.28	Decisions of the licensing authority should be open to administrative and legal appeal. Adequate protections to preclude arbitrary action on the part of the licensing authority should be in place.
	Additional Comments on Implementing Guidelines The possibility to launch an administrative or legal appeal encourages licensing authorities to make decisions that withstand judicial scrutiny, while on the other hand giving the opportunity to pension entities to express their grievances and ensure decisions that are fair.

Core Principle 3:
Pension Plan Liabilities, Funding Rules, Winding Up and Insurance

Private occupational plans should be funded. While full-funding exists in principle for defined contribution plans, other types of plans should be subject to minimum funding rules or other mechanisms to ensure adequate funding of pension liabilities. Rules based on winding-up approach may be promoted as a minimum level to complement the ongoing approach. Flexibility can be allowed for temporary limited under-funding under restricted circumstances. Consideration should be given to the development of adequate but flexible requirements for minimum capital/guarantee in pension funds, taking account of the long term nature of their liabilities. Tax and prudential regulations should encourage a prudent level of funding. Private unfunded pay-as-you-go plans at individual company level should generally be prohibited.

Appropriate calculation methods for asset valuation and liabilities funding, including actuarial techniques and amortisation rules must be set up and based on transparent and comparable standards.

Proper winding-up mechanisms should be put in place. Arrangements (including, where necessary, priority creditors' rights for pension funds) should be put in place to ensure that contributions owed to the fund by the employer are paid in the event of his insolvency, in accordance with national laws.

The need for insolvency insurance and/or other guarantee schemes has to be properly evaluated. These mechanisms may be recommended in some cases but in an adequate framework. Recourse to insurance mechanisms (group and reinsurance) may be promoted.

3.1. Introduction

Funding is a concept that primarily pertains to occupational pensions in which one or more sponsoring employers promise a definable outcome and the financing risk remains with the employer or employers. Such pensions generally are labelled defined benefit plans. Defined benefit pensions may be single employer or multiple-employer with risk sharing within the sponsoring group. Defined benefit plans may offer different kinds of promises. Traditionally, such plans calculated benefits as a percent of final earnings or as a percent average of career earnings. More recently, hybrid arrangements such as cash balance or return guarantees have emerged. Most of the provisions outlined below apply to employer sponsored defined benefit plans.

Where such plans are financed from an autonomous pension fund, the legal provisions should establish a framework for ensuring the adequacy of the assets to meet benefit payments. The main alternative to funding is book reserve financing (non-autonomous pension fund), but this is not a method to be recommended as international best practice and is only accepted in a few countries, where they are used in conjunction with insolvency insurance, a guaranty pool, a contingency bond or similar arrangement. Private unfunded pay-as-you-go plans at individual company level should generally be prohibited.

In some countries, instead of establishing an autonomous pension fund the plan sponsor may buy pension insurance policies, hence shifting the plan's risks covered by these policies to the insurance company. The regulation and supervision of insurance companies is designed as to ensure that these institutions build up sufficient internal reserves to meet any pension plan promises.

In a few OECD countries yet another alternative is permitted. Plan sponsors may establish non-autonomous pension funds, and finance retirement benefits through, for example, book reserves. The insurance of employer pension liabilities in these cases is often mandatory.

The primary objective of funding rules is benefit security; that is, to make it more likely that promised benefits will be paid, regardless of the financial fortunes of the employer(s). Generally, this means investing in diversified assets mostly unconnected with the employer(s). Such rules also minimize financial uncertainty for the shareholders and bondholders of those firms that sponsor pensions and may minimize claims against the public, directly or indirectly, in the event of pension promises not being delivered by insolvent employers.

In contrast, in a defined contribution arrangement, an employer's financial liability is mainly limited to paying contributions. However, there are other potential liabilities tied to the fiduciary responsibility of adhering to the terms of the plan and the duties of the managing trustee.

In defined benefit pensions, ongoing funding rules require that the value of the plan's liabilities in respect of all potentially promised benefits are periodically calculated, taking into account relevant contingencies, with respect to existing and former plan members (the actuarial value of projected benefits). Secondly, funding requires the plan's liabilities with respect to existing plan members be allocated over time in relation to service (work) under the plan. Thirdly, with the exception of book reserve financing, funding rules seek to assure that dedicated assets – that is, past contributions and investment returns – match this potential ongoing liability as it accrues and matures over time (accrued liability on an ongoing basis).

In addition, countries may need to have funding rules that seek to assure that plan assets at least equal all promised benefits to date if the plan were to be terminated/wound-up (the accumulated benefit obligation or termination liability). In general, holding assumptions constant, the accrued ongoing liability is greater than the termination liability. However, there are exceptions where this is not the case, and in some countries, experience has been that the tighter rules in defining the termination liability are necessary to complement the normal discretion given to trustees and actuaries in defining ongoing liability.

3.2. Implementing guidelines of Core Principle 3 and commentary

Funding of occupational pension plans

3.1	Occupational pension plans should be funded.
	Additional Comments on Implementing Guidelines Benefit security in both defined benefit and defined contribution occupational plans calls for the funding of pension benefits, that is, the identification and accumulation of assets to be used exclusively to meet pension commitments and related expenses. Different methods of funding exist in occupational plans.
3.2	Occupational defined contribution plans should be funded through the establishment of pension funds, pension insurance contracts or the purchase of other authorised retirement savings products from financial institutions.
	Additional Comments on Implementing Guidelines For defined contribution plans, where sponsoring employers do not make any benefit or performance commitments, the legal separation of pension plan assets from those of the employer should be mandatory. The assets may be held in a pension fund or they may be managed directly by financial institutions through pension insurance contracts or other authorized products.
3.3	Occupational defined benefit plans should in general be funded through the establishment of a pension fund or through an insurance arrangement (or a combination of these mechanisms). Additional protection may be provided through the recognition of creditor rights to the pension fund or the plan members and beneficiaries and, in some cases, through insolvency guaranty schemes that protect pension benefits in the case of insolvency of the plan sponsor or the pension fund.

	Additional Comments on Implementing Guidelines For occupational defined benefit plans, plan assets should normally be legally segregated from the plan sponsor through a pension fund or an insurance arrangement (a pension insurance contract) in order to ensure a minimum level of protection against the possible insolvency of the sponsor. Countries sometimes buttress these funding requirements with priority creditor rights in the case of insolvency of the sponsor and, more occasionally, with insolvency guaranty schemes that protect benefits against the insolvency of the sponsor. In most countries, insolvency guarantee schemes only insure benefits promised in a pension plan up to a specific ceiling.
3.4	Private unfunded plans should generally be prohibited. The establishment of an insolvency guaranty scheme should in general be required for occupational defined benefit plans that are financed through the book reserve system.
	Additional Comments on Implementing Guidelines In occupational defined benefit pension plans financed through the book reserve system benefits should be protected against the risk of default of the plan sponsor through an insolvency guaranty scheme. In practice only certain defined benefit plans offered by some companies to specific workers (*e.g.* senior executives or so-called "top-hat" schemes) are sometimes managed on an unfunded basis without such insolvency guarantee schemes. Such practices may be permitted but should not benefit from tax advantages. Plans that benefit from tax deductibility (and which are normally expected to cover most of the sponsoring company's workers) should not be run on an unfunded basis without insolvency insurance.
3.5	Insolvency guaranty schemes should rely on appropriate pricing of the insurance provided in order to avoid unwarranted incentives for risk-taking (moral hazard). The level of benefits guaranteed should also be limited.
	Additional Comments on Implementing Guidelines Insolvency guaranty schemes may be privately or publicly managed. In general, it is important that such schemes rely on appropriate pricing of the insurance provided in order to avoid unwarranted incentives for risk-taking (moral hazard). These arrangements also function most effectively when the underwriting entity has priority rights for missed or unpaid contributions in the case of insolvency of the plan sponsor. Some countries require insolvency guaranty schemes for defined benefit plans financed via pension funds, in order to provide an additional layer of protection against bankruptcy of the plan sponsor. The need for such schemes should be evaluated taking into consideration the effectiveness of funding and investment rules in mitigating the consequences of sponsor bankruptcy on benefit security and the potential impact of such schemes on the plan sponsor's ability to raise capital and, consequently, on its ability and willingness to continue to support the pension plan. It is important also that insolvency guaranty schemes rely on appropriate pricing of the insurance provided, taking into account, inter alia, the extent of under/overfunding and the default risk of the sponsoring entity.

Measurement of occupational pension plan liabilities

3.6	Legal provisions should be in place requiring the determination of occupational pension plan liabilities corresponding to the financial commitments or obligations which arise out of the pension arrangement. The ongoing liability is normally defined as the accrued benefit rights of pension plan members and beneficiaries excluding future service but taking into account the projected benefits to be received under estimated retirement, mortality, and early leaver (also known as membership termination or job separation) patterns. The termination liability takes into account the pension benefits accrued if the plan were to be terminated at the time of the valuation.
	Additional Comments on Implementing Guidelines Legal provisions usually define one or more measures of ongoing liability to be used in determining annual contribution requirements to occupational pension plans. Ongoing liabilities are normally valued by presuming that the plan remains in place and by treating current members and beneficiaries of the pension plan at the time of valuation as a closed group. An actuarial cost method is then consistently applied to allocate an appropriate part of the total projected cost of the pension plans to the period ending on the valuation date (the "accrued liability") and subsequent years (the "normal costs"). One such method is the projected unit credit method, with includes a provision for the effect of future salary increases in the plan's liabilities. The reporting of the total projected cost of the pension plan, net of projected future contributions, should be required if measurement of the accrued liability and normal cost alone may fail to disclose future deficits to be funded by plan members and beneficiaries. In calculating ongoing liability plan sponsors and pension entities should take into account the particular of all plan benefit formulas and rights using appropriate financial and demographic assumptions. A clear measure of termination liability that reflects the country's laws about the rights of participants if the plan were to be terminated on or about the time of the valuation may also be required. These rights often correspond to the rights of workers who leave plan coverage before retirement with a vested benefit payable at the plan's annuity starting date. The termination liability is calculated with reference to current salaries (and indexation, if required). The concept of termination liability can be important for minimum funding rules, as well.
3.7	Any definitions of ongoing and termination liability should reflect any benefit indexation factors prescribed by law or plan terms (unconditional indexation) that apply from membership or plan termination to the annuity starting date and, if relevant, after the annuity starting date, provided that these factors are predictable. These definitions should also reflect benefits that become vested upon plan termination.
	Additional Comments on Implementing Guidelines The legal provisions should promote guidance on how indexation and vesting should be considered in the measures of ongoing and termination liability. Requirements should properly reflect vesting of benefits triggered by plan termination, as well as the indexation expectations of deferred pensions and pensions in payment.

3.8	These legal provisions should require the use of appropriate calculation methods, including actuarial techniques and amortisation rules that are consistent with generally recognised actuarial standards and methods.
	Additional Comments on Implementing Guidelines Funding rules should be consistent with generally recognized actuarial standards and methods. Guidance on such standards is generally made by the national association of actuaries in the country in question. Guidance can also be sought from the International Association of Actuaries.
3.9	The legal provisions (referencing generally recognised actuarial standards and methods) should require the use of prudent actuarial assumptions which are considered appropriate for the calculation of the pension plan's liabilities. These assumptions would include, among others, the mortality table (representing the assumed level of mortality of plan members and beneficiaries as at the date at which the plan's liabilities are calculated), future trend in mortality (representing permanent changes in mortality that are assumed to occur after the date at which the liabilities are calculated) and retirement and early leaver patterns at different ages (taking into account the actual retirement and early leaver behaviour of those covered by the plan).
	Additional Comments on Implementing Guidelines The legal provisions need to provide guidance concerning the appropriate range of financial and demographic actuarial assumptions for the measurement of ongoing liabilities. There will normally be distinct assumptions with respect to early leaver (separation) and disability during active service, mortality, discount rate, salary growth and indexation levels. Guidance is required in order to promote the adoption of prudent assumptions that encourage adequate funding levels. Separate guidance should be provided for the determination of assumptions for calculating the termination liability where required. The legal provisions should also provide guidance on longevity after benefits become payable (retirement age or annuity starting date). Specific guidance is needed with respect to the use of mortality tables that are up to date and relevant to the population covered. The pension regulator may require that any standard tables used (*e.g.* those from census/statistical offices or tables based on annuity transactions of life insurance companies) are appropriately adjusted to take account of any systematic differences in longevity characteristics between pension plan retirees and beneficiaries and the population covered by those standard tables. The legal provisions should require that retirement assumptions take into account the actual retirement and early leaver (also known as membership termination or job separation) behaviour of those covered by the plan.
3.10	The legal provisions (referencing generally recognised actuarial standards and methods) should require the use of prudent discount rates for determining liabilities that are consistent with the methodologies used in the valuation of assets and other economic assumptions. These legal provisions (or the actuarial profession) should provide guidance as to the factors that may be considered in determining the discount rate for ongoing and termination liabilities.

	Additional Comments on Implementing Guidelines The legal provisions should require that the discount rates used to calculate pension liabilities are prudently chosen taking into account the plan liabilities' risk and maturity structure. Those used for the calculation of ongoing liabilities usually differ from those used in calculating termination liabilities, but both normally take into account the market yield of high-quality corporate or government bonds. Discount rates used for calculating the termination liability may alternatively be based on the yields implicit in annuities sold by market providers for benefits equivalent to those offered by the pension plan. When choosing discount rates, due attention should be paid to the maturity and risk profile of the pension plan's liabilities.
3.11	The calculation of pension liabilities should take place at least once every three years, while a certification or report of the adjusted development of the liabilities and changes in risks covered should be required for the intervening years. All actuarial valuations should be carried out by an actuary, or by another equivalent specialist, who has had appropriate training and experience in the field of pensions.
	Additional Comments on Implementing Guidelines Regular monitoring of the plan's pension liabilities is important to ensure that any imbalances in funding levels are identified at an early stage and hence corrective measures can be implemented on a gradual manner. Valuations should take place at least every three years, but the regulator may deem it necessary to require more frequent valuations on plans that may be more prone to funding imbalances. Such intervening valuations may be limited to a certification or report reflecting the adjusted development by a qualified actuary.
3.12	As part of the process of defining its funding policy, the governing body of the pension fund should seek the advice of the actuary or other relevant specialist regarding the assumptions and methods to be used in calculating pension liabilities and funding levels. This advice should be provided in a clear and timely fashion.
	Additional Comments on Implementing Guidelines The actuary should be qualified by a nationally recognized actuarial organisation. Actuaries should have clear reporting and whistle-blowing responsibilities. (see Core Principle 6) Actuaries should be required to disclose to the pension plan's governing body in a clear and timely manner the actuarial assumptions and methods used for calculating pension liabilities and funding levels.

Funding Rules for occupational defined benefit plans

3.13	The legal provisions require the identification and maintenance of a level of assets that would be at least sufficient to meet accrued benefit payments. The targeted funding level may be based on the termination or the ongoing liability. It should also take account of the plan sponsor's ability and commitment to increase contributions to the pension plan in situations of underfunding, the possibility of benefit adjustments or changes in retirement ages, as well as the link between the pension fund's assets and its liabilities.

	Additional Comments on Implementing Guidelines The legal provisions should provide guidance concerning the appropriate actuarial funding methods to allocate a pension plan's actuarial liability over time, balancing the security of members' benefits and the plan sponsor's ability to pay. These provisions should require a regular contribution obligation derived from the plan's actuarial normal cost, either based on the ongoing or the termination liability. The target funding level should take into account the plan sponsor's ability and its commitment to raise contributions if the plan were to become underfunded, as well as the extent to which benefits can be adjusted or the retirement age changed. The relationship between the fund's assets and its liabilities, and in particular, the extent of matching between their respective future cashflows, should be reflected in the target funding level.
3.14	Approved funding methods (also known as actuarial cost methods) for the ongoing liability should attempt to prevent sharply rising cost curves over time by spreading the actuarial (or accrued) liability over the expected career path of plan members. In order to ensure adequate funding levels over time, ongoing funding methods should take into account factors such as future salary growth, mortality, disability, early leaver (separation) and other relevant events.
	Additional Comments on Implementing Guidelines Funding methods (or actuarial cost methods) allocate the cost of benefits, in present value terms, over the accrual period of benefits. Recommended methods should allocate the cost of benefits smoothly over the working lifetime of actively employed plan members. Funding rules should require the setting aside of assets consistent with the actuarial cost method used.
3.15	In addition to normal costs (the present value of benefits that have accrued on behalf of the members during the valuation period), contributions should reflect other factors, including, to the extent appropriate to the accrual of benefits under the plan, work before a plan's inception, plan amendments that increase liability attributable to past service, deviations of actual results from assumptions (experience gains and losses), and the effects of changes in assumptions (actuarial gains and losses). These supplemental costs should be amortised as even currency units or at a minimum as even percentages of payroll. Amortisation periods should in general not be longer than the expected future period of service of active plan participants.
	Additional Comments on Implementing Guidelines The periods for the amortization of funding costs arising from work before a plan's inception, plan amendments that increase the liability attributable to past service, and actuarial gains and losses should keep plan contributions on a path consistent with the plan's normal cost and should smooth volatility. By spreading these funding costs over time (as even currency units or at a minimum as even percentages of payroll), the short-term volatility of funding contributions can be reduced. Amortization periods should not be longer than the expected future service of active plan

	participants. Long amortization periods should be discouraged as they can lead to low funding levels. Short amortization periods are preferable for actuarial gains and losses in order to more rapidly correct underfunding.
3.16	The legal provisions should not prevent funding methods that seek to dampen the short term volatility in firms' funding contributions. Prudent amortisation of supplemental costs over time might help achieve a smoother contribution schedule and more stable funding levels.
	Additional Comments on Implementing Guidelines The amortisation periods for liabilities related to work for plan sponsors prior to plans being adopted should balance prudential interests and allow sponsoring employers to provide retirement benefits to workers who were employed by the firm sponsoring the plan before the plan's inception. Similarly, with respect to changes in the law that require sponsors to recognise or accelerate the recognition of liabilities, legally established amortisation periods who should balance prudential interests, the effects on sponsors' reported earnings and cash flows, and the willingness of sponsors to establish and maintain occupational pension plans.
3.17	These legal provisions set out the different mechanisms and the recovery period for correcting a situation of underfunding, taking into account the sources of underfunding and the type of underfunding (ongoing or termination basis). Funding rules may grant some reprieve on contribution obligations only under restricted circumstances and to defined limits. Temporary reductions of contribution obligations may be considered with a clear waiver procedure managed by the pension regulator.
	Additional Comments on Implementing Guidelines Corrective measures in the case of underfunding should take into account the source of the underfunding and the type of underfunding (ongoing or termination basis). In particular, it should firstly be established whether the underfunding is due to changes in the valuation of the assets or liabilities or to a failure to collect the required contributions from the sponsoring employer or/and plan members. The latter should be addressed through appropriate channels, including judicial procedures where relevant. Funding rules should also set out the different mechanisms permitted for correcting underfunding, such as the payment of a lump-sum by the plan sponsor, an increase in future contributions by the sponsor or/and plan members, and adjustments in future benefit accruals and other benefit parameters such as the retirement age. Funding rules should also provide for recovery periods for correcting underfunding, taking into account the source and type of underfunding. The chosen recovery period needs to balance the goal of benefit security of accrued benefits and that of plan continuity. Exemptions to funding requirements may also be granted on a discretionary basis by the pension regulator, but only under defined circumstances with a clear waiver procedure managed by the regulator. The procedure should have the option to require any sponsor granted a waiver to collaterise the waived contributions with secured liens on company assets or otherwise provide security on behalf of the pension plan and, if relevant, any public or private insolvency insurer or guaranty fund.

	Optimally, sponsoring employers should be permitted to more rapidly recognise and amortise unfunded liabilities and make deductible contributions that exceed annual contribution obligations. Such provisions may include more rapid amortisation of unfunded liabilities attributable to past service or acceleration recognition of the future liabilities over a worker's remaining expected service with the sponsoring employer.
3.18	Funding rules should aim to be countercyclical, providing incentives to build reserves against market downturns. They should also take market volatility into account when limiting contributions (or their tax deductibility) as a certain funding level is reached. Tax regulations should not discourage the build-up of sufficient reserves to withstand adverse market conditions and should avoid restricting the full funding of the ongoing or termination liability. Temporary suspension of contribution obligations may be appropriate in circumstances of significant overfunding (calculated on an on-going basis).
	Additional Comments on Implementing Guidelines Funding rules should aim to create reasonable buffers against market downturns and allow flexibility in contributions when markets are performing well. Funding rules should also avoid putting in danger the employer's continuation of the sponsoring of the plan. The building of reserves is all the more important when the spreading of experience and actuarial gains and losses is restricted. Asset price and discount rate volatility can then cause wide swings in funding ratios and funding requirements. Tax regulations, which set ceilings on contributions or their tax deductibility when a certain funding level is reached, should not discourage the build-up of sufficient reserves to withstand adverse market conditions and should avoid restricting the full funding of the ongoing liability. When setting such ceilings it is of paramount importance to consider the potential volatility of discount rates and asset values.
3.19	Funding rules should take into account the extent to which the autonomous pension fund itself as opposed to the plan sponsor or the plan members is directly responsible partly or wholly for the commitments represented by the pension liabilities. Where the pension fund itself underwrites the pension liability without any guarantee from the plan sponsor or members, it should be required to hold additional assets over and above those necessary to fully fund the pension liabilities on a plan termination basis. This capital requirement or solvency margin should be determined taking into account the nature and size of assets held and liabilities due that are the responsibility of the pension fund and the extent to which benefits may be reduced.
	Additional Comments on Implementing Guidelines In some countries, the pension fund itself may be directly responsible for ensuring that assets are sufficient to meet liabilities without any guarantee from the sponsoring employer or members. This is the case for accrued liabilities in some countries. Where autonomous pension funds underwrite directly some of the pension liabilities without an employer or member guarantee, they should be subject to a capital requirement over and above the level of assets necessary to fully fund the pension liabilities on a plan termination basis. Such pension funds act to a certain extent in a similar way to life insurance companies. Solvency rules regarding pension funds should therefore also take into account the specific role and functions of other institutions providing occupational retirement benefits.

Winding Up

3.20	The allocation of plan assets and the responsibility for underfunding in the event of plan termination should be clearly established. In the event that assets exceed promised benefits on a termination basis, there should be rules in place as to the allocation of the funding excess or surplus. In the event that assets are insufficient to cover promised benefits, there should be rules concerning the benefit payment allocation.
	Additional Comments on Implementing Guidelines In the event that a plan is terminated and promised benefits exceed assets, there should be rules to allocate available assets to members and other beneficiaries in accord with accrued rights. There should also be rules concerning the responsibility of plan sponsors for any unfunded liabilities. In the event that assets exceed promised benefits on a termination basis, there should be rules in place as to the allocation of the funding excess or surplus between plan sponsors, plan members and other beneficiaries. In some jurisdictions, however, excess assets may only be returned to the plan sponsor while in others they may be shared only among members and other beneficiaries. There is also a need for clarity in allocating plan assets to cover benefits due to current pensioner and active workers when assets are insufficient to cover promised benefits.
3.21	Whenever plan benefits are guaranteed by sponsoring employers, the creditor rights of pension plan members and beneficiaries (either directly, via the pension fund, or, where relevant, via insolvency guarantee schemes) should be recognised in the case of bankruptcy of the plan sponsor. Priority rights relative to other creditors should be required for at least due and unpaid contributions.
	Additional Comments on Implementing Guidelines Bankruptcy and company insolvency laws should provide priority position for due and unpaid contributions at the time of plan termination. The position should equal at least the position of due and unpaid taxes at the time of plan termination. Where insolvency guaranty schemes are present, the underwriting entity normally becomes a preferential creditor of the insolvent sponsor. Priority rights may also be appropriate for underfunded pension commitments (with reference to the termination liability) that are the responsibility of the plan sponsor. The need for granting such rights will depend on various factors, such as the extent to which there are in place insolvency guaranty arrangements that may help recoup any funding gap in the case of plan termination as a result of bankruptcy of the plan sponsor. Due consideration should also be given to the likely impact of such rights on a plan sponsor's ability to raise capital and, consequently, on its ability or willingness to continue to support the pension plan.

Core Principle 4: Asset Management

Investment by pension funds should be adequately regulated. This includes the need for an integrated assets/liabilities approach, for both institutional and functional approaches, and the consideration of principles related to diversification, dispersion, and maturity and currency matching. Quantitative regulations and prudent-person principles should be carefully assessed, having regard to both the security and profitability objectives of pension funds. Self-investment should be limited, unless appropriate safeguards exist. Investment abroad by pension funds should be permitted, subject to prudent management principles.

Increased reliance on modern and effective risk management, industry-wide risk management standards for pension funds and other institutions involved in the provision of retirement income should be promoted. The development of asset liability management techniques should be given proper consideration.

4.1. Introduction

The investment of pension fund assets is one of the core activities of a pension entity. In the case of defined benefit plans, the goal of the investment function is to help the governing body generate the highest possible returns consistent with the liabilities and liquidity needs of the pension plan, in light of the risk tolerances of affected parties. In a defined contribution plan, the main goal of the investment function is to generate gains that accrue to individual member account balances in light of investment goals and the risk tolerance of plan participants. In participant-directed defined contribution plans, this function is in large part carried out by plan or fund members themselves, albeit with varying degrees of intervention and responsibility for oversight or monitoring remaining with the pension entity. In all these cases, it is critical that the investment function be responsibly implemented, managed and regulated.

Investment regulation should be based on prudential principles such as diversification, dispersion, and maturity and currency risk management. A prudent person rule can be included in the legal provisions to embody these principles. Under this rule, the pension plan or pension entity's governing body or another responsible party will have broad authority to invest the pension assets in a prudent fashion in light of the particular needs of the plan or fund. In addition, the authorities may restrict the ability of the governing body or responsible party explicitly by quantitative regulations, for instance

by asset class. Quantitative limitations, which for example, inhibit adequate diversification or impede maturity matching should be avoided.

Additionally, separate regulatory considerations may arise in individual account type plans or funds where members are able to direct their own investments (typically among a specified array of choices). These types of plans or funds may require distinct regulation addressing the unique concerns that may arise in those circumstances.

4.2. Implementing guidelines of Core Principle 4 and commentary

Retirement income objective and prudential principles

4.1	The regulation of pension fund asset management should be based on the basic retirement income objective of a pension fund and assure that the investment management function is undertaken in accordance with the prudential principles of security, profitability, and liquidity using risk management concepts such as diversification and asset-liability matching.
	Additional Comments on Implementing Guidelines The regulation of pension fund asset management should be based on the basic objective of a pension fund which is to serve as a secure source of retirement income for members. The regulation should identify a set of prudential principles that address security, performance, and liquidity of the portfolio as a whole. The regulations should address the need for risk management concepts such as diversification and asset-liability matching.

Prudent person standard

4.2	The governing body of the pension plan or fund and other appropriate parties should be subject to a "prudent person standard" such that the investment of pension assets is undertaken with care, the skill of an expert, prudence and due diligence. Where they lack sufficient expertise to make fully informed decisions and fulfil their responsibilities the governing body and other appropriate parties should be required to seek the external assistance of an expert.
	Additional Comments on Implementing Guidelines The basic regulations should be built around the concept of the "prudent person" standard. Under a prudent person standard, the pension fund's governing body or another responsible party is given broad authority to invest the pension assets in a prudent fashion in light of the particular needs of the plan or fund. Under this standard, a governing body is expected to undertake obligations related to the investment management function with the requisite level of skill to effectively carry out that function, and absent that level of skill or knowledge, to obtain the external assistance of an expert in the particular matter in which the governing body is deficiently skilled or lacking in knowledge. The trend has been to require that prudent persons undertake their obligations with the skills and knowledge that an "expert"

	(rather than an "ordinary person") would bring to their required tasks. The "expert" standard should be applied in light of the sophisticated and complex issues that arise in the area of portfolio asset management. The prudent person standard focuses on behaviour and process rather than on outcomes. It seeks to assure that those responsible for managing pension fund assets do so in a professional manner with the sole aim of benefiting the pension fund and its members. Because of its procedural focus, the prudent person standard places significant emphasis on the ability of pension fund governing bodies to hire qualified assistance and establish appropriate internal controls and procedures to effectively implement and monitor the investment management process. The establishment and use of a comprehensive investment policy is considered a crucial aspect of satisfying the prudent person standard. Portfolio limits can serve to establish important boundaries that prevent or inhibit inappropriate or extreme investment management decisions, but they alone cannot effectively regulate the manner in which pension fund asset management decisions are made within those boundaries, and, in fact, are silent with respect to activity that is "within bounds." Therefore, jurisdictions that rely solely on a series of quantitative portfolio limits to regulate pension fund asset management should consider establishing a prudent person standard to work in tandem with portfolio limits. In this regard, countries that rely primarily on portfolio limits should, at a minimum, also set forth prudent person standards for pension fund governing bodies.
4.3	The governing body of the pension plan or fund and other appropriate parties should be subject to a fiduciary duty to the pension plan or fund and its members and beneficiaries. This duty requires the governing body and other appropriate parties to act in the best interest of plan members and beneficiaries in matters regarding the investment of pension plan assets and to exercise "due diligence" in the investment process.
	Additional Comments on Implementing Guidelines The standard of prudent behaviour should include a fiduciary duty which is an obligation to make investment management decisions in the best (sometimes expressed in the terms of the "sole" or "exclusive") interest of plan or fund members, and a duty to exercise "due diligence" in the investment process which is an obligation to adequately research and monitor investments and those to whom the investment management function is delegated. The fiduciary duty often is accompanied by additional rules to avoid circumstances in which it may be challenged. For example, many countries prohibit pension fund governing bodies and those working for the governing body from entering into situations, relationships or transactions that would create (or give the appearance of creating) a conflict of interest that would undermine their ability to carry out their fiduciary duty to the pension fund and its members. Policymakers and regulators should give serious and due consideration to the promulgation of such rules in addition to establishing a fiduciary duty. It is also important that policymakers and regulators determine to whom the prudent person standard and the related fiduciary and due diligence duties should apply. At a minimum, these standards and duties should apply to the governing body of the pension fund and to other relevant parties, such as asset managers to whom discretionary investment responsibilities have been delegated.

4.4	The legal provisions should require the governing body of the pension plan or fund to establish a rigorous process by which investment activities are carried out (see Implementing Guidelines 4.5 to 4.11 on investment policy), including the establishment of appropriate internal controls and procedures to effectively implement and monitor the investment management process.
	Additional Comments on Implementing Guidelines The prudent person standard needs to be supported by legal provisions requiring the establishment of a rigorous investment management process to set investment objectives, monitor performance and select investment managers.

Investment policy

4.5	The governing body of the pension fund should set forth in a written statement and actively observe an overall investment policy.
	Additional Comments on Implementing Guidelines Parties responsible for managing the investment management of pension assets should establish an investment policy and describe it in a written statement. This should be required regardless of whether the investment regulations use the prudent person standard, portfolio limits or some combination of the two. An investment policy should be established regardless of plan type, whether defined benefit or defined contribution. As noted in the guidelines, pension programmes that include member direction may be required to address additional or different issues in their investment policies. Similarly, the investment policies of defined benefit plans may differ from those of defined contribution plans. In particular, the relationship between actuarial determinations, funding obligations and investment management is significantly more complex for defined benefit plans, and the relationship should be adequately considered in an investment policy.
4.6	The investment policy should establish clear investment objectives for the pension fund that are consistent with the retirement income objective of the pension fund and, therefore, with the characteristics of the liabilities of the pension fund and with the acceptable degree of risk for the pension fund, the plan sponsor and the plan members and beneficiaries. The approach for achieving those objectives should satisfy the prudent person standard taking into account the need for proper diversification and risk management, the maturity of the obligations and the liquidity needs of the pension fund, and any specific legal limitations on portfolio allocation.
	Additional Comments on Implementing Guidelines The investment policy should establish clearly the financial objectives of the pension fund and the manner in which those objectives will be achieved. The investment objectives should be consistent with the retirement income objective of the pension funds, and therefore, with the fund's liabilities. They should also satisfy the relevant legal provisions (prudent person standard and portfolio limits), and more generally, the principles of diversification, and the matching of assets and liabilities (maturity, duration, currency, *etc.*). The investment policy should take into consideration the short and long term obligations of the pension fund, including any necessary funding and actuarial matters that may impact on

	those obligations. Short term obligations include the obligation to pay benefits to those in or who will enter pay status (retirement); salaries, administrative costs and fees that are to be paid by the pension plan from pension fund assets; and anticipated costs arising from portability provisions that might apply to the plan.
4.7	The investment policy should at a minimum identify the strategic asset allocation strategy for the pension fund (the long-term asset mix over the main investment categories), the overall performance objectives for the pension fund, and the means of monitoring and, when necessary, modifying allocations and performance objectives in the light of changing liabilities and market conditions. The investment policy should also include any broad decisions regarding tactical asset allocation, security selection and trade execution.
	Additional Comments on Implementing Guidelines The investment policy should identify the strategic asset allocation (the long-term asset mix over the main investment categories), the overall performance objectives of the pension fund, and the means of monitoring and, when needed, modifying broad asset allocations and performance objectives in the light of changing liabilities and market conditions. More specifically, the policy statement should include appropriate performance benchmarks and assessment timeframes and address the extent to which deviations from the strategic asset allocation will be tolerated.
4.8	A sound risk management process that measures and seeks to appropriately control portfolio risk and to manage the assets and liabilities in a coherent and integrated manner should be established.
	Additional Comments on Implementing Guidelines The implementation of a sound risk management process is essential to appropriately measuring and controlling portfolio risk and the overall risk profile of the pension fund, including the extent of matching between assets and liabilities. The governing body may establish a target level of asset-liability matching that can be monitored through appropriate risk management techniques that take into account the main risk factors influencing the assets and liabilities of the pension fund.
4.9	The investment policy for pension programmes in which members make investment choices should ensure that an appropriate array of investment options, including a default option, are provided for members and that members have access to the information necessary to make investment decisions. In particular, the investment policy should classify the investment options according to the investment risk that members bear.
	Additional Comments on Implementing Guidelines In plans that offer members a range of investment options, legal provisions should require that these options offer a sufficiently diverse range of risk-return characteristics so that members can select according to their preferences. The default option for those members that make no active choice should reflect member characteristics and have an appropriate risk-return profile. Sufficient information on investment options and the default option should be made available to members so that they can make informed choices.

4.10	Parties who are responsible for the overall implementation of the investment policy should be identified together with any other significant parties that will be part of the investment management process. In particular, the investment policy should address whether internal or external investment managers will be used, the range of their activities and authority, and the process by which they will be selected and their performance monitored. An investment management agreement should be required if external investment managers are used.
	Additional Comments on Implementing Guidelines The investment policy should address whether internal or external investment managers will be used, the range of their activities and authority, and the process by which they will be selected and their performance monitored. Where delegation of the asset management function is envisaged, an investment management agreement should also be required. Similarly, the investment policy should consider the costs of investment management and related activities, including research and transaction costs and compensation, especially of external service providers.
4.11	There should be procedures and criteria by which the governing body or other responsible party periodically reviews the effectiveness of their investment policy and determines whether there is a need to change the policy, its implementation procedures, the decision-making structure, as well as the responsibilities linked to its design, implementation, and review.
	Additional Comments on Implementing Guidelines The legal provisions should set out a requirement for the regular review of the investment policy. An annual review in conjunction with the annual performance assessment would be advisable.

Portfolio limits

4.12	The legal provisions may include maximum levels of investment by category (ceilings) to the extent that they are consistent with and promote the prudential principles of security, profitability, and liquidity pursuant to which assets should be invested. Legal provisions could also similarly include a list of admitted or recommended assets. Within this framework, certain categories of investments may be strictly limited. The legal provisions should not prescribe a minimum level of investment (floors) for any given category of investment, except on an exceptional and temporary basis and for compelling prudential reasons.
	Additional Comments on Implementing Guidelines By setting forth portfolio limitations, regulators explicitly restrict the range of asset allocation strategies available to those charged with pension fund asset management responsibilities by establishing quantitative limits on investment, typically by asset class. Typically these limits are established as maximum permitted levels of investment (ceilings) in various asset categories and markets. The general intent of such portfolio limits is to implement the prudential principles of security, profitability and liquidity at the regulatory level, rather than pension fund level, and to effect or make an initial strategic asset allocation decision applicable to all pension funds subject to the legal provision. Portfolio limits may be applied to ensure a minimum degree of diversification and asset-liability matching.

	A list of admitted/recommended assets and markets could also be established (possibly at a broad level only). In some circumstances, such a list could be compulsory. It could also be optional, but in that case there should be the possibility to require the firm to justify any substantial deviation from the list. Certain categories of investment may be strictly limited (as for instance loans without appropriate guarantee, unquoted shares, certain equities which may raise major risks of conflicts of interest, illiquid assets, and, in general, investments that lack sufficient transparency). It may also be relevant to set limits on investment by pension funds in companies (or investment vehicles) holding a large volume of such categories of assets. For member-directed occupational pension plans, the principle of diversification and rules prohibiting or limiting self-investment may be important aspects of pension fund investment regulation, and regulators should assess whether their regulation of such pension programmes adequately addresses these issues in member-directed pension fund accounts. These concerns can be reviewed and addressed at two levels. First, the pension funds (or other pooled investment vehicles) in which members are permitted to invest can be regulated to prevent the portfolios from inappropriate self-investing or investing in a manner that would violate the principle of diversification. Second, additional rules could be placed on members to whom investment choice is available. Certain types of portfolio limitations should generally be avoided. In contrast to the establishment of maximum levels of investment levels, the establishment of minimum levels of investment (floors) for a given category of investment should be prohibited. "Floors" force pension funds to invest specified portions of their portfolios in particular asset categories, leaving pension fund asset managers no or little ability to walk away from what they might determine to be unwise investments or investments inappropriate for their portfolios. "Floors" might also artificially inflate prices in particular asset classifications. As stated in the guideline, legal provisions should not prescribe a minimum level of investment for any given category of investment, except on an exceptional and temporary basis and for compelling prudential reasons. Investment floors have also been used when a new private pension system starts functioning and it is felt that only certain financial assets offer sufficient transparency or liquidity. In such cases, it is usually preferable to impose ceilings on those assets not considered apt for investment.
4.13	Portfolio limits that inhibit adequate diversification or impede the use of asset-liability matching or other widely-accepted risk management techniques and methodologies should be avoided. The matching of the characteristics of assets and liabilities (like maturity, duration, currencies, etc) is highly beneficial and should not be impeded.
	Additional Comments on Implementing Guidelines Quantitative portfolio limitations that inhibit adequate diversification or impede matching of the characteristics of assets and liabilities (maturity, duration, currencies, etc) should be avoided. In this regard, policymakers and regulators should take account of and give proper consideration to modern and effective risk management methods, including the development of assets/liabilities management techniques. Application of these techniques may result in portfolios that are heavily weighted in bonds, for example, and, which, as a result, could violate portfolio limit regulatory regimes, and yet not necessarily be regarded as inadequately diversified or imprudent. It is important that the regulation of investment portfolios take into account the portfolio of commitments and obligations of pension funds, and legal provisions should, therefore, set out a framework of general principles that

	adequately addresses the matching and similar risk management techniques. In this regard, it may be useful to tailor regulations to the nature of contractual guarantees (with regard, for example, to returns, interest rates, indexation, etc), maturities, and payout terms (*e.g.*, annuities or lump sums) of the particular pension programme.
4.14	Where the legal provisions establish maximum levels of investment by category (ceilings), there should be an established procedure for correcting excesses within specified time limits.
	Additional Comments on Implementing Guidelines Where the legal provisions establish maximum levels (ceilings) of investment by category in accordance with the principle of diversification, there should be an established process by which pension funds are required to correct any excesses within specified time limits. Similarly, it may also be necessary to address temporary violations caused by unanticipated or unusual fluctuations in market valuations of pension fund portfolios. Policymakers and regulators should account for the fact that simultaneous decreases in the value of one asset category and increases in the value of another may have substantial implications on portfolio allocations that are tested against portfolio limits on a percentage of portfolio basis.
4.15	Self-investment by those undertaking investment management of pension funds should be prohibited or limited, unless appropriate safeguards exist. Investment in assets of the plan sponsor, in parties related or affiliated with any pension entity or pension fund managing company is prohibited or strictly limited to a prudent level (*e.g.* 5 percent of the pension fund assets). When the plan sponsor, the pension entity or the pension fund managing company belong to a group, investment in undertakings belonging to these same groups should also be limited to a prudent level, which may be a slightly higher percentage (*e.g.* 10 percent of the pension fund assets).
	Additional Comments on Implementing Guidelines Portfolio limits that prohibit or significantly limit self-investment by those undertaking investment management of pension assets are also recommended. These limitations either may be set forth explicitly, or they may be incorporated within a prudent person approach to regulation. Where explicit limitations rather than outright prohibitions are set, the legal provisions should establish a prudent ceiling (*e.g.* no higher than 10 percent of the pension assets) on the ability of pension fund managers to invest pension assets in shares or other financial instruments of their own company and affiliated companies. Similar limits should be placed on the ability to invest pension assets in the shares or other financial instruments of the employer sponsoring a pension plan or fund and affiliated companies of that employer. The specific limit should take into account the risks that come with the investment in the sponsoring company. In the case of a single sponsor, investment in sponsor assets should be limited to a prudent level (*e.g.* 5 percent of the pension fund assets). When the sponsor belongs to a group the total investment in companies that are part of this group may be limited to a slightly higher percentage (*e.g.* 10 percent of the pension fund assets). Similarly, legal provisions should include maximum limits on the investment of pension assets in parties related to or affiliated with any of the service providers of a pension plan, in order to address conflict of interest concerns. (As noted in the discussion of the prudent person standard, legal provisions addressing conflicts of interest situations are often used in conjunction with (or in lieu of) an explicitly stated fiduciary duty.)

4.16	Investments in assets issued by the same issuer or by issuers belonging to the same group should not expose the pension fund to excessive risk concentration.
	Additional Comments on Implementing Guidelines The legal provisions should require that pension funds are not excessively exposed to individual issuers or single assets. Portfolio limits regulation may be used in accordance with the principle of diversification to establish maximum levels of investment in a given asset, in a single issue, or in securities of the same issuer (single or group issuer) as a proportion of a pension fund's total portfolio. This is one of the most widely-used types of portfolio limits regulation and is often used in prudent person-oriented jurisdictions.
4.17	Investment abroad by pension funds should not be prohibited and, among other risks, should take into account the currency matching needs between pension plans assets and liabilities.
	Additional Comments on Implementing Guidelines Prohibitions on investments abroad can undermine the key goals of portfolio limits regulation – to assure appropriately diversified pension fund portfolios and should be avoided. These limitations may also undermine the profitability objective. To the extent that national markets are not correlated, the ability to diversify investment internationally should reduce risk. Additionally, in some countries domestic markets may be inadequately diversified, for example by being dominated by a small number of large firms or unduly exposed to one type of industry. (The benefits of international portfolio diversification for pension funds, however, might need to be weighed against other policy considerations. For instance, in many countries pension funds are a significant component of national savings and play an important role in the development of domestic markets.) When investing in foreign assets, political and currency risks should be duly considered and adequately addressed. Countries may also consider rules addressing currency risks and the location of the title to foreign assets or of the pension trust.
4.18	Legal provisions should address the use of derivatives and other similar commitments, taking into account both their utility and the risks of their inappropriate use. The use of derivatives that involves the possibility of unlimited commitments should be strictly limited, if not prohibited.
	Additional Comments on Implementing Guidelines Derivatives are complex financial instruments that have an increasing place in pension fund portfolios. The use of derivatives as a management instrument may prove useful and effective if done in a prudent fashion in order to reduce investment risks or facilitate efficient portfolio management. Specific rules may need to be established in order to ensure that their use is consistent with appropriate risk-management systems. The use of derivatives that involves the possibility of unlimited commitments and, more generally, the use of derivatives for speculative purposes should be prohibited.

4.19	All legal provisions setting forth quantitative portfolio limits should be regularly assessed to determine whether they are unnecessarily inhibiting the ability of pension fund asset managers to implement optimum investment strategies and amended to the extent necessary.
	Additional Comments on Implementing Guidelines Policymakers and regulators maintaining portfolio limits should regularly assess whether or not their legal provisions are creating adverse incentives that might be undermining or unnecessarily inhibiting the ability of pension fund asset managers to implement optimum investment strategies. Amendments to such legal provisions should be made if it is found that they are unnecessarily constraining. To the extent that the security of pension fund assets is not put at risk, they should also consider making quantitative portfolio limits less restrictive and increasing reliance on a prudent person standard. As noted in the discussion of the prudent person standard, although the prudent person rule and portfolio limits are sometimes viewed as competing forms of regulation, they can work as effective complements to one another – and policymakers and regulators should strive to obtain the appropriate balance.

Valuation of pension assets

4.20	The legal provisions should establish a proper, transparent and disclosed basis for valuing pension assets.
	Additional Comments on Implementing Guidelines In all cases, the methodology used for valuing pension fund assets should be transparent to the pension fund's governing body and those involved in the investment management process for the pension fund. Valuations and methods used should be readily available or disclosed to members and beneficiaries.
4.21	Where national rules do not require valuation at current market value or under a fair valuation methodology, it is recommended that the valuation be accompanied by the disclosure of the results that would have been obtained using a current market value or fair valuation methodology.
	Additional Comments on Implementing Guidelines In order for pension fund assets to be appropriately managed, the pension fund's governing body and other parties involved in pension fund asset management must be able to readily ascertain the value of the pension assets for which they are responsible, regardless of the nature of the investments held in the pension fund. In general, current market values should be used where available. If not available, a fair valuation methodology acceptable under general accounting standards should be used. Where alternative methodologies are used, it is recommended that the use of such methods be accompanied by the disclosure of the results that would have been obtained using a current market value or fair valuation methodology.

4.22	The legal provisions should require pension assets to be valued for accounting, reporting, actuarial and funding purposes. Ideally, permitted valuation methodologies for these purposes should be consistent, and where inconsistent, the differences in methodologies should be transparent. In appropriate circumstances, rules may permit methods that reduce short-term volatility of values over time for actuarial and funding purposes.
	Additional Comments on Implementing Guidelines Some jurisdictions permit the use of various methods of smoothing asset values over time in the context of actuarial and funding determinations for defined benefit pension plans and defined contribution plans with guarantees. Where smoothing is employed, regulators and supervisors should seek to assure it does not mask significant underlying concerns regarding the overall asset allocation of a pension fund portfolio or the performance of any specific investments or asset classification. Because smoothing techniques may have a significant impact on actuarial and funding determinations, regulators and supervisors that work in an environment where the smoothing of asset values is permitted should fully understand the nature of the potential impact. Smoothing of asset values may be unnecessary if funding obligations pertaining to experience and actuarial gains and losses can be spread over time.
4.23	Special methods may be needed to value securities in less liquid markets and assets such as real estate. The legal provisions may set out specific methodologies for valuing such assets which should, as far as possible, take into account the risk inherent to illiquid markets.
	Additional Comments on Implementing Guidelines Legal provisions should set out acceptable methodologies and mechanisms for the valuation of less liquid assets. Appropriate methods could include a fair value approach, a discounted cash flow approach or a capital income approach. Direct real estate investments could be valued by professionally designated, certified or licensed commercial property appraisers.
4.24	The methodology used for valuing pension fund assets should be transparent to the pension fund's governing body, all others involved in the investment management process for the pension fund, and members and beneficiaries.
	Additional Comments on Implementing Guidelines The legal provisions should require the disclosure of the methodology used for valuing pension fund assets to interested parties. Such disclosures should detail in a simple and clear way the valuation methods used for different assets.

Core Principle 5:
Rights of members and beneficiaries and adequacy of benefits

Non-discriminatory access should be granted to private pensions schemes. Regulation should aim at avoiding exclusions based on age, salary, gender, period of service, terms of employment, part-time employment, and civil status. It should also promote the protection of vested rights and proper entitlement process, as regard to contributions from both employees and employers. Policies for indexation should be encouraged. Portability of pensions rights is essential when professional mobility is promoted. Mechanisms for the protection of beneficiaries in case of early departure, especially when membership is not voluntary, should be encouraged.

Proper assessment of adequacy of private schemes (risks, benefits, coverage) should be promoted, especially when these schemes play a public role, through substitution or substantial complementary function to public schemes and when they are mandatory. Adequacy should be evaluated taking into account the various sources of retirement income (tax-and-transfer systems, advance-funded systems, private savings and earnings).

Appropriate disclosure and education should be promoted as regards respective costs and benefits characteristics of pension plans, especially where individual choice is offered. Beneficiaries should be educated on misuse of retirement benefits (in particular in case of lump sum) and adequate preservation of their rights. Disclosure of fees structure, plans performance and benefits modalities should be especially promoted in the case of individual pension plans.

5.1. Introduction

The protection of the rights of members and beneficiaries is one of the main pillars of the regulatory framework of private pensions systems. Regulations need to ensure a fair treatment of plan members, the protection of benefits and non-discriminatory access to pension plans. Plan members also need appropriate information and education that will allow them to make adequate choices and to understand the quality of their expected benefits and the quality of service provided by pension entities and their pension providers.

The key distinctions among pension programmes that may affect the precise nature and scope of rights and protections are first, whether the pension programme is mandatory or voluntary; second, whether the pension

programme is intended to be primary or only a supplementary source of retirement income; third, whether and to what extent the programme is subsidized by the state; and fourth, whether the plan design is defined benefit or defined contribution, and if defined contribution, whether plan members direct their own investments. In the case of pension plans voluntarily established by employers for their employees, countervailing labour market constraints, including the role of collective bargaining and the extent to which certain rights may impose additional costs or unwarranted burden on employers, must also be taken into account. Put more directly, there is a risk that overly proscriptive member rights and protections may lead to a decrease in pension plan formation or upset the balance of collective bargaining over such issues. These concerns must be taken into account and be balanced against the need for such rights and protections.

In addition to these distinctions, one may distinguish between substantive rights and procedural rights, although the line between the two may not always be clearly drawn. Substantive rights would include, an employer's pension plan, as well as benefit accrual and vesting rules. To the extent that a right is characterized as substantive, the nature of the pension plan (voluntary/mandatory, primary/supplementary, defined benefit /defined contribution, *etc.*) will be reflected in the expansive or limited nature of the right granted. By contrast, procedural rights are more universal in character, less dependent on the nature of the pension plan, and are, therefore, less likely to vary substantially in degree or quality. These procedural rights would include, for example, certain juridical rights, such as the right to a transparent and fair process whereby member and beneficiary claims and grievances may be timely heard and appealed and adequate redress obtained.

One basic right that should be granted to members and beneficiaries regardless of the type of plan is the right to disclosure about relevant information concerning the pension plan and fund. Members and beneficiaries who have regular access to clear descriptions of their rights and responsibilities relating to plan or fund membership – and who understand those rights and obligations – will serve an important monitoring function to assure the appropriate governance of the plan or fund. Disclosure and education is also appropriate to help members and beneficiaries understand (1) the extent to which their plan or fund may provide them with a satisfactory level of income in retirement, (2) the extent to which they and/or the pension plan or fund bear the risks and responsibilities of providing and protecting their expected retirement income, and (3) the decisions that they may need to make regarding the form and timing of occupational pension plans, regardless of plan or fund type. Beneficiaries should also be able to obtain upon request relevant information regarding their benefits and rights.

5.2. Implementing guidelines of Core Principle 5 and commentary

Access to plan participation, equal treatment and entitlements under the pension plan

5.1	Employees should have non-discriminatory access to the private pension plan established by their employer. Specifically, regulation should aim at avoiding exclusions from plan participation that are based on non-economic criteria, such as age, gender, marital status or nationality. In the case of mandatory pension plans, those plans that serve as the primary means of providing retirement income, and those that are significantly subsidised by the state, regulation should also aim at avoiding other unreasonable exclusions from plan participation, including exclusions based on salary, periods of service and terms of employment, (*e.g.*, by distinguishing between part-time and full-time employees or those employed on an at-will and fixed-term basis). Regulation of voluntary and supplementary pension plans also should aim towards similarly broad access, although the extent of such access may take into account factors including the voluntary nature of the arrangement, the unique needs of the employer establishing the pension plan, and the adequacy of other pension benefits.
	Additional Comments on Implementing Guidelines The extent of an employee's right of access to an occupational pension plan will depend on the nature of the pension programme and the particulars of the pension system of each country (or other relevant jurisdiction). Nonetheless, at a minimum, it is recognised that regulation should aim at assuring that employees are not unreasonably barred from participation in a pension plan. In the case where employee participation in a pension plan is voluntary on the part of the employee, this right of access should apply to the provision by the employer of the opportunity to elect to participate in the plan. As a matter of public policy, it is clearly desirable that certain types of restrictions on plan access, such as those based upon age, gender, marital status and nationality, be avoided. Countervailing policy considerations, for example, in the cases of age and marital status, might be appropriately considered in some circumstances. Other restrictions that are based on more rational, economic criteria may be permitted, but should be carefully reviewed by regulators. For instance, salary restrictions that limit pension plan participation to only employees earning above a certain amount, in many cases, should be strongly discouraged. Similarly, rules limiting plan access based on whether an employee is a part-time rather than a full-time employee, or on the basis that the employee has been hired on a fixed-term rather than open-ended contract, should be discouraged. On the other hand, other categories of exclusion may be less problematic if moderate in application and appropriate in light of the nature of the pension programme and the balance policy makers have struck between the need for access to occupational pensions and labour market considerations. Where the provision of pensions is voluntary for employers, they should be permitted to retain some degree of control about which categories of employees have access to their pension plan. For example, period-of-service rules – such as those which require an employee to complete a specified period or number of hours of service prior to entering the pension plan or to work a certain number of hours annually to continue to participate – may be permitted to be imposed by the employer (or as a result of collective bargaining) in certain

	appropriate circumstances if not unreasonably exclusionary. Similarly, in some circumstances, employers may be permitted to differentiate between various groups of employees, particularly on the basis of an intervening labour agreement. It is for the policy makers and regulator to decide whether such restrictions or exclusions strike the correct balance between pension plan access and other policy matters and to set outer limits on the flexibility permitted employers to set limitations to plan access. All restrictions or exclusions to plan access should be clearly defined in writing in plan documents.
5.2	Employees should be equally treated under the plan rules with respect to portability rights, disclosure requirements, governance and redress mechanisms, and other rights associated with the plan.
	Additional Comments on Implementing Guidelines Once participating in a pension plan, individuals in that plan should be equally treated under the pension plan, although, again, as noted above, this rule must be applied with consideration to the context in which the plan is provided. Many regulators choose to establish rules for benefit levels and accrual or contribution rates for occupational plans aimed at developing a fair (if not equal) distribution of benefits among pension plan members. Regulators that establish such rules may take into account other sources of retirement income available to pension plan members and "integrate" across public and private pension systems – even if this results in plan members receiving different levels or rates of benefit under the pension plan alone.
5.3	If establishing rules for benefit levels and accrual or contribution rates, regulators may take into account the extent of integration of occupational plans with other public or mandated sources of retirement income and the adequacy of the totality of the benefits provided.
	Additional Comments on Implementing Guidelines In establishing rules for coverage, the issue of retirement income adequacy must also be considered. The extent of any right of access provided by regulation must take into account existing governmental retirement programmes and the expected role of the private occupational plans in providing an adequate level of retirement income. Thus, for example, in countries in which occupational plans are intended to only supplement state-provided pensions (or other sources of retirement income), there may be a lesser case for universal access among all employees, because the pension plan is intended to provide only a small portion of individuals' retirement incomes. Even in these cases, however, regulators should take into account the (frequently substantial) public subsidy (tax incentives, *etc.*) of occupational pension programmes and, in light of such subsidisation, seek to ensure the broadest possible access to plan membership and participation.
5.4	Employees should be protected from retaliatory actions and threats of retaliation by their employer or pension plan representatives with respect to pension benefits and the exercising of rights under a pension plan. For example, they should be protected from terminations of employment carried out with the intent to prevent the vesting of an accrued benefit under the pension plan. Similarly, individuals exercising their rights under a pension plan, including but not limited to their filing of a claim or appeal or their initiation of administrative or judicial action, should be protected from retaliatory action, such as termination of employment, suspension, discipline, fine or any other type of discrimination.

	Additional Comments on Implementing Guidelines Having acquired rights to plan participation and plan benefits, individuals must be protected from retaliatory activity that would undermine their exercise of those rights. This protection may take the form of regulations or contractual provisions that specifically prohibit retaliatory activity with respect to pensions, or may be part of a broader legal framework in which employees are protected more generally from unfair dismissal or a variety of retaliatory acts by their employers.

Benefit Accrual and Vesting Rights

5.5	Regulations should promote the protection of benefits that an employee accrues by participating in an occupational pension plan, prevent the retroactive reduction of the value of benefits previously accrued in the plan and provide that plan members obtain timely notice regarding any reduction in the rate of future benefit accruals in the pension plan.
	Additional Comments on Implementing Guidelines A member's benefits begin to accrue upon his entry into a pension plan. In some pension plans and under the regulations of some countries, accrued benefits are immediately vested. In others, however, they may vest only after a defined period of time, typically linked to years of service with the employer sponsoring the plan. Regardless of whether accrued benefits are vested or not, employees participating in occupational pension plans should be protected from the retroactive reduction of the value of benefits that they have already accrued. Thus, amendments to a pension plan's benefit or contribution formula generally should affect only the rate of future benefit accrual. Pension plan members should be appropriately notified if the rate of future benefit accrual will be reduced as a result of changes in the pension plan's benefit or contribution formulas. Countries, however, will vary with respect to the precise manner in which these protections are extended. Protections should apply in both defined benefit and defined contribution environments, although certain practices that regulators should review (*e.g.*, excessive back-loading as discussed below) may more typically occur in a defined benefit plan environment.
5.6	Accrued benefits should vest immediately or after a period of employment with the employer sponsoring the plan that is reasonable in light of average employee tenure. Benefits derived from member contributions to the pension plan should be immediately vested.
	Additional Comments on Implementing Guidelines An accrued benefit is considered to be "vested" if the member has acquired an immediate, fixed right to the present or future receipt of his accrued benefit. The scope and nature of vesting rights should be clearly defined. In defined contribution plans, for example, the account value of the vested benefit may fluctuate with market performance; in defined benefit plans, the value of a vested benefit may depend on interest rate assumptions. In most countries, employees covered by a company retirement plan have vesting rights that reflect an irrevocable commitment from the employer and ensure that plan members will receive benefits related to their past years of service (assuming adequate funding of the plan). Vesting rules should be designed to provide for the vesting of accrued benefits after a reasonable period of employment. The reasonableness of a vesting period should be judged

	relative to average employee tenure, so that vesting is typically attainable by plan members. In appropriate circumstances, especially where there is collective bargaining, there may be different vesting schedules for different categories of employees. In practice, the scope of vesting rights, like rules pertaining to the protection of accrued benefits, varies significantly from one country to another. Generally, vesting periods range from immediate vesting to five years, although in some cases they may be longer. The length (number of years) and design of vesting periods (cliff – i.e. an "all or nothing" rule – versus graduated vesting scales) may vary with the particular labour market conditions of a country and the need to balance the cost to employers of shorter vesting periods against the desire to reduce "job lock" associated with longer vesting periods. Where the employer funds or contributes to the pension plan, shorter vesting periods are costly to them because they increase funding demands (unless the employer reduces benefit levels). Shorter vesting periods also reduce a pension plan's utility as an employee retention tool. Longer vesting periods may reflect the legitimate desire of employers to retain workers for a certain period of time in light of their investment in employee training. From the standpoint of retirement income adequacy alone, it is desirable to encourage the immediate vesting of accrued benefits, but in practice, this is a difficult goal, because of the costs imposed, especially in cases where pension plans are voluntarily established by employers. Generally, individual member contributions to pension programmes should be immediately vested. There will be exceptional instances, however, where the rate at which member contributions (and benefits derived from them) are vested may be appropriately subject to collective bargaining.
5.7	Practices that substantially undermine or eviscerate benefit accrual and vesting rights should not be permitted.
	Additional Comments on Implementing Guidelines While in many jurisdictions, the precise design of benefit or contribution formulas in occupational pension plans – especially plans that are voluntarily established – is left to the employer and/or the collective bargaining process, certain practices should be avoided, as they may substantially undermine or eviscerate benefit accrual and vesting rights. Such practices may include, for example, the excessive back-loading of benefit accruals or the use of an extremely long vesting period (especially when used in combination with a cliff, rather than graduated vesting schedule). The back-loading of benefit accruals, like vesting, however, may reflect legitimate employer desire to retain workers and to reward older, longer serving employees. It is the responsibility of policy makers and regulators to strike the appropriate balance between benefit protection and employer flexibility on such matters and to assure that plan design features and other practices that are permitted to be adopted do not in their judgment substantially undermine benefit accrual and vesting rights.
5.8	Vested benefits of those individuals who have severed employment with an employer should be protected and not subject to forfeiture, regardless of reasons for severance, except in the limited case of dismissals resulting from acts of gross malfeasance that are clearly defined.
	Additional Comments on Implementing Guidelines Severed employees, whether separated from service voluntarily, through mutual agreement or at the will of the employer, should be assured that at least the nominal value of their vested benefit in a pension plan is protected. In defined contribution plans the nominal value of an individual's account with the plan may be subject to the investment performance of the assets in the account, even after the employee has left the service of the employer. The

	ability of a severed employee to "port" the assets in the account or the present value of the accrued benefit (in the case of a defined benefit plan) may be an important adjunct to the protection of the vested benefit required by this guideline. Certain limited exceptions to vesting protections may be appropriate: for instance, in the case of individuals dismissed by the employer for gross malfeasance, especially if related to the pension plan or fund, the loss of vested benefits may be warranted. Such exceptions, however, should be drawn narrowly and should generally exclude any amounts associated with an individual's own contributions to the pension plan. (Assets associated with the lost benefits generally should be retained by the plan and not appropriated by the employer.)
5.9	Vested benefits should be protected from the creditors of the plan sponsor and plan service providers (including any financial institutions or other entities managing the pension plan or plan assets or acting as a custodian of pension fund assets associated with the plan) – at a minimum by the legal separation of plan assets. Vested benefits also should be protected when the plan sponsor or a plan service provider changes ownership due to merger, acquisition, sale, or other corporate transaction, or files for bankruptcy. Similarly, the extent to which vested benefits are protected from the creditors of individual plan members and beneficiaries should be addressed.
	Additional Comments on Implementing Guidelines Regulators should seek to assure that vested benefits are protected from the creditors of plan sponsors and plan service providers. Vested benefits also should be protected in cases where the ownership of the employer sponsoring a pension plan (or that of a plan service provider) changes as the result of a merger, acquisition or sale. There should be a clear delineation of who is responsible for the pension plan, its assets and its administration under these circumstances. Similarly, if the employer or other entities managing or safekeeping plan assets become bankrupt, vested benefits should be protected by regulation. In many cases, these matters also may be addressed under corporate, bankruptcy and other bodies of law; in these cases, regulators should assure consistency of law and regulation with respect to the pension plan and with respect to the extent of a plan sponsor's obligations to it. Requiring pension assets to be legally segregated will substantially assist in protecting pension plan assets in bankruptcy and change-of-ownership situations, but will not fully address them. Regulations should also assure that in the event of changing corporate circumstances it is clear who remains responsible for the maintenance of records related to the pension plan, including work, compensation and contribution histories that determine the value of benefit accrual and extent to which plan members are vested under the pension plan. Additionally, in the case of defined benefit plans there may be funding deficiencies resulting from the nature of funding rules that make it impossible for the plan to pay all vested benefit amounts. Some countries have resorted to additional insurance programs to address this issue.

Pension portability and rights of early leavers

5.10	Individuals who are changing jobs should be able, upon request, to move the value of their vested account balance in a defined contribution plan from their former employer's pension plan either to the plan of their current employer (where permitted) or to a similar, tax-protected environment provided by an alternative financial instrument or institution. Where feasible, a similar portability right also should be available to individuals in defined benefit plans. There may be diminished need for individual portability rights where there are industry-wide and other types of multiple-employer pension plans.
	Additional Comments on Implementing Guidelines Like vesting rights, portability rights are often associated, as a matter of policy, with labour mobility. The inability to move one's vested benefit from one employer to another may constrain individuals who are considering a job change. It is frequently a desirable goal of policy makers to avoid such constraints, without imposing unnecessary costs on employers. The guidelines do not address portability rights, except in the context of changes in employment. It may also be desirable, however, to provide portability rights to employees participating in member-directed pension plans so that they may choose to participate in a personal pension plan, rather than participate in the pension plan sponsored by their employer. This may be desirable, for instance, if plan members are provided only a limited choice of investment options under their employer's pension plan. The desirability of extending portability rights in these circumstances will depend on many factors. These factors include the extent that competition among financial providers would be enhanced, the financial sophistication of the working population, the costs of investments on an individual basis versus those achieved in pension plan environments that experience certain economies of scale, and the transaction costs associated with transferring accounts. Extending portability rights to current employees also may impose an unacceptable administrative burden on employers or undermine the economies of scale advantages employers may have in managing their pension plans. These factors must be considered before extending portability rights to current employees.
5.11	Individuals should have the right to timely execution of the request to transfer the value of their vested benefit accruals.
	Additional Comments on Implementing Guidelines Portability rights may also assist individuals in managing their retirement assets as they change employers throughout their working lives by enabling their consolidation. The consolidation of retirement assets makes retirement accumulations (and the extent of their adequacy) significantly more transparent. This may be particularly true for defined benefit plan accumulations that are converted into a lump sum equivalent for purposes of transfer. Additionally, many defined benefit plans do not index the vested benefit amounts of early leavers for inflation. In such circumstances, it may be beneficial to permit former plan members to transfer their benefit accumulations elsewhere.

5.12	With respect to defined benefit pension plan benefits, the actuarial and interest rate assumptions used in valuing an individual's vested benefit accrual that is to be transferred should be fair and reasonable. These assumptions should be made readily available to the individual transferring the value of his accrued benefit.
	Additional Comments on Implementing Guidelines It is important that individuals have an adequate understanding of their portability rights and their potential impact on their pension benefits. Specifically, individuals should be provided sufficient information to enable them (and their financial advisors) to understand the nature of their pension benefits and the costs and benefits of "porting" their vested benefit amounts. When deciding to move pension benefit accruals, individuals should have the right to the transfer of an appropriately valued benefit, ready access to the economic assumptions underlying the valuation (in the case of a defined benefit plan), and timely execution of their portability request.
5.13	Portability rights should be available to members of a pension plan when they separate from service with an employer, regardless of whether the separation is voluntarily, involuntary or by mutual agreement.
	Additional Comments on Implementing Guidelines Regulators should be encouraged to address other portability issues not specifically identified in the guidelines themselves, including those that arise when employees change jobs with the same employer. Such job transfers may result in the employee leaving one pension plan and entering another offered by the employer. Policy makers and regulators should be sensitive to the administrative difficulties for employers and the unnecessary confusion for employees in such circumstances and should seek to assure that rules and regulations reduce the difficulties of benefit portability on these occasions. Similarly, this guideline only contemplates portability in a domestic context. Regulators should also consider portability issues that arise in an international context, because individuals are increasingly moving from employer to employer or within a single firm across borders. It is recognised, however, that issues arising in this context are numerous and complex.
5.14	Portability rights should not be inhibited by the assessment of unreasonable charges or fees, such as excessive transaction charges or excessive back-end fees. At a minimum, members and beneficiaries should be informed of the presence of any such charges or fees.
	Additional Comments on Implementing Guidelines The extension of portability rights, in addition to taking into account the needs of pension members, must also take into account the potential administrative burdens that portability obligations may impose on employers. In certain situations, the costs of certain portability mechanisms may be determined to be unacceptably high. For example, the administrative burdens and costs of providing portability to and from defined benefit plans are often perceived to be high. Moreover, substantial portability-related distributions could, in the extreme, have an impact on a plan's funding status. For these reasons, the guidelines recognize that portability rights may be more easily established in the defined contribution context. Concerns also are frequently expressed that undue costs are imposed on employers who are asked to accept pension assets from other pension plans. In such cases, it is not unusual to permit, but not require, an individual's new employer to accept a

	transfer of pension assets from the individual's previous employer. Similarly, an individual's portability rights may be limited to a right to transfer the value of vested benefit to a personal pension plan or individual account at a financial institution. Moreover, it may be less necessary to institute extensive portability mechanisms in pension systems that are organized on an industry-wide or multiple-employer basis, because individuals are more likely to remain within the same pension plan when they change jobs. Finally, there may be costs associated with the retention of vested benefits in cases where former employees elect not to exercise their portability rights. This is especially true of short-term employees with small vested benefit values or accounts. Regulators should consider whether, in light of the costs associated with retaining records for de minimus vested benefit amounts, a narrow exception is warranted.
5.15	Individuals should not be required to exercise their portability rights and, generally, should be permitted to leave their vested benefits in the pension plan of their former employer.
	Additional Comments on Implementing Guidelines The legal provisions should also permit departing employees to leave their pension rights with the former employer, although lump sum payout of de minimus amounts may be permitted to ease administration. Deferred benefits may be easier to administer than transfer rights. However, employees may suffer if deferred benefits are not indexed to the cost of living.

Disclosure and availability of information

5.16	Members and beneficiaries in pension plans, as well as potential plan members, should have a legal right to ready access or disclosure to basic information about the pension plan, including adequate information regarding their rights of access, anticipated contribution and/or benefit accrual rates, vesting schedules, other rights and obligations, investment policy, the names and manner of contacting responsible parties for plan administration and governance, and claims processes or procedures.
	Additional Comments on Implementing Guidelines Rights may be meaningless, unless they are adequately disclosed and understood. Therefore, it is important that sufficient, readily understood information about the pension plan is provided to plan members and beneficiaries in a timely manner. Moreover, any significant changes in rights, rules and obligations should similarly be disclosed. Adequate disclosure, in addition to helping to effectuate the substantive and procedural rights of members and beneficiaries, may also lead to more effective pension plan governance by enabling members to monitor certain aspects of plan administration.
5.17	Plan documents, annual accounts, and annual financial and actuarial reports, if not automatically disclosed, should be made readily available to plan members (and to beneficiaries where relevant) for copying for no more than reasonable charge or fee.

	Additional Comments on Implementing Guidelines When joining a plan, members should be provided with sufficient information about plan rules so that they may understand their expected benefits and basic rights. In addition, plan documents and financial information should be automatically disclosed to plan members or made available upon request.
5.18	Members and beneficiaries should be notified in timely fashion if required employer and member contributions have not been made to the pension plan.
	Additional Comments on Implementing Guidelines Regulations should stipulate that required employer contributions that are not paid should be disclosed to plan members in a timely manner. Required employee contributions should as a general rule be deducted on an automatic basis by the employer. Plan members should be notified in a timely manner if required employee contributions are missed. Employees should be notified before any punitive action is taken due to missing required employee contributions.
5.19	Timely, individualised benefit statement should be provided to each plan member (and to beneficiaries where relevant). The information included on the benefit statement and the frequency of its delivery will depend on the type of pension plan. The information included should enable the plan member to identify current benefit accruals or account balances and the extent to which the accruals or account balances are vested. For pension plans with individual accounts, the information should include the date and value of contributions made to the account, investment performance and earnings and/or losses. For member-directed accounts, a record of all transactions (purchases and sales) occurring in the member's account during the relevant reporting period should be provided. This information and other similarly personal data should be maintained and delivered in a manner that takes full account of its confidential nature.
	Additional Comments on Implementing Guidelines Certain disclosure should be required to be provided to each individual prior to initiation of participation in the pension plan and upon request thereafter. These required disclosures would include the following: (1) information regarding the governing body of the plan, (2) explanation of the nature of the benefit promised (including identification of the risks and whether or not benefits are inflation-indexed), (3) information about the consequences of leaving the plan early, and (4) information about the investment policy pursued by the plan. In addition, certain information should be disclosed regularly, such as: (1) information on the performance of investments and (2) the value of the individual's accrued benefit or account balance. When establishing disclosure rules, regulators should take into account the need of plan members to have certain information on the one hand, and on the other hand, whether or not the information might be too voluminous or sophisticated for the average plan member. Consideration should also be given to the cost of providing certain

	information. Similarly, regulators should consider whether, given the nature of the specific pension programme, different rules should apply to former employees that are no longer actively accruing benefits in a plan and to beneficiaries; in many cases however there will be little justifiable distinction.
5.20	Individuals should be provided adequate information about the rules associated with the portability of their vested benefit accruals, especially where the transfer of these assets may entail a loss of certain benefits or rights that were associated with the pension plan in which the benefit originated.
	Additional Comments on Implementing Guidelines Plan members should be fully informed of the rules and procedure pertaining to the portability of their vested benefits. Loss of benefits or value due to withdrawing deferred vested benefits from the plan should be clearly communicated to members.
5.21	Disclosure materials should be written in a manner expected to be readily understood by the members and beneficiaries to whom they are directed.
	Additional Comments on Implementing Guidelines Clear and easily understood language should be used in plan materials disclosed to plan members. If appropriate, information of a very technical nature may be communicated in summarized form using every-day language, with full information disclosed upon request.
5.22	Consideration should be given to adequate forms of delivery of disclosure materials, including, mail, delivery at the workplace and via email or websites, where feasible.
	Additional Comments on Implementing Guidelines The best way of communicating with plan members, whether electronic or in written form, should take into account accessibility and readability of various communication mediums to the target group of plan members.
5.23	Amendments or changes to the pension plan that will significantly impact members and beneficiaries, their rights and their benefits must be disclosed to them in timely fashion and in a manner expected to be readily understood by them.
	Additional Comments on Implementing Guidelines Significant changes to plan provisions or terms should be communicated clearly to the affected plan members, using direct language and appropriate communication means (*e.g.* electronically or by mail depending on accessibility and readability). Verbal communication and question-answer sessions with affected members may be useful as a complementary means of communicating significant changes.

Additional rights in the case of member-directed, occupational plans

5.24	Where members direct their own investments in an occupational pension plan, they have the right to a number and diversity of investment choices sufficient to permit them to construct an appropriate investment portfolio in light of their own individual circumstances and in the context of the particular pension programme.
	Additional Comments on Implementing Guidelines Individuals participating in member-directed pension plans, that is, pension plans in which members direct their own investments or select an investment manager, should be provided adequate rights and protections that take into consideration the responsibilities delegated to them. As an initial matter, individuals participating in member-directed plans must have an appropriate array of investment options from which to choose. This array of investment options will likely include both higher-risk and lower-risk options (which may include an option guaranteeing the amounts of the employee's own contributions paid in), and an option suitable for the typical plan member. The extent of investment choice, however, will vary depending on the nature of the pension plan, the conditions in the relevant securities markets, the role of the pension plan in the broader retirement income security scheme of the particular country, and other similar factors. In assuring that members have a sufficient number and diversity of investment choices, it may also be appropriate to consider whether to limit the number of investment choices in cases where members may be overwhelmed by an excess of investment options. There may be a variety of methods to limit choice, such as by imposing a specific limit on the number and/or type of available investments or by imposing a legal obligation on plan sponsors or fiduciaries to consider this concern in light of the particularities of their pension plan and member population. The decision to limit choice should be weighed against the need to provide sufficient diversity of choice and assure a competitive market.
5.25	Members should be provided with complete information regarding investment choices that is standardised and readily comparable. At a minimum this information should include disclosure of all charges, fees and expenses associated with each investment choice, as well as portfolio composition and historical investment performance data.
	Additional Comments on Implementing Guidelines Individuals in member-directed pension plans may be responsible for assessing and selecting an asset allocation strategy, making specific investment decisions, monitoring investment performance, and buying and selling securities (or switching from one investment vehicle or management company to another). They therefore have a need for adequate information, including comprehensive and comparable information regarding portfolio composition, risks, fees and investment performance to effectively carry out these tasks.
5.26	Members managing their own individual accounts have the right to timely and fair execution of their investment decisions and to written confirmation of these transactions. The right (or responsibility) to make and execute investment decisions should not be inhibited by the assessment of any unreasonable charges or fees.
	Additional Comments on Implementing Guidelines

	Individuals in member-directed plans also must be able to execute their decisions in a timely fashion, as dictated by their own individual retirement planning needs, risk preferences and time horizons, market volatility, and their individual assessments of the performance of specific investments and trends in the economy and securities markets. Regulators must take steps to assure that pension plan administration is suitably robust to enable timely and accurate execution of these transactions. Finally, regulators should take care that the fees associated with member-directed programmes do not significantly undermine their effectiveness, either by making investments themselves unreasonably expensive (for instance, as compared to fees and expenses associated with similar retail investment products in the relevant markets), or by imposing transaction costs that significantly inhibit plan members from effectuating appropriate investment strategies. Transaction costs that regulators might review include, for example, one-time administrative or service fees and front-end or back-loaded fees charged upon the purchase or sale of a particular investment.
5.27	Members and beneficiaries who are required to manage their own individual accounts should be provided sufficient opportunity to acquire the financial skills or education and other assistance that they need in order to make appropriate investment decisions in their pension plans.
	Additional Comments on Implementing Guidelines Members and beneficiaries in member-directed pension plans should be provided sufficient opportunity to acquire the financial skills and other assistance they may need to make the investment decisions expected of them. Regulators and policy makers should therefore assess the needs in their particular pension systems and consider the best manner in which these needs can be met. Action in this area may take a variety of forms, including consideration of the role of public programmes to increase financial literacy, employers and other plan sponsors, trade unions and other social partners, as well as financial service providers and other entities involved in pension plan administration, management and investment. There may be the need for additional types and frequency of disclosure in the case of member-directed defined contribution plans, which require members to select and monitor their own investments, thus imposing additional responsibilities and risks on them. Where members have the right to direct the investment of their individual accounts, the disclosure should provide adequate information upon which each plan member can base educated investment decisions. In particular plan members need to be informed about the precise nature of the financial instruments available, including data on investment performance and risk. In this connection it also may be important that members obtain an adequate understanding of these types of pension plans, the investment risks they bear, and the extent of their responsibilities for managing investments or selecting an asset manager under the plan. Regulators and employers are encouraged to consider ways of improving members' understanding and knowledge of these matters and ways to provide them with adequate assistance in making investment-related decisions. The entities responsible for the provision of disclosure materials, education and member assistance should be clearly identified. Entities that might play a role in educating plan members as to their rights and responsibilities, especially in member-directed plans, could include governmental agencies, schools, and trade unions, as well as employers and other plan sponsors, plan trustees, financial institutions and other plan service providers. The particulars will very much depend on the nature of the pension programme.

Entitlement process and rights of redress

5.28	Members and beneficiaries (and individuals claiming the right to be deemed a member or beneficiary under a pension plan) shall be entitled to a fair process or procedure in which their entitlements, rights and benefits under the pension plan may be claimed or asserted.
	Additional Comments on Implementing Guidelines A fundamental right of members and beneficiaries is the right to a fair, transparent process by which to assert claims against the pension plan. Individuals should be able to initiate and pursue at reasonable cost claims to the right to participate in a plan, to accrue benefits and vest in them at specified rates, and to take benefit distributions in the manner set forth in regulations or in the pension plan documents or contract. This right should be disclosed. There are numerous ways to establish a claims process, including by the establishment of an internal dispute resolution procedure. Good practice would also ensure that the procedure made use of an independent arbitrator or a board or tribunal, which may include member representatives. Individuals also should have access to an independent appeal mechanism, which may be especially warranted if claims are first considered by individuals or bodies internal to the pension plan or sponsoring employer. Consideration should be given to conciliatory approaches to dispute resolution and informal procedures that are easier for members and beneficiaries to use and are less costly to maintain. The use of a pension ombudsman should also be considered.
5.29	The claim process or procedure should be expeditious and transparent. It should be easy to understand and have only reasonable or no cost to the individual claimant.
	Additional Comments on Implementing Guidelines The claims process would be meaningless if it could not result in meaningful redress and, therefore, the process should include an effective way to assess and enforce adequate remedial measures. Employers and pension plan representatives should not be able to inhibit or undermine an individual's exercise of these rights by retaliatory action (or threats of retaliatory action).
5.30	The process should include independent administrative or judicial recourse if initial claims of rights or benefits are denied by the pension plan administrator, fiduciary, or employer. This process should provide for adequate remedial measures to redress the loss of rights or benefits suffered by the member or beneficiary whose claim has been found to be valid.
	Additional Comments on Implementing Guidelines The regulatory system should allow for independent, objective and accessible legal recourse in the event that the claim process is not satisfactorily resolved between the claimant and the pension entity. Individual claimants with valid claims should have adequate judicial support to redress damage or loss of benefits.

Core Principle 6: Governance

Regulations on pension governance need to be guided under the overriding objective that pension funds are set up to serve as a secure source of retirement incomes. The governance structure should ensure an appropriate division of operational and oversight responsibilities, and the accountability and suitability of those with such responsibilities. Pension funds should have appropriate control, communication, and incentive mechanisms that encourage good decision making, proper and timely execution, transparency, and regular review and assessment.

6.1. Introduction

Governance is one of the key aspects of maintaining sound, effective and compliant pension plans. Strong governance is essential as regulation alone cannot achieve the good practice necessary for integrity and effectiveness. Pension entities and sponsors must develop internal rules and systems in order to reach these goals. The role of regulation in the governance process is to provide guidelines and recommendations to steer the governance process.

There is evidence to show that strong governance can lead to superior pension fund performance. Good governance also brings indirect benefits to pension funds. It can spare them the costs of overregulation and it can facilitate supervision by the authorities. In particular, as pension fund supervisors adopt an increasingly risk-based approach to supervision, pension fund governance has become central to deciding whether or not an institution should be closely monitored. Good pension fund governance can also have positive collateral effects on economy-wide efficiency, strengthening the pension fund's role as an effective shareholder – a role which is becoming more key given the increasing size of pension fund assets globally.

Weak governance in pension funds is a serious problem with potentially major and damaging consequences for pension entities and plan members. There are several challenges that must be addressed. First, trustees and fiduciaries require suitable knowledge, experience and training which allow them to understand and challenge advice they receive from outside experts. Second, conflicts of interest within boards and in relation to independent, commercial trustees and other service providers must be addressed. Finally,

suitable governance mechanisms need to be put in place for defined contribution schemes.

Many of the problems in pension fund governance emerge from weaknesses in the governing board. Some of the more egregious cases of governance failures could be solved through a more balanced representation of stakeholders in the governing body, higher levels of expertise - which may be achieved via training as well greater use of independent, professional trustees – and the design and implementation of a code of conduct that effectively tackles conflicts of interest. In defined contribution plans, there is a strong need to strengthen the fiduciary responsibilities of sponsoring employers (in occupational plans) and providers (in personal plans) in order to ensure that plans are managed with appropriate care and with the interest of the members in mind. Other solutions include establishing for defined contribution plans a management committee, although this is only relevant for occupational plans. In countries with highly concentrated pension fund markets, the pension fund supervisory authority can also play a central role in monitoring pension fund governance.

In addition to addressing these governance challenges, regulators and industry associations should also work together to promote pension funds that are large enough in size to facilitate their governance. Smaller pension funds have a governance handicap, as they tend to have more limited access to good trustees and may have insufficient scale to establish fully developed governance structures. For many countries, the consolidation of the pension fund industry is therefore a critical step to improve pension fund governance.

6.2. Implementing guidelines of Core Principle 6 and commentary

Identification of responsibilities

6.1	There should be a clear identification and separation of operational and oversight responsibilities in the governance of a pension fund. To the extent that a pension entity is established that owns the pension fund on behalf of plan/fund members, the legal form of this entity, its internal governance structure, and its main objectives should be clearly stated in the pension entity's statutes, by-laws, contract or trust instrument, or in documents associated with any of these. If the pension fund is established as a separate account managed by financial institutions, the pension plan or contract between plan sponsors/members and the financial institution should clearly state the responsibilities of the latter with respect to the management of the pension fund. As good pension fund governance should be 'risk-based', the division of responsibilities should reflect the nature and extent of the risks posed by the fund.

Additional Comments on Implementing Guidelines

Good governance calls for a clear identification and separation of the operational and oversight responsibilities of a pension fund. To the extent that a pension entity is established that owns the pension fund on behalf of plan/fund members and beneficiaries, the assignment of these responsibilities needs to be clearly stated in the pension entity's statutes, by-laws, contract, or trust instrument, or in documents associated with any of these. These documents also need to state the legal form of the pension entity, its internal governance structure, and its main objectives. If the pension fund is established as a separate account managed by financial institutions, the pension plan or contract between plan sponsors/members and beneficiaries and the financial institution should clearly state the responsibilities of the latter with respect to the management of the pension fund. In addition, there need to be a mechanism for ensuring appropriate independent oversight of the decisions taken by these third parties.

Pension entities are established in accordance to statutes, by-laws, contract (including collective agreements with trade unions), or trust instrument. These documents, sometimes together with associated material, should define the legal form of the pension entity as well as its internal governance structure and main objectives. The main objectives of the pension entity will vary depending on the type of plan that they support. In defined contribution plans, the main objective of the pension entity may be to invest the pension assets in order to maximise risk-adjusted returns, taking into consideration any costs borne by members. In defined benefit plans, the pension entity may have several objectives, such as ensuring an adequate match between the pension plan assets and its liabilities and paying benefits upon the death or retirement of plan members and beneficiaries.

Some of the operational functions of the pension entity that should be identified and assigned include collection of contributions, record-keeping, actuarial analysis, funding and contribution policy, asset-liability management (or equivalent concepts in defined contribution plans), investment strategies, asset management, disclosure to plan members and beneficiaries, regulatory compliance and, where appropriate, financial education. These responsibilities and their assignment should be clearly stated in the pension entity's documents, and where outsourced, monitored via service level agreements.

As good pension fund governance should be 'risk-based', the division of responsibilities should reflect the nature and extent of the risks posed by the fund. For example, where funds adopt a sophisticated investment strategy, an investment sub-committee may be appropriate.

The role of the plan sponsor and the rights of the plan/fund members and beneficiaries with respect to the governance of the fund should be also clearly documented. Appointment of the governing body should be ruled by the pension entity's statutes and/or legal provisions. The plan sponsor may appoint some of the members of the governing body. Pension plan/ fund members and beneficiaries or their representative organisations may also play a role in appointing members of the governing body of the pension fund. If the plan is established as part of a collective agreement, the contracting trade union(s) have responsibility for the appointment of the governing body on behalf of plan/fund members and beneficiaries. Where the pension fund is established as an independent legal entity, some of the professional staff of this entity, such as actuaries and asset managers, may also be employees of or external advisors to the plan sponsor. However, in general, it should be the governing body's responsibility to appoint the professional staff and the external service providers of the pension entity.

When the pension fund is established as a separate account managed by financial institutions, their responsibilities should be clearly stated in the plan or contract documents. In occupational plans, plan sponsors should sign a contract with the financial institutions

	responsible for the management of the pension fund, where the objectives of the fund are also clearly stated. In personal plans, the contract is signed directly between the plan member and the financial institution.

Governing body

6.2	Every pension fund should have a governing body[3] vested with the power to administer the pension fund and who is ultimately responsible for ensuring the adherence to the terms of the arrangement and the protection of the best interest of plan members and beneficiaries. The responsibilities of the governing body should be consistent with the overriding objective of a pension fund which is to serve as a secure source of retirement income. The governing body should retain ultimate responsibility for the pension fund, even when delegating certain functions to external service providers. For instance, the governing body should retain the responsibility for monitoring and oversight of such external service providers. Appropriate oversight mechanisms should also be established where the governing body is a commercial institution.
	Additional Comments on Implementing Guidelines Pension funds are controlled by a governing body that is responsible for the operation and oversight of the pension fund. The governing body may also be responsible for other (or indeed all) aspects of the administration of a pension plan. This governing body may be a person, a committee or committees of persons (*e.g.* a board of trustees) or a legal entity. In a two-tier board system the managing board or body which is responsible for all strategic decisions is considered the governing body. In some countries various entities have fiduciary duties and may therefore be considered on a par with the governing body. In general, it is appropriate to split operational and oversight responsibilities, with the governing body focusing solely on strategic decisions and oversight functions. Operational tasks should be delegated to the pension entity's executive staff or a sub-committee and, where appropriate, external service providers. A separate supervisory board or oversight committee may be established whose main functions are the selection and oversight of the body in charge of strategic decisions. The supervisory board may have other responsibilities, and may, for example, appoint the auditor or actuary of the pension fund and control potential conflicts of interest. The supervisory board may form part of the internal governance structure of the pension entity (as in a two-tier board system) or it may be established externally. Its members may be elected by the plan sponsor and plan/fund members and beneficiaries. In pension funds established in the corporate form, the general meeting of plan/fund members and beneficiaries also exerts some oversight functions. On-going, independent oversight by such a supervisory board is especially advisable where the governing body is also a commercial institution. Though the governing body may delegate operational duties to the pension entity's internal staff or external service providers, it remains ultimately responsible for ensuring that pension funds fulfil their overriding objective which is to serve as the sources of funds for retirement benefits. In particular, the governing body should retain the responsibility for monitoring and oversight of those service providers, preferably via service level agreements. Core functions, such as formulating the investment policy and risk monitoring should also normally rest with

3. In a two-tier board system, involving a managing board and a supervisory board, the body which is responsible for all strategic decisions (usually the managing board) is considered the governing body.

	the governing body taking advice from subcommittees, though external advice may of course be requested. The governing body's main strategic and oversight responsibilities should include at least: • setting out the pension fund's key goals or mission, identify the main risks, and lay out the main policies, such as the investment policy – including the strategic asset allocation -, the funding policy, and the risk management policy; • monitoring the administration of the pension fund in order to ensure that the objectives set out in the fund by-laws, statutes, contract or trust instrument, or in documents associated with any of these, are attained (*e.g.* timely payment of pension benefits promised or targeted, adequate management of risks, including a diversified asset allocation, cost-effectiveness of administration, paying proper plan expenses from the fund, etc); • selecting, compensating, monitoring, and, where necessary replacing internal executive staff as well as external service providers (*e.g.* asset managers, actuaries, custodians, auditors, etc); in a two-tier board system the appointment of external service providers (*e.g.* actuaries, auditors) may be the responsibility of the supervisory board; • ensuring the compliance of the activities of the entity with the pensions law and other applicable statutes (*e.g.* investment regulations, reporting and disclosure requirements, control of conflicts of interest situations, improper use of privileged information, etc); With DC pension funds, additional key tasks of the governing body include ensuring that: (i) suitable investment choices are offered to members (including a suitable default fund), (ii) the performance of these funds is monitored, (iii) costs charged to members are optimised and disclosed in their disaggregated form, and (iv) members are offered guidance and where relevant projections on expected benefits. To enable the governing body to undertake its role effectively, safe-harbour rules may be appropriate. While the governing body should best serve the interest of the pension plan members and beneficiaries, it may also be required to avoid imposing an unnecessary financial burden on the plan sponsor (i.e. where the interest of plan members and beneficiaries could be equally best served through other means, which are more beneficial for plan sponsors). The expenses of administering the pension fund should be managed efficiently, and the governing body may be required to minimise the cost to employers where these expenses are borne exclusively by the plan sponsor.

Accountability

6.3	The governing body should be accountable to the pension plan members and beneficiaries and the competent authorities. Accountability to plan members can be promoted via the appointment of members of the governing body by pension plan members or their representative organisations. The governing body may also be accountable to the plan sponsor to an extent commensurate with its responsibility as benefit provider. In order to guarantee the accountability of the governing body, it should be legally liable for its actions which fail to be consistent with the obligations imposed on it, including prudence. In defined contribution plans,

	accountability calls for safe harbour rules that clarify the responsibilities and liabilities of the governing body.
	Additional Comments on Implementing Guidelines Accountability over governance functions is particularly important in order to allow the supervisory authority and the plan members and beneficiaries to discipline the governing body or seek other means of redress in case of mismanagement. The governing body may also be accountable to the plan sponsor to an extent commensurate with its responsibilities as a benefit provider. In order to guarantee the accountability of the governing body, it should be liable for its actions which are in breach of its duties. Such liability may include in some instances personal financial responsibility. In such cases, insurance of this liability can strengthen the ability of the pension fund to recover losses in case of mismanagement. In cases where the plan sponsor acts as the governing body or directs a third party provider in a DC plan, safe harbour rules may be appropriate to ensure that plan sponsors are accountable for their decisions but have a liability commensurate with the scope of those decisions. For instance, such rules can allow the plan sponsor to carry out due diligence in the choice and ongoing monitoring of service providers, investment alternatives and default options, whilst limiting his liabilities. The accountability of the governing body also requires: • regular meetings of the governing body; • diffusion of decision-making power in the governing body (for example, a requirement for decisions to be taken on a majority basis); • appropriate disclosure of the decisions reached in these meetings to affected plan members and beneficiaries; • regular reporting of important and significant information about the operation of the pension fund to the supervisory board, where relevant; • reporting of information about the operation of the pension fund to the supervisory authorities; • transparent selection mechanisms for the members of the governing body (including the possibility of appointments of representatives of plan members and beneficiaries through a fair selection system); • appropriate succession planning processes. Disclosure to plan members and beneficiaries may be required for plan changes that could have a material impact on future pension benefits, such as a material change in the plan terms or their application. In order to reduce the administrative burden on the governing body, disclosure could be made on a regular basis, for example, once a year, rather than after every meeting of the governing body. The selection and succession planning structure should deal with the term, appointment/election and removal of members of the governing body of the pension fund. The term of appointment of the members of the governing body may vary depending on the type and context of particular plans.

	Accountability to plan members and beneficiaries can be also enhanced by requiring representation of plan members and beneficiaries on the governing body. When the pension plan is established as part of a collective agreement, the nomination process normally involves the contracting trade unions. In some countries, paritarian representation of employers and employees in the governing body is required by law, ensuring that their respective points of view are represented. In other countries, labour laws governing union-management relations may prescribe when employee representation on pension funds is necessary. The appointment of independent professionals to the governing body is also an effective way to promote good governance. Election through a fair voting system (*e.g.* majority voting) is recommended in cases where plan members and beneficiaries can elect some of the members of the governing body. Biographical information on the member of the governing body seeking election should be provided to those involved in the selection process. The information should be provided in a timely manner and should be sufficient including age, length of time he/she has been associated with the pension fund, qualifications and experience. Having said this, existing associations of employees (*e.g.* trade unions) already have internal electoral systems in place which may make these additional elections redundant.

Suitability

6.4	Membership in the governing body should be subject to minimum suitability (or non-suitability) standards in order to ensure a high level of integrity, competence, experience and professionalism in the governance of the pension fund. The governing body should collectively have the necessary skills and knowledge to oversee all the functions performed by a pension fund, and to monitor those delegates and advisors to who such functions have been delegated. It should also seek to enhance its knowledge, where relevant, via appropriate training. Any criteria that may disqualify an individual from appointment to the governing body should be clearly laid out in the regulation.
	Additional Comments on Implementing Guidelines Members of the governing body should be subject to minimum suitability standards, such as "fit and proper" criteria. Causes of automatic disqualification could include conviction for fraud, theft or other criminal offences, and gross mismanagement of a pension or other fund that led to significant civil penalties, and, in some cases, personal bankruptcy. Each member of the governing body should also contribute to a balanced set of skills that enables the board, acting as a collective body, to execute successfully its obligations. For this purpose, the governing body may establish a template of the skills set needed and identify any gaps. The qualifications and experience required of the members of the governing body will depend on their responsibilities. It is advisable for at least some members to possess appropriate professional qualifications and experience to assist in some key decisions such the design of the investment strategy. In general, it is desirable that all members of the governing body have sufficient knowledge and experience to be able to understand the decisions of the professionals that operate the fund. Where the governing structure includes a general assembly of the plan members and beneficiaries (as is sometimes the case in pension funds set up in the corporate form), these would evidently not be subject to fit and proper criteria. The governing body should regularly review its collective skill set and consider whether it is adequate. Where relevant, it should seek to enhance its collective knowledge of pension fund matters via appropriate training, paid for by the pension entity. An annual skills inventory and training plan may be prepared for this purpose. In general, training is recommended both

	initially on appointment and on an on-going basis (at least every two years). Such training could be supported by pension fund regulatory or supervisory bodies (for example via free on-line courses, other material or approval of other education providers). Alternatively, the supervisory authorities may identify or approve suitable courses. More advanced training may be needed to ensure that the governing body fully understands investment in complex financial instruments.

Delegation and expert advice

6.5	The governing body may rely on the support of sub-committees and may delegate functions to internal staff of the pension entity or external service providers. Where it lacks sufficient expertise to make fully informed decisions and fulfil its responsibilities the governing body could be required by the regulator to seek expert advice or appoint professionals to carry out certain functions. The governing body should assess the advice received, including its quality and independence, and should verify that all its professional staff and external service providers have adequate qualifications and experience.
	Additional Comments on Implementing Guidelines Where it is appropriate to do so, the governing body should seek expert advice and may delegate functions to sub-committees of the pension entity, internal executive staff, or to external service providers. Some of the functions where the governing body may require external advice from consultants and other professional service providers include setting the investment and funding policies and asset-liability management. The governing body should have power and the ability to appoint, assess and remove such advisors. It should also take care not to rely exclusively on one source of information and ensure that the advice is independent / non-conflicted. The governing body may also delegate operational duties, such as asset management, record keeping, and benefit payment, to internal executive staff and / or professional service providers. It may also utilise the resources of the plan sponsor, though this may not always have qualified staff to carry out specific functions, such as actuarial analysis. The governing body should ensure that all its professional staff and, where appropriate, the external service providers have the relevant qualifications and experience required to carry out their functions in accordance with the objectives of the pension entity and the pension plan.

Auditor

6.6	An auditor, independent of the pension entity, the governing body, and the plan sponsor, should be appointed by the appropriate body or authority to carry out a periodic audit consistent with the needs of the arrangement. Depending on the general supervisory framework, the auditor should report promptly to the governing body and - if the governing body does not take any appropriate remedial action - to the competent authorities and other appropriate persons wherever he or she becomes aware, while carrying out his or her tasks, of certain facts which may have a significant negative effect on the financial situation or the administrative and accounting organisation of a pension fund.
	Additional Comments on Implementing Guidelines The auditor is responsible for reviewing the financial accounts for the pension plans and/ or

	the pension fund with an appropriate periodicity. The extent and frequency of the audit will vary depending on the nature, complexity, and size of the pension plan/fund. The auditor may also be in charge of verifying the controls relating to risk management and conflicts of interest. Auditors should also play also a "whistle-blowing" function. If, in the course of the exercise of their duties, they become aware of any significant threat to the financial position of a pension fund or its administrative and accounting organisation, they should promptly report to the governing body. If appropriate remedial action is not taken by the governing body, the auditor should report to the competent authorities and other appropriate persons. If appropriate remedial action is not taken, the auditor should also take this into account in the issuance of any audit opinion. The authorities or relevant professional bodies should issue guidance for auditors on the significance of actions of non-compliance with the pension fund statutes and/or current legislation. In some countries, some of the functions normally carried out by auditors may be carried out by other entities, such as the custodians. The independence of the auditor from the pension entity, the governing body, and the plan sponsor is important to ensure the impartiality of the audit. Normally, the auditor should be appointed by the governing body of the pension entity and in a manner consistent with fiduciary duties. In a two-tier board system the supervisory body may appoint the auditor. In some instances, the supervisory authority may appoint the auditor directly.

Actuary

6.7	An actuary should be appointed by the governing body for all defined benefit plans financed via pension funds. As soon as the actuary realises, on performing his or her professional or legal duties, that the fund does not or is unlikely to comply with the appropriate statutory requirements and depending on the general supervisory framework, he or she shall inform the governing body and - if the governing body does not take any appropriate remedial action - the supervisory authority and other appropriate persons without delay.
	Additional Comments on Implementing Guidelines The governing body should appoint an actuary for all pension funds that support plans where the plan sponsor insures the plan member against investment or/and biometric risk. In a two-tier board system the supervisory body may appoint the actuary. Even in defined contribution plans, however, an actuary with a limited role may be advisable, since investments should be made taking into account the adequacy of all retirement income assets. The actuary may not always be an employed member of the staff of the pension entity or the financial institution managing the fund. For example, the actuary may be employed directly by the employer or plan sponsor or he/she may be an external service provider (*e.g.* a professional actuary or a benefits consultant firm). Members of the governing body should not normally be appointed as pension plan/fund actuaries. Where the actuary is employed directly by the employer or plan sponsor, the possible conflict of interest should be properly managed. The role of the actuary should include at least the evaluation of the fund's present and future pension liabilities in order to determine the financial solvency of the pension plan following recognised actuarial and accounting methods. The actuary should also identify the funding needs for the pension plan, and estimate the level of contributions taking account of the nature of the liabilities of the pension plan. The actuary should also play a "whistle-blowing" function, and report to the governing body immediately when he or she realises that the fund does not or is unlikely to comply with the appropriate statutory requirements (*e.g.* minimum

	funding requirement). If the governing body does not take appropriate remedial action (*e.g.* establish a recovery plan to eliminate a funding deficit), the actuary should report to the competent authorities and other appropriate persons. If appropriate remedial action is not taken, the actuary should also take this into account in the issuance of any actuarial report or opinion. The authorities or relevant professional bodies should issue guidance on the significance of actions of non-compliance with the pension fund statutes and/or current legislation.

Custodian

6.8	Custody of the pension fund assets may be carried out by the pension entity, the financial institution that manages the pension fund, or by an independent custodian. If an independent custodian is appointed by the governing body to hold the pension fund assets and to ensure their safekeeping, the pension fund assets should be legally separated from those of the custodian. The custodian should not be able to absolve itself of its responsibility by entrusting to a third party all or some of the assets in its safekeeping.
	Additional Comments on Implementing Guidelines Where appropriate, it may be required that a custodian, different from the pension entity or the financial company that manages the pension fund, is appointed by the governing body of the pension fund. The appointment of an independent custodian is an effective way to safeguard the physical and legal integrity of the assets of a pension fund. The custodian holds the pension fund assets and should be in a position to ensure their safekeeping. They may also provide additional services such as securities lending, cash management, investment accounting and reporting, and performance measurement. In some cases, the custodian may also play an external whistleblowing function similar to that of the auditor with respect to, for example, the investment of pension assets.

Risk-based internal controls

6.9	There should be adequate internal controls in place to ensure that all persons and entities with operational and oversight responsibilities act in accordance with the objectives set out in the pension entity's by-laws, statutes, contract, or trust instrument, or in documents associated with any of these, and that they comply with the law. Such controls should cover all basic organisational and administrative procedures; depending upon the scale and complexity of the plan, these controls will include performance assessment, compensation mechanisms, information systems and processes, risk management procedures and compliance. The governing body should develop a code of conduct and a conflicts of interest policy for them and the staff of the pension entity as well as for any party with operational responsibilities. There should also be appropriate controls to promote the independence and impartiality of the decisions taken by the governing body, to ensure the confidentiality of sensitive information pertaining to the fund and to prevent the improper use of privileged or confidential information.
	Additional Comments on Implementing Guidelines The scope and complexity of internal control measures should be 'risk-based' and will vary according to the type and size of pension plan, fund and entity and the type and extent of risks faced. However, there are certain basic organisational and administrative procedures

that are central to risk management and control and sound business practice:

- Regular assessment of the performance of the persons and entities involved in the operation and oversight of the pension fund, particularly where the governing body is also a commercial institution;
- Regular review of compensation mechanisms, in order to ensure that they provide the correct incentives for those responsible for the operation and oversight of the pension fund;
- Regular review of information processes, operational software systems, and accounting and financial reporting systems;
- Identification, monitoring, and, where necessary, correction of conflicts of interest situations. A policy for dealing with conflicts of interest situations should be in place;
- Mechanisms to sanction the improper use of privileged information;
- Implementation of an adequate risk measurement and management system including effective internal audit
- Regular assessment of regulatory compliance systems

Mechanisms are needed to assess regularly the performance of the pension entity's internal staff as well as the external service providers (*e.g.* those providing consultancy, actuarial analysis, asset management, and other services for the pension entity). It is also good practice for the governing body to undertake self-analysis and for an independent, external person/organisations (or, where it exists, the supervisory board) to undertake a review of the internal controls of the pension entity and the performance of the governing body. The governing body could also restate annually that they are aware of the governance obligations and other key documents relating to the fund, that they are in compliance or have notified any potential conflicts.

Objective performance measures should be established for all the persons and entities involved in the administration of the pension fund. For example, appropriate benchmarks should be established for external asset managers. Performance should be regularly evaluated against the performance measures and results should be reported to the relevant decision maker, and, where appropriate, to the supervisory board, the supervisory authority, and the pension fund members and beneficiaries. The benchmarks should be reviewed regularly also to ensure their consistency with the pension fund objectives (*e.g.* the investment strategy).

Appropriate compensation can provide the right incentives for good performance. The establishment of a compensation committee and chairperson may optimise the process of evaluating the compensation of those responsible for the operation and oversight of the pension fund, such as asset managers, custodians, actuaries, as well as the members of the governing body.

The compensation policy of sales forces of pension plan providers may also warrant close scrutiny by the governing body, since these costs can reduce pension benefits significantly. There is a risk also that sales staff may not act in the best interest of plan members and beneficiaries, offering products that are not suitable for certain individuals. The governing body should therefore ensure that the remuneration structure for sales staff does not create distorted incentives or and lead to ill-advised decisions by consumers.

	A conflict of interest policy should be in place and members of the governing body and staff should regularly report compliance with these rules. Conflicts of interest situations should be identified and dealt with in a suitable manner. Conflicts should be disclosed and recorded in the minutes of the board, as should the role of third parties in settling policy/ strategy for the fund, including trading policies, and the commission and other fees paid by the fund. In certain cases, banning the concentration of functions in a single person or entity that would otherwise lead to a conflict of interests may be the preferred solution. In other cases, disclosure of the conflict of interest to the governing body may suffice, who should be required to monitor these cases closely. It may be in the fund's best interest to adopt policies which prevent even the appearance of a conflict of interests. One effective way of doing so is for the conflicted individual to abstain from voting on any decisions related to the matter of the conflict. Where the conflict involves a member of the governing body, the case should be reviewed and monitored by the members of it who are not conflicted. Where appropriate, the governing body may seek independent advice or guidance regarding the service or transaction. In the event of the governing body not being able to resolve a conflict of interest situation that may be judged by some of the members of the governing body as harmful to the interest of the plan members and beneficiaries, this should be reported to the supervisory board or supervisory authority, which will make a decision on whether they should be permitted, and if so under what conditions. In some cases, the supervisory authority may decide to appoint an independent professional to the governing body. The governing body should also establish appropriate controls to promote the independence and impartiality of the decisions taken - ensuring an equal treatment of all plan members -, ensure the confidentiality of sensitive information pertaining to the fund and prevent the improper use of privileged or confidential information. Employees of the pension entity may also be required to notify to the governing body any breaches of legislation, by-laws or contracts in the operational tasks that they are responsible for. A code of conduct should be established to implement these goals, requiring employees to observe high standards of integrity, honesty, and fair dealing. Internal review mechanisms may be put in place to verify and sanction the compliance with the code of conduct. An adequate risk measurement/management system and an effective internal audit should be also established. The risk management system should cover the main risks that a pension fund is exposed to, such as investment, biometric and operational risks. These control mechanisms form the basis of good business conduct, enhanced transparency, consistency as to management decisions, and for the protection of all stakeholders of the pension fund. Prudent risk management practices should also consider intangible risk factors such as environmental, political and regulatory changes, as well as the pension fund's potential market impact through its investment decisions. The risk management strategy should seek to proactively identify and explicitly balance short- and long-term, considerations. Finally, pension entities should have mechanisms to assess the compliance with the law. A compliance officer may be assigned to carry out this activity on a regular basis. Compliance assessment should include documentation related to functions that have been delegated to external service providers.

Reporting

6.10	Reporting channels between all the persons and entities involved in the governance of the pension fund should be established in order to ensure the effective and timely transmission of relevant and accurate information.
	Additional Comments on Implementing Guidelines Processes need to be put in place to ensure that the members of the governing body receive appropriate, timely, accurate, complete, consistent, and easily comprehensible information so they may discharge their responsibilities effectively, in accordance with the code of conduct, and ensure that delegated responsibilities are fulfilled. For its part, the governing body should ensure that actuaries, asset managers, consultants, custodians, and other professional service providers also receive relevant and accurate information in a timely manner in order to ensure they carry out their duties as assigned by the governing body.

Disclosure

6.11	The governing body should disclose relevant information to all parties involved (notably pension plan members and beneficiaries, plan sponsors, supervisory authorities, auditors *etc.*) in a clear, accurate, and timely fashion.
	Additional Comments on Implementing Guidelines The governing body should disclose relevant information to all parties involved (notably pension plan members and beneficiaries, the supervisory board- where relevant -, the plan sponsor, and supervisory authorities, *etc.*) in a clear, accurate, and timely fashion. The specific information that plan members and beneficiaries should receive is described in the OECD Guidelines for the Protection of the Rights of Members and Beneficiaries. In the case of pension funds that support personal pension arrangements, certain information (*e.g.* costs and investment returns) may also need to be disclosed to the public at large via appropriate mechanisms (*e.g.* websites and printed media). The governing body may also be required to disclose publicly if, and if so how, environmental, social, and governance considerations are taken into account in the investment policy. Two useful references in this regard are the OECD Guidelines for Multinational Enterprises and the OECD Principles of Corporate Governance.

Core Principle 7:
Supervision (IOPS Core Principles of Private Pension Supervision)

Effective supervision of pension funds and plans must be set up and focus on legal compliance, financial control, actuarial examination and supervision of managers. Appropriate supervisory bodies, properly staffed and funded, should be established in order to conduct when relevant off and on site supervision, at least for some categories of funds and in particular when problems are reported. Supervisory bodies should be endowed with appropriate regulatory and supervisory powers over individual plans, in order to prevent mis-selling cases arising from irregularities in the distribution and expenses methods.

7.1. Introduction

The Core Principles of Private Pension Supervision were published by the International Organisation of Pension Supervisors in 2006. The IOPS' Core Principles of Private Pension Supervision are presented in this section. A questionnaire designed by the IOPS to assist in the supervisory assessment process has been included in Appendix II.

IOPS Core Principles of Private Pension Supervision: Preamble

The main objective of private pension supervision is to promote, the stability, security and good governance of pension funds and plans, and to protect the interests of pension fund members and beneficiaries. Pension supervision involves the oversight of pension institutions and the enforcement of and promotion of adherence to compliance with regulation relating to the structure and operation of pension funds and plans, with the goal of promoting a well functioning pensions sector. In addition, achieving stability within the pension sector is an important part of securing the stability of the financial system as whole. Pension supervision should be mindful of financial innovation. Pension supervision should also pay attention to financial crime.

The provision of pensions is of fundamental economic and social importance, ensuring the successful delivery of adequate retirement income. The effective supervision of pensions, and of the institutions that provide pension products and services, is required to ensure the protection of consumers – a necessary task with any financial product being sold to non-professionals. Pension supervision is required to achieve the degree of

protection needed to support privately managed savings and is a means to help pensions adapt to market risks. Such risks can be particularly problematic with regard to pensions due to the unique characteristics of these financial products, such as:

- The long-term nature of the contract involved, and the subsequent requirement for incentives or even compulsion to overcome individual's 'myopia' towards long-term savings;
- their coverage of a wide social and economic range of the population (particularly where incentives or compulsion are applied);
- the low risk tolerance of pension members and beneficiaries, as subsistence rather than discretionary savings is often involved;
- the complexity of the products, involving tax issues, assumptions over future salaries, longevity, difficulty in the valuation of assets and liabilities *etc.* – a complexity which is beyond the financial literacy of most investors and which gives rise to asymmetrical information between pension providers or financial intermediaries and consumers;
- limited competition and choice, with decisions often made collectively by employers or unions;
- their potential impact on financial market and economic stability given their large and increasing size relative to financial markets and countries' GDP; and
- their 'social' as well as financial role, which is becoming more important as reforms in many countries have given an increasing role to private pensions (through tax incentives and other public policy), as aging populations are in some cases making social security an ever increasing burden on government resources, forcing public pensions to be reduced.

Consequently pension supervision faces unique challenges: in terms of breadth, including the number of pension funds or plans being supervised, the number of members and beneficiaries, the different types of pension products involved, and the fact that supervision may need to be coordinated across sectors due to the diverse nature of providers; as well as in the depth of supervision which is required, due to the vulnerability of members and beneficiaries and, in many cases, the mandatory nature of the system.

Though pension supervision has many unique aspects, the IOPS recognizes that many pension supervisors work in integrated financial

supervisory structures and it is therefore important that these principles are not inconsistent with international principles covering other financial service institutions. The IOPS will therefore strive to consult with other international organisations.

IOPS Core Principles of Private Pension Supervision: Scope and Coverage

The IOPS Principles for Pension Supervision are designed to cover occupational and personal pension plans and pension funds[4]. Pension supervision includes the monitoring of the activities of pension plans and funds to ensure that they remain within the requirements of the regulatory framework, essentially enforcing compliance with the rules[5]. Supervisory activities vary depending on the regulatory and legal environment, policy choices and a variety of other factors. In general they may be defined as influencing changes in pensions provision that contribute to the achievement of pension supervisory objectives, either through direct intervention or guidance. The scope of supervision can encompass any supervisory activity that is primarily concerned with ensuring the requirements and limitations imposed on pension funds or plans are adhered to[6]. Pension Supervisory Authorities referred to in the Principles are defined as any entity, responsible in whole or in part for the supervision of pension funds, plans, schemes or

4. Principles may not apply to those pension plans and pension fund in European Union countries which fall outside the scope of the Directive 2003/41/EC of the European Parliament and the Council of the 3 June 2003 on the activities and supervision of institutions for occupational retirement provision (for example pensions funded via book reserves). The Principles do not cover insurance contracts as such (although they may be used in both occupational and personal pension plans). Principles for the supervision of insurance is are provided by the International Association of Insurance Supervisors: 'Insurance Core Principles and Methodology' – see http://www.iaisweb.org/358coreprinicplesmethodologyoct03revised.pdf

5. Pension regulation encompasses all actions having the common objective of delineating the form, rules and standards that will define permissible organisations and activities, essentially establishing the parameters within which institutions will be required to function. Principles of pension regulation are provided by the OECD: 'Core Principles of Occupational Pension Regulation' – see http://www.oecd.org/dataoecd/14/46/33619987.pdf The IOPS Principles are drawn from and are compatible with OECD Core Principle 6 on Supervision.

6. As reflected in the IOPS by-laws, supervision mainly involves 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.

arrangements in a country or in the subdivision of a country, whether invested with its own personality or not. The Principles are designed to cover the different types of supervisory structure (specialized, partially integrated and integrated). Pension products also come in many different forms (defined contribution vs. defined benefit, mandatory vs. voluntary *etc.*) and the pension systems of countries also differ greatly, having been shaped by many factors (from the nature of the state, to the level of economic development, and the pension market structure). The IOPS has taken account of such diversity, and intends that these Principles identify good practice which can be applied universally.

7.2. Implementing guidelines for Core Principle 7 (IOPS Principles of Private Pension Supervision) and commentary

7.1	National laws should assign clear and explicit objectives to pension supervisory authorities.
	Additional Comments on Implementing Guidelines The principal strategic objectives of the pension supervisory authority should be clearly and publicly specified. They should include a focus on the protection of pension members and beneficiaries' interests. Objectives can also be directed towards the stability and security of pension funds and plans, the sustainability of the pension sector as a whole, the promotion of good governance and the encouragement of pension provision. The responsibilities of the pension supervisor should be clearly and objectively stated, giving a clear mandate and assigning specific duties. The objectives to which the Supervisor is subject and working should be clear to the supervisor and other stakeholders, and are appropriate for an effective supervisor of private pensions.
7.2	Pension supervisory authorities should have operational independence.
	Additional Comments on Implementing Guidelines Operational independence is taken to mean that at the day to day operational and decision making level the supervisory authority has autonomous management of its activities. At a higher, more policy orientated level, supervisory agencies may be subject to national governmental and political influences which are out of their control. There may be an intermediate stage where Ministerial approval is required for enforcement actions that involve removal or deregistration of an industry participant. The pension supervisory authority should have operational independence from both political authorities and commercial interference in the exercise of its functions and powers. To ensure independence, stability and autonomy are particularly required at the senior director level of the pension supervisory authority. The nomination, appointment and removal of the head of the pension supervisory authority should be done via explicit procedures and transparent mechanisms. The head of the authority may be appointed for a fixed term.

	The pension supervisory authority should also be funded in such a way as to ensure independence and there should be a transparent budgetary process. Supervisory acts should be over-ruled only by judicial decision, including tribunals with relevant powers, or by parliamentary process.
7.3	Pension supervisory authorities require adequate financial, human and other resources
	Additional Comments on Implementing Guidelines The Pension supervisory authority should be granted adequate staff and access to resources. The Authority should have its own budget sufficient to enable it to conduct proportionate, effective and independent supervision. Funding, in part or in full, of the Authority by supervised pension funds and plans could be considered, provided independence is maintained. The Authority should hire, train and maintain sufficient staff with high professional standards, including appropriate standards of confidentiality and disclosure (*e.g.* of interests in regulated entities). The directors and head of the Authority should be suitably qualified, with sufficient education, experience, capacity and reputation. If its own capacities are insufficient, or for other reasons deemed necessary, the Authority should be able to outsource to third parties (*e.g.* auditors, actuaries) supervisory tasks – though it remains responsible for the supervisory process and decisions. Where pension supervisory functions are outsourced to third parties, the Authority should be able to assess their competence, monitor their performance and ensure their independence from the pension fund or any other related parties. If required, the Authority must have the ability to take actions against these third parties, directly or through the appropriate professional body. The Authority's decision making and application of sanctions should not be outsourced.
7.4	Pension supervisory authorities should be endowed with the necessary investigatory and enforcement powers to fulfill their functions and achieve their objectives
	Additional Comments on Implementing Guidelines Pension supervisory authorities should be legally charged to undertake supervision and should be granted adequate powers and the capacity to exercise these powers. The pension supervisory authority should have the power to conduct necessary supervisory functions, according to the nature of the pension system being supervised. Effective supervision of pension funds or plans should focus on legal compliance, financial control, minimum capital requirements, investment activity, good governance and integrity, actuarial examination, the supervision of pension plan or fund managers, and the provision of adequate disclosure and information to members. Powers should allow for relevant off-site and on-site inspection. Pension supervisory authorities should have comprehensive investigatory and enforcement powers. On the suspicion of problems, they should have the power to conduct a full investigation, to oblige funds to submit documents and information, and to impose corrective measures and remedial actions if their orders are not obeyed –up to and

	including the power to impose administrative sanctions such as fines, the power to direct management, the power to revoke licences and the power to refer matters for criminal prosecution. In some cases, powers may include the ability to issue binding regulation.
7.5	Pension supervision should seek to mitigate the greatest potential risks to the pension system.
	Additional Comments on Implementing Guidelines The objectives of private pension supervision should be risk-based. Pension supervisory authorities should have a strategy for allocating their finite resources which targets mitigating actions on pension funds or plans which represent the highest risks to achieving the supervisor's objectives. This assumes that they understand the probability and impact of potential risks. Pension supervisory authorities should be pro-active, seeking to avoid significant problems before they occur and intervening, in a proportionate way, at as early a stage as possible and searching for those supervisory instruments which add most value to the desired supervisory result.
7.6	Pension supervisory authorities should ensure that investigatory and enforcement requirements are proportional to the risks being mitigated and that their actions are consistent
	Additional Comments on Implementing Guidelines The remedial actions and if necessary sanctions imposed by the pension supervisory authority should be proportional to the problem which is being addressed. In taking or promoting mitigating actions, pension supervisory authorities should choose between the powers available to them according to the assessed seriousness of the risk or compliance failure being addressed. The extent of supervisory demands placed on pension funds or plans and associated parties being supervised should be in accordance with the value expected to be derived. In fulfilling its supervisory powers, the pension supervisory authority should give pension funds and plans flexibility, where appropriate, in the way they achieve compliance with regulatory requirements. Supervisory decisions and intervention should be consistent, taking appropriately into account circumstances of each individual case. Supervisors should have procedures (for example, documentation, training and review) for ensuring that similar decisions are taken in similar circumstances and that these decisions are taken on objective and unbiased grounds.
7.7	Pension supervisory authorities should consult with the bodies they are overseeing and cooperate with other supervisory authorities
	Additional Comments on Implementing Guidelines The pension supervisory authority should consult, as appropriate, with the pensions sector when determining its approach to supervision. The pension supervisory authority is empowered to exchange information with other

	relevant supervisory authorities, subject to legal and confidentiality requirements. This includes cooperation with other authorities or departments involved in pension supervision both nationally and internationally (particularly where cross-border pensions are involved), as well as with authorities supervising other relevant financial institutions or markets and law enforcement agencies. Cooperation should be for both efficiency purposes (avoiding overlaps and promoting economies of scale and scope) as well as promoting pro-active preventative measures (*e.g.* tackling financial crime).
7.8	Pension supervisory authorities should treat confidential information appropriately.
	Additional Comments on Implementing Guidelines The pension supervisor should only release confidential information if permitted by law. The pension supervisor in regard to non-public information should when requested by the providing authority keep information confidential and maintain appropriate safeguards for the protection of confidential information within its possession. Where unsure of the status of the information, the supervisory authority should treat it as confidential if not publicly available or should check the status with the provider. If agreed by the providing authority, the receiving supervisory authority may pass on information to other supervisory bodies or law enforcement agencies with legitimate supervisory interests and equivalent confidentiality standards. Where staff transfer between the supervisory authority and the private sector, mechanisms should exist to ensure against the disclosure of confidential information. Third parties to whom the pension supervisory authority has outsourced supervisory tasks should be subject to the same confidentiality requirements as the staff of the pension supervisory authority itself.
7.9	Pension supervisory authorities should conduct their operations in a transparent manner.
	Additional Comments on Implementing Guidelines Pension supervisory authorities should adopt clear, transparent and consistent supervisory processes. The rules and procedures of the pension supervisory authority, and updates thereof, should be published. The pensions supervisory authority should generally operate in a transparent environment and should provide and publish a regular report – at least annually and in a timely manner – on the conduct of its policy, explaining its objectives and describing its performance in pursuing those objectives. The pension supervisory authority should be subject to regular audit and reporting requirements which allow for the assessment of how well the authority is fulfilling its responsibilities and ensuring the mandate and functions of the pension supervisory authority cannot be changed on an ad hoc basis. When directing the management of pension funds or plans pension supervisory authorities should explain to those affected why they are acting. Pension supervisory authorities should provide and publish clear and accurate information for the pension industry and the general public on a regular basis – such as the financial situation of the pension fund industry and observations on major developments in the pension sector. Disclosure will generally be on an aggregate basis, but could also be on

	individual pension funds, in which case the rules of confidentiality may be particularly relevant.
7.10	The supervisory authority should adhere to its own governance code and should be accountable.
	Additional Comments on Implementing Guidelines The pension supervisory authority should establish and adhere to a governance code, outlining suitable internal controls, checks and balances, and effective processes for risk and performance management. A code of conduct should be established and enforced in relation to all staff members. There should be clearly documented procedures for decision-making, with processes for referring decisions up to the appropriate level of seniority, reviewing and documenting decisions. For interventions with serious impact there should be some separation between those within the authority proposing interventions and those taking the final decision, so the scope for emergency action is balanced by a review process. Pension supervisory authorities should be clearly accountable for their general conduct and activity. Pension supervisory authorities should have accountability arrangements, which may vary according to specific country circumstances and which may include accountability to a range of bodies, from parliament to the members and beneficiaries of pension funds or plans. Procedures should be in place for the governing body of a pension plan or fund to appeal to the pension supervisory authority or relevant tribunal for decisions taken by the pension supervisory authority that affect them and which they consider inconsistent with legal provisions.

IV. Overall Assessment

This Methodology is intended to underpin an assessment that will identify the nature and extent of specific strengths and weaknesses of the private pensions systems in a jurisdiction in order to help identify reform priorities through policy dialogue so as to ultimately improve the performance of private pensions in delivering deferred remuneration and to provide security to plan members. The emphasis is on how the private pensions regulatory framework actually functions as a whole or as a system: the whole can be greater than the sum of the parts which is important to take into account when considering policy priorities.

This section of the paper deals with how all the Core Principles, Implementing Guidelines and associated assessments should be drawn together in a final assessment, including a discussion of policy priorities and specific measures that might be considered for the future. The final assessment would cover not just the assessed strengths and weaknesses of individual principles but also indicate how they serve to determine the operation and efficiency of the overall system of private pensions. In discussing policy priorities, the final assessment also needs to consider the presence of interrelationships whereby some policy measures might be ineffective until accompanied by other initiatives, either by companies or by the authorities.

The private pension governance landscape

In order to formulate a holistic final assessment, the reviewer will need to review all aspects of the pension system and consult with relevant authorities, as appropriate. The reviewer should pay particular attention to stakeholders' views on the following questions:

- Do stakeholders view that the private pension system adequately and efficiently provides deferred salary in retirement to current employees?

- Do stakeholders believe that the private pension system together with any additional state-provided pension benefits provide an adequate income level for pensioners?
- Do employers believe that employer-sponsored occupational pension plans are a powerful and efficient tool for recruiting and retaining employees?

Further, the reviewer needs to identify the nature and extent of any problems or issues within the private pensions system by considering the structure of private pensions, regulation, supervision, governance and control systems, and how these have become established and evolved in recent years. The reviewer should consider the forces underlying the current situation, the current forces for change, including international developments and their implications. To maintain transparency of the review process, the legal, regulatory and enforcement structures would be considered and the lessons drawn from any recent "scandals" discussed. In short, this element of the review process would identify how the major issues are arising and why the situation, covered in more detail as part of the assessment of some principles, has arisen.

Summarizing what has been learnt from the assessment of individual principles

In reporting the results of the overall final assessment, the reviewer needs to provide a summary of assessments for each Core Principle and the associated Implementing Guidelines together with the main reasons behind them. In some cases, it will be useful to specify which Implementing Guideline is the primary reason of a particular assessment result. Such a comprehensive process serves to make clear that the jurisdiction has been reviewed against the Core Principles as a whole, and minimises any chance of overlooking important elements. Not all Implementing Guidelines need to be covered in the same detail depending on a judgement about their importance.

The essential interrelationships between Core Principles and Implementing Guidelines should also be considered. The review should consider those areas where the jurisdiction is judged to have broadly or fully implemented a Core Principle, and indeed might have gone beyond the requirements of the Core Principles and is now developing "good practices". Areas of strength as well as weaknesses should be taken into account. Detailed assessments for each Core Principle and the corresponding Implementing Guidelines with brief notes may or may not form part of the final report depending in part on whether confidential information has been

used in forming an assessment. However, detailed assessments are an essential input for the reviewer in forming a judgement about priorities.

Forming a judgement about policy implications and priorities

This final, and arguably, most significant part of the process involves moving from the assessment stage as detailed in this Methodology to formulating future policy options and priorities. For the reviewer, a judgement that a principle is only partly or even not implemented carries by itself little information about the relative importance of any deficiencies. They key message to take from the assessment is a better understanding of what measures will be required going forward.

Developing future policy options and priorities requires a careful review of the results of this assessment and its identification of current strengths and weakness. The reviewer may refer to the experiences and lessons learned from other jurisdictions. Decisions about policy developments going forward must be fully considered in the context of the current state of the jurisdiction's system of private pensions, the recommendations of the Core Principles and a holistic understanding of the jurisdiction's goals and priorities for the future.

Appendix I.

Questions to assess a jurisdiction's private pension system

A list of questions has been compiled as an aid to the reviewer in the assessment process. The purpose of the questions is to gather relevant information and background material in order to be able to form a comprehensive understanding of the pension system in the jurisdiction to be assessed.

PRIVATE PENSION SYSTEM

A. Structure and operation of the pensions system (including both state and private pensions)

1. Overview of the State pension system and a brief historical review

a) Please give a general overview of the history of the State pension system in your country and describe any major reforms or intended reform proposals.

b) Please broadly describe the State pension system, the benefits that it provides and the method of financing (*e.g.* benefits are paid on a pay-as-you go basis out of general tax revenues).

c) What are the main challenges faced by the State pension system in your country?

d) What percentage of the working population is covered by the state pension system? What percentage of the elderly population receives benefits from the state pension system?

e) What is the average annual benefit received by a male pensioner from the State pension system? A female pensioner?

f) What is the expected pension benefit that a low-salary employee could expect from the State pension system as a percentage of final salary at retirement after a full-career? A mid-salary employee? A high-salary employee? (*e.g.* A mid-salary employee could expect to receive a total pension benefit from the State pension system of roughly 30% - 40% of final salary at age 65, after 35 years of contributions.)

g) What annual contributions do employers and employees, respectively, make to the State pension system as a percentage of salaries? Are there any other sources of contributions?

h) Have there been any recent official projections of the future evolution of the finances of the State pension system? In particular, have there been any official appraisals of the risks to long-run budgetary sustainability of the state pension system from the impact of demographic change on welfare and public sector pension spending? Please summarize the main conclusions of such projections.

2. Overview of the private pension system and a brief historical review

a) Are private pensions in your country mandated by law or collective agreements or are they voluntary? Are private pensions in your country provided mainly via personal pension plans or via company-sponsored occupational pension plans?

b) Give a general overview and history of the private pension system in your country.

c) Describe any major recent private pension system developments.

d) Are any expected reform measures to the private pension system under consideration in your country?

e) What is the role (past and future) of the private pensions system in the economy?

f) What are the main challenges faced by the private pension system in your country?

3. Profile of the private pension industry

a) Please provide recent statistical information (preferably as of December 2007) on the private pension system following the format in the Global Pension Statistics questionnaire. Any supplementary statistical information can be provided. In particular, it would be helpful to receive historical data showing the evolution of the private pension system and any official projections on its future development.

b) What is the percentage of companies that provide an occupational pension plan to its employees and/or contributes to its employees' personal pension plans? Also, what generally determines if a company sponsors an occupational pension plan and/or contributes to its employees' personal pension plans? (*e.g.* Private pension plans are required for most industries due to collective agreements; or, private pension plans are provided on a voluntary basis, but are generally considered necessary by companies in order to be a competitive employer.)

c) What is the percentage of the country's workforce that is covered by a private pension plan (occupational and/or personal pension plan), including a breakdown of the coverage percent within the following subcategories:

   i) Male / female

   ii) Age 20 – 35 / age 35 – 50 / age 50 and up

   iii) Low pay / mid-level pay / high pay

   iv) Blue-collar workers / white-collar workers / executives

d) What are the average administration costs of the private pension system and what are the main sources of these costs? (*e.g.* investment management fees, administration, marketing/distribution, *etc.*) How have these costs evolved in recent years? Please express administration costs in absolute amounts and as a percentage of assets under management.

e) What has been the investment performance of pension assets in recent years?

f) What is the prevalence of private pension plans funded using the following funding vehicles:

   i) Company-specific pension funds

   ii) Industry-wide pension funds

   iii) Insurance company funding

   iv) Pay-as-you-go funding

   v) Company book-reserves

   vi) Individual employee savings accounts in pension funds sponsored by an employer

   vii) Individual employee savings accounts / personal pension plans within retail pension funds offered by financial institutions

   viii) Other (please describe)

g) Have there been any major insolvencies of pension funds or pension plan wind-ups in recent years? If so, please describe?

h) Have there been any major cases of fraud, abuse or gross mismanagement of pension funds in recent years?

4. Typical plan design

a) Please indicate the prevalence of private pension plans that can be described as follows (as a percent of all plans and as a percent of all pension plan members):

   i) Personal pension plans

   ii) Occupational defined benefit pension plan

   iii) Occupational defined contribution pension plan

   iv) Occupational hybrid pension plan (*e.g.* cash-balance pension plan)

   v) Other (please describe)

b) Many countries have experienced a significant shift from traditional defined benefit plans to hybrid or defined contribution plans in recent years. Has this shift taken place in your country? If so, what

particular issues or challenges have arisen as of this shift? How have regulatory and supervisory bodies responded to this shift?

c) Describe how pension plan benefits are generally paid out. Also, what is the prevalence of the following forms of payment within pension plans in your country?

   i) Life-time annuity

   ii) Temporary annuity (for example, benefits are paid from age 65 to age 75)

   iii) Lump sum payment

   iv) Programmed withdrawals

   v) Other (please describe)

d) Is there a typical design for a private pension plan? If so, please describe.

e) What is the expected pension benefit that a mid-salary employee could expect from a typical private pension plan in your country as a percentage of final salary at retirement after a full career? (*e.g.* A mid-salary employee could expect to receive a total pension benefit from private pension plans of roughly 30% - 40% of final salary at age 65.)

f) Are benefits from private pension plans typically integrated with benefits from Social Security? If so, please describe how the benefits are integrated?

g) Are employer and/or employee contributions generally required in the private pension plans? If so, what are typical levels? (*e.g.* Employees typically contribute 3% - 4% of salary to the private pension plan.)

h) Are benefits typically indexed?

   i) During retirement?

   ii) During deferment?

   iii) If so, then what is the typical indexation level? (*e.g.* inflation, average salaries, excess investment returns, *etc.*)

i) What spouse and/or orphan benefits are typically provided by a private pension plan?

j) Do defined contribution plans in your country offer individual investment choice to plan members? If so, what kinds of options are generally available? Is there a default investment option for members who do not exercise a choice, and if so, what is it?

k) What types of institutions are the main providers of pension plan administration? Custodianship of assets? Payments of annuities? (*e.g.* employers, insurance companies, banks, mutual funds, *etc.*)

5. Taxation

a) How are pension benefits taxed for pension plan participants? (*e.g.* benefits are taxed when they are accrued, or benefits are taxed when they are paid out in retirement, *etc.*) How does this tax treatment compare to the taxation of other forms of compensation?

b) How are contributions to pension funds and/or balance sheet provisions taxed for companies sponsoring private pension plans?

c) How are investment returns on pension fund assets taxed?

6. Financial education

a) Is the level of financial education of pension plan members generally seen as an issue or challenge in your country?

b) What financial education programs are currently available in your country aiming to build financial knowledge and improving awareness about private pension plans? Who generally provides this financial education? (*e.g.* the employer, the State, insurance companies, *etc.*) Do any special financial education rules apply to defined contribution plans?

c) Describe any formal initiatives that have been taken in your country to improve the financial education of plan members?

d) Are there any performance metrics in place to gauge the effectiveness of financial education? If so, please describe.

B. Regulatory and supervisory system

1. Conditions for effective regulation and supervision

a) Summarize the main legal provisions that regulate the operation of private pension plans. (Please state whether the various summarized regulations apply to company-sponsored occupational plans or personal pension plans). In particular, describe how these legal provisions address the following issues:

   i) The protection of pension plan members and beneficiaries and the soundness of pension funds.

   ii) The efficient operation of private pension plans.

   iii) The oversight and the enforcement of legal requirements.

b) Describe any regulatory initiatives under consideration, especially initiatives that relate to OECD's Core Principles on private pension plans?

c) Describe the accounting standards required for companies sponsoring private pension plans. In particular, describe how they compare or differ from international accounting standards.

d) Describe any competition policies applied to the private pension industry.

e) Describe to what extent and how private pension regulations account for the state of development of financial markets.

2. Establishment of pension plans, pension funds, and pension fund managing companies

a) Describe major criteria, standards, or legal requirements for the licensing or registration of pension entities in your country. What is the process for the licensing or registration of pension entities? What is the role of the licensing authority in supervisory matters?

b) What types of governing documents are required of pension entities?

c) What types of risk control mechanisms are required by pension entities in order to address investment, operational and governance risks? What internal reporting and auditing mechanisms are required?

d) Describe the requirements for pension entities to have a funding policy and an investment policy.

e) Describe the requirements for a governing body for the pension entity.

f) How are the members of the governing body chosen?

g) What types of qualifications or experience requirements are required of the members and of the governing body as a whole?

h) How are potential conflicts of interest of the members of the governing body addressed?

i) What are the minimum capital requirements of pension entities to be licensed (exclusive of start-up costs)?

j) Are pension entities required to have a business plan and if so what does this business plan need to contain?

k) What are the circumstances, regulations and procedures with respect to license withdrawal for pension entities?

3. Pension plan liabilities, funding rules, winding up and insurance, and the related defined benefit regulatory system

a) Are pension plans required to be fully funded at all times? If not, then what percentage of pension plan liabilities is required to be funded?

b) Do pension assets need to be invested with an external provider or can they be held within the company in a segregated account?

c) Is there some type of external credit insurance or government fund to safeguard against the insolvency of a pension plan or a pension entity? If so, please describe.

d) Describe the funding requirements for private pension plans with defined benefit elements. Describe the funding requirements for private pension plans with defined contribution elements.

e) What types of contribution requirements are made for underfunded pension plans?

f) Under what circumstances are sponsors of funded private pension plans entitled to recover pension fund surplus?

g) Describe the requirements for the actuarial assessment of pension plan liabilities for funding purposes.

h) How are pension assets measured for purposes of determining the funding level of a pension plan? (*e.g.* market value)

i) How frequently does a full actuarial valuation of the pension plan's liabilities and a pension plan's funding status need to be made?

j) Is there a formal and required qualification process for the actuaries undertaking these calculations? If so, please describe the process.

k) Describe the funding process for the wind-up of a private pension plan.

4. Asset management

a) Please describe the investment regulation that applies to private pension plans.

b) How do these regulations reflect the concept of the "Prudent Person" standard?

c) Describe any investment limits for pension funds? (*e.g.* Are there limits on investment in foreign assets or in certain asset classes.)

d) Is there a limitation on self-investment for the pension fund? If so, please describe?

e) Describe any formal diversification requirements? (*e.g.* Are there any limits on investment in single issues or issuers?)

f) Describe any specific valuation rules that apply to pension fund assets?

g) What are the regulations as to pension funds having investment policies, a risk management process, and other such governance and risk control measures?

h) Are the pension plan fund assets required to be separate from the assets of the sponsoring company?

5. Rights of members and beneficiaries and adequacy of benefits

a) Describe any different or particular rules with respect to membership of private pension plans that apply to employees based on non-economic criteria such as age, gender, marital status or nationality? To what extent are different or particular rules such as these legally allowed within private pension plans?

b) Are certain types of employee groups allowed to be excluded from private pension plans? (*e.g.* part-time or seasonal employees?)

c) Is there a maximum waiting period for employees before they are entitled to join their company-sponsored private pension plan?

d) Under what conditions are accrued pension benefits allowed to be reduced within private pension plans?

e) What legal protections are given to accrued pension benefits in the case of a merger or acquisition, sponsoring-company insolvency, fraud, pension fund mismanagement, or some other major event?

f) What is the priority status of pensioners and beneficiaries in the event of a pension plan bankruptcy?

g) Over what period of time are benefits typically fully vested? (*e.g.* after 5 years, immediately, *etc.*)

h) Is there a maximum allowed vesting period within a private pension plan? If so, what is it?

i) Describe what happens to an employee's vested accrued pension rights if the employee leaves service with the sponsoring company prior to retirement.

j) What legal rights to plan participants have to basic information about the pension plan such as plan provisions, vesting schedules, investment policies, service providers, etc?

k) If a plan participant leaves, is he or she legally entitled to be notified of his or her accrued pension rights?

l) Describe what redress mechanisms and/or legal assistance are available to plan members in the case of a conflict, violation or denial of plan member rights. Describe the claims process, and in particular, if and how it is transparent, expeditious and independent.

m) In defined contribution pension plans:

i) Are members allowed to direct their own investments?

ii) If so, what legal requirements are there to the number of funds available, their diversity and their risk profile?

iii) If members are not allowed to direct their own investments, what are the legal requirements for the types of investments that are made with the employees' defined contribution savings accounts?

iv) What requirements are there for providing information regarding investment choices, fees, portfolio composition, historical performance, etc?

v) What legal requirements are there for the sponsoring company to provide financial education to the employees?

n) Describe members' ability to designate heirs/beneficiaries for their pension benefits and provide examples.

6. Governance

a) Describe the governance structure of a private pension plan. In particular, what is the structure of operational and oversight responsibilities. How are accountability and suitability ensured? (*e.g.* legal liability, board composition requirements, "fit and proper" rules)

b) Is an independent and qualified auditor required to audit the pension plan?

c) Is an independent and qualified actuary required to assess the funding and accounting status of the pension plan?

d) Is an independent custodian required to maintain the safety of the pension plan fund assets?

e) What controls are required to be in place to ensure that all persons and entities with operational and oversight responsibilities act in accordance with the objectives set out in the pension entity's by-laws, statutes, contract, or trust instrument, or in documents associated with any of these, and that they comply with the law?

f) What requirements are there for disclosure of relevant information to pension plan members, beneficiaries, and supervisory authorities?

7. Supervision

(In answering the following questions, reference may be made to the standards of the IOPS if so desired and if relevant.)

a) Describe the mandate, organisation, objectives and responsibilities of the pension supervisory authority as decreed by national law.

b) Describe how and to what extent pension supervisory authorities have operational independence. Further, describe the governance structure of the pension supervisory authority.

c) Describe the financial and staffing resources of the pension supervisory authority, as well as the qualifications of its leadership and staff.

d) Describe the investigatory and enforcement powers of the pension supervisory authority. Describe how these powers are made proportional, consistent, yet flexible to the various situations that could arise in the course of their supervisory duties.

e) How does the pension supervisory authority seek to mitigate the big potential risks to the pension system? How does the pension supervisory authority engage with pension entities and other supervisory bodies in mitigating these risks?

f) Describe the laws and practices governing how the pension supervisory authority treats confidential information. What laws and practices are in place to ensure that their operations are conducted in a transparent manner?

8. Anti-money laundering and combating the financing of terrorism

Please describe, if and how, your country regulatory regime and private pension funds deal with money laundering and financing of terrorism activities?

C. Other information

1. Assessments carried out by multilateral organisations of the private pension system, such as those that may be have been carried out as part of the IMF and World Bank's Financial Sector Assessment Programme.

2. Please provide a copy of any self-assessment exercise conducted in respect of *the IOPS Principles of Private Pensions Supervision*.

3. Main and key laws, decrees and other regulations on the private pension system if available in one of the official OECD languages.

4. Parliamentary reports and ministerial white papers on the private pension system.

5. Information on any other aspect of the broader policy framework, including tax, competition, social and labour policy, trade and other policy areas which may have a direct impact on the private pension system.

Appendix II

Questions to assess the supervision of a jurisdiction's private pension system

A list of questions has been compiled as an aid to the reviewer in the assessment process. These questions were designed by the IOPS specifically to aid the reviewer in the assessment of a jurisdiction's supervision of its private pension system.

Principle 1: Objectives - National laws should assign clear and explicit objectives to pension supervisory authorities.

The principal strategic objectives of the pension supervisory authority should be clearly and publicly specified. They should include a focus on the protection of pension members and beneficiaries' interests. Objectives can also be directed towards the stability and security of pension funds and plans, the sustainability of the pension sector as a whole, the promotion of good governance and the encouragement of pension provision.

The responsibilities of the pension supervisor should be clearly and objectively stated, giving a clear mandate and assigning specific duties.

Key considerations for the review:

The review needs to determine whether the objectives to which the Supervisor is subject and working are clear to the supervisor and other stakeholders, and are appropriate for an effective supervisor of private pensions.

Assessment Questions:

1.1.	Is there governing legislation providing for a pension supervisor,	
1.2.	Does the legislation provide objectives?	
1.3.	If not, have objectives been specified by the	

Executive or Legislature in a way that is public, binding and can only be changed through transparent due process? 1.4. Are these objectives high level, related to desired outcomes and covering some (at least) of the subjects referred to in the text of the Principle? 1.5. Does legislation, or other public documents, explicitly and clearly set out responsibilities and duties for the Supervisor? 1.6. Has the Supervisor explicitly stated the objectives, responsibilities and duties it believes to be working to, including in its strategy documents, and are these statements consistent with the answers to the above questions? 1.7. What impact would any planned changes to the objectives have on the answers to the above questions?	
Overall assessment (with reasons):	
Suggested recommendations:	
Types of supporting evidence	
• Governing legislation for the Supervisor • Concordats, memoranda of understanding and other documents produced by the Executive or Legislature applying to the Supervisor • Governmental statements on the responsibilities and duties of the Supervisor • Strategies or plans produced by the Supervisor • The Supervisor's annual reports • Information on how the Supervisor interprets its objectives	

Principle 2: Independence - Pension supervisory authorities should have operational independence

The pension supervisory authority should have operational independence from both political authorities and commercial interference in the exercise of its functions and powers.

To ensure independence, stability and autonomy are particularly required at the senior director level of the pension supervisory authority. The nomination, appointment and removal of the head of the pension supervisory authority should be done via explicit procedures and transparent mechanisms. The head of the authority may be appointed for a fixed term.

The pension supervisory authority should also be funded in such a way as to ensure independence and there should be a transparent budgetary process.

Supervisory acts should be over-ruled only by judicial decision, including tribunals with relevant powers, or by parliamentary process.

Key considerations for the review:

Operational independence is taken to mean that the supervisor has autonomous management of its activities at the day to day operational and decision making level. At a higher, more policy-oriented level, supervisors, who are after all unelected, need to act consistently with broad government objectives, may properly be subject to national governmental and political influences, and should take account of the views of other stakeholders. There may be an intermediate stage where Ministerial approval is required for enforcement actions that involve removal or deregistration of an industry participant.

The review needs to determine whether the Supervisor is sufficiently isolated from improper influence from government, politicians and supervised entities. In doing so, it should look for any significant ways in which such parties can influence day to day decisions, for instance through meaningful threats of negative consequences for the supervisor were a decision to go a particular way, or through the abuse of accountability mechanisms.

Assessment Questions:

2.1	Is the Supervisor legislatively (or by some other robust means) established as a body with operational independence from the Executive?	
2.2	Are there sufficient and effective restrictions on the ability of the government and other parties to make directions to the Authority, especially if they conflict with its mandate?	
2.3	Do the procedures for nominating, appointing the head and other senior members of the Authority provide for transparency and independence, for instance, through specified fit and proper' tests or minimum qualifications or experience requirements?	

2.4 Are senior members of the Authority appointed for specified terms and would termination of the member within the term be used as a mechanism to influence operational decisions? 2.5 Have the procedures in 2.3-2.4 been applied, and seen to be applied, in practice? 2.6 Does the Authority have a legally established budget established through a due process that provides short term financial security and hence operational independence? 2.7 Where the Authority is funded by a levy on supervised entities, is this free from any interference by the entities? 2.8 Can supervisory acts be over-ruled only through due judicial, quasi-judicial or legislative process, and have there been any exceptions? 2.9 Are there indemnities from the prosecution of the Authority's directors or staff or to cover any costs or penalties so incurred, and are these effective in preventing or mitigating the impact of civil actions against the Authority? 2.10 Are the circumstances, if any, in which supervisory decisions on licensing or registration can be influenced by government clearly specified and transparent? 2.11 Does the Supervisor withhold from all external parties details relating to day to day decisions that are pending, so as to reduce the possibility of external influence? 2.12 Has the Supervisor been free in practice from undue external influence in relation to operational matters? 2.13 What impact would any planned changes affecting the Supervisor have on the independence of the supervisor?	
Overall assessment (with reasons):	
Suggested recommendations:	

Types of supporting evidence

- Governing legislation for the Supervisor
- Concordats, memoranda of understanding and other documents produced by the Executive or Legislature applying to the Supervisor
- Information on reporting lines and accountability to government
- Structure and responsibilities of governing body (or equivalent) including split between executive and non-executives, whether the CEO is also Chair, representational nature of non-execs, lengths of terms of appointment and limitations on re-appointment.
- Information on nomination and appointment processes
- Information on background of, and recent changes to, senior members of the Authority
- Descriptions of budgetary processes
- Information on how any levy on supervised entities is set.
- Details of any indemnities and the prevalence of civil actions taken against the Authority
- Details of the licensing/registration regime operated by the Supervisor
- Details of any particularly robust actions taken by the Supervisor
- Perceptions of the extent of independence in practice

Principle 3: Adequate Resources - Pension supervisory authorities require adequate financial, human and other resources

The Pension supervisory authority should be granted adequate staff and access to resources.

The Authority should have its own budget sufficient to enable it to conduct proportionate, effective and independent supervision. Funding, in part or in full, of the Authority by supervised pension funds and plans could be considered, provided independence is maintained.

The Authority should hire, train and maintain sufficient staff with high professional standards, including appropriate standards of confidentiality and disclosure (*e.g.* of interests in regulated entities).

The directors and head of the Authority should be suitably qualified, with sufficient education, experience, capacity and reputation.

If its own capacities are insufficient, or for other reasons deemed necessary, the Authority should be able to outsource to third parties (*e.g.* auditors, actuaries) supervisory tasks – though it remains responsible for the supervisory process and decisions. Where pension supervisory functions are outsourced to third parties, the Authority should be able to assess their competence, monitor their performance and ensure their independence from the pension fund or any other related parties. If required, the Authority must have the ability to take actions against these third parties, directly or through the appropriate professional body. The Authority's decision making and application of sanctions should not be outsourced.

Key considerations for the review:

The review needs to determine whether there are transparent and effective processes aimed at ensuring that the Supervisor is sufficiently resourced to discharge its mandate effectively. The allocated resources may be less than the level desired by the Authority, but if this is so the Authority should still be satisfied, and satisfy the reviewer, that it can discharge its mandate effectively. Implicit in this is some process for determining what resources (number and skills) are needed. A particular issue to watch is whether the Authority is able to engage (in-house or through contract) experts of sufficient calibre to make properly informed decisions and sustain its credibility.

Assessment Questions:

3.1	Do the (budgetary) arrangements for funding the Supervisor reflect in a transparent manner how it needs to discharge its responsibilities?	
3.2	Does the Supervisor have longer term financial perspective (e.g 3 years or longer) that provides some stability for planning and recruitment?	
3.3	Has the Supervisor been funded to enable it to discharge its primary responsibilities at or above a level that the supervisor considers to be the defensible minimum?	
3.4	Is the Supervisor free from constraints on the number (or identity) of staff it can hire, and the amount it can pay, that prevent it from achieving its plans?	
3.5	Is the Supervisor able to obtain sufficient resources in expert disciplines?	
3.6	Does the Supervisor have processes intended to ensure that staff have necessary skills, competencies and independence?	
3.7	In particular, are senior staff appropriately qualified and of sufficient stature?	
3.8	Can the Supervisor outsource functions in support of its supervisory responsibilities where it deems it necessary or where in-house resources are insufficient?	
3.9	If so, does it have appropriate processes to oversee these functions, that secure satisfactory and proper performance and ensure that the ultimate supervisor decision is taken by the Authority?	
3.10	What impact would any planned changes to the way the supervisor is resourced have on the answers to the above questions?	

Overall assessment (with reasons):

Suggested recommendations:

Types of supporting evidence

- Information on reporting lines and accountability to government
- Descriptions of budgetary processes
- Information on budget allocated compared with proposals made by the supervisor or its calculations of what is needed as a minimum
- Size of budget for pension supervision relative to the number of supervised entities and value of funds under management
- Human resource policies covering recruitment, training, assessment and conflicts of interest.
- Information on senior members of the Authority
- Numbers (full time equivalents) and qualifications of staff involved with or supporting pension supervision
- Information on the scope and extent of outsourcing, and how the Supervisor oversees any outsourced supervisory functions
- Representations as to the adequacy of resourcing in practice

Principle 4: Adequate Powers – Pension supervisory authorities should be endowed with the necessary investigatory and enforcement powers to fulfil their functions and achieve their objectives

Pension supervisory authorities should be legally charged to undertake supervision and should

be granted adequate powers and the capacity to exercise these powers.

The pension supervisory authority should have the power to conduct necessary supervisory functions, according to the nature of the pension system being supervised. Effective supervision of pension funds or plans should focus on legal compliance, financial control, minimum capital requirements, investment activity, good governance and integrity, actuarial examination, the supervision of pension plan or fund managers, and the provision of adequate disclosure and information to members. Powers should allow for relevant off-site and on-site inspection.

Pension supervisory authorities should have comprehensive investigatory and enforcement powers. On the suspicion of problems, they should have the power to conduct a full investigation, to oblige funds to submit documents and information, and to impose corrective measures and remedial actions if their orders are not obeyed –up to and including the power to impose administrative sanctions such as fines, the power to direct management, the power to revoke licences and the power to refer matters for criminal prosecution. In some cases, powers may include the ability to issue binding regulation.

Key considerations for the review:

The review needs to determine whether the Supervisor has sufficient powers to discharge its mandate effectively. In doing so, it should consider whether the powers cover all elements of the Supervisor's mandate include a sufficient range to enable responses to be targeted to the seriousness of the problem and can be used effectively in practice. Where the supervisor licences pension entities this can potentially provide strong powers to promote the good running of pension plans, and the review should look for substantive compliance with the OECD/IOPS Licensing Guidelines as they relate to supervision.

Assessment Questions:

4.1	Are the Supervisor's powers clearly established by its governing legislation?	
4.2	Is the Supervisor empowered to obtain the information it needs?	
4.3	Does the Supervisor have sufficient powers to investigate potential problems and conduct supervision on and off site, without being constrained by reliance on others?	
4.4	Are the responsibilities of supervised entities sufficiently defined in legislation to enable the Supervisor to meet its objectives by enforcing them?	
4.5	Is the Supervisor empowered to act to resolve breaches of the responsibilities of supervised entities?	
4.6	Where the supervised entities' responsibilities, or the Supervisor's powers to enforce them, are insufficient, is there a process available (and used) for the Supervisor to seek appropriate changes?	
4.7	Is there a clear licensing or registration process that enables the Supervisor (if the licensing authority) to obtain sufficient information and to reject/revoke/amend the licence/registration of a seriously non-compliant entity (or sufficiently involves the supervisor where it is not the licensing authority)?	
4.8	Can the Supervisor enforce legislation relating to funding and capital adequacy, so far as appropriate (including any reserves that need to be held by DC funds)?	
4.9	Can the Supervisor enforce legislation relating to the governance of supervised entities, including fitness and propriety?	
4.10	Do the Supervisor's powers include measures to correct and remedy problems as well as an	

appropriate range of sanctions (e.g fines)? 4.11 Is the Supervisor empowered to take control of or appoint new management to a supervised entity in serious difficulties? 4.12 Has the Supervisor successfully used a range of its powers? 4.13 Where the Supervisor has not used significant powers, is this because the necessity has not yet arisen and does it have the capacity to use them where necessary? 4.14 Where powers have proved to be too unwieldy or costly to use in most cases, has the Supervisor successfully implemented alternative approaches? 4.15 What impact would any planned changes to the Supervisor's powers have on the answers to the above questions?	

Overall assessment (with reasons):

Suggested recommendations:

Types of supporting evidence

- Governing legislation
- The Supervisor's enforcement policies.
- The Supervisor's role in the process for licensing or registering pension entities and information on licences or registrations rejected, amended or revoked.
- Information on the Supervisor's inspection programme(s)
- Information on actions (including enforcement) taken by the Supervisor in response to problems at supervised entities.
- Representations made as to adequacy of powers in practice

Principle 5: Risk Orientation -Pension supervision should seek to mitigate the greatest potential risks to the pension system

The objectives of private pension supervision should be risk-based. Pension supervisory

authorities should have a strategy for allocating their finite resources which targets mitigating actions on pension funds or plans which represent the highest risks to achieving the supervisor's objectives. This assumes that they understand the probability and impact of potential risks.

Pension supervisory authorities should be pro-active, seeking to avoid significant problems before they occur and intervening, in a proportionate way, at as early a stage as possible and searching for those supervisory instruments which add most value to the desired supervisory result.

Key considerations for the review:

As the relevant IOPS working paper states: "Risk-based supervision specifically attempts to vary the scope and intensity of supervision according to the level of risk to which individual pension funds are estimated to pose (in regard to the individual members and beneficiaries of the pension fund and also to the pension fund itself). This is seen as a more 'sophisticated' approach than the former 'compliance' based attitude to supervision, where all pension funds are treated the same. A risk based approach allows scarce supervisory resources to be targeted at the pension funds which are seen to be at most risk and allows supervisors to take a more proactive approach, attempting to avoid potential problems before they occur. A broad definition of risk-based supervision would include the whole risk management architecture, including risk-based regulations and risk-based supervisory procedures. A narrower definition would consider only the supervisory part of the overall risk management architecture."

The review needs to determine whether the supervisor has moved towards some form of risk orientation appropriate to its circumstances and objectives. In doing so, it is important to recognise that the way risk orientation is implemented can vary substantially, as indicated above, reflecting local circumstances. Risk orientation can potentially encompass supervisory objectives, its strategic resource allocation, the way it seeks to focus on the identified risks, reliance on entity risk management, the use of risk assessment or scoring models or applying quantitative risk-based models to assess compliance. It would be unusual, however, to find all these approaches in any one supervisor.

Assessment Questions:

4.16 Are the Supervisor's objectives (mandated and operational) risk-based, for instance being focused on risk mitigation or outcomes, rather than, or as well as, compliance?	
4.17 Does the Supervisor have a robustly based strategy for allocating resources to the highest risks so as to achieve its objectives?	
4.18 In devising such a strategy does the Supervisor in particular consider macro-economic issues and impacts where appropriate?	
4.19 Does the Supervisor, on the basis of evidence	

understand the probability and impact of potential risks? 4.20 Is the Supervisor proactive, identifying and acting upon risks before problems occur? 4.21 Does the Supervisor risk assess (all or the most significant) individual supervised entities, for instance through a risk scoring model or measures of exposure to risk? 4.22 Does the Supervisor, decide on interventions (including guidance) on the basis of assessed risk? 4.23 Does the Supervisor seek to encourage risk management practice by supervised entities, and where appropriate place some reliance on it? 4.24 What impact would any planned changes to the Supervisory mandate or approach have on the answers to the above questions?	

Overall assessment (with reasons):

Suggested recommendations:

Types of supporting evidence

- The Supervisor's objectives
- The Supervisor's strategy or plans.
- Information on the Supervisor's risk assessment methodology and tools
- The Supervisor's enforcement policies.
- Information on the Supervisor's inspection programme(s)
- Information on actions taken by the Supervisor in response to problems at supervised entities.
- The Supervisor's guidelines etc on pension entity risk management
- Representations as to the Supervisor's risk focus in practice

Principle 6: Proportionality and Consistency - Pension supervisory authorities should ensure that investigatory and enforcement requirements are proportional to the risks being mitigated and that their actions are consistent

The remedial actions and if necessary sanctions imposed by the pension supervisory authority should be proportional to the problem which is being addressed. In taking or promoting mitigating actions, pension supervisory authorities should choose between the powers available to them according to the assessed seriousness of the risk or compliance failure being addressed.

The extent of supervisory demands placed on pension funds or plans and associated parties being supervised should be in accordance with the value expected to be derived.

In fulfilling its supervisory powers, the pension supervisory authority should give pension funds and plans flexibility, where appropriate, in the way they achieve compliance with regulatory requirements.

Supervisory decisions and intervention should be consistent, taking appropriately into account circumstances of each individual case. Supervisors should have procedures (for example, documentation, training and review) for ensuring that similar decisions are taken in similar circumstances and that these decisions are taken on objective and unbiased grounds.

Key considerations for the review:

The review needs to determine whether the Supervisor discharges its mandate with appropriate proportionality and has effective processes to secure consistency.

Assessment Questions:

4.25 Do the Supervisor's powers enable it to vary its supervisory actions according to the magnitude of risks being addressed?	
4.26 Does the Supervisor have procedures for helping the choice of a proportionate response, such as an enforcement pyramid or intervention ladder?	
4.27 Has the Supervisor chosen interventions that, on the basis of available evidence, are proportionate to the problems and risks it has encountered?	
4.28 Does the Supervisor check that demands (e.g for information) placed on supervised entities are proportionate?	
4.29 Does the Supervisor allow supervised entities appropriate flexibility in deciding how to comply with legislation?	
4.30 Does the Supervisor from time to time review whether its interventions are achieving the	

desired effect in a proportionate manner? 4.31 Does the Supervisor have processes designed to ensure appropriate consistency between interventions in similar circumstances, such as review processes and precedent documentation? 4.32 What impact would any planned changes to the Supervisory approach or procedures have on the answers to the above questions?	
Overall assessment (with reasons):	
Suggested recommendations:	

Types of supporting evidence

- Governing legislation
- The Supervisor's strategy or plans
- The Supervisor's enforcement policies.
- Information on the Supervisor's inspection programme(s)
- Information on the Supervisor's decision making and review processes
- Information on actions taken by the Supervisor in response to problems at supervised entities.
- Representations as to proportionality and consistency in practice

Principle 7: Consultation and Cooperation - Pension supervisory authorities should consult with the bodies they are overseeing and cooperate with other supervisory authorities

The pension supervisory authority should consult, as appropriate, with the pensions sector

when determining its approach to supervision.

The pension supervisory authority is empowered to exchange information with other relevant supervisory authorities, subject to legal and confidentiality requirements. This includes cooperation with other authorities or departments involved in pension supervision both nationally and internationally (particularly where cross-border pensions are involved), as well as with authorities supervising other relevant financial institutions or markets and law enforcement agencies. Cooperation should be for both efficiency purposes (avoiding overlaps and promoting economies of scale and scope) as well as promoting pro-active preventative measures (*e.g.* tackling financial crime).

Key considerations for the review:

Exposing supervisory policy decisions to public scrutiny, through consultation before they are taken, should result in better decision making and buy-in by supervised entities, while co-operation with other agencies is important where responsibilities for supervised entities are shared. The review needs to determine whether the Supervisor therefore discharges its mandate in an appropriately consultative and co-operative manner

Assessment Questions:

4.33 Does the Supervisor consult with the pensions sector when determining strategic supervisory approaches?	
4.34 Are these consultation processes designed so as to facilitate considered responses that can influence its approaches, for example allowing sufficient time for responses?	
4.35 Does the Supervisor have other processes or forums to facilitate 2-way communication with supervised entities and other interested parties?	
4.36 Is the Supervisor empowered to exchange information with other relevant national authorities, subject to appropriate requirements?	
4.37 Is the Supervisor empowered to exchange information with pension supervisors in other countries as appropriate?	
4.38 Does the Supervisor have effective processes for information sharing and conflict resolution with relevant authorities, subject to confidentiality constraints, for example through memorandums of understanding?	
4.39 What impact would any planned changes to the Supervisor's procedures have on the answers to the above questions?	

Overall assessment (with reasons):

Suggested recommendations:

Types of supporting evidence
• Governing legislation • The Supervisor's strategy or plans • Information on the Supervisor's consultation processes. • Information on the Supervisor's processes for sharing information with other authorities, including memorandums of understanding • Information on actions taken by the Supervisor in response to problems at supervised entities. • Representations made as to the extent of consultation or effectiveness of co-operation

Principle 8: Confidentiality - Pension supervisory authorities should treat confidential information appropriately

The pension supervisor should only release confidential information if permitted by law.

The pension supervisor in regard to non-public information should when requested by the providing authority keep information confidential and maintain appropriate safeguards for the protection of confidential information within its possession.

Where unsure of the status of the information, the supervisory authority should treat it as confidential if not publicly available or should check the status with the provider.

If agreed by the providing authority, the receiving supervisory authority may pass on

information to other supervisory bodies or law enforcement agencies with legitimate supervisory

interests and equivalent confidentiality standards.

Where staff transfer between the supervisory authority and the private sector, mechanisms should exist to ensure against the disclosure of confidential information.

Third parties to whom the pension supervisory authority has outsourced supervisory tasks

should be subject to the same confidentiality requirements as the staff of the pension supervisory

authority itself.

Key considerations for the review:

The review needs to determine whether the Supervisor can maintain the confidences with which it is entrusted

Assessment Questions:

4.40 Does the Supervisor have a confidentiality policy which sets out the Authority's procedures to prevent inappropriate disclosure of non-public information (as	

defined by law)? 4.41 Do these procedures appropriately cover disclosure to other government agencies or supervisory bodies? 4.42 Are there mechanisms to prevent disclosure of confidential information by staff, including after they have left the Supervisor? 4.43 Are confidentiality requirements applied similarly to third parties to which supervisory functions are outsourced? 4.44 What impact would any planned changes to the Supervisor's mandate or procedures have on the answers to the above questions?	
Overall assessment (with reasons):	
Suggested recommendations:	
Types of supporting evidence	
• Governing legislation • The Supervisor's confidentiality and information management policy and procedures • Staff code of conduct • Information on how the Supervisor applies confidentiality to outsourced supervisory functions • Representations as to any issues with confidentiality	

Principle 9: Transparency - Pension supervisory authorities should conduct their operations in a transparent manner

Pension supervisory authorities should adopt clear, transparent and consistent supervisory processes. The rules and procedures of the pension supervisory authority, and updates thereof, should be published. The pensions supervisory authority should generally operate in a transparent environment and should provide and publish a regular report – at least annually and in a timely manner – on the conduct of its policy, explaining its objectives and describing its performance in pursuing those objectives. The pension supervisory authority should be subject to regular audit and reporting requirements which allow for the assessment of how well the authority is fulfilling its responsibilities and ensuring the mandate and

functions of the pension supervisory authority cannot be changed on an ad hoc basis.

When directing the management of pension funds or plans pension supervisory authorities should explain to those affected why they are acting.

Pension supervisory authorities should provide and publish clear and accurate information for the pension industry and the general public on a regular basis – such as the financial situation of the pension fund industry and observations on major developments in the pension sector. Disclosure will generally be on an aggregate basis, but could also be on individual pension funds, in which case the rules of confidentiality may be particularly relevant.

Key considerations for the review:

The review needs to determine whether the Supervisor's objectives, frameworks, decisions and their rationale, data and other information are provided to stakeholders in a comprehensive, assessable manner. Such transparency helps to enable accountability to key stakeholders and to command the understanding and respect of the supervised community. It should also help to reduce market uncertainty and counter poor operating practices and policies. Reporting on supervisory interventions after they have been made, with reasons, should help supervised entities understand better what is expected of them.

Assessment Questions:

4.45 Does the Supervisor publish its rules and procedures?	
4.46 Is the Supervisor subject to appropriate audit and reporting requirements that do not compromise the independence of its mandate?	
4.47 Does the Supervisor publish an annual report explaining how it meets its objectives?	
4.48 Does the Supervisor publish information supporting its proposed strategic decisions and plans, including any assessment of cost/benefit?	
4.49 Does the Supervisor's website provide information to help supervised entities	

understand what is expected of them? 4.50 Has the Supervisor explained to individual supervised entities subject to its actions why it has taken the action? 4.51 Has the Supervisor published its supervisory decisions, with appropriate explanations (subject to confidentiality constraints) in a way that should help supervised entities understand better what is expected of them? 4.52 Is there evidence of the Supervisor regularly publishing clear and accurate aggregate information on the pension sector, including its assessment of risks in the sector? 4.53 What impact would any planned changes to the Supervisor's communications approach or media have on the answers to the above questions?	
Overall assessment (with reasons):	
Suggested recommendations:	
Types of supporting evidence	
• Governing legislation • Information on reporting lines and accountability to government and the legislature (including audit) • The Supervisor's annual reports or equivalent • The Supervisor's website • Strategies or plans produced by the Supervisor • The Supervisor's enforcement policies (covering how it explains its interventions) • Explanations of its decisions that the Supervisor has provided to supervised entities and published • The aggregate information the Supervisor publishes on the pension sector • Representations made as to the transparency of supervision	

Principle 10: Governance - The supervisory authority should adhere to its own governance code and should be accountable

The pension supervisory authority should establish and adhere to a governance code, outlining suitable internal controls, checks and balances, and effective processes for risk and performance management. A code of conduct should be established and enforced in relation to all staff members.

There should be clearly documented procedures for decision-making, with processes for referring decisions up to the appropriate level of seniority, reviewing and documenting decisions.

For interventions with serious impact there should be some separation between those within the authority proposing interventions and those taking the final decision, so the scope for emergency action is balanced by a review process.

Pension supervisory authorities should be clearly accountable for their general conduct and activity. Pension supervisory authorities should have accountability arrangements, which may vary according to specific country circumstances and which may include accountability to a range of bodies, from parliament to the members and beneficiaries of pension funds or plans.

Procedures should be in place for the governing body of a pension plan or fund to appeal to the pension supervisory authority or relevant tribunal for decisions taken by the pension supervisory authority that affect them and which they consider inconsistent with legal provisions.

Key considerations for the review:

The review needs to determine whether the Supervisor's governance arrangements set a good example to the supervised community and ensure that supervisory processes are fair, subject to due process and do not involve conflicts of interest. In particular, the governance arrangements (taken with arrangements for transparency) should secure accountability of staff to the board/senior management, and hence to government and the legislature. This necessitates effective processes for internal scrutiny and review including appropriate performance measurement.

Assessment Questions:

4.54 Does the Supervisor have appropriate codified procedures for internal governance, and is compliance with these monitored and enforced?	
10.1 Is there a code of conduct applying to all staff that includes rules on receipt of gifts, hospitality et, claiming expenses and declaring conflicts of interest?	
10.2 Are there effective arrangements for managing actual and potential conflicts of interest affecting supervisory management or staff, such as obligations to step aside from the decision making process where conflicted.	
10.3 Are there clearly documented procedures and	

business rules for taking, reviewing decisions and recording and disseminating decisions?	
10.4 Does the Supervisor have processes to ensure that actions against supervised entities are taken, and seen to be taken, on the basis of unbiased evidence?	
10.5 Is there independent review, within the Supervisor (for example at board level), of decisions with serious implications for supervised entities?	
10.6 Is responsibility for authorising the use of sanctions against supervised entities separated from executive functions and subject to due process?	
10.7 Is there an appeals process against such decisions where they apply to individual supervised entities?	
10.8 Are there appropriate arrangements for holding the Supervisor to account to the legislature or other stakeholders, such as reporting to parliamentary or stakeholder committees, annual meetings or independent reviews?	
10.9 Does the Supervisor regularly measure its performance against objectives, and provide the board/senior management and external stakeholders with the results?	
10.10 Does the Supervisor have documented internal controls and risk management processes (appropriate to its size)?	
10.11 What impact would any planned changes to the Supervisor's procedures have on the answers to the above questions?	
Overall assessment (with reasons):	
Suggested recommendations	

Types of supporting evidence
• Governing legislation (for accountability and appeals) • Structure and responsibilities of governing body (or equivalent) including split between executive and non-executives, whether the CEO is also Chair, representational nature of non-execs, lengths of terms of appointment and limitations on re-appointment. • Information on reporting lines and accountability to government • Codification of the Supervisor's governance procedures • Staff code of conduct • Information on the Supervisor's decision making processes • Information on the appeals process • The Supervisor's performance measurement framework, measures and reports • The Supervisor's annual reports or equivalent • The Supervisor's website • Information on the Supervisor's internal control and risk management framework • Representations made as to issues with governance

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OECD Principles of Occupational Pension Regulation

METHODOLOGY FOR ASSESSMENT AND IMPLEMENTATION

Occupational pensions play a major role in OECD countries and worldwide, complementing retirement income from state sources. At the end of 2009, private pension savings reached USD 25 trillion. Population ageing has led many OECD countries to undertake a wide range of pension reforms – the overall effect of which has been to reduce public pension promises and, in turn, to increase the importance of private pension savings for retirement.

The Core Principles cover seven key areas: i) Conditions for effective regulation and supervision; ; ii) Establishment of pension plans, pension funds, and pension fund managing companies; iii) Pension plan liabilities, funding rules, winding up, and insurance; iv) Asset Management; v) Rights of members and beneficiaries and adequacy of benefits; vi) Governance; and vii) Supervision. Each of the seven core principles consists of a main text and a set of implementing guidelines. In the case of the core principle of supervision, the supporting guidelines integrate the IOPS Principles of Private Pension Supervision.

The Methodology provides a structured approach for evaluating a jurisdiction's occupational pension regulatory system in relation to the OECD Core Principles of Occupational Pension Regulation.

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