Methodology for Review of Supervisory Systems using IOPS Principles

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THE INTERNATIONAL ORGANISATION OF PENSION SUPERVISORS (IOPS)

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Background to the Principles

The IOPS Principles of Private Pension Supervision (the Principles), initially approved in 2006 and revised in 2010, provide a set of globally accepted principles covering the organisation and activities of pension supervisors.

As the introduction to the Principles states, they are "designed to cover occupational and personal pension plans and pension funds. 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[1]. 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."

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 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) with specified exceptions[2].

It should be noted that 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 its Principles identify good practice which can be applied universally.

The assessment framework

This framework provides a structured means of assessing the extent to which a pensions supervisory authority complies with the letter and spirit of the Principles.

The Framework, below, translates the text supporting each Principle into the key considerations to be taken into account in making the assessment along with a series of specific questions. The considerations and questions have been informed as appropriate by IOPS work, currently in progress, on good governance

[1] 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 the draft OECD Core Principle 6 on Supervision.

[2] Principles need not necessarily 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 3June 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*

in pension supervisory authorities, as well, where relevant, by the OECD/IOPS Guidelines on the licensing of pension entities and the IOPS Working Paper on the implementation of risk-based supervision[3] . It also indicates the types of evidence that may help to answer the questions. For each Principle, there is a box for an overall assessment, along with space for supporting comments, and a box for suggested recommendations to improve compliance.

The evidence to support the reviewer's assessment should be drawn from relevant legislation and publications by the supervisor, along with the available results of other external assessments undertaken in recent years (e.g. WPPP and FSAP). The supervisor should be asked to provide unpublished documents that fill in gaps in the published material or provide material evidence of what the supervisor has done or achieved. The reviewer should speak to senior staff of the supervisor(s) and, if practicable, representatives of some key stakeholders, notably supervised entities and the sponsoring ministry.

The assessment of each Principle can conclude that compliance is achieved to varying degrees, following the OECD methodology used in relation to occupational pension regulation,[4] namely:

- **Fully implemented** – the IOPS Principle is implemented in all material respects;

- **Broadly implemented –** the Principle is implemented in all but one or two material respects and the exceptions do not significantly detract from the overall opinion. It should be possible to say something positive about compliance in answer to nearly every question ;

- **Partly implemented** – while a negative answer is given to some questions, the responses to the majority of the questions are consistent with compliance;

- **Not implemented -** there are major shortcomings against the Principle;

- **Not applicable** – the Principle does not apply due to structural, legal or institutional features.

In making the assessment reviewers will need to consider not just the current position but also the plans that exist for changing the way the supervisor operates. These changes will, of course, not generally have been tested in practice, which means that they are unlikely to result in a fully compliant assessment that would not otherwise have been made. But they enable enough of a positive conclusion to be drawn on some questions to convert a 'partly' to a 'broadly' implemented. It may lead to an assessment that it would appear that the supervisor is likely to become more compliant. Prospective changes that have not been tested in practice should not result in a down-grading of the compliance assessment unless they patently represent a retrograde step.

Where there is more than one authority with supervisory responsibilities, the reviewer should assess those authorities responsible for supervising a large proportion of pension entities (in terms of numbers and market share) and for most aspects of the entities' activities. Hence the assessment would not usually cover the tax authority unless it has significant supervisory responsibilities beyond those relating to tax collection. Where there is both a prudential and conduct of business supervisor, it would only cover the former, unless the latter is responsible for the supervision of a substantial element of pensions regulation. Where the assessment needs to cover more than one supervisor, conclusions on each Principle should

[3] IOPS Working Paper No. 4 (August 2007) "*Experiences and Challenges with the Introduction of Risk-Based Supervision for Pension Funds".*

[4] OECD Working Party on Private Pensions "*Methodology for assessing the implementation of the OECD consolidated core principles of occupational pension regulation*", issued 23 May 2008 (DAF/AS/PEN/WD(2008)1/REV1.

distinguish between the supervisors to the extent that compliance by them materially differs. The overall assessment for each Principle, however, would be that of the least compliant supervisor, unless the role of that supervisor is not material to the Principle concerned.

Given the variations in country's pensions, regulatory and supervisory systems and approaches, some creativity may also be needed in applying the questions and assessment in individual cases. The assessment of each principle will inevitably be based to some extent on the reviewers' judgement. As well as looking at individual answers the reviewer will need to look at the overall picture, bearing in mind that the questions have different degrees of importance in relation to the overall conclusion. Where a Principle is not fully implemented, the report should indicate whether the constraints are within or external to the Supervisor's control. The report should make recommendations may be made for actions that would improve compliance, indicating whether the proposed change is within the scope of the existing legislative and regulatory framework.

The Framework also includes an overall assessment sheet to facilitate drawing an overall conclusion from the judgements made about compliance with each Principle, using the same headings as applied to each Principle, above. While the performance under each Principle can be aggregated to give an overall impression, the reviewer may consider that poor performance against one or more Principles may be sufficiently serious to consider the supervisor non-compliant. For instance, a supervisor that is non-compliant with, say, the independence principle may be found non-compliant overall, given the importance of operational independence to effective supervision, regardless of the extent of compliance with the other principles. In any event, just because the supervisor is considered to be fully or broadly implementing the Principles does not necessarily mean that there is not room for improvement and recommendations may still be made.

The completed documentation will support a written report summarising the conclusions of the review, including the results of any mission to the supervisor and the views expressed by the supervisor on the conclusions drawn. Information supplied in confidence will not be included in the final report although it may influence the findings included in the report.

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 should 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.[5] 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 is usually appointed for a fixed term normally between 3-6 years with subsequent reappointment allowed (in order to retain skilled practitioners). 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, including the use of enforcement and sanction powers, 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	

[5] 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.

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 term/s (if so how long) 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 (including enforcement and sanction powers) 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.[6]

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 or plans could be considered, provided independence is maintained. Where fees are charged, the fee structure should be transparent.

The Authority should hire, train and maintain sufficient staff with high professional standards, and expertise including appropriate standards of confidentiality and disclosure.

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 supervisory tasks to third parties (e.g. auditors, actuaries), or to second ('borrow') staff with appropriate experience to work internally – 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 ensure they maintain the required level of confidentiality, assess their competence, monitor their performance and ensure their independence from the pension fund or any other related parties in order to avoid conflicts of interest. 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 Is any fee structure transparent?	
3.3 Does the Supervisor have longer term financial perspective (e.g 3 years or longer) that provides some stability for planning and recruitment?	
3.4 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	

[6] For details see *IOPS Guidelines for Supervisory Intervention, Enforcement and Sanctions* http://www.iops.org/dataoecd/47/40/43972432.pdf and *IOPS Guidelines for the Supervisory Assessment of Pension Funds* http://www.iopsweb.org/dataoecd/38/47/41042660.pdf?contentId=41042661

defensible minimum? 3.5 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? 3.6 Is the Supervisor able to obtain sufficient resources in expert disciplines? 3.7 Does the Supervisor have processes intended to ensure that staff have necessary skills, competencies and independence? 3.8 In particular, are senior staff appropriately qualified and of sufficient stature? 3.9 Can the Supervisor outsource functions in support of its supervisory responsibilities where it deems it necessary or where in-house resources are insufficient? 3.10 Can the Supervisor second staff with appropriate experience where it deems it necessary or where in-house resources are insufficient? 3.11 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? 3.12 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 secondments, and how the Supervisor oversees any outsourced or seconded 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 empowered to undertake supervision and should be granted adequate powers and the capacity to exercise these powers.[7]

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 soundness and control, minimum capital requirements, investment activity, good governance and integrity, actuarial examination, the supervision of pension plan or fund managers, and the provision for adequate disclosure of information to members. Powers should allow for relevant off-site and on-site inspection.

Pension supervisory authorities should have comprehensive investigatory and enforcement powers. The legal framework that defines conditions and circumstances under which the pension fund supervisor must intervene should be flexible enough to enable the pension supervisor to undertake preventative, protective or punitive actions.

The pension supervisory authority should have the power to conduct a full investigation when a problem is suspected or observed, obliging funds and other relevant parties (such as asset managers, custodians, auditors) to make documents and information available. Necessary powers include the ability to impose corrective measures and remedial actions if the authority's orders are not carried out. The scope of the powers may extend to the power to impose administrative sanctions such as fines, to direct management, to revoke licences and to refer matters for criminal prosecution. In some cases, powers may include the ability to issue binding regulation.

The pension supervisory authority should have clear and well-defined supervisory goals for the use of intervention, enforcement and sanction powers, clearly establishing whether the goal of their action is preventative, protective or punitive and use the appropriate tools and powers accordingly. The supervisory authority should have a coherent, well thought-out policy for deciding on the mix of supervisory tools adopted and the ability to adapt this approach to changing circumstances.

A sufficient gradation of powers is required to enable the supervisory authority to tailor its response accordingly and sufficiently punitive powers are needed to enforce action.

Though not all powers may be used 'actively', the supervisory authority should still have certain powers to either use in exceptional circumstances – thereby avoiding what could be time consuming delays in dealing with other supervisory authorities – or, by acting as a deterrent, serving to modify the behaviour of supervised entities.

Pension supervisory authorities should have the power to take exceptional measures, if needed, in times of acute financial and economic difficulty and/or volatility (for example increasing reporting requirements, strengthening stress tests or temporarily suspending certain regulatory or supervisory requirements which may have a pro-cyclical, adverse impact on financial markets in the short-term).

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

[7] For details see IOPS Guidelines as above.

look for substantive compliance with the OECD/IOPS Licensing Guidelines as they relate to supervision. The review should also establish whether the Supervisor has clear goals and a robust yet flexible policy for deciding on which supervisory tools should be used in different circumstances to achieve these goals.
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, flexible 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 conduct full investigations where problems occur in 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? 4.16 Does the Supervisor have a policy for deciding which supervisory tools to apply in different circumstances? 4.17 Does the Supervisor have a sufficient gradation of powers (including the ability to take exceptional measures when circumstances require)?	
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 • Enforcement pyramid or intervention ladder • Policy responses to the economic and financial crisis	

Principle 5: Risk based supervision -*Pension supervisory authorities should adopt a risk-based approach*[8]

In order to use their resources efficiently, pension supervisory authorities should adopt a risk-based approach, and a suitable risk-assessment methodology should be established.[9]

The move towards risk-based supervision can be undertaken gradually, combining this technique with more traditional rules-based supervision as the supervisory authority and pension industry develop the necessary expertise.

The move towards risk-based supervision should be seen as a movement along a continuum from one extreme of complete reliance on a rules-based system to one where the emphasis of supervision is a function or risk. Rules-based supervision does not mean having no rules or compliance procedures.

A legal framework allowing suitable discretion in terms of interpretation and exercise of supervisory powers is required, which should also provide pension supervisory authorities with the necessary powers to adopt a risk-based approach.

Staff reorganisation and training, in terms of the philosophy as well as the process of risk-based supervision, should be undertaken as the transition to the new approach takes place.

The pension supervisory authority should communicate its risk-based approach to the pension industry, explaining what is expected of them – particularly in relation to risk-management- via guidance notes and possibly providing training.

Risk-based supervision will require different types of information, which the pension supervisory authority should obtain from existing sources where possible. Where specific supervisory returns are required they should be designed with care and focused on obtaining information regarding the main risks which the pension supervisory authority is concerned with.

Where quantitative risk assessment tools are used, the models involved should be carefully designed and their limitations fully understood.

Risk-scoring models should reflect the risk-focus of the pension supervisory authority (which is driven by its objectives and resources), and the net risk of relevant individual entity and systemic risk factor. These factors should be suitably weighted according to the nature of the pension system (including the size and number of pension funds overseen), and a risk-score derived from the probability and impact of their occurrence.

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 'rules-based'

[8] As outlined in the IOPS Toolkit for Risk-based Supervision (www.iopstoolkit.org), risk-based supervision (RBS) is a structured approach which focuses on the identification of potential risks faced by pension funds and the assessment of the financial and operational factors in place to minimize and mitigate those risks. This process then allows the supervisory authority to direct its resources towards the issues and entities which pose the greatest threat.

[9] For further details see IOPS Toolkit for Risk-based Supervision (www.iopstoolkit.org) and *IOPS Guidelines for Supervisory Intervention, Enforcement and Sanctions http://www.iopsweb.org/dataoecd/47/40/43972432.pdf*

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.

The review needs to determine whether the supervisor is moving 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:

5.1 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? 5.2 Is the Supervisor’s adoption of risk-based supervision well planned and developed within a realistic timetable? 5.3 Does the Supervisor have the necessary legal framework to undertake risk-based supervision? 5.4 Are all staff being suitably trained? 5.5 Is the risk-based approach being explained to the pension industry? 5.6 Does the Supervisor collect the necessary information to undertake risk-based supervision? 5.7 Does the Supervisor have a robustly based strategy for allocating resources to the highest risks so as to achieve its objectives? In devising such a strategy does the Supervisor in particular consider macro-economic issues and impacts where appropriate? 5.8 Does the Supervisor understand any quantitative models used to measure risk? 5.9 Does the Supervisor, on the basis of evidence understand the probability and impact of potential risks? 5.10 Is the Supervisor proactive, identifying and acting upon risks before problems occur? 5.11 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? 5.12 Does the Supervisor, decide on interventions	

(including guidance) on the basis of assessed risk? 5.13 Does the Supervisor seek to encourage risk management practice by supervised entities, and where appropriate place some reliance on it? 5.14 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
- Legislative environment
- Staff training programmes
- Information on the Supervisor's risk assessment methodology and tools, including risk assessment tools and weightings
- 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*

A logical connection should be made between the results of the risk assessment undertaken by the pension supervisory authority and its actions (for example through the use of a supervisory response matrix).[10] The remedial actions and if necessary sanctions imposed by the pension supervisory authority should be proportional to the amount of risk posed by the fund to its members and beneficiaries and the pension system as a whole – taking into account the nature, scale, complexity and seriousness of the potential compliance irregularities relating to the relevant party – and should represent the most efficient use of supervisory resources.[11] The long-term nature of pension funds should be taken into consideration and unnecessary pro-cyclical behaviour should be avoided.

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. During the decision making process, a balance should be struck between the potential benefits of the supervisory action and the costs and impact on pension fund members and beneficiaries and where appropriate, plan sponsors.

Once a problem is identified, a clear and well-defined 'due process' should be followed. Due process describes the checks and balances that a supervisory authority should have in place to ensure that supervised entities are treated fairly, consistently and transparently.

To ensure proportionality, requirements should be set out in legislation, secondary regulation or detailed industry guidance (outlining various circumstances and risk as well as the associated intervention measures). Appropriate documentation, guidance and examples should be regulated or provided to staff.

Subject to the availability of regulatory and administrative powers and measures, the response should be escalated appropriately to achieve the desired regulatory objectives. Depending on the nature, scale and complexity of the problem detected, a graduated response or exceptional measures should be adopted.

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 (both horizontally between pension funds and vertically over time), taking appropriately into account circumstances of each individual case. Supervisors should have well-documented procedures (for example, documentation, training, peer review, specialist team reviews and/or senior oversight) 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.

[10] For further details see the IOPS Toolkit for Risk-based Supervision.

[11] *IOPS Guidelines for the Supervisory Assessment of Pension Funds* http://www.iopsweb.org/dataoecd/38/47/41042660.pdf?contentId=41042661

Assessment Questions:	
6.1 Do the Supervisor's powers enable it to vary its supervisory actions according to the results of risk assessments? 6.2 Does the Supervisor have procedures for helping the choice of a proportionate response, such as an enforcement pyramid or intervention ladder? 6.3 Are requirements appropriate laid out to ensure proportionality? 6.4 Has the Supervisor chosen interventions that, on the basis of available evidence, are proportionate to the problems and risks it has encountered? 6.5 Is there an awareness of the cost / benefit analysis of interventions? 6.6 Does the Supervisor check that demands (e.g for information) placed on supervised entities are proportionate? 6.7 Does the Supervisor allow supervised entities appropriate flexibility in deciding how to comply with legislation? 6.8 Does the Supervisor from time to time review whether its interventions are achieving the desired effect in a proportionate manner? 6.9 Does the Supervisor have processes designed to ensure appropriate consistency between interventions in similar circumstances, such as review processes and precedent documentation? 6.10 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 domestically and internationally*

The pension supervisory authority should consult, as appropriate, with the pensions sector when determining its approach to supervision.[12]

The pension supervisory authority should be 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 (for example conduct of business supervisors) 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).

Pension supervisory authorities should ensure that intensified coordination between financial sectors and internationally takes place when necessary and particularly during periods of economic difficulty and financial system volatility, though confidentiality requirements should be met.

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:

7.1 Does the Supervisor consult with the pensions sector when determining strategic supervisory approaches?	
7.2 Are these consultation processes designed so as to facilitate considered responses that can influence its approaches, for example allowing sufficient time for responses?	
7.3 Does the Supervisor have other processes or forums to facilitate 2-way communication with supervised entities and other interested parties?	
7.4 Is the Supervisor empowered to exchange information with other relevant national authorities, subject to appropriate requirements?	
7.5 Is the Supervisor empowered to exchange information with pension supervisors in other countries as appropriate (for example during	

[12] For further details see *IOPS Guidelines for Supervisory Intervention, Enforcement and Sanctions* http://www.iopsweb.org/dataoecd/47/40/43972432.pdf

periods of economic volatility)? 7.6 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? 7.7 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 • Policy responses to the economic and financial crisis	

Principle 8: Confidentiality - *Pension supervisory authorities should treat confidential information appropriately* The pension supervisor should only release confidential information if permitted by law (with fines or even prison sentences imposed for breaches). Staff should be bound by internal codes of confidentiality – also after leaving the authority. IT systems used by supervisors should include limited access restrictions to protect confidentiality and special care should be taken regarding the security of the supervisory authority's database for reasons of effective data protection. The supervisory authority should publish its policy on how confidential information will be treated. A suitable balance should be struck between conduct of business supervision (where disclosure can be used to influence the behaviour of the supervised community), prudential supervision (where confidentiality is important to protect the interests of particular supervised entities), and system integrity, according to the nature of the pension system. 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. Only if agreed by the providing authority, the receiving supervisory authority may pass on confidential information to other supervisory bodies or law enforcement agencies provided they have legitimate supervisory interests and equivalent confidentiality protection standards. Where staff transfer between the supervisory authority and the private sector, mechanisms should exist to ensure the protection 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:	
8.1 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)? 8.2 Do these procedures appropriately cover disclosure to other government agencies or supervisory bodies? 8.3 Are staff bound by internal codes of confidentiality – even after leaving the authority? 8.4 Does the Supervisor have suitable controls within its IT systems? 8.5 Does the Supervisor have a policy which considers	

publishing information vs. confidentiality, suitably balancing prudential regulation and conduct of business issues? 8.6 Are there mechanisms to prevent disclosure of confidential information by staff, including after they have left the Supervisor? 8.7 Are confidentiality requirements applied similarly to third parties to which supervisory functions are outsourced? 8.8 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 • IT systems • Internal staff codes	

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. Where appropriate, the broad outlines of any supervisory response framework (such as an enforcement pyramid)[13] should be made public by the supervisory authority, so that its actions will be understood by supervised entities and are unexpected. When directing or replacing the management of pension funds or plans pension supervisory authorities should explain and give due notice of the reasons for the supervisory action.[14] A transparent information disclosure mechanism and timely publication of intervention and sanction decisions, where appropriate, should be in place, subject to relevant confidentiality requirements. 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:	
9.1 Does the Supervisor publish its rules and procedures? 9.2 Does the Supervisor explain its supervisory response framework (enforcement pyramid)? 9.3 Is the Supervisor subject to appropriate audit and reporting requirements that do not compromise the independence of its mandate?	

[13] For further details see IOPS Toolkit for Risk-based Supervision www.iopstoolkit.org

[14] For further details see *IOPS Guidelines for Supervisory Intervention, Enforcement and Sanctions* http://www.iopsweb.org/dataoecd/47/40/43972432.pdf

9.4 Does the Supervisor publish an annual report explaining how it meets its objectives? 9.5 Does the Supervisor publish information supporting its proposed strategic decisions and plans, including any assessment of cost/benefit? 9.6 Does the Supervisor's website provide information to help supervised entities understand what is expected of them? 9.7 Has the Supervisor explained to individual supervised entities subject to its actions why it has taken the action? 9.8 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? 9.9 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? 9.10 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 • Enforcement pyramid	

Principle 10: Governance - *The supervisory authority should adhere to its own good governance practices – including governance codes, internal risk-management systems and performance measurement -* ***and should be accountable***

Supervisory authorities should establish and operate sound governance practices in order to maintain credibility and moral authority to promulgate good practices in the entities under their supervision.[15]

Pension supervisory authorities should be overseen by a governing board of a manageable size. The remuneration of the senior executives of the authority may be published for transparency.

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.

An internal audit should be considered good practice for pension supervisory authorities, which reviews the consistency and transparency of the decision making process, the effectiveness of risk management practices and the efficiency and propriety in the use of resource. These internal audits should be carried out as part of the legal and functional oversight of the supervisory authorities and their findings should be presented to the overseeing (parent) ministry or other statutory.

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.

As part of good governance practices, pension supervisory authorities should monitor their own performance using a range of measures.

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

Pension supervisory authorities should be subject to an external audit by a state or independent audit institution.

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 unreasonable or inconsistent with legal provisions. Individual members of staff at the supervisory authority should have indemnity from civil prosecution.[16]

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[15] Good governance of pension supervisory authorities can be summarised in four categories : **independence:** requiring clarification of the authority's responsibilities and powers, processes for appointing its governing board and the ability to secure resources and operate without undue influence; **accountability:** involving external audits, suitable internal organization and measuring performance; **transparency:** ensuring that the authority's objectives and achievements are understood, and that a consultative relationship with industry is established; **integrity:** requiring codes of conduct, discretion to apply powers, internal controls and competent staff.

[16] For further details see *IOPS Guidelines for Supervisory Intervention, Enforcement and Santions* http://www.iopsweb.org/dataoecd/47/40/43972432.pdf

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:	
10.1 Does the Supervisor have appropriate codified procedures for internal governance, and is compliance with these monitored and enforced?	
10.2 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?	
10.3 Is the governing board of the Supervisor of a manageable size?	
10.4 Does the Supervisor publish the remuneration policy of the Board?	
10.5 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 and indemnity from civil prosecution.	
10.6 Are there clearly documented procedures and business rules for taking, reviewing decisions and recording and disseminating decisions?	
10.7 Does the Supervisor undertake a regular internal audit?	
10.8 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?	
10.9 Is there independent review, within the Supervisor (for example at board level), of decisions with serious implications for supervised entities?	
10.10 Is responsibility for authorising the use of sanctions against supervised entities separated from executive functions and subject to due process?	
10.11 Is there an appeals process against such	

decisions where they apply to individual supervised entities? 10.12 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? 10.13 Does the Supervisor regularly measure its performance against objectives, and provide the board/senior management and external stakeholders with the results? 10.14 Does the Supervisor have documented internal controls and risk management processes (appropriate to its size)? 10.15 What impact would any planned changes to the Supervisor's procedures have on the answers to the above questions? 10.16 Is the Supervisor subject to an external audit?	
Overall assessment (with reasons):	
Suggested recommendations	
Types of supporting evidence	

- Governing legislation (for accountability and appeals)
- Structure, size 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
- Internal and external audits
- 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

OVERALL ASSESSMENT

The following table can be used for making an overall assessment of the implementation of the Principles.

Principle	**Assessment of implementation**				
	Fully	**Broadly**	**Partly**	**Not**	**N/A**
1: Objectives					
2: Independence					
3: Adequate Resources					
4: Adequate Powers					
5: Risk Orientation					
6: Proportionality and Consistency					
7: Consultation and Cooperation					
8: Confidentiality					
9: Transparency					
10: Governance					
Total					