REVIEW OF

Fiji National Provident Fund Act

Policy Paper

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Following Consultation with FNPF management and Board and an initial rounds of consultation conducted in December 2010 & February 2011

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Promontory Financial Group Australasia, LLP (Promontory) has been engaged to provide technical assistance to the Fiji National Provident Fund (FNPF) Board to develop a modern and efficient legislative framework that provides for the prudent and sustainable delivery of retirement savings and related services that are in the best interests of the people of Fiji in the long term.

The Promontory team comprises:

- Shauna Tomkins — who is an expert in financial sector reform and policy development (previously Head of Policy at the Australian Financial Institutions Commission and member of the Wallis Inquiry Secretariat)
- Stephen Mason — who is an expert in legal drafting for the finance sector (Special Counsel with major Australian law firm Blake Dawson, previously member of the Australian Law Reform Commission. He has worked as parliamentary counsel).

REVIEW OF
Fiji National Provident Fund Act: Policy Issues

Executive Summary

1. Fiji's Retirement Savings Policy and supporting scheme administered under the FPNF Act is based on design and laws developed in the early 1960s. The key objective for the Scheme remains to provide financial security in old age but the objective is not supported consistently under the current law and administrative arrangements. Successive Boards and Management of FNPF and various amendments have tried to balance savings for retirement versus early access to funds to meet life events. The result has been that FNPF has become less effective in helping members Secure their Future. Reform to ensure a sustainable, transparent and fair scheme that delivers on the objective of self funded retirement is long overdue.

2. The current approach to provision of pensions was not subject to sound actuarial assessment. As a result, payment of these pensions requires cross subsidisation by existing members in the form of lower crediting rates on member savings. Further, contrary to sound prudential practice, the provision of pensions, which is a life insurance activity, is provided from the same balance sheet that accepts contributions and is essentially a collective investment scheme. Therefore, the law needs to provide for the sustainable delivery of pensions – current and future – through separation of the pensions business, allocation of sufficient reserves to meet the payments promised under existing contracts and actuarial assessment of future pension offerings.

3. The primary objective of the scheme remains financial security in old age. Therefore, to complement a life time of savings, members should be required under Law to convert some minimum amount of their savings into retirement income replacement through conversion to a life annuity, account based pension, term annuity or similar. Further, while FPNF should retain its monopoly position with respect to the savings aspects of the Scheme, particularly given its administrative and enforcement role, the provision of retirement products could be opened up to new participants that would be licensed by the Reserve Bank of Fiji.

4. The current Law imposes on FNPF a promise that it guarantees the value of contributions as well as a minimum crediting rate of 2.5%. To ensure that FNPF can meet this statutory promise, it needs sufficient free reserves (excluding intangibles) to absorb the volatility in investment values and returns under most economic conditions. With the proposed allocation of existing reserves to meet future pension payments, FNPF will not meet actuarial reserving expectations to support the existing statutory promise. Estimates are that required solvency will be between 10-20% of assets or some $350M to $800M. To accumulate such reserves in the medium term will require FNPF to cut back the crediting rate to the minimum 2.5% for 5-7 years, assuming a continuation of current returns and no bad investment years. Alternatively, the legislation could be amended to provide for FNPF to manage investments on a best endeavours basis which means that members' balances may be more volatile – up and down – but with potential for greater returns on their investments which has a significant compounding effect on the ultimate retirement savings amassed.

5. To refocus the Scheme on the objective of saving for old age, it is proposed that the Law provide for introduction of two accounts for every member: a Preserved Account that would receive 70% of contributions and be strictly preserved until entitlement and a General Account that would receive

the balance of contribution plus any voluntary payments. The balance in the General Account would be available for early access benefits such as medical, education etc in accordance with the conditions set under Law and by FNPF policies. To address concerns with respect to housing finance opportunities, a one-off access to and additional amount in the Preserved Account for the purposes of first home purchase could be considered with the condition that future contributions be paid into the Preserved Account to reinstate those savings.

6. To improve coverage and inclusion, the Law will align definitions as far as possible with the Tax Laws. Further, the new Law will provide for information and service sharing arrangements with FIRCA to improve efficiency and effectiveness. To encourage all employers to join the Scheme and provide lawful benefits to the employees, it is proposed to provide a 6 month amnesty to all employers to update all records, register employees and pay overdue contributions without penalty.
7. To improve Governance, it is proposed to amend the law to expand the Board to 7 (no more than 8) comprising three representative directors (one each from employers, employee groups and Government) and four independent appointments that will include the Chairman. The law will provide for selection and skills criteria, fit and proper requirements and fiduciary responsibilities to the members of the fund.
8. Other administrative matters include: the role of FNPF in the education of members, the need for a financial industry ombudsman, the need for appropriate whistleblowing obligations and protections and administrative accommodation of family court rulings.

REVIEW OF
Fiji National Provident Fund Act: Policy Issues

Overview

1. The Promontory Team (Promontory) conducted desk reviews of a number of independent reports, analyses and associated recommendations with respect to the design of Fiji's retirement savings arrangements, and their administration by FNPF. Consultative interviews with stakeholders were conducted from 29 November 2010 to 3 December 2010. A further visit was conducted mid-February 2011 to test assumptions and policy and design matters identified and to receive actuarial advice and comments on a number of the issues. There are a number of high level policy principles with respect to the design, administration, operation and supervision of Fiji's retirement savings scheme that need to be resolved to support the drafting of the new Law.

2. We assume that the reader is broadly familiar with the existing FNPF arrangements. This paper sets the scene with a brief review of Fiji's retirement savings scheme. The remainder of the paper identifies major policy issues, and makes recommendations or otherwise identifies at a high level alternatives that aim to balance preferred outcomes with accepted best practice while accommodating their practical application in the Fiji context. The discussion is not exhaustive, and does not provide extensive technical or administrative details. Rather, it is aimed at obtaining consensus on major policy outcomes to be incorporated into the revised Law that is being prepared by the Promontory Team. It needs to be remembered that a revised Law (a new Decree) will not be the only Laws relevant to post-retirement income policy. As well as the new Decree, related Laws (such as the Insurance Act), secondary Laws (regulations), and supervisory and prudential standards and guidelines and Codes of Conduct may need to be amended or developed.

3. The Promontory Team is scheduled to return to Fiji at the end of March or early April. The visit is to continue the socialisation process and to obtain direction on policy outcomes that will then be reflected in drafting the Law.

Fiji's retirement savings scheme

FNPF history

4. The FNPF was established in 1966 as a typical universal provident fund in the British colonial tradition. Similar funds were established across the Pacific, including in PNG and Solomon Islands, as well as in parts of Asia and Africa.

5. There are three elements to the FNPF Law:

    - a retirement savings scheme, comprising legislative provisions for, among other things, coverage, contribution requirements and rates, obligations on employers and employees and entitlements to benefits (including, in some cases, access to funds before retirement);

- the establishment of the FNPF as the entity to manage these savings, comprising legislative provisions for, among other things, the Board and its governance, the administration and investment of the savings; and

- some limited regulatory elements through more recent amendments to establish the role of the Reserve Bank of Fiji (RBF) in regulating and prudentially supervising FNPF's operations.[1]

Objectives and structure

6. In the absence of a Government provided safety net, the objective of this type of provident fund was to mandate savings by workers and additional contributions by employers, which would provide post-retirement financial security for Fund members and their dependents.

7. Typically, and as established in Fiji, the structure involved:

   - a single fund;

   - compulsory membership by private sector (and, in Fiji, public sector) employees; and

   - mandatory contributions by employers on behalf of those employees, comprising an employer component and an employee component through salary deduction.

Benefits and access

8. As originally enacted, benefits were payable out of the FNPF in 3 cases:

   - when the member left the workforce on retirement, on or after reaching a specified age (in Fiji's case, 55);

   - when the member left the workforce because of a permanent disability; or

   - on the member's death, when an additional payment — a special death benefit payment — was also paid to the member's nominees.[2]

9. In the 1990s, the scheme attempted to address a shortcoming of the original design by providing an income replacement product for retiring members in the form of a life pension or annuity. Unfortunately, the conversion rates at the time were not subject to sound actuarial advice and savings were converted at a generous 25% (ie that equates to an expectation that retiring members live on average less than 5 years after retirement). Even subsequent reforms in the early 2000s, did not take into account the actuarial risk, principally the longevity risk that a member would continue to draw a pension long after the value of savings transferred to buy the annuity had run out. Losses have occurred, with FNPF and more particularly current members, who cross-subsidise the payment of pensions through the lower crediting rates applied than would have otherwise been available.

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1 The Law relevant to supervision includes the FNPF Act, the Life Insurance Act, the Reserve Bank of Fiji Act and guidelines published by the RBF. Labour law, taxation and family law are also relevant.

2 Effectively, this is a kind of a life insurance risk product, although not presently regulated as such.

10. Further, the annuity business is life insurance and has been conducted, not as a separate business, but from the same balance sheet that accepts and invests active members' contributions. This results in a mix of long-tail insurance liabilities with the collective investment scheme that is managing members' contributions. These two activities have inherently different risks and are most usually established and regulated through separate legal structures with quite different prudential requirements and risk management arrangements.

11. It is of interest to note that more than 80% of members turning 55 have chosen to take their entitlement. Mostly as a lump sum with only around 30% of members opting to take their benefits as either a single life or joint life pension (not indexed for inflation).

12. Several stakeholders advised us that there is no strong savings tradition in Fiji. It would appear that members have keenly sought early access to benefits, to the extent that the FNPF appears to have become a de facto social security and emergency funding provider. Over time, the FNPF Law has been amended to provide, and successive FNPF Boards have facilitated, additional options for members to gain early access to benefits on compassionate, wealth building, family care and a number of less compelling grounds. In effect this means that there has been no true preservation of savings for retirement purposes as intended.

13. Prior to the current review, FNPF provided early access to benefits for some 22 different purposes, including:

    - housing;
    - medical assistance;
    - funeral assistance;
    - unemployment assistance;
    - education assistance;
    - investment; and
    - on migration from Fiji.

14. There is a substantial cost in administering early access arrangements. A right to early access also means that members who do not seek early access cross-subsidise those who do (in the form of reduced crediting rates). In addition, many of the expert reviews undertaken on the FNPF scheme and its operations have pointed out that early access to benefits weakens the goal of financial security in retirement.

15. The FNPF Board has made changes to early access arrangements and reduced the number of purposes. It has also sought actuarial advice with respect to pension offerings.

Role of FNPF in Fiji economy

16. The FNPF has a monopoly as the only institution authorised to accept and invest the mandated employer and employee contributions. FNPF also accepts voluntary contributions, although the level of voluntary contributions remains quite low.

17. FNPF is the largest financial institution (bank or non-bank) in the country, with a reported total asset value of some FJ$3.5 billion (around 40% of total financial sector assets and equal to about 60% of GDP). This makes FNPF larger than Fiji's banking system.[3]

18. Given its size relative to the financial system and GDP, the FNPF is the single biggest influence in Fiji's finance sector. As noted by several commentators and reports, most notably the joint IMF/World Bank sponsored *Financial Sector Assessment Program* (FSAP), this distorts the efficient operation of capital markets, particularly with respect to liquidity, depth and pricing. Given FNPF's exposure to Government bonds and its take up of new bond issues, there is little opportunity for Fiji to see the benefit of its quite strong savings rate through savings mobilisation and the efficient allocation of financial resources. Key recommendations of the FSAP (and most other commentators) with respect to FNPF included:

- diversifying the FNPF investments (and financial institutions more generally), including offshore investments, to address vulnerabilities and improve efficient operation of capital markets and allocation of resources;
- putting pension payments / the annuity program on an actuarially sound basis; and
- promoting greater diversification in the provision of financial services through transition away from FNPF's current monopoly.

Key issues for policy decision

19. Over the years, there have been a substantial number of studies and reports on the FNPF and substantial technical assistance has been provided. A number of actuarial reviews have been conducted. The RBF has produced supervisory reports. Based on these studies, discussions with stakeholders and on our own experience undertaking provident fund and pension scheme reform in a number of countries, we have identified drivers for change so as to ensure that reforms of Fiji's retirement savings scheme deliver sustainable, transparent and fair outcomes. To this end, the following key policy issues have been identified for decision:

- how to ensure that the provision of pensions is sustainable, transparent and fair;
- how to manage existing pension obligations;
- whether the retirement savings policy should provide for both mandatory savings and mandatory conversion of those savings to income replacement in retirement through purchase of an annuity or conversion of savings to an account based pension or other alternative;
- whether FNPF should be a "pure" defined contribution scheme, that is, whether current capital guarantee of savings and guaranteed minimum crediting should continue and be prudentially sustainable through establishing appropriate reserves, or whether the Fund should convert to an accumulation fund and FNPF manage investments and provide returns on a best endeavours basis – that is gains and losses be reflected in member accounts;

[3] See, for example, the *Financial Sector Assessment Program Report 2007*(FSAP Report).

- how to ensure that the Scheme delivers on the prime objective to support post-retirement financial security;[4]
- how to improve coverage and collection of contributions;[5]
- how to update enforcement provisions to ensure that members' rights can be properly protected;
- how to provide for greater competition;[6]
- how to improve the governance of FNPF; and
- how to improve equity, consumer protection and dispute resolution in relation to the FNPF.

Sustainable provision of pension obligations – current and future

Meeting the pension promise

20. An important aspect of Retirement Savings Policy is that the lifetime of savings should be able to be converted into income replacement or retirement income stream post-retirement. Since the mid-90s, FNPF has offered members the option to convert their savings into a life pension (single or joint) as an alternative to taking their savings as a lump sum when they reach the entitlement age. Around 30% of members have opted to take the pension. In insurance terms, the pension is a life annuity. In exchange for the lump sum savings, FNPF promises to make future regular payments to the member for life (or, if a joint pension, when that member dies, to his or her spouse).

21. This contract or promise to make regular payments has an unknown duration, as it depends on how long the member lives. In the event of death of the member (and spouse, if a joint pension), the contract to make these payments terminates. The money paid by the member for the contract is forfeited, whether the contract has run for one year or 30 years. Therefore, by taking a life annuity, the member transfers the uncertainty of his or her lifespan to the annuity provider. The insurer (in this case FNPF) would usually deal with this uncertainty by pooling the risk of member longevity over a large pool, on the basis that some members will die sooner rather than later.

22. Almost every review of FNPF (FSAP, SCE, Mercer's etc) identified that FNPF's pension offering is not sustainable and should be delivered through a mechanism separate to the savings scheme.

23. The sustainability problem is that neither the initial conversion rate in the 1990s nor the adjustments made in the early 2000s were calculated on a sound, actuarial basis. An actuarially-based conversion factor takes into account the age, life expectancy and gender of the member as well as expected investment returns and inflation. Such estimates can have high margin for error and therefore pose a

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4 Involving establishing minimum preservation requirements on savings and limiting early access to savings for a specified number of special purposes.

5 This may involve, among other things, alignment of contribution obligations of employers with their obligations under tax law, removing restrictions on re-joining the Fund, encouraging voluntary contributions and providing an amnesty period for employers to remediate non-complying employee registration and accounts.

6 This may involve licensing alternative providers of post-retirement products, such as life and term annuities, account-based pensions and other investment services.

high risk to the provider of the pension (FNPF). They require specialist actuarial advice. Reserves to support the risk that the forecasts for life expectancy and investment returns are wrong are also required to ensure the contracted payments are made as promised.

24. The initial conversion factor applied in the mid 90s was 25% for members taking their entitlement as a single pension at age 55yo. That is, 25% of the value of the lump sum savings at retirement would be paid every year. On a very basic calculation (and ignoring the 5-8% investment returns), a 25% conversion rate assumes that, on average, members only live for 4 years after retirement. In fact, the average that the life tables predict is 15 – 20 years. Clearly, to continue to pay such generous pensions requires cross-subsidisation by current members, who receive a lower crediting rate because investment income is redirected from paying current members accounts to making pension payments to retired members. While later pension conversion rates were less generous, they were still not actuarially based, and so require continued cross-subsidisation. Such an approach is not sustainable and has been a matter of some urgency for FNPF.

25. There have been some suggestions that existing pensions should be withdrawn, capped or reset at a discount. However, from commentary and discussion with stakeholders to date, there is little support for such an approach. Any retrospective adjustment of existing pension benefits would be difficult under contract law. Express provisions under a new Law would be required. This has obvious difficulties politically. Therefore, it is paramount that the provision of pensions both existing and new be put on a sound actuarial footing going forward. While an adjustment to existing pensions remains a possibility, it is not further considered in this paper.

26. Therefore, the two matters for Law are to quarantine the long-tail insurance activity of pensions and ensure their future delivery on a sustainable and prudent basis. Assuming existing pension are not adjusted, this means setting aside sufficient funds to ensure that future payments at the contracted rate are met. For new pensions, it means applying proper actuarial techniques to convert the lump sum savings into a future income stream. Further, to ensure transparency and avoid future cross-subsidisation, and in keeping with best practice principles, the insurance liabilities (pension) businesses should be separated from the collective investment (contributions management) operations of the general fund of FNPF. This separation may be achieved a number of ways, including through establishment of a separate corporate entity, a separate fund or a separate accounting entity.

27. To this end, FNPF has commissioned actuarial work to value the current pension obligations with the view of setting aside enough assets to support the existing pension liabilities as they are run off, and to identify actuarial assumptions for new pension conversion rates to ensure that they are sustainable.

28. In discussing these issues with stakeholders, there was acknowledgement and consensus that pension conversion rates in the past had been overly generous. Further, the need to separate the annuities business from the general fund was well understood and accepted, as was the principle that there should not be any further cross-subsidisation of the pensions business to the detriment of current members.

29. Similarly, it may be appropriate to establish other businesses in separate funds or accounting vehicles to provide transparency and ensure that they are also on a sound actuarial footing. To this end, FNPF should obtain actuarial advice to determine whether the offer and administration of other insurance risk products, such as special death benefits and funeral benefits, should be undertaken through separate funds.

30. In anticipation, the Law should provide for the establishment of additional funds to support provision of different insurance products. These products would then be regulated under the Life Insurance Act as appropriate.

Proposals

31. Policy principle: Pensions must be provided on a sustainable and prudent basis.

32. It is proposed that the Law provide:

- for the delivery of pensions (annuities) – current and future – through a separate fund (pension fund), to be accounted for separately to the fund that accepts, invests and administers the mandatory contributions (the latter is the "general fund"); and
- for the transfer/attribution of assets from the general fund (as appropriate, depending on the vehicle) to support the present value of existing pension liabilities through run off (subject to actuarial advice);
- any transfer should be protected under law and not trigger any event of default or crystallise tax liabilities;
- clarification that FNPF, as provider of the annuity, owns any surplus arising from allocation of excess reserves that support the run off of existing pensions and the provision of future pensions (that is, if the reserves to support pension payments are found to be in excess of reserving requirements as determined by an actuary, those reserves are not owned by annuitants). Such surplus may be transferred back to the general fund;
- no transfer of surplus reserves back to the general fund should occur for a reasonable period, (say 5 years) from the start date of the new Law; and
- provide for the establishment of one or more funds to conduct other business activities such as the offer of term insurance policies (such as death benefits and funeral benefits).[7]

A lifetime of saving for retirement must deliver some level of financial security in old age

Requirement to convert retirement savings accumulated throughout working life into income replacement in retirement

33. All stakeholders agreed that the primary objective for the mandatory savings scheme is to provide financial security after retirement. Currently, the majority of members take benefits as a lump sum at retirement; fewer than 30% of members convert these savings to a retirement income stream through the pension plan. While there is little data on how retired members who opt for lump sums invest and

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7 Term Insurance covers the risk of a particular event occurring during the term of the policy, usually a year. A premium must be paid annually to keep the policy current and coverage lapses otherwise. There is no residual or surrender value in the policy. Such products are likely to be subject to the Insurance Act, including in relation to product disclosure, accounting and actuarial requirements.

manage these funds in retirement, concerns were expressed by a number of stakeholders that, for too many retiring members, these savings are exhausted in a short period, including because of lack of experience in money management, family demands and the lack of thrift tradition. These concerns are supported by the results of surveys of retired members who opted to receive a lump sum.

34. Many countries have mandatory retirement savings schemes to ensure that workers save through their working life to provide for their financial security in retirement. To ensure maximum effectiveness of these mechanisms, many of these countries[8] mandate conversion of these savings into an income stream in retirement through the purchase of an annuity or other retirement product.

35. Therefore, a basic policy proposition to be considered for drafting the new Law for Fiji is whether the retirement savings scheme should, in addition to mandatory contributions, also require conversion of part or all of the retirement savings into regular payments at retirement to replace the wages no longer earned.

36. One of the challenges for Fiji is that the value of retirement savings for some members will not be enough to provide a meaningful income stream through purchase of a life annuity. There will also be members whose savings are well in excess of the amount required to provide a living pension. The Singapore's Central Provident Fund (CPF) provides some useful guidance for how Fiji may implement a policy that would require conversion of the mandatory retirement savings under the scheme into a retirement income stream.

37. Briefly, the Singapore CPF has set a "minimum sum" (SGD126K) that must be applied to either purchase an annuity or otherwise provide an account based pension. If an annuity, the annuity provider bears the risk of member longevity and the member retains no right to savings converted to the annuity. In an account based pension, on the other hand, the member bears the risk of longevity but retains ownership of the savings (that is, any undrawn savings go to the member's estate at death).

38. Account based pensions can also be used to provide an income stream for a limited period for those members who have not accumulated enough funds to be able to purchase a meaningful lifetime annuity. Savings could be drawn down over a period of 2, 5 or 10 years, depending on the initial value of savings and any provisions for minimum/maximum drawdown. The duration of payments will depend on the underlying value of investments and returns. As an alternative to an account based pension, a term annuity may provide a similar income stream where again, the annuity provider bears the risk of value of investments and performance but the duration is known.

39. Those members who have saved in excess of a "minimum sum" should be able to take the surplus as a lump sum or use it to purchase a higher value annuity or account based pension (or some combination).

40. Income replacement in retirement may also be achieved through the conversion of savings for an approved business purpose where the member will apply a portion of the savings to establish an income producing business. If such a policy is supported guidelines and an approval process would need to be established and should ideally be administered by a third party agency (not FNPF).

41. Some exemptions from mandatory conversion may need to apply. These could include:

[8] Singapore, Austria, Colombia, Uruguay, Chile, Costa Rica, Mexico and Peru all require mandatory conversion of all or part of retirement savings into an annuity or account based pension.

- the amount saved does not meet a specified minimum threshold;
- the member lives in a remote location where access to the post office or other financial institution to collect regular payments is not practicable;
- when the member permanently leaves Fiji.

De-monopolisation of Retirement Savings Industry in Fiji

42. A number of commentators have called for the de-monopolisation of FNPF. While a move to a competitive model for savings has some attractions, it requires a substantial redesign and restructuring of the existing arrangements especially given FNPF's responsibility for administration and enforcement of the law to protect employee rights and ensure employers meet their obligations. However, while a move away from a single savings scheme is not practical at this time, there is opportunity to provide competition and choice with respect to the post-retirement financial services business.

43. If the proposal regarding conversion of retirement savings to income replacement is accepted, this would be an ideal opportunity to introduce additional products and providers. RBF would need to license providers giving consideration to financial strength experience and commitment to Fiji as well as future investment management (clearly, the current foreign investment restrictions may need to be considered).

44. Additional retirement products should include account based pensions and possibly term annuities. RBF would determine the types of products that would be approved for the purposes of conversion of the proposed Preserved Account savings.

45. Opening this part of the business to new players would have little negative impact on FNPF activities because currently only a minority of members take up a pension and the annuity business has been a drain on FNPF finances.

Proposals

46. Policy principle: That a lifetime of savings for retirement should be converted into an approved income replacement option in retirement with members given the choice of provider.

47. It is proposed that the Law:

- establish the concept of a "minimum sum" that must be converted to a retirement income stream — the value of the minimum sum would be prescribed after actuarial assessment;
- provide that, on retirement, a member must convert up to the minimum sum[9] into a pension, annuity, account based pension or other similar approved product, that will provide him or her with a monthly income of not less than the amount prescribed after actuarial assessment for at a period of at least 3 years;

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[9] See discussion on Preserved and General Accounts below. It is envisaged that only amounts in the Preserved Account (70% of contributions) would be counted towards the Minimum Sum.

- require that the value of the minimum sum and minimum monthly income be subject to review every 3 to 5 years; and

- open up the provision of alternative retirement income products by providers to be licensed and approved by the Reserve Bank of Fiji (this has the potential effect to attract additional participants to Fiji's financial sector and capital markets).

Further, if the conversion of savings principle is accepted, it may be appropriate to provide the option for savings to be applied to an approved business purpose in accordance with guidelines. These arrangements would need to be administered by a third party agency such as National Planning.

Defined contribution scheme – guaranteed benefits or best endeavours management

Current Act creates a guarantee without financial backing

48. The current FNPF Act establishes a defined contribution (DC) scheme with certain "defined benefit" (DB) characteristics. The 3 key provisions are:

    - section 8 — which provides for a minimum crediting rate of 2.5%;

    - section 17 — which, in effect, provides a "capital guarantee" of the value of member contributions and the value of past crediting rates, that is, the amount to the member's credit does not relate to the actual value or performance of investments but rather is an accounting figure that corresponds to member's account activity – credits and debits; and

    - section 10 — which provides for the Government to provide liquidity support to FNPF in the event that FNPF cannot meet its payment obligations, and for Government priority in repayment of any such advances. This may be described as a "Lender of Last Resort" facility and given the size and liquidity of FNPF's assets, and its position in the Fiji economy, events that would result in the Government providing support under this section would appear to be highly unlikely.

49. In a 'pure' DC scheme, contributions accumulate and the value of the benefit at retirement is based solely on the amount contributed and performance of investments (investment value and earnings). The individual members bear the investment risk.

50. The International Organisation of Pension Supervisors (IOPS) has set out certain core principles, guidance and best practice on the regulation and supervision of pension schemes. With respect to DC schemes that provide absolute or relative guarantees of performance, such as those provided by sections 8 and 17, IOPS guidance is that the

    > ... providers need to have sufficient capital to honour these promises regardless of economic circumstances.[10]

    The amount of capital needed to support a continuation of the statutory guarantees in the Fiji context depends on supervisory requirements (not yet issued by RBF) and an actuarial assessment of risk and

[10] *Managing and Supervising Risks in Defined Contribution Pension Schemes*, IOPS Working Paper No 12, October 2010.

volatilities of assets. Initial estimates by actuaries suggest reserves of between 10-20% of assets (FJD400-700 million in allocated capital, excluding intangible assets). This would be in addition to the capital required to meet operational risks and failures and is substantially more than is currently reflected in the balance sheet of FNPF once reserves to meet the pension liabilities are allocated.

51. Moving to a pure DC scheme has advantages beyond eliminating the need to accumulate substantial reserves. The current FNPF scheme provides a "one size fits all" investment strategy – regardless of whether the member is 20 and has just entered the workforce or is 54 and considering taking their entitlement, the same investment strategy is applied. Yet an investor's risk appetite changes over his or her working life. Younger members should be looking to invest in high growth investments that give the best opportunities to build capital, although they are likely to carry higher risks. Members approaching retirement should be looking for conservative investments, to give them certainty and avoid volatility before the potential purchase of an annuity or pension stream. The current FNPF scheme cannot meet these alternatives needs.

52. A move to a pure DC scheme and removal of statutory guarantee of contributions and minimum crediting rate removes the need to accumulate free capital to support investment volatility and should provide for better returns to members in the short to medium term. That is, if FNPF is to accumulate surpluses to support continuation of the guarantees over say, 5-7 years. Optimistically, this will reduce potential crediting rates by only 3% or more per year for the 5-7 years and also assumes that there is no deterioration in the value and performance of investments

Removal of guarantees may impact confidence in the scheme

53. The view of a number of stakeholders was that it would be politically difficult to move away from the guarantee of the value of contributions provided under section 17 (capital guarantee of contributions) and, to a lesser degree, the guaranteed crediting rate under section 8. Several reviews have acknowledge a potential difficulty of moving away from capital guarantees on contributions but suggested that reforms at the least remove the 2.5% minimum crediting rate. This would reduce the amount of solvency but not eliminate the requirement.

54. The reality is that members currently bear this investment risk even though they may not realise it. In the absence of financial backing in the form of free capital, section 17 provides false comfort. There is potential for the total realisable value of investments to fall below the total value of member liabilities. Such a scenario is possible if there was a repeat of losses such as those experienced in 2009. If left unaddressed (no solvency reserves), this could create substantial inequities between generations of members. Older members who leave the fund early would receive 100 cents in the dollar, creating a growing shortfall of assets to liabilities that would be borne by new and younger members whose entitlement age is some years off.

55. In discussions with stakeholders, there was some confusion with respect to whether the Government provided a guarantee. In fact, it was suggested that the "Government guarantee" justifies both representation of Government on the FNPF Board and the Board's appointment by the Minister. However, while there may be an implicit guarantee of FNPF as "too big to fail", the guarantee is implied and not contained in the Act.

56. Section 10 provides:

> If the Fund is, at any time, unable to pay any sum which is required to be paid under the provisions of this Act, the sum required shall be advanced to the Fund by the Government and the Fund shall, as soon as practicable, repay to the Government the sums so advanced.

This section has not been used. Given the temporary nature of any advance and the priority for Government to be repaid, it would be more accurately characterised as a liquidity or "lender of last resort" facility rather than a guarantee of member contributions. Further, given the usual holding of government paper and liquidity, it is difficult to imagine circumstances whereby the facility would need to be activated even if the fund was technically insolvent (ie value of liabilities greater than the value of assets).

Proposals

57. Policy principles: FNPF must be well capitalised if it is to keep the current statutory promise to bear the investment risk and guarantee a minimum crediting rate. Alternatively, FNPF needs to move to management of investments on a best endeavours basis.

58. Consideration must be given to legislative amendment that EITHER:

- converts the scheme to a conventional DC scheme and provide for:
  - removal of the "capital guarantee" under section 17 and the guaranteed crediting rate under section 8;
  - the Fund to operate along the lines of a mutual fund or collective investment scheme, with each member's balance converted to units that reflect the value of underlying investments; and
  - the future potential for members to nominate alternative investment strategies for their savings within the Fund;

OR

- maintains the current basis of valuation of member savings (supported by appropriate solvency measures); and
  - continues to provide the equivalent of a capital guarantee of contributions and past annual crediting under section 17 with drafting amendments to provide transparency; and
  - charges RBF as supervisor with explicit responsibility to set solvency standards and transition arrangements to support the capital guarantee.

In the event that the policy decision is to continue with a capital guarantee of contributions supported by an appropriate solvency measures, it is recommended that a section 8 minimum crediting rate *not* be carried forward.

Early withdrawals from members' accounts

Saving for retirement versus saving for a rainy day

59. The primary objective of provident funds, as established, was to provide financial security post retirement, particularly where there was no Government provided pension or safety net. In discussions with stakeholders, there was universal support that saving for retirement should be the prime purpose of the FNPF scheme, although there was some variation in views with respect to a

member's ability to access funds prior to entitlement. Some stakeholders would like to see 100% of contributions preserved.

60. Most stakeholders made the point that, culturally, Fijians were generally poor savers and therefore, the only source of savings to meet life events – from education to medical emergencies – was in the account held with the FNPF. Unfortunately, with a savings rate of 16%, saving for financial security in retirement and providing early access to these savings are mutually exclusive [11] — that is, savings drawn and spent on education, family funerals, medical expenses or housing cannot be available in retirement (while there has been some encouragement for repaying such advances the response generally has been poor). Many stakeholders shared anecdotes of people who had worked all their lives and reached entitlement age but, because of early access, there were little or no savings for old age.

61. This retirement savings/early access conundrum has challenged successive FNPF Boards and management. Not only is it problematic from a retirement savings policy perspective, but early access is very costly to administer. It requires service centre infrastructure and staff, management and Board time, staff time to review applications and grounds for access, complaints handling, security to maintain "banking" chamber and so on. The nominal administration fee charged does little to offset these costs which are, in effect, cross-subsidised by those members who do not utilise early access arrangements and do not create such administrative costs. Further, early access has implications for liquidity management of the Fund.

62. Members may access savings for multiple purposes and can make multiple early withdrawals. The result is that there is no true preservation of savings until retirement. For example, in any year, a member could access 20-60% of funds standing to their credit (for a stated purpose) with the effect of virtually full withdrawal in 2 or 3 years.

63. To implement a balance that addresses the retirement savings/early access conundrum, the Malaysian and Singapore models may be instructive. Briefly, the Malaysian Employee's Provident Fund provides 2 accounts for each member – dubbed Account I and Account II. Account I stores 70% of the employer and member's monthly contribution, with the remainder of 30% going into Account II. Account I savings are strictly preserved until the member reaches 55 years old, is incapacitated, migrates or dies. Withdrawals from Account II are permitted for certain purposes related to housing (first home only), education and medical expenses. The Singapore model has a third account (Medisave) to meet medical costs.

64. This type of model was discussed briefly with a number of stakeholders including FNPF Board, RBF, Department of Finance and some union and employer representatives. At a high level, all considered that something similar would be a good compromise in the Fiji setting. Some stakeholders, while positive about this model, noted that the 30% may be too small a sum to provide a meaningful deposit for a house. Suggestions of 50/50 or 30/70 have been made.

65. The suggested 70/30 split between a "Preserved" account and a "General" account is based on the potential income replacement rate given contributions of 16% (See Figure 1 below). It is the rate that will provide meaningful income replacements at between 55-65%

[11] By way of comparison, Singapore's Central Provident Fund is a DC scheme with a rate of 35% (employer/employee) and provides early access for housing and medical reasons. An increase in the contribution rate in Fiji is outside the scope of this review.

Figure 1 – Example of Effects of Preservation Accounts and Income Replacement Potential

Age	20	Retirement Age	55yo
Gender	Male	Investment Return av	4%
Wages	10,000	Value in Preserved Account	~$80,000
Preserved Account – Contribution pa (70%)	1,280	Value of single life pension	~$110/wk
		Income Replacement Rate	~60%
General Account – Contribution (30%)	480	Value of General Account (assuming no early withdrawal)	~$32,000

Additional one off withdrawal to support first home construction or purchase

66. A possible solution to the concern regarding a housing deposit would be to allow each member a one-time only special drawdown of an additional 20% (ie 2/7th of the value to the credit of their Preserved Account) for the exclusive purpose of supporting the purchase or construction of a first home. That is, a member could access funds to their credit in their General Account (up to 30% plus any voluntary contributions) and 2/7th (20% of contributions made) of their Preserved Account. A restriction based on first home purchase or construction would mean that this additional access is not available for the purposes of renovations, loan repayments, purchase of investment property or similar (although such purposes may still be permitted for early access to funds in General Account depending on FNPF's early access and benefits policy). If the member subsequently sold the property, they would not be entitled to access this special drawdown facility a second time.

67. The first home access benefit should then be subject to the proviso that 100% of future contributions be allocated to the Preserved Account balance until the special drawdown is topped back up at which time, contributions will return to a 70/30 allocation. This would then ensure meaningful savings are accrued for financial security in retirement.

68. Early access to savings in the General Account would still be subject to conditions and purposes as set out in the Law or by the FNPF Board – compassionate grounds, education, medical, funeral and so on. It is not intended that the General Account be considered a bank deposit or current account. The goal remains to maximise savings to provide financial security in retirement.

Withdrawal on grounds of migration

69. As part of the reform process, FNPF Board and management have reviewed and limited early access benefits and conditions. One aspect that attracted particular comment in discussion with stakeholders was early access on the grounds of migration. While hard data was not reviewed, a policy may nevertheless be formulated and supported by Law without the need to quantify the size of the problem. Briefly, there have been incidents of member declaring that they are migrating, accessing funds and departing for a short period (1 or 2 years), only to return and re-join the Fund. A similar problem was experienced in Australia with dual citizens declaring that they were migrating permanently, only to return within 2 or 3 years.[12]

[12] The explanatory memorandum for the Law that removed the 'permanent departure from Australia' condition for early access stated that removal "... is based on a number of reasons, including that there is anecdotal evidence that this condition has been abused by people providing inconclusive or false evidence to trustees of their proposed permanent departure. In addition, removal of this condition will bring Australian arrangements more into line with overseas practice and make it easier for the Government to negotiate reciprocal social security agreements with other countries".

70. Australia has adopted a policy that as long as Australian citizens have the option to retire to Australia, superannuation funds should be preserved until retirement age either in Australia, or an equivalent fund in the country where they now live. There are certain reciprocal arrangements in place to meet this requirement.

71. A similar approach is recommended under Fiji's retirement policy with FNPF taking a similar stance and either retaining the funds until entitlement age or transferring the funds to a similar retirement savings scheme in the new country of residence under reciprocal agreements (these will need to be negotiated). Such reciprocal arrangements would see Fiji benefit by the return of Fiji citizens who have been working in countries such as Australia whereby superannuation contributions could be transferred into FNPF (or converted to deliver a retirement income stream).

72. Where no reciprocal arrangements are in place or are otherwise pending, to ensure that early payment for the purposes of migration is genuine, it is suggested to introduce a waiting period for release of funds (say 1-2 years). An exception may be where the amount standing to the credit of the member is less than a specified threshold, in which case funds could be released rather than bear the cost of administration of small value accounts.

Proposals

73. Policy principle: Fiji's retirement savings policy should ensure that members accumulate a meaningful level of savings through their working through appropriate preservation and limited early access arrangements.

74. It is proposed that the law:

- provide for the establishment of 2 accounts for each member:
  - Preserved Account — the balance would be strictly preserved until an entitlement event, that is, attaining entitlement age (currently 55), mental or physical incapacity or death of the member;
  - General Account — the balance would be available to early access for a number of limited grounds including certain compassionate, education and housing purposes as determined by the FNPF Board or under Law or otherwise preserved until an entitlement event;
- provide for the allocation of future mandatory contributions on the basis of 70% to Preserved Account and 30% to the General Account 2;[13]
- existing members' Accounts would be established by allocating the current balance for each member on a 70/30 basis;
- provide for voluntary contributions by or on behalf of members to be made to either Account, as nominated by the payer[14].

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[13] While 70/30 is suggested, another proportion may considered although to emphasise the retirement savings objective of the scheme, a higher percentage to the Preserved Account is appropriate is necessary to deliver meaningful retirement replacement options.

[14] If the voluntary contributions are to be pre-tax, there maybe some limits under taxation laws

75. With respect to special housing withdrawal from the Preserved Account, the law should provide that, if a member meets the criteria for first home purchase or construction (which should be prescribed by regulation), in addition to early drawdown of savings in General Account, the member may also draw up to 2/7th of the amount in his or her Preserved Account subject to the following conditions:

- "first" home ownership — each member may exercise this early access only once in a lifetime (a member who has previously withdrawn funds from an FNPF account for a housing purpose, would not qualify for the special housing withdrawal);
- 100% of future contributions will be directed to Preserved Account to repay the drawdown, after which time, future contributions will be allocated on a 70/30 basis.

76. With respect to migration, the Law should provide as follows:

- FNPF should have power to enter reciprocal arrangements, MOUs or other arrangements necessary to give effect to the transfer or receipt of benefits for members who migrate from / to Fiji;
- where a member advises the Fund of his or her intention to migrate permanently:
  - the FNPF will transfer funds to an equivalent fund in the member's new country if reciprocal arrangements are in place; or
  - if no such arrangements are in place, a waiting period of not less than 12 months will apply for the release of the funds.

These requirements should not apply if the value of funds to the credit of the member is under a specified threshold value, in which case payment will be made to the member on production of satisfactory evidence (for example, of proposed residency and visas, and proof of travel; if the member has dual citizenship, the waiting period should apply).

Improving coverage and collections

Fiji should maximise coverage of retirement savings arrangements

77. For the purpose of coverage and inclusion, the FNPF Act provides definitions of employer, employee and wages. In the past, some employers have acted against the spirit of the social policy of a retirement savings scheme and exploited shortcomings in definitions to avoid registering employees and paying contributions. In recent years, the FNPF Act has been amended to improve coverage but there remain a large number of casual, seasonal and contracted workers who are not covered.

78. Rather than attempt to develop new exhaustive definitions under the new Law, as a general policy proposition, the starting point for definitions of employers, employees and wages/salaries should rely generally on definitions under the Income Tax Act (Cap 201) administered by FIRCA. There may need to be some modification to align FNPF deductions with wages/payroll records rather than the broader definition of emoluments. Further, while employees earning less than $2,000 per annum threshold are exempt income tax, it is not intended that they be exempt from FNPF contributions.

Additional matters to be aligned with taxation administration

79. In addition to aligning definitions, FNPF collections and administration regime should align with tax requirements wherever practicable including identification of employers, identification and registration of employees, alignment of forms prepared by employers, leverage systems for the electronic submission of returns and contributions and alignment of collections timings.

80. The Law should provide for co-operative arrangements between FIRCA and FNPF for information sharing, systems development to improve efficiency, secondments, the possibility of joint inspections and similar.

Coverage campaign and amnesty

81. An objective of reforms supported by the new Law is to improve coverage and participation. Discussions with FNPF staff and stakeholders suggest that there are a number of employers who, over the years, have failed to register under the scheme meaning employees are not covered. FNPF staff advised that there have been cases of workers seeking benefits from FNPF even though they were never registered nor contributions made.

82. While the extent of the problem is undetermined, by offering a short-term amnesty, the reforms provide an opportunity to create a "clean slate" to encourage all employers to remedy any non-compliance – non-registration as employers, of employees or even unpaid contributions.

83. The Law could provide a statutory amnesty for all employers to register, register all employees and pay up outstanding contributions without penalty. This may include entering into a scheme of arrangements for payment, where payment in a lump sum would cause financial distress for the employer/company. A suggested amnesty period is 6 months (effectively around 12 months when combined with lead time for Law to be passed). In the intervening period, FNPF may consider suspension of investigations and proceedings but leverage the amnesty opportunity to obtain resolution to current actions against recalcitrant employers.

84. For the amnesty to be effective, FNPF would need a well-coordinated media and education campaign, aimed at both employers – to understand their obligations and employees – to understand their rights and put pressure on the employer to do the right thing. In addition, FNPF would need to put resources to assistance and field visits to educate and assist employers to comply.

Proposals

85. Policy principle: Fiji's retirement savings should cover as many workers as possible regardless of the type of employment contract, basis of remuneration or administrative location of employer. Employers should not be permitted to use technical loopholes to avoid paying employees their rightful benefits.

86. It is proposed that the Law:

- provide for alignment of definitions for employer, employee and wages with those in the Income Tax Act (Cap 201);
- provide for FNPF to enter co-operative arrangement with FIRCA including information sharing, systems development and joint efficiency initiatives;

- provide for alignment of administrative and collection schedules with taxation obligations;

- provide an amnesty (for 6 months from commencement of the Law) for employers to register, registration of employees and remediation of unpaid contributions and loss of earnings (either in a lump sum or by instalments as agreed with FNPF).

Governance of FNPF

Board members' duty should be to ensure that the Fund is maintained solely for the benefit of members

87. The current Act provides for the Ministerial appointment of six Board members, representing employers, employees and the Government. The Act does not address skills requirements or experience, and applies a mix of fiduciary responsibilities, explicitly excluding application of Part III the Trustee Act (which limits trustee investments).

88. In discussion with stakeholders (more so than reports and analysis), the appointment of Board members, their role and past performance came in for considerable criticism. Over the years, appointments have been seen as highly politicised and blamed for some of the poorer investment outcomes. A common theme was that Government had interfered too much in the operations and decision making of the Fund. The challenge of ensuring independence, avoiding of conflicts of interest and duties for appointees to statutory funds is not confined to Fiji.

89. Further, it is clear that the demands on Board members' time are substantial,[15] particularly given that some appointees are likely to have full-time jobs or hold demanding Government positions. In our view, the Board needs to be expanded, not only to share the workload, but also to engage Board members with appropriate finance, accounting, risk management and legal skills or other professional qualifications, as well as an unaligned chairman. The IOPS provided some guidance on governance boards of retirement savings schemes. While there is no hard and fast rule on Board size, the number of directors should reflect the size, complexity and expected workload of the institution.

90. The appointment of Board members by the relevant Minister is the typical model in many countries. The potential for conflicts of interest and politicising of such appointments is recognised and, while it is not possible to eliminate the risk, related laws often prescribe specific conditions to minimise problems. These include:

    - charging directors/trustees with clear responsibilities, for example, the *Superannuation Industry (Supervision) Act 1993 Australia* provides that a trustee of a regulated superannuation fund must ensure that the fund is maintained solely for the benefit of its members;

    - identifying the skills set and experience for appointment;

    - appointment terms that do not align with political terms;

[15] The appointment to the FNPF Board is complicated currently by diplomatic actions by Australia and others placing travel on appointees.

- appointment of independent[16] Board members (this is sometimes problematic since, by the nature of Ministerial appointment, independence may be challenged; however, this can be countered through a public expressions of interest/nomination process measured against transparent selection criteria);

- strict fit and proper person criteria imposed by the supervisor which may include licensing conditions on the individual (used in the UK and USA).

Board membership — proposals

91. Policy principle: The FNPF Board should comprise a majority of independent members. The Board's primary fiduciary responsibility is to act first and foremost in the best interest of Fund members – not representative groups, Government or even the wider interests of Fiji.

92. The Law should provide as follows:

    - the Board should be expanded to 7 or at a maximum 8 directors;
    - appointment of 1 representative from each of employers groups, trade union and Government (this would best be an ex-officio appointment from an appropriate Department);
    - appointment of 4 (or 5) independent Board members, one of whom is to be appointed as Chairman;[17]
    - specific criteria for appointment to be included in the Law;
    - all Board members must meet fit and proper person and suitability criteria to be set by the supervisor (these may include conditions for completion of initial and continuing training); and
    - the criteria that would disqualify an individual from appointment to the governing body should be clearly laid out in Law.

93. Further, the Law needs either to address, directly or possibly by reference to trustee laws, the duties and obligation of Board members with respect to acting in the best interest of members.

94. The Law should provide indemnities to Board members and FNPF staff who act in good faith.

95. In addition to guidance in the Law on criteria and skill set, it may be appropriate to develop guidelines on nomination, screening and selection process to provide greater transparency and confidence in appointments made by the Minister of independent directors.

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16 Please note, contrary to some comments received, we do not believe that independence is compromised merely by virtue of being a "member" of the fund. Independence problems and conflicts of interest arise as a result of representation, closeness or obligations to Government, other related party activities.

17 "Independent" would mean not nominated by the employer or trade union interests, or be the holder of Government office and not relate to fund membership.

Other Matters

Education, consumer protection and complaints resolution mechanisms

96. In Fiji, there is a general need to improve the level of financial understanding Fijians in the formal economy (tax payers) are exposed on an almost daily basis to the need to use the services of financial institutions, from deposits and withdrawals and transfers with banks, through consumer loans and credit cards to insurance activities and retirement savings with FNPF and ultimately post-retirement finances. FNPF should play an active and leading role in improving financial knowledge of its membership. This objective could be included in the Law.

97. New consumer protection laws are currently being drafted under a project sponsored by the European Union. While it is beyond the scope of this paper to address or review those proposals, the project is not expected to address FNPF explicitly. Therefore, the new Law for Fiji's retirement savings scheme should provide for a dispute resolution as a matter of good public policy.

98. The RBF is the prudential supervisor of Fiji's financial sector and has certain responsibilities for consumer protection and laws administered. However, central banks generally have no tradition of dealing with members of the public and consumer protection or resolution of disputes between individuals and financial institutions. We understand that the RBF has received some criticism from the Consumer Council and other commentators for being too passive in matters related to direct consumer complaints. The RBF's new Consumer Complaints Unit has been established to address some of these problems.

99. Given both the FNPF reforms and review of consumer protection laws, it seems timely to suggest that as part of these reforms, consideration be given to establishment of a Financial Industry Ombudsman. Given RBF's responsibility for regulation and supervision of the sector, it makes some sense to establish an Ombudsman under the auspices of RBF but with independence and powers to deal with all financial sector related consumer issues. There are a number of highly regarded models that could provide a blueprint.

Family Law provision

100. Through discussions with stakeholders, it is understood that clarification is required with respect to entitlements in the event of breakdown of a marriage or de facto relationship. The general principle should be that retirement savings are treated the same way as other assets.

101. While the division of assets is a matter for the Family Law Act and associated proceedings, the FNPF Act needs to be able to implement any decision on a "clean break" basis, rather than waiting until actual retirement of the affected members to allocate the funds. Therefore, FNPF must be able to establish a new account for the ex-spouse receiving the savings even if not otherwise employed.

Whistleblower obligations and protections on staff and auditors

102. In the absence of more general whistleblowing laws and protections, the new Law should provide for:

- protections on whistleblowing by internal staff; and
- an obligation on the external auditors and actuaries to report to the RBF on certain matters and associated protections.

FIJI NATIONAL PROVIDENT FUND

AUDIT COMMITTEE PAPER

DRAFT AUDITED FINANCIAL ACCOUNTS FOR YEAR ENDED 30 JUNE 2006

1.0 DRAFT AUDITED ACCOUNTS FY2006:

This paper presents the Draft Audited Consolidated Accounts for FNPF and its subsidiaries for the Financial Year ended 30 June 2006.

KPMG had finalized the audit of the Financial Accounts for the Fiji National Provident Fund (The Fund) during the month of August. However, we were unable to finalise the Consolidated Accounts due to the delay in the receipt of the Home Finance audited accounts, which was only received last week on 6th September. Delays were also experienced in the compilation and confirmation of financial statements for FNPF Investments Limited.

The Pre-issuance review (by a second partner of KPMG) will be completed by 14th September, and the Audited Accounts will technically be ready for signing by Friday 15th September 2006. This is in line with Management target to have the accounts signed within 3 months of year-end.

The Audit Management Letter is expected to be received within two weeks. Most issues identified during the Audit have been discussed thoroughly between Management and the Auditors. However, a couple of reconciling issues relating to Contributions and Pensions Payable still needs to be addressed, and Management is currently reviewing this process to determine whether any further adjustments are necessary before the Board meeting on 19th September 2006. The reconciling amounts are deemed immaterial and should not affect the finalization of the Audited Accounts for FY2006.

2.0 COMPLIANCE TO RECENT CHANGES IN ACCOUNTING STANDARDS:

The preparation of the Consolidated Financial Statements has, as far as possible, taken into account recommendations from Professor Michael White of USP, to ensure that FNPF is in compliance with recent changes to the Fiji Accounting Standards that are applicable to accounts prepared in FY2006.

Further changes will be effected during the course of the current Financial Year (FY2007), to align the Financial reporting to International Financial Reporting Standards (IFRS) that will become effective from 1st January 2007. IFRS will replace the Fiji Accounting Standards (FAS) as the acceptable standards for financial reporting in Fiji. FNPF Management is opting for early adoption of IFRS.

2.0 FINANCIAL PERFORMANCE IN FY2006:

The following is a summary of FNPF's Financial performance for the year ended 30 June 2006, as extracted from the draft Financial Statements:

2.1 AT THE FUND LEVEL:

SUMMARY OF KEY INDICATORS – At the FUND level;

Key indicators:	(Draft Audited) FY2006	Audited FY2005	Comments
OPERATIONS			
Contributions Collected	$267.655m	$245.678m	Growth rate of 8.95%
Member withdrawals	$213.194m	$185.038m	Increase of 15.22%
Net Contribution [C]-[WD]	+$54.46m [267.65-213.19]	+$37.99m (245.68-207.69)	FY target $34m ($260m-$226m).
Net Pensions [P-A]	($10.97m) [23.84-34.81]	($10.48m) [21.26-31.74]	Excess paid from Pension reserve
Member Balance YTD 30/06/2006:	**$2.325billion**	**$2.166billion**	**Growth 7.36% (FY target 7.00%)**
General Reserve Account (GRA)	**$915.607m**	**$832.315m**	**Growth 10.01%**
Total Operating Expenditure (Net)	$13.106m	$11.43m	Savings of $3.814m on budget of $16.92m
Total Operating Expenditure Ratio	4.90% (Net TOER)	4.43% (Net TOER)	FY target less than 6.5%.
Net Surplus for the Year	**$490.644m**	**$398.931m**	**Growth 23%**
INVESTMENT			
Total investment Portfolio (ex. Cash)	**$3.149billion**	**$2.930billion**	**Growth 7.47% (FY target +5%)**
Cash (Bank/Hand)	$23.857m	$16.26m	Uninvested funds
Interest received	$130.219m	$121.911m	Increase by 6.81%
Dividend received	$25.738m	$24.230m	Increase by 6.22%
Property Rental	$3.943m	$3.708m	Increase by 6.34%
Realised capital gains	$36.74m	$12.475m	Large gains due to $200m repatriated .
Realised exchange gains	$1.985m	0	On repatriation
Unrealized capital gains	$32.697m	($1.605m)	On balance of AUD shares
Unrealised exchange loss	($1.404m)	$7.869m	On conversion of AUD balance to FJ
Unrealised gains – on revaluation	$10.877million	0	Booking of Market Values for properties
Investment Income Changes in net MV Total Inv Income	$159.90m + $80.90m $240.80m	149.85m +$18.74m) $168.59m	Income return 5.08% Capital return 2.57% Total return 7.65%
ROI (Gross)	**7.65%**	**5.74%**	**FY target 6%.**
Net Assets	**$3.241billion**	**$2.998billion**	**Growth 8.11%**

2.2 AT THE CONSOLIDATED LEVEL:

SUMMARY OF KEY INDICATORS – At the Group level;

Key indicators:	(Draft Audited) FY2006	Audited FY2005	Comments
Total Revenue	$730.855m	$659.796m	Growth 10.77%
Total Expenses	$224.011m	$207.788m	Increased by 7.81%
Income tax Expense	$24.925m	$12.494m	Increased by 99.50%
Net Surplus for the Year	**$454.694m**	**$417.281m**	**Growth 8.97%**
Net Assets	**$3.359billion**	**$3.145billion**	**Growth 6.80%**

2.3 General Information

The Board is requested to note the following pertinent information in relation to the Financial Statements for FY2006:

- Private Equity Shares: An independent valuation of the shares held by FNPF in FNPF Investments Limited and Home Finance was carried out in 2006 by the firm of Ernst & Young. The valuers have recommended the following values as an appropriate measure for;
    - **Home Finance – Share value of $1.95 (using FME)**
    - **FNPF Investments Ltd – Share value of $1.01 (using NTA)**
- The above values have been reflected in the Accounts

- Revaluation of Investment Properties: An independent valuation of the Investment Property portfolio was carried out in 2006 by Rolle Valuers. The Investment Property portfolio is now booked at Fair Value.

- Goodwill Impairment Tests: As a result of Impairment tests carried out on the carrying value of the Goodwill for ATH and Home Finance, a total of **$5.874million** was booked as impairment loss, of which **$5.75million** is the write down of the Goodwill relating to ATH shares, while the balance of **$124,000** represents the complete write-off of the Goodwill relating to the acquisition of Home Finance shares.

- Use of Same Auditor for Home Finance: The FNPF Board had previously recommended to the Board of HFC that the company's external audit be conducted by the Fund's Auditors to ensure alignment of accounting policies and reporting standards and timely completion of the audit. This needs to be pursued again this year.

3.0 RECOMMENDATION:

Board Audit Committee is requested to review the Draft Audited Financial Accounts for FY2006, and to authorize that the draft Accounts be dated 15th September 2006, and that it tabled to the Board at its meeting on 19th September.

Otr/ftn/jyf 12/09/2006

HOUSE OF REPRESENTATIVES QUESTIONS

SESSION OF JUNE 2006

THE MEMBER FOR Member for Nadi Indian Rural CONSTITUENC

(Hon. Perumal Mupnar)

TO ASK The Minister for Education, Youth & Sports

FOR AN ORAL/WRITTEN REPLY ON THE DAY FOR WHICH NOTICE HAS BEEN GIVEN

Registration No	QUESTION	Notice given For Reply
28/06	Would the Minister for Finance and National Planning inform the the House on the following – (a) What is the percentage of Fiji National Provident Funds money that has been loaned or owed by the Government of Fiji for its direct operation and 100% Government owned subsidiary companies in the form of Direct Loans, Treasury Bills, Bonds and Government Guarantees) and (b) If breakdown in figures for Government of Fiji and its subsidiary companies could be tabled separately.	23/6/06

Response to Parliament Question No 28/06 by the Minister for Finance & National Planning.

1. Mr Speaker Sir, on the question of how much is owed by the Fiji Government to the FNPF, I wish to inform the House that as at 31 May 2006 the total amount owed is F$1,611,954,108. This amount makes up 50.84% of the Fund's total portfolio of F$3,170,597,606.

2. On the question of how much is owed to the Fund by the Government owned institutions I also wish to inform the House that the total amount owed is F$368,771,656 which makes up 11.63% of the Fund's total portfolio. All these loans are currently guaranteed by the Fiji Government but the institutions have been given notice that the guarantee may not be available in future. These institution includes Housing Authority, Fiji Development Bank and Fiji Electricity Authority.

3. On the breakdown of the amount owed by these institutions, Mr Speaker Sir it is as follows:

Fiji Development Bank	F$161,891,789
Fiji Electricity Authority	F$ 75,362,022
Housing Authority	F$ 92,667,995
Fiji Pine Ltd	F$ 15,752,306
Fiji Hardwood Corporation	F$ 7,031,068
Suva City Council	F$ 10,163,759
Others	F$ 5,902,722

- (Labasa Town Council - $ 346,849.90
  (Ba Town Council - $3,369,975.52
  (Fiji Sports Council - $2,185,897.27
  $5,902,722.69

22 June 2006