



BANK OF PAPUA NEW GUINEA
SUPERANNUATION PRUDENTIAL STANDARD 1/2014
AUTHORISED SUPERANNUATION FUND INVESTMENTS
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PART I PRELIMINARY

- 1) **Title:** This Standard may be cited as *Superannuation Prudential Standard 1/2014 Authorised Superannuation Fund Investments*.
- 2) **Authorization:** The Bank of Papua New Guinea (“Bank”), acting under Section 43 of the *Superannuation (General Provisions) Act 2000* (“Act”) and all other powers enabling it, determines this Standard.
- 3) **Application:**
 - a) This Standard applies to all Licence Holders licensed under the Act unless the context indicates otherwise.
 - b) Where provisions of this Standard apply specifically to a Licensed Fund Administrator and Licensed Investment Manager, these Licence Holders shall be referred to collectively as ‘*Licensed Service Providers*’.
 - c) This Standard applies to all Officers as defined under Section 3 of the Act unless the context indicates otherwise, the term director, chief executive or a manager is specifically used.
- 4) **Definitions/Interpretations:** In this Standard, unless the contrary intention appears, capitalised terms that are defined in the Act, have the same meaning when appearing in this Standard. The following definitions also apply.

“Investment Framework” means a document setting out the ASF's investment objective and investment strategy, including selection and management of investments and management of risks, that is consistent with the matters prescribed in paragraphs 10 to 34 of this Standard.

 - a) “Trustee Board”- For the purpose of this Standard, the Board of the Licensed Trustee is referred to as the “Trustee Board”.
 - b) “Investment Management Agreement” means an agreement between the Licensed Trustee of an ASF and an Investment Manager for the provision of investment management services to the ASF.
 - c) “Custodian” means the party which the Trustee Board has contracted to provide safekeeping services for the assets of the ASF.
- 5) **Commentary:** Commentaries in this Standard are included for guidance.

PART II STATEMENT OF POLICY

6) Purpose:

- a) This Standard prescribes requirements about an ASF's investments and related matters. It should be read in conjunction with Section 71 and 71A of the Act.
- b) The ultimate responsibility for the sound and prudent investment of members' funds rests with the Trustee Board.
- c) It is essential that the Licensed Trustee has a sound Investment Framework for the selection, management and monitoring of investment risks and conducts its affairs with a high degree of integrity for the benefit of the members.
- d) An Investment Framework is the totality of systems, structures, policies, processes and people to address the Trustee Board's responsibilities with regard to investments of the ASF.

7) **Scope:** All ASFs and relevant Licence Holders must comply with this Standard except where specific provisions are stated to apply only to a Licensed Investment Manager or Licensed Fund Administrator.

8) **Responsibility:** It is the responsibility of the board of directors of all Licence Holders to comply with this Standard.

PART III IMPLEMENTATION AND SPECIFIC REQUIREMENTS

9) Investment Framework

- a) The Trustee Board must develop, document and maintain an Investment Framework, in consultation with the Licensed Investment Manager.
- b) In developing the Investment Framework, the Trustee Board must take into account the size, complexity and risk profile of the ASF.
- c) The Trustee Board must review the Investment Framework on a regular basis (at least annually).
- d) The Trustee Board must consult with and obtain the advice of the Licensed Investment Manager when formulating or amending the Investment Objective and the Investment Strategy.

- e) The Trustee Board may consult other experts it considers necessary in the analysis, review and management of the ASF's investments.
- f) A copy of the Trustee Board's approved Investment Framework must be submitted to the Bank. Where any changes or revisions are made to the Investment Framework or to any part of the Investment Framework, a revised version must be submitted in 'track changes' mode.
- g) The Investment Framework must include, as a minimum, the requirements in paragraphs 10 to 34 of this Standard.

10) *Responsibility for Investment Decisions*

- a) The Investment Framework must provide that the Trustee Board is responsible for making investment decisions.
- b) The Trustee Board may delegate particular functions to its investment committee or the Licensed Investment Manager, but the Trustee Board cannot delegate responsibility for investment decision-making.
- c) All delegations of authority must be documented, approved by the Trustee Board and reviewed on a regular basis.
- d) The Trustee Board must put in place mechanisms to monitor the exercise of delegated authority.
- e) The Trustee Board cannot abrogate its responsibility for any functions that it delegates.

11) *Separation of Functions*

- a) There must be clear separation between the decision making function of the Trustee Board and the investment advisory function of the Licensed Investment Manager.
- b) The Investment Framework must clearly define the investment functions to be undertaken by the Trustee Board and the delegated investment functions to be undertaken by the Licensed Investment Manager.

12) *Written Agreement with the Investment Manager*

- a) The Investment Framework must provide that the ASF must at all times have in place a written agreement with its Licensed Investment Manager.
- b) The written agreement must provide that the Licensed Investment Manager must fully disclose all fees, commissions or any other benefits, which are to be

derived directly or indirectly by the Licensed Investment Manager or any related party.

13) *Investment Objective and Investment Strategy*

- a) The Trustee Board must consider and document the investment objective and the investment strategy for the superannuation benefits held for members of the ASF and document how it has complied with each of the requirements of Section 71 (2)(f) of the Act.
- b) The Investment Objective must be measurable and quantifiable.

14) *Investment Objective and Investment Strategy for Reserves*

- a) The Trustee Board must:
 - i) consider and document the objective and purpose of each reserve which it maintains;
 - ii) determine an investment objective and an investment strategy for each of the reserves it maintains, which must be appropriate for the objective and purpose of maintaining each reserve.
- b) develop and document a comprehensive Reserving Management Policy, in consultation with the Licensed Investment Manager, for all reserves which it maintains.
- c) The Reserving Management Policy must be part of the Investment Framework for the ASF and must be reviewed on a regular basis (at least annually).
- d) The Reserving Management Policy must be published in the Annual Report to members including being published in the public section of the ASF's web site.

Commentary:

1. Investment fluctuations reserves are generally held for the purpose of maintaining a reserve to enable the Trustee Board to minimise the likelihood of negative crediting rates. As such, the assets held as reserves should be invested in a manner consistent with that objective and not invested in line with the general pool of assets held by the ASF for members.
2. Section 71A of the Act currently limits reserves to a maximum of not more than 2% of the total value of the assets of the ASF at that time. Where an ASF wishes to operate a reserve or reserves, which in aggregate, exceed 2% of the total value of the assets of the ASF at any time, the Trustee Board must request approval in writing from the Bank

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for the higher percentage and for the investment objectives and strategies for each of the reserves.

3. If such approval is granted, the Bank may require that the Trustee Board undertake a membership education program to enhance the understanding and acceptance by the members and the general public of investment fluctuations and investment volatility.

15) *Application and Management of Reserves*

- a) The Trustee Board must ensure that, each reserve, which it maintains must only be used in accordance with the purpose for which each reserve was established.

Commentary:

1. The reserves of an ASF are monies forming part of the net assets of the ASF that have been set aside for a clearly stated purpose. Not all unallocated monies constitute reserves and this includes such things as defined benefit fund surpluses and suspense accounts used to record contributions and rollovers pending allocation to their specific members' accounts. Main classes of reserves include:
 - a. Administration reserve used to fund future administration and operational expenses of an ASF;
 - b. Investment fluctuation reserve used in conjunction with crediting rates in an ASF to smooth the impact of market fluctuations on members' account balances over a number of years.
 - c. Operational risk reserve used to hold the financial resources to meet an ASF target amount.
2. Reserves are largely concerned with contingent events and, as such, it is expected that the Trustee Board must exercise judgement in determining the need for them, their scope, size and operation.

16) *Review of the Investment Objective and the Investment Strategy*

- a) The Investment Framework must provide that the investment objective and the investment strategy are to be regularly reviewed by the Licensed Investment Manager and the Trustee Board and that a review must be conducted at least annually.
- b) The triggers which would result in a more frequent or immediate review must be documented in the Investment Framework.

17) *Interim Crediting Rate Policy*

- a) The Trustee Board must develop and document an Interim Crediting Rate Policy, in consultation with the Licensed Investment Manager, for the

members who exit the ASF before the final crediting rate has been approved, must be included in the Investment Framework.

- b) The Interim Crediting Rate Policy must be fair and equitable for all of the members of the ASF, including the exiting, current and prospective members.
- c) The Interim Crediting Rate Policy must be reviewed on a regular basis (at least annually).
- d) The Interim Crediting Rate Policy must be published in the Annual Report to members and the public section of each ASF's web site.

18) *Annual Crediting Rate Policy*

- a) The Trustee Board must develop and document an Annual Crediting Rate Policy, in consultation with the Licensed Investment Manager, for the members of the fund which is fair and equitable for all of the members of the fund, including exiting, current and prospective members.
- b) The Annual Crediting Rate Policy must be reviewed on a regular basis (at least annually).
- c) The Annual Crediting Rate Policy must be published in the Annual Report to members and be published in the public section of each ASF's web site.

19) *Annual Review and the Crediting Rate Process*

- a) The Trustee Board must ensure that the Annual Review of member records in the ASF, is completed before applying the Annual Crediting Rate.
- b) The Trustee Board must have in place an Annual Review Policy detailing the annual review process to reconcile the financial accounts of the ASF kept by the Licensed Trustee with the administration system maintained by the Licensed Fund Administrator.
- c) The Annual Review Policy must detail the process to reconcile the financial accounts to the administration system.
- d) The Trustee Board must ensure that:
 - i) the differences and the reasons for the differences between the financial accounts and the administration system are recorded; and
 - ii) that there is adequate control over the differences including a detailed plan of the actions to be taken by both the Trustee Board and the Licensed Fund Administrator to deal with all differences.

- e) The Annual Review Policy must be documented and included in the Investment Framework.
- f) The Annual Review Policy must be reviewed on a regular basis at least annually.

20) *Liquidity Management Policy*

- a) The Trustee Board must develop, document and maintain a Liquidity Management Policy in consultation with the Licensed Investment Manager, and include the policy as part of the Investment Framework.
- b) The Liquidity Management Policy must be reviewed on a regular basis and the triggers for more frequent review must be considered and documented in the Liquidity Management Policy.

21) *Unlisted Asset Valuation Policy*

- a) The Trustee Board must develop, document and maintain an Unlisted Asset Valuation Policy, in consultation with the Licensed Investment Manager, and include the policy as part of the Investment Framework.
- b) The Unlisted Asset Valuation Policy must be reviewed on a regular basis and the triggers for more frequent review of the Unlisted Asset Valuation Policy should be considered and documented in the policy.

Commentary:

1. The Trustee Board needs to consider the valuation issues that are posed by the various types of investment structure through which it may gain access to private markets.
2. Similarly, valuation issues specific to different asset classes need to be considered by the Trustee Board. Examples include direct property, infrastructure assets and private equity.
3. The following aspects of the valuations process for unlisted assets should be considered by the Trustee Board (this should not be taken as an exhaustive list):
 - a. Select the optimal valuation source, in terms of transparency and appropriateness.
 - b. The valuation methodology should be appropriate for the investment, robust and applied consistently from one period to the next.
 - c. Frequency of revaluation. Periodic valuation for assets that are not regularly traded should be obtained independently and updated regularly, particularly in times of market volatility. The Bank

expects the Trustee Boards to apply the latest available valuation for the calculation of performance. There should be a clear basis for determining the frequency of valuation, and a clear policy indicating circumstances that would necessitate an immediate revaluation in between periodic valuations.

- d. Monitoring the process around any use of indexation as a proxy for asset value movements (for the period between formal valuations of the asset).
- e. Determination of the events and circumstances upon which the assumptions underlying the valuation would need to change, which may result in a revaluation of the unlisted asset.
- f. When adopting a particular valuation (whether or not internally sourced), the Trustee Board needs to demonstrate what considerations have been made, including consistency with previous valuation exercises.

4. External advice

- a. The Bank notes that Trustee Boards will engage external parties to provide input into the valuation process. Aspects to consider by the Trustee Board in relation to its external valuers' include reputation; resourcing; qualifications; areas of specialisation; experience and methodology/process undertaken.
- b. As with all examples of reliance on external advice, the Bank expects the Trustee Board to make appropriate enquiries into the results of the advice. This would include, for example, querying the basis for valuations that appear to depart from economic fundamentals.
- c. While the Bank does not expect the Trustee Board to substitute their own technical judgment for that of appropriate experts, the Bank does expect the Trustee Board to ask questions to ensure they understand the basis for valuations and if not satisfied, initiate further appropriate action.

22) Conflict of Interest Policy

- a) The Investment Framework must include a conflict of interest policy and procedures to recognise, assess, monitor and manage all material conflicts, both potential and actual on an on-going basis.
- b) The Conflict of Interest Policy must provide that the first priority is to avoid any conflict of interest and only where that is not possible to avoid the conflict of interest, the policy must detail the procedures to be followed.

- c) The Conflict of Interest Policy must be part of the overall Governance Framework of the ASF as required by *Superannuation Prudential Standard 7/2012 Corporate Governance*.

23) *Submission of Investment Proposals*

- a) The Investment Framework must provide that all investment proposals, wherever they are sourced, must be submitted directly to the Licensed Investment Manager and not to the Trustee Board.

24) *Minimum Requirements for Preparing and Submitting Investment Proposals*

- a) The Trustee Board must ensure that the Investment Framework contains the minimum requirements for preparing and submitting investment proposals specified in paragraph 24 (c) below.
- b) The Trustee Board must ensure that the Licensed Investment Manager complies fully with all of the minimum requirements for preparing and submitting investment proposals.
- c) The minimum requirements for preparing and submitting investment proposals must include, where relevant:
 - i) Whether the investment complies fully with the Act and other relevant legislation;
 - ii) Whether the investment proposal complies with the investment objective and the investment strategy approved by the Board;
 - iii) A business case or viability analysis;
 - iv) The total cost of the investment;
 - v) An assessment of the investment risk including counter-party risk and currency risk (if it is likely to involve international transactions);
 - vi) An assessment of the key assumptions made in the proposal;
 - vii) An assessment of the stress testing or sensitivity analysis;
 - viii) An assessment of the investment risk determinations, risk mitigations to be applied and recommendations;
 - ix) All fees and commissions that will be derived by any party as a result of a decision by the Trustee Board to make the investment;
 - x) The effect of the acquisition or disposal on the investment objectives of the ASF;

- xi) The effect of the acquisition or disposal on the investment strategies of the ASF;
- xii) The effect of the acquisition or disposal on the performance of the investment portfolio;
- xiii) The valuation of the annual return on the investment on a stand-alone basis;
- xiv) An assessment of the method applied in arriving at the annual return, comparison of the applied method with alternative methods and the reasons why the method applied has been adopted;
- xv) An assessment of the current value of the investment;
- xvi) The method applied in arriving at the current valuation, comparisons of the applied method with alternative methods of valuation and the reasons why the method applied has been adopted;
- xvii) An assessment of the future value of the investment;
- xviii) The method applied in arriving at the future valuation, comparisons of the applied method with alternative methods of valuation and the reasons why the method applied has been adopted;
- xix) An assessment of the exit strategy for the investment; and
- xx) An assessment of the events that will require a review of the exit strategy for the investment.

Commentary:

1. Paragraph 24 of this Standard does not apply to minor adjustments to current asset holdings.
2. Paragraph 24 of this Standard does not apply to Treasury Bills issued by the Bank.
3. Exit Strategy is the plan for disposing of the asset. This would include the means by which the ASF would exit the investment, the timing of the exit, triggers for the exit such as valuation and return on investment movements. For joint ventures, the exit strategy would include the ability of the ASF to dispose of its holding in the joint venture or other parties.
4. The Bank expects that proper due diligence, including assessment of conflicts of interest and analysis of the purchaser would be conducted as part of the consideration of any decision to dispose of an asset.

5. The Bank expects that for any new development project, that there would be an analysis of the project management and project engineering plans prior to making the decision.

25) *Trustee Board Consideration of Investment Proposals*

- a) The Investment Framework must provide that investment proposals may only be considered by the Trustee Board on receipt of an analysis of each investment proposal with a recommendation from the Licensed Investment Manager.
- b) Subject to paragraph 25 (a), the Trustee Board must ensure that each Director fully understands and is able to explain the potential risks of the proposed investment.

26) *Regular Review of Investment Proposals against Investment Outcomes*

- a) The Investment Framework must provide a process for the Trustee Board to conduct regular reviews of a representative sample of the investment proposals which have been made, including where possible those rejected by the Trustee Board, against actual outcomes.
- b) The Trustee Board must then review and revise the Investment Framework including the minimum requirements for investment proposals and the minimum requirements for considering investment proposals to take into account the outcomes of the reviews.

27) *Regular Review of the Assets of the ASF*

- a) The Investment Framework must provide that the Trustee Board and the Licensed Investment Manager will conduct regular reviews of the investment portfolio as a whole and of each of the assets held by the ASF under its existing asset allocation at least annually.
- b) The triggers for a more frequent review of each asset or each asset class must be considered by the Trustee Board and documented in the Investment Framework.

28) *Asset Transfers and Titles*

- a) The Investment Framework must contain a process for authorisation and transfer of assets and must document the means by which the Trustee Board will ensure that the assets are:
 - i) to be transferred on acquisition;
 - ii) to be transferred on disposal; and

iii) to be held safely and securely whilst they are owned by the ASF.

- b) The Trustee Board must ascertain that all assets of the ASF exist, are in the legal possession and control of the ASF, are correctly valued and registered in the appropriate name of the Licensed Trustee Company as trustee for the ASF.

29) *Custodian*

- a) The Trustee Board must be satisfied that it has a clear understanding of the custodian arrangements in place to hold the assets of the ASF and that these arrangements are safe and transparent.

Commentary

1. It is the duty of the Trustee Board to make certain they have a complete understanding of the risks and responsibilities associated with the custody arrangements of the ASF. Custody services must be monitored on an ongoing basis.
- b) Where the assets are not held directly by the ASF, the Trustee Board must ensure that the ASF's assets (other than cash) are kept distinct and separate from the custodian's own assets. The ASF's assets must be accurately and completely identified in the account books of the custodian, and this should be verifiable during the internal and external audit processes.
- c) The Trustee Board should consider whether the custodian's controls ensure that the ASF's assets are secure and whether the custodian has appropriate procedures for the acceptance and implementation of authorised instructions.
- d) The Trustee Board should seek periodic information from the custodian in respect of the adequacy and effectiveness of such controls and actions taken or planned to address any concerns.
- e) The Trustee Board must ensure that the custodian has and continues to have, the appropriate organizational structure, staffing capabilities, administrative resources and arrangements for holding the ASF's assets.
- f) In assessing the custodian's financial soundness, the Board must consider the adequacy of the custodian's capital and its insurance or guarantee arrangements.
- g) The Trustee Board must ensure that there is in force at all times a written agreement and that it must be subject to PNG Law unless the assets held via that contract are foreign assets and there are local laws that prevent the contract being subject to PNG law.

- h) The following issues must be addressed in the custodian agreement:
- i) that the custodian is prohibited from taking a charge, mortgage, lien or other encumbrance over, or in relation to, assets of the ASF. The custodian may, however, do this for expenses and outlays made within the terms of the agreement (but not including unpaid custodian or subcustodian fees)
 - ii) that the custodian accepts responsibility for liability arising from its failure, or failure of its agents and/or its subcustodians, to exercise reasonable care based on the standards applicable to the custodian in the relevant market
 - iii) that in the event that the ASF suffers loss due to those acts or omissions for which the custodian is liable, or for which it accepts liability, the custodian will first restore the ASF to its position prior to the loss and then independently pursue its rights against other parties;
 - iv) that the custodian will, prior to arranging for assets of the ASF to be held by a subcustodian, provide the Board of the ASF with written notice of the identity of each subcustodian with which the assets of the ASF are intended to be placed;
 - v) that the custodian will notify the ASF in writing of any subsequent appointments of new or replacement subcustodians, at the earliest practicable time but in any event, no later than 10 business days after the appointment has been made;
 - vi) the process for the Board of the ASF providing authorised instructions to the custodian;
 - vii) the process for and timing of the custodian providing periodic reports, including notifications of any transfers to, or from, the ASF's account; and
 - viii) that the agreement may be varied, if necessary and with the consent of both parties, in order to meet any changes to the Central Bank's prudential requirements or other relevant legislation;
 - ix) that the agreement will facilitate for each material and/or systemic breach of the agreement to be brought to the Board's attention for consideration. The agreement must provide for such reporting to be within a reasonable time of the custodian becoming aware of the breach.

- x) the agreement must provide that it is able to be terminated where the ASF has reasonable grounds to believe that the custodian is not complying with, or is unlikely to comply with, this Standard or any requirements of the Prudential Standards, the agreement, or other relevant legislation.

Commentary

1. Further grounds for termination may be set out in the agreement at the election of the ASF. These may include:
 - (a) where the custodian is unable or is about to become unable, to meet its liabilities; and
 - (b) where there is a change in the effective control of the custodian. This may occur, for example, through an acquisition or merger.
- xi) The agreement must provide that upon termination, assets must be transferred into the name of the ASF (if not already held in the name of the ASF) or otherwise be transferred as the ASF lawfully directs (including to another custodian). The timeframe within which assets are to be transferred following termination must be determined by the ASF and must be set out in the agreement.
- xii) Other obligations of the parties at the termination of the agreement must be set out in the agreement. These may include, for example, the payment of any outstanding fees and charges to the custodian.
- i) The Trustee Board must have appropriate mechanisms in place to ensure that any directions issued by the Bank to the ASF in relation to assets held by the custodian are effectively relayed to the custodian. The Trustee Board must be satisfied that the custodian has adequate processes in place to implement any relevant directions issued by the Bank. The agreement must contain a provision to the effect that, in the event the ASF is issued a relevant direction by the Bank, the custodian will undertake appropriate action to ensure that the ASF is in compliance with the direction.
 - j) The Trustee Board must consider the custodian's processes as part of the ASF's systems for ensuring compliance with the Prudential Standard on Risk Management.
 - k) The custodian must accept liability based on the standards of reasonable care applicable in relevant markets. Accordingly, it is the duty of the Trustee Board to periodically monitor relevant market practices to gauge the standards of

reasonable care that should apply and to ensure that they are acceptable in the context of the ASF's obligations to its members.

- l) The Trustee Board must have a clear understanding of the provisions of the agreement setting out the risks borne by each party to the agreement. In particular, the Trustee Board must satisfy itself with respect to:
 - i) the types of risk it is carrying; and
 - ii) the risks for which the custodian does not accept liability. For example, the custodian may not accept liability for losses arising from the insolvency of its subcustodians or investment related events, such as counterparty default.
- m) The Trustee Board must notify the Bank as soon as possible after the ASF enters into any custodian agreement. The Board must also clearly specify that:
 - i) the Trustee Board is aware, in relation to the services of the custodian, that it is responsible for the custody and control of the assets of the ASF and for compliance with the Act and other laws and regulations relevant to the ASF;

Commentary

1. Notification about whether an ASF is using a custodian should also be communicated to the Licensed Investment Manager
- ii) the Trustee Board has assessed the various risks that could arise from the use of a custodian and has systems in place to manage those risks;
- iii) there are adequate systems in place to monitor the operation of the custodian arrangements including the identification of, and acting in respect of, material and/or systemic breaches;
- iv) the Trustee Board is satisfied with the procedures, processes and standard of care of the custodian to safeguard the interests of the policyholders, including to ensure that only properly authorised transactions are accepted and settled;
- v) the Trustee Board is satisfied that the custodian's administration and reporting systems are adequate to ensure that legislation is complied with and the risk control measures required by the Trustee Board are implemented; and
- vi) any risk to the entitlements of members resulting from provisions of the custodian agreement, which reduce the liability of the custodian,

are acceptable in the context of the totality of the custodian arrangements.

30) *Maximum Exposure in Single Entity*

- a) The Investment Framework must include a 5% maximum investment risk exposure limit, directly or indirectly to any one single entity, individually or in aggregate at any time.
- b) Where an ASF wishes to exceed the maximum of 5% maximum investment risk exposure limit, directly or indirectly to any one single entity, individually or in aggregate at any time, the Trustee Board must request prior approval in writing from the Bank, stating the basis for exceeding the maximum percentage.

Commentary:

- 1. Investment risk exposure limit includes direct and indirect investment exposure including counterparty risk, reputational risk and governance risk.
- 2. Where the current exposure exceeds 5% maximum investment risk exposure limit, the Trustee Board must develop and adhere to an Exposure Exit Plan which is acceptable to the Bank to reduce the exposure to 5% within an agreed timeframe.

31) *Offshore Investments*

- a) The Investment Framework must provide that offshore investments are limited to a maximum of 35% of the total value of the assets of the ASF at any time.
- b) Where an ASF wishes to exceed the maximum of 35%, the Trustee Board must request prior approval in writing from the Bank for increasing the exposure to a higher percentage.

32) *Currency Risk*

- a) The Trustee Board must develop, document and maintain a Currency Risk Management Policy in consultation with the Licensed Investment Manager, and include the policy in the Investment Framework.

33) *Regular Review of Currency Risk*

- a) The Investment Framework must provide that the currency risk of the investment portfolio as a whole and its compliance with the Currency Risk Management Policy are to be reviewed by the Licensed Investment Manager and the Trustee Board regularly, at least annually.

- b) The triggers which would require a more frequent or immediate review must be included in the Currency Risk Management Policy.

34) *Derivatives*

- a) The Licensed Trustee and the Licensed Investment Manager of an ASF must ensure that the assets and liabilities of an ASF may not include a derivative, except where allowed under paragraph 32 (b) to (e) below.
- b) The Trustee Board must ensure that the assets and liabilities of an ASF at any time do not include a derivative either directly or indirectly unless each Director on the Trustee Board fully understands and is able to explain the potential risks of any derivatives positions taken directly or indirectly.
- c) The Trustee Board must ensure that the Policy on the use of Derivatives must provide that derivatives will only be used to reduce the risk of existing investments or currency positions.
- d) The Trustee Board must ensure that the Policy on the use of Derivatives must provide that derivatives may only be utilized when the exposure is fully covered by assets of the ASF.
- e) The Trustee Board must develop, document and maintain a Policy on the use of Derivatives, in consultation with the Licensed Investment Manager, and include the policy as part of the Investment Framework.
- f) The Trustee Board in consultation with the Licensed Investment Manager, must develop, document and maintain an appropriate risk management framework to capture, measure, monitor and manage the potential risks of any derivatives positions taken directly or indirectly. The risk management system must be sophisticated enough to measure risks on an aggregate basis.

Commentary:

- 1. The risk management framework here is specific to the use of Derivatives and should form part of the overall Risk Management Framework of the ASF as required by *Superannuation Prudential Standard 9/2014 Risk Management*.
- g) The Policy on the use of Derivatives must be reviewed on a regular basis, at least annually.
- h) The Policy on the use of Derivatives must be published in the Annual Report to members and be published in the public section of each ASF's web site.

PART IV CORRECTIVE MEASURES

35) Remedial Measures and Sanction:

- a) Any Licence Holder which anticipates difficulty in complying with sections of this Standard by 1 January 2015 should advise the Bank forthwith in writing.
- b) If a Licence Holder fails to comply with this Standard, the Bank may impose or vary conditions on the licence to ensure compliance or, if necessary, suspend or revoke the licence.

PART V EFFECTIVE DATE

36) *Effective Date:* The effective date of this Standard shall be 1 January 2015 with full compliance required by 31 December 2015.

37) *Supersedence:* This standard supersedes and replaces *Superannuation Prudential Standard 1/2008 Authorised Superannuation Fund Investments*.

38) *Questions and enquiries:* Questions and enquiries relating to this Standard should be addressed to:

The Manager

Superannuation and Life Insurance Supervision Department

Bank of Papua New Guinea

Tel: 322 7370



Loi M Bakani

GOVERNOR