SM/01/217
Correction 2

CONTAINS CONFIDENTIAL INFORMATION

September 26, 2001

To: Members of the Executive Board

From: The Secretary

Subject: **Israel—Financial System Stability Assessment**

The attached corrections to SM/01/217 (7/11/01) have been provided by the staff:

Page 3, Table of Contents, Chapter VII title: page number corrected
Chapter IX, Sub-section B title: "Main findings" added
Chapter XIII title: for "Insurance and Pension Supervision" read "Insurance Supervision"

Page 4, Table of Contents, Chapter XIII, Sub-section B: removed
Sub-section C: for "C. Transparency..." read "B. Transparency..." page numbers revised
Text Table 15: title removed

Page 44, lines 15–17: for "the...Fund Supervision:" read "and the...Supervision Procedures."

Page 72, Chapter XIII title: "and Pension" removed

Pages 77–81, paras. 302–319: removed
Sub-section B: for "Observance of Principles of Pension Supervision." read "B. Transparency of Insurance and Pension Supervision Policies."

Pages 81–82: paragraphs renumbered

Page 87, Table 10, column 2, line 3: "Largely observed." removed
line 7: "Materially non-observed." removed
line 10: "Non-observed." removed
line 14: "Observed." Remove

Page 87, Table 10, column 2, line 15: " Observed." removed
line 19: "Largely observed." removed
line 22: "Observed." removed
line 23: "Observed." removed
line 26: "Non-observed." removed

Page 88, Table 11, column 2, line 1: "Largely observed." removed
line 8: for "Observed."
read "Adequate"
line 11: for "Observed."
read "Information is publicly available."
line 12: for "Observed. However, detailed"
read "Detailed...assessment."

Page 91, Table 14, column 2, line 1: "This principle is observed, but" removed
lines 4–6: for "This principle...composites."
read "Capacity...improved."
lines 7–9: for "This principle...covered."
read "Key...covered"
lines 11–12: for "This principle...practices."
read "The supervisor's...practices."
lines 16–19: "This principle is largely observed except for derivatives." removed
for "is also lacking...criteria."
read "and coverage of derivatives are also lacking...criteria."
line 20: "This principle is observed, although" removed
lines 24–26: for "This principle...capacity"
read "On-site capacity is limited"
lines 27–28: "This principle is materially non-observed because" removed
lines 30–31: for "This principle...requires..."
read "Confidentiality requires..."

Page 92, Table 15: removed

Page 93, Table 16, column 2, line 1: "This principle is largely observed." removed
line 9: for "This principle is observed."
read "The process is open and transparent."
line 12: "This principle is observed." removed
line 16: for "This principle is observed."
read "The framework for accountability and assurance is fully adequate."

Questions may be referred to Mr. Coats (ext. 38422).

Att: (15)

Other Distribution:
Department Heads

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Table 7. Stress Tests for Five Largest Banking Groups as of December 2000

	Five Largest Banking Groups
DATA (NIS billion)	
Tier 1 capital	36.2
Tier 2 capital	13.6
TOTAL	49.8
All problem loans net of specific provisions	31.5
Problem Loans net of provisions in the Construction and Real Estate Sectors	9.5
Problem Loans net of provisions in the Commerce Sector	2.5
Problem Loans net of provisions in the Restaurants and Hotels Sector	1.7
Problem Loans net of provisions in the Transportation and Storage Sectors	0.4
Problem Loans net of provisions in the Communications and Computer Services Sectors	0.3
Sum of all Problem Loans net of provisions in the sensitive sectors indicated above	14.5
Var due to inflation and exchange rate risk	0.1
Var due to interest rate risk	0.9
SCENARIO 1	
Banks suffer losses due to a shock to changes in interest rates, inflation and the exchange rate that have a probability of occurrence of 1 percent or less (based on changes in those variables over the last 5 years). Holding period is one month. At the same time all the problem loans in the sectors that are sensitive to the recent shocks fail. It should be noticed that due to the lack of information on collateral, the recovery value of defaulted loans is assumed to be zero.	
Total losses in NIS billion	15.5
As a % of Tier 1	42.9
As a % of Tier 1 + Tier 2	31.2
SCENARIO 2	
Banks suffer losses due to a shock to changes in interest rates, inflation and the exchange rate that have a probability of occurrence of 1 percent or less (based on changes in those variables over the last 5 years). Holding period is one month. At the same time all problem loans default. It should be noticed that due to the lack of information on collateral, the recovery value of defaulted loans is assumed to be zero.	
Total Losses in NIS billion	32.5
As a % of Tier 1	89.8
As a % of Tier 1 + Tier 2	65.3

Sources: Bank of Israel; and Fund staff estimates.

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SECTION II: OBSERVANCE OF FINANCIAL SYSTEM STANDARDS AND CODES: SUMMARY ASSESSMENTS

This section contains information for the Financial System Stability Assessment for Israel on compliance and consistency with international standards and codes relevant for the financial sector. The assessment has helped to identify the extent to which the supervisory and regulatory framework have been adequate to address the potential risks in the financial system; and has also provided a source of good practices in financial regulation and supervision in various areas.

As part of the FSAP, the following detailed assessments of standards were undertaken: Basel Core Principles for Effective Banking Supervision: Wayne Byres (Australian Prudential Regulation Authority) and Göran Lind (Sveriges Riksbank); the IMF's Code of Good Practices on Transparency in Monetary and Financial Policies: Mark Stone (IMF) and Mark Robson (Bank of England); the International Organization of Securities Commission (IOSCO) Objectives and Principles of Securities Regulation: Melinda Roth-Alexandrowicz (World Bank); the Committee on Payment and Settlement Systems (CPSS) Core Principles for Systemically Important Payment Systems (CPSIP): Simon Kappelhof (De Nederlandsche Bank); ~~the~~ and the International Association of Insurance Supervision (IAIS) Supervision Procedures, ~~; and the FSAP team's own Core Principles for Pension Fund Supervision:~~ Rodney Lester (World Bank). These assessments were prepared by drawing on the authorities' self-assessments, answers to questionnaires, and field work during September 2000.

Israel has relatively well developed, capable, and transparent financial sector supervision and monetary policy formulation, especially in the area of banking supervision which has developed over a longer period. Two areas of particular weakness concern the design and lack of oversight of payment systems, and inadequate coordination of supervision among different regulators because of legal impediments to information sharing. Steps are underway to address these deficiencies. As a general matter, supervision in all areas seems to be of better quality than the laws on which it is based. The exception is securities supervision, which has both good supervision and a modern law.

269. The assessment was based on the *Code of Good Practices on Transparency in Monetary and Financial Policies* and its three supporting documents, as approved by the Executive Board of the IMF July 9, 1999, and July 24, 2000, respectively.

Main findings

270. **Securities supervision is well defined, with a clear fundamental law that has been regularly updated to reflect the need of the regulator to keep abreast of changing market conditions.** The ISA's policies and rules are clearly communicated to market participants, but as it already recognizes, the agency needs to do more to explain its role and responsibilities to the general public and overseas investors in particular. A web site is being developed, to be launched shortly. The ISA is directly accountable to the Minister of Finance and the Knesset Finance Committee. Changes to its regulations, including a new proposed method of funding, are therefore the subject of public hearings. Its relationship with the Tel Aviv Stock Exchange, and the by-laws and directives of the Exchange, which the ISA has to approve, is transparent.

Observance of the Code

271. **Observance of the Code is summarized below and in Table 13.**

272. **The ISA observes the Code with respect to clarity of roles, responsibilities and objectives, which are clearly set out in legislation and regulations.** The only aspect with which the team had some concerns was in the relationship with the two other financial regulators, the Banking Supervision Department of the Bank of Israel and the Capital Markets, Insurance and Savings Division of the Ministry of Finance. Although the ISA's broad objective is clear and statutory—to protect the interests of the public investing in securities—it was not clear to the team how, in practice, it could be sure of fulfilling that role efficiently in cases where passing information to one of the other regulators quickly was desirable, given the strength of the privacy and secrecy laws. The team was unable to form a clear and consistent view of what happens in practice, except when there was clear evidence of criminal action or an order of the Court.

273. **With regard to open process for formulating and reporting of policies, the Code is clearly observed in relation to market professionals for whom most of the work of the ISA is directly relevant, including the Tel Aviv Stock Exchange.** It is less clear, however, that to date the ISA has paid adequate attention to the desirability of engaging the general public, and in particular overseas investors, in its policy formulation and reporting. The annual report has only been available in Hebrew, and the ISA has not had a web site.

274. **It will however, soon have rectified the position and plans to devote more resources to public availability of information on securities supervision policies.** Use of a web site will enable links to be created to the TASE web site. This already contains information on sectoral developments and aggregate data envisaged by the Code to be made readily available to the public but which the ISA has not itself made available, because it saw

no point in duplicating information available from TASE or felt that there was likely to be insufficient interest its work from the general public. In so far as current practice falls short of the Code, therefore, the deficiency will soon be rectified.

275. **The ISA appears fully to observe the Code on accountability and assurances of integrity by securities supervision agencies.** The ISA reports at least annually to the Minister of Finance and Knesset Finance Committee. There are strong statutory restrictions on personal securities dealing and business interests by Members of the ISA, to avoid possible conflicts of interest.

Authorities' response and recommended next steps

276. **The ISA agreed with the team's assessment and recommendations. The ISA is very transparent**. However, the team recommended launching an informational web site that includes English translations of important laws and regulations. This is now planned for the summer of 2001. In addition, the ISA should establish MOUs with the other two financial sector supervisors setting out the relationship between them.

277. **Little needs to done by the ISA to achieve full observance of the transparency code.** The most important change is already under way, since a web site will be launched before the end of the year. In developing this new service, the ISA needs to bear in mind that there may be a very broad and diverse audience for information on its activities, certainly including foreign investors of varying degrees of sophistication.

278. **Coordination among the three financial regulators should be more formalized.** A Memorandum of Understanding between the three financial regulators should set out precisely the relationship between them, including a procedure for dealing with any overlaps or gaps which might arise from time to time and clarification of the circumstances in which supervisory information can be exchanged between them, or with overseas regulators. This would be worthwhile both under current legislation and after reform.

XIII. INSURANCE ~~AND PENSION~~ SUPERVISION

A. Observance of IAIS Core Principles of Insurance Supervision

279. **This is an assessment of the observance of the core principles of the International Association of Insurance Supervisors (IAIS) in Israel.** Insurance is supervised in Israel by the Capital Markets, Insurance, and Savings Division of the Ministry of Finance (MOF). This assessment was undertaken as part of a Financial Sector Assessment Program (FSAP) mission.

280. **The assessment was conducted by Rodney Lester, Lead Specialist in the Financial Sector Development Department of the World Bank under the supervision of Warren Coats, Assistant Director of the Monetary and Exchange Affairs Department of the International Monetary Fund.** Major sources of information used for the assessment included the answers to the questionnaire submitted by the IMF prior to the mission,

supervisor are subject to professional secrecy constraints. A unique, but undesirable feature of the supervisory scene is Israel is the necessity to share confidential information with an industry-based advisory committee.

299. **The team discussed the medium-term challenges for insurance supervision.** These include developing a viable on-site inspection capacity, building up actuarial capacity, developing key actuarial standards, producing a workable model for controlled competition in the MBI market, enforcing boards of directors' accountability for risk management, developing an information exchange capacity with other financial sector supervisors and continuing the current market reform program. In addition a number of specific issues need to be dealt with including earthquake reserves and annuity conversion options.[19]

Authorities response and recommended next steps

300. **The authorities generally agreed with the mission's assessment and recommendations.** The key and most urgent recommendation is the recruitment of additional skills in the life insurance actuarial area and the strengthening of the on-site inspection capacity of the supervisor. Introducing an on-site inspection manual based on overseas best practices (probably Canada) would support such moves, as would working with the actuarial and accounting professions to establish a formal actuarial standards setting process.

301. **The Insurance Commissioner should have more independent authority.** The Commissioner should be given greater and more flexible powers of intervention before an insurance company gets into serious trouble.

~~B. Observance of Principles of Pension Supervision~~

~~302. **This is an assessment of the observance of the core principles of pension fund supervision by the Capital Markets, Insurance and Savings Division of the Ministry of Finance (MOF).** It was undertaken as part of a Financial Sector Assessment Program (FSAP) mission.~~

~~303. **The assessment was conducted by Rodney Lester, Lead Specialist in the Financial Sector Development Department of the World Bank under the supervision of Warren Coats, Assistant Director of the Monetary and Exchange Affairs Department of the IMF.** Major sources of information used for the assessment included the answers to the questionnaire submitted by the IMF prior to the mission, extensive information available on the MOF web site, special papers prepared by the Actuary to the Ministry of Finance, an advance English language copy of the 1998 annual report of the Capital Markets, Insurance and Savings Division of the MOF, an English language summary of the Public Committee on Income Tax Reform and unofficial English language versions of the new companies law and~~

[19] However, it is important to see footnote [4] above.

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~~the key insurance statutes. In addition, extensive interviews were conducted with senior offices of the above-mentioned division, members of the actuarial profession and senior managers of two pension fund managers and a provident fund manager. All those interviewed gave generously of their time and were anxious to be helpful.~~

~~304. **This assessment has been largely based on a draft set of principles for the supervision of pension plans prepared by Rodney Lester.** These in turn are based on the report "Rebuilding Pensions" prepared under the auspices of the EU as a precursor to a directive on pension supervision. The assessment deals only with legitimate pension plans as approved under the taxation ordinance and the Insurance Business (Control) Law. Provident funds with a strong retirement element are described but not assessed pending further reform to separate these more explicitly into short and long-term savings vehicles.~~

~~Background~~

~~305. **Supplementary retirement incomes in Israel (that is second pillar arrangements) may be secured through tax deferred savings using multi employer pension funds, 'managers insurance' arrangements, benefit and employee severance pay provident funds, and non-funded pay-as-you-go (PAYGO), budget-based, plans for various classes of public employee.** Of these, the core product is the multi-employer funds, which had assets of NIS 107 billion at end-1999. These funds offer the lowest expense rates of all the long-term savings mechanisms (0.32 percent of funds for old pension plans), and the government of Israel guarantees a large part of their investment performance. The old funds offered a defined benefit (DB) structure, but were not subject to actuarial overview for several decades after they were founded—about the time Israel became a nation. They were closed in 1995 by agreement with the union movement and replaced by a hybrid deferred annuity arrangement with some of the characteristics of a cash balance fund [defined contribution (DC) with some guarantee of investment returns]. The old funds have an actuarial deficiency of approximately NIS 60 billion and substantially more if government subsidies of investment returns are ignored. The key actuarial assumption underlying this calculation is a return/ wage growth gap of 3.3 percent. One of the 18 old funds is already suffering a negative cash flow and several others are approaching this stage. The one with the negative cash flow is being funded out of a reserve fund, which has been established from part of the real return the government offers comprehensive benefit pension funds through several series of non-tradable special bonds. The old funds hold approximately 94 percent of their assets in this form and the new funds 70 percent. The 1995 agreement did allow for the creation of supplementary pension arrangements with more liberal investment rules however it is not clear how actively these have been promoted.~~

~~306. **While history would indicate that the government has some responsibility to cover the deficiency in the old funds, there is no legal liability to do so, giving the government some leverage during the development of recovery plans.** The 1995 and subsequent agreements also saw a concerted effort on the part of the Ministry of Finance (MOF) to introduce modern pension plan management and governance principles for the new funds, however, they were not able to separate them from the old pension fund managers.~~

~~The largest and oldest fund (and manager), Mivtahim controls 47 percent of the old funds and 54 percent of the new funds.~~

~~307. **As part of the 1995 reform process, it was also agreed that the public sector PAYGO system, which requires no employee contribution, would be transferred to the new funds with suitable transition arrangements.** The logic for this has more to do with ensuring that the long-term costs of decisions to increase benefits are brought home to decision makers than any immediate demographic or economic imperatives. The agreement was until recently stalled because of disagreement over a side agreement on benefit structures. This delay has also been exacerbated by a Court challenge by non-union fund managers over the right of unions to nominate, to employers, which fund managers will manage the new funds (although individual member choice was built into the rules this is unlikely to lead to a more competitive market). Another part of the 1995 reforms anticipates the creation of special purpose pension arrangements that would have many of the characteristics of provident funds.~~

~~308. **While a special unit in the MOF supervises pension funds, provident funds come under the Capital Markets Division.** This reflects the fact that the most active part of the provident fund market is concerned with short-term, tax subsidized savings plans for individuals, which have many of the characteristics of securities under typical securities law. Like insurance companies, provident funds lost their access to guaranteed-return, non-tradable government paper in the early 1990s and for individual fund members they are now effectively just another form of collective investment. Given the volatility of real investment returns in Israel, reflecting tight monetary policy and rapidly reducing inflation, withdrawals by individuals from provident funds have been extremely volatile. Employee plans have shown greater stability within a general pattern of secular decline.~~

~~309. **"Managers insurance," which is a form of life insurance providing disability, mortality and longevity (pension) coverage, now accounts for 80 percent of new business in the life** insurance savings market. These products do not offer the same value as pension funds in terms of expense rates and governance and there is some question as to whether less sophisticated consumers are being given dispassionate advice on their alternatives for retirement savings; the commission rates on the non-savings component of these contracts (typically 28 percent of premium) can typically be in excess of 100 percent, spread over four years. There are moves under way to improve the value of this product.~~

~~310. **The reforms introduced in 1995 provided secure and adequate member entitlements, rights of access and movement, and adequate disclosure and reporting requirements.** Security is the responsibility of a board with trustee levels of accountability to members and achieved through professional management. They also provided an appropriate regulatory and supervisory structure. However, Israeli is a well-developed capital market offering a wide range of securities and good liquidity. The government has in practice acted as a surrogate market, particularly when inflation was very high and matching would have been problematic for private issuers.~~

~~**Main findings**~~

~~311. **The reforms introduced following the 1995 agreement have gone a long way to bringing Israel up to best practices in terms of pension supervision. Israel observes or largely observes seven of the eight principles.** The major deviations from the principles reflect history and the difficulties of changing embedded structures that have created their own adherents. These revolve around a number of problems: (i) the lack of investment freedom available to boards and managers because of a historical symbiotic relationship between the government and all long-term savings mechanisms (a factor which has also carried over for pension funds); (ii) the lack of a legal separation of the of the old funds and managers (which has led to a number of undesirable practices, including cross subsidies from old to new funds); (iii) a chronic tendency to create unfunded liabilities (backed by an assumption that the government is underwriting benefit levels); and (iv) limited capacity for the supervisor to conduct on-site inspections.~~

~~312. **Reform is also complicated by the desire of the nonunion fund managers to break the union cartel with regard to new funds and possible mis-representation in marketing manager's pension contracts.** These are relatively minor problems compared to the issues listed in the previous paragraph and should be resolved as soon as possible so that the major reform program begun so auspiciously could be allowed to move on.~~

~~313. **The issue of unfunded liabilities in the old multi-employer funds and the budget PAYGO system are discussed as a special topic in Volume II of the FSAP report.** The main findings by category of Principle are as follows.~~

~~314. **Benefit Security (CPs 1–4) - observed except for the Asset Management criterion. The 1995 reforms introduced most of the requirements under the benefit security heading.** Pension funds were separated from management, directors were given clear responsibilities and accountabilities, and licensing rules were clarified. Actuarial reporting is now an integral part of the system; listed securities are marked to market; some minimum funding requirements are in place; and moral hazard from insolvency insurance has been avoided. On the other hand, while the board of a fund has to include an investment committee, there is no requirement to produce an annual statement of investment principles. This will become more relevant as freedom to invest is introduced. Investment choice is currently highly constrained, however a continuation of a low-inflation environment will put increasing pressure on fund management and boards to seek wider investment powers and introduce modern custodial arrangements. The deficiencies in the old funds and the growing unfunded liability in the budget-based public sector plans still need to be addressed along with some lesser matters mentioned in the detailed assessment.~~

~~315. **Disclosure and Transparency (CP 5) - observed. Information is disclosed at least annually to members, including publication of a detailed annual report in at least two national newspapers.** Members are usually provided with information on joining a fund and receive member statements. Pension benefits may only be sold by licensed entities, although there is some question about the rigor of the licensing process for insurance agents. There is~~

~~also some doubt as to whether all members of new funds realize that they are not in a traditional DB plan. The question of risk and return for DC style plans has not been an issue to date because the government underwrites much of the investment return.~~

~~316. **Supervision (CPs 6-7) – largely observed.** A board subcommittee has responsibility for the published accounts, the supervisor receives copies of actuarial reports, information required by the supervisor is standardized, and the supervisor has the right to ask for supplementary information. The supervisor has a section devoted to the monitoring of pension plans and publishes an extremely comprehensive overview in the Division's annual report. An annual statement of investment principles is not, as yet, required. The major concern is a lack of resources with only off-site inspection currently being undertaken.~~

~~317. **Taxation of funds (CP 8) – observed. Israel has an EET[20] basis of taxation, within defined income limits for pension plans.** This is not necessarily the case for provident funds and some shorter-term savings vehicles. The recommendations of the Report of the Public Committee on Income Tax Reform are intended to rationalize the situation and encourage long-term savings.~~

~~318. **Medium-term challenges for the pensions sector include coping with the introduction of investment freedom, fully explaining the nature of the new funds and introducing a rational across-the-board taxation structure for savings vehicles.**~~

~~**Authorities response and recommended next steps**~~

~~319.~~ 302. ~~**The MOF broadly agreed with the FSAP team's assessment and recommendations.** The team stressed the need to separate the governance overview and management of pension funds. Boards should be independent of and have overview of the fund managers (including the right to seek competitive tenders for services) and boards should have full trustee responsibility for the security of members' benefits. As investment options are liberalized, boards should be required to prepare annual statements of investment principles (SIPs).~~

~~C.~~ B. Transparency of Insurance and Pension Supervision Policies

~~320.~~ 303. **This assessment is of the transparency of insurance and pension supervision policies as they are currently conducted by the Capital Markets, Insurance, and Savings Division of the Israeli Ministry of Finance.** Although it is one among several Divisions of the Ministry of Finance, it is headed by a Commissioner of Insurance, a statutory appointment under the 1981 Insurance Business (Control) Law. The assessment was made in the course of the FSAP evaluation.

[20] This refers to a tax structure in which contributions, investment income and benefits are not taxed.

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~~321.~~ 304. **The assessment was conducted by Mark Robson, a Senior Advisor from the Financial Stability Area of the Bank of England, acting as consultant to the Monetary and Exchange Affairs Division of the IMF.** It was based mainly on an examination of the relevant laws, particularly the Insurance Business (Control) Act, 5741–1981, and regulations made under that Act; the comprehensive annual public reports issued by the Division and its web site; and discussions with many officials of the Division, including the Commissioner, Vice Commissioner, Deputy Commissioner for Pensions and their Assistants, the Chief Actuary and officials from the Legal and Budget Divisions of the Ministry of Finance. Discussions with partners of the leading accountancy firm of KPMG Somekh Chaikin and officials of the Bank of Israel and Securities Authority also provided helpful information. The authorities were fully co-operative.

~~322.~~ 305. **The assessment was based on the *Code of Good Practices on Transparency in Monetary and Financial Policies* and its three supporting documents, as approved by the Executive Board of the IMF July 9, 1999, and July 24, 2000, respectively.**

Main Findings

~~323.~~ 306. **In practice, insurance (but to a lesser extent, pension) supervision is fairly well defined.** Although the 1981 Act appointing the Commissioner of Insurance does not specify objectives for insurance supervision, in practice, various objectives that are currently not prioritized have been developed, all with a view to protecting the interests of policyholders. In the case of pension funds, the objective is not clear given continuing political controversy arising from the 1995 reform program. In its comprehensive annual reports and increasingly through its web site, the Division provides the public with a lot of information of high quality on its policies and activities and on the financial results of the government traded bond market, life and general insurance, provident and pension funds and savings plans. The Code standards on open formulation of policy and accountability appear to be fully met.

~~324.~~ 307. **Although current insurance and pension supervision practices observe most of the provisions of the Code, the main weakness noted is regarding clarity of roles, responsibilities and objectives.** The enabling legislation, which is focused on insurance policies rather than pension funds, does not specify objectives for the Commissioner. The mission was told that the key responsibility of the Division was regarded as protecting the interests of policyholders, which could be furthered in several different ways, including minimum capital and liquidity rules, financial reporting rules, approval of premium rate bands and increased competition in the sector. A Consumer Ombudsman Unit within the Division deals with complaints and other inquiries from the public. It would be helpful if objectives could be explicitly prioritized. Responsibilities are not fully transparent in all respects. Since the formal sanctions provided for in the Law are very limited (essentially limited to revocation of licenses), the Commissioner relies heavily on the cooperation and openness of insurance companies finding themselves in difficulties.

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Table 10. Summary of Main Findings for Payment Systems Supervision

Subject	Main Findings
CP 1 Well-founded legal basis in all relevant jurisdictions	~~**Largely observed.**~~ Rules and regulations applicable to the payment system are properly founded to address the issues given the present practice.
CPs 2–3 Understanding of the system's impact on risks; and procedures for the management of risks	~~**Materially non-observed.**~~ The practice of the BOI in the settlement process does not give the banks the proper incentives for managing risks.
CPs 4–5 Final settlement; inability to settle by the participant with the largest single settlement obligations	~~**Non-observed.**~~ In general, settlement does not take place on the same day and, where netting takes place, the systems do not have provisions to settle the position of the largest defaulter.
CP 6 Assets for settlement	~~**Observed.**~~ All systems settle in central bank money.
CP 7 Security and operational reliability; and contingency arrangements	~~**Observed.**~~ All systems have adequate provisions to ensure a high degree of security and operational reliability and have contingency arrangements for timely completion of daily processing.
CP 8 Systems are practical for the markets and efficient for the economy	~~**Largely observed.**~~ Systems are efficiently organized, within the restrictions mentioned under CP2–3 and 4–5.
CP 9 Objective and publicly disclosed criteria for participation	~~**Observed.**~~ The criteria for participation can be regarded as objective and are well known.
CP 10 Governance of the system should be effective, transparent and accountable	~~**Observed**~~ Governance of the systems is in principle adequate due to the involvement of the BOI under its legal basis.
CP 11 Responsibilities of the Central Bank in Applying the Core Principles	~~**Non-observed.**~~ The BOI approaches payment systems issues very much from a supervisory perspective, which does not properly reflect the central bank responsibilities for the payment system that are assumed in the Core Principles approach.

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Table 11. Summary of Main Findings for Monetary Policy Transparency

Subject	Main Findings
1. Clarity of roles, responsibilities, and objectives of monetary policy	~~Largely observed.~~ The BOI law is weak with regard to objective of policy, instrument autonomy, and tenure of the Governor. Inflation target and exchange rate band are potentially inconsistent.
2. Open process for formulating and reporting of monetary policy	~~Observed,~~ Adequate-though views of the Monetary Forum, which advises Governor, could be published.
3. Public availability of information on monetary policy	~~Observed.~~ Information is publicly available.
4. Accountability and Assurances of Integrity by the Central Bank	~~Observed. However, d~~Detailed information on expenses and revenue of the BOI should be made available to the public. Improvements were made after this assessment.

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Table 14. Summary of Main Findings for IAIS Supervision

Subject	Main Findings
Organization of a supervisory body, CP 1	~~**This principle is observed**, but r~~esources and powers need to be expanded and made more flexible.
Licensing and changes in control, CPs 2–3	~~**These principles are observed,** except for e~~Capacity to approve of composites could be improved.
Corporate governance, CP 4	~~**This principle is materially non-observed** because although many criteria are observed through company's law, k~~Key risk management issues are not covered.
Internal controls, CP 5	~~**This principle is materially non-observed** because t~~The supervisor's powers are not attuned to ongoing enforcement of good management practices.
Prudential rules, CPs 6–10	~~**This principle is largely observed** except for derivatives.~~ The risk management perspective ~~is~~and coverage of derivatives are also lacking under these criteria.
Market conduct, CP 11	~~**This principle is observed,** although I~~Inspection capacity need to be strengthened, with selling practices upgraded.
Monitoring, inspection and sanctions, CPs 12–14	~~**This principle is observed** except for limited o~~On-site inspection capacity is limited.
Cross-border operations and cooperation, CPs 15–16	~~**This principle is materially non-observed** because t~~The key capacity to exchange information is not available.
Confidentiality, CP 17	~~**This principle is largely observed,** but~~ Confidentiality requires excessive disclosure by firms and has inadequate sharing of information among supervisors.

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~~Table 15. Summary of Main Findings in Pension Supervision~~

~~Subject~~	~~Main findings~~
~~Structure and governance, CP 1~~	**~~Largely observed~~** ~~Boards need to be more independent from management. An annual SIP should become mandatory once investment freedom is introduced.~~
~~Licensing, CP 2~~	**~~This principle is observed~~**
~~Funding and solvency, CP 3~~	**~~This principle is largely observed~~** ~~for new funds but not for old ones.~~
~~Asset management, CP 4~~	**~~This principle is materially non-observed;~~** ~~investment freedom is highly constrained.~~
~~Disclosure and transparency, CP 5~~	**~~This principle is observed,~~** ~~although there is still some question about the public understanding of the new funds and insurance selling practices.~~
~~Supervision, CP 6~~	**~~This principle is observed.~~**
~~The Supervisor, CP 7~~	**~~This principle is largely observed,~~** ~~although the pensions section is understaffed if on-site inspections are to be properly carried out.~~
~~Taxation, CP 8~~	**~~This principle is largely observed.~~** ~~The taxation status of the plethora of savings instruments needs to be rationalized.~~

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Table ~~15~~16. Summary of Main Findings for Insurance and Pension Transparency

Subject	Main Findings
5. Clarity of roles, responsibilities and objectives of insurance and pensions supervision policy	~~**This principle is largely observed.**~~ No objectives are specified in the law. Those developed for insurance in annual reports need to be prioritized. Objectives need to be established and stated for pension supervision. The relationship between the three financial authorities should be clarified in legislation.
6. Open process for formulating and reporting of insurance and pensions supervision policy	~~**This principle is observed.**~~ **The process is open and transparent.**
7. Public availability of information on insurance and pensions supervision policy	~~**This principle is observed.**~~ Current enhancements to the Division's web site will provide full and detailed information. More simple, summary information could be produced in print for the public.
8. Accountability and assurance of integrity by insurance and pensions supervision agencies	~~**This principle is observed.**~~ **The framework for accountability and assurance is fully adequate.**