CONFIDENTIAL

March 30, 2011
Approval: 4/6/11

PENSION COMMITTEE

Meeting 10/3

2:30 p.m., December 14, 2010

M. Portugal, Acting Chair

Committee Members	**Alternate Members**
	M. Daïri (MD)
	A. Ducrocq (FF)
	J. Prader (BE)
P. Alonso-Gamo	M. Petri

E. Psalida, Committee Secretary
F. Jamaludin, Assistant

Also Present

A. Al Nassar (SA)
W. Chetwin (AU), Temporary
N. Choudhary (IN), Temporary
R. Elder (UK)
P. Garcia-Silva (AG)
S. Geadah (MI)
A. Gerdes (GR), Temporary
N. Giammarioli (IT), Temporary
M. Maciá (BR), Temporary
M. Makino (JA), Temporary
E. Meyer (UA), Temporary
R. Pokharel (ST), Temporary
J. Rojas (CE)
J. Rolle (CO), Temporary
M. Saho (AE)
M. Sidi Bouna (AF), Temporary
A. Sutt (NO), Temporary
J. Wang (CC), Temporary
Y. Yakusha (NE)
K. Zajdel-Kurowska (SZ)

Finance Department: T. Krueger. Human Resources Department: A. Carpenito, K. La Fleur-Cephas, D. Marzouk, M. Rodlauer, M. Vicini, S. Zhang. Office of Budget and Planning: G. Conway, M. Henderson. SAC Representatives: G. El-Masry, W. Oliver, E. Rosa. Secretary's Department: P. Martin. Statistics Department: B. Shannon. Western Hemisphere Department: E. Baker. Senior Advisors to Executive Directors: S. Antic (SZ), A. Ndyeshobola (AE), S. Toh (ST), M. Zaher (Mi). Advisors to Executive Directors: A. Conceicao (AE).

PENSION COMMITTEE

Documents: RP/CP/10/8; RP/CP/10/9

The Acting Chair (Mr. Portugal) made the following statement:

We are now starting a meeting of the Pension Committee to examine two papers that have been circulated. But, before we start, SAC has asked to send two representatives to attend this meeting. It is management's recommendation that we accept it, which is our normal practice.

These two papers have been the subject of an informal meeting on which we discussed the contents and the proposal with all Directors on November 18, 2010. The first paper proposes some amendments to the SRP to implement reforms that have already been approved by the Executive Board last April, and also make a few additional technical updates. And this paper, if it is endorsed by the Pension Committee here, then it would be submitted for approval by the Executive Board, hopefully on a lapse-of-time basis.

The second paper that we are going to discuss is the actuary's five-year review of the SRP actuarial methods and assumptions, which recommends some changes to some of the assumptions in the plan. This does not need to go to the Board, and only requires the approval of the committee. SAC has also circulated a written statement this morning, which I hope members of the committee have had a chance to see, so we will begin with the first paper, but before giving the floor to staff to present it, I will just welcome Mr. Nearpass, our actuary, who is present here.

So, the staff at the moment has nothing to add to this first paper. I would like to open the floor to committee members to see if they have any comments, questions, or additional requests. So, the floor is open initially to committee members, and then after they speak, I am going to open the floor to all Executive Directors present.

Mr. Daïri made the following statement:

We thank staff for a very useful set of papers, and support the proposed amendments. We support the proposed proportional adjustment to the grossing-up formula to broadly equal the statement of salaries across pay brackets, and in this regard, we support the prorated adjustment of benefits for service earned before and after May 2011, as well as the introduction of minimum benefit guarantees to protect shorter service staff approaching retirement.

The additional proposed changes on consistent use of the new mortality tables, allowing staff hire after age 62 to join the SRP and can benefit from a short-term extension of their employment to maintain their participation as well clarifying the death benefit under the Rule of 50 seem well justified. We are pleased to note the significant improvement in the SRP financial outlook, notwithstanding these changes.

We see no need for increasing the 14 percent normalized Fund contribution and in 2032, instead of 2121 as projected in April, reflecting the strong asset recovery in fiscal year 2009/10. However, we wonder if the depreciation of reserves implied in these projections is acceptable.

Mr. Prader made the following statement:

I have a more general point on the proposed amendment to the SRP. I know it follows from the meeting we had in April 2009, but there is one conspicuous absence. Mr. Kiekens and others suggested looking into the question of longevity of staff and whether the underlying pension plans we have, the Rule of 85 and now the Rule of 50 should not be considered in light of longer life expectancy of staff. I know that we have a paper on actuarial assumption, but the question is, really, whether this Rule of 85 or now the Rule of 50 is really up to modern times. It is based on life expectancy in 1945, for the British model, and in most western countries we have a different model. I know this is not popular in the Fund, but it is, I think, a problem of reputation of the Fund.

We are assessing a number of amendments. I would really hope that on the way forward, we will take up this question. It is also not clear what is the pension fund regime now. Is it the Rule of 85 or Rule of 50? The Rule of 50 was introduced in the context of downsizing of the Fund. This is like an experience in my own country where for the sake of restructuring in the heavy industries of Austria in the 1970s, for one particular company, an early retirement scheme was introduced. Now it is the general rule for the whole country. Generations afterwards will have to deal with the long-term consequences of a scheme which the Fund introduced for a short-term situation. If this management and this Board do not address it, future generations will have to face it, despite all the very reassuring reports we get today.

> My final point applies to the second paper. When it comes to pension funds and in particular defined benefits plans, everyone always makes the mistake of being too optimistic. This is not only true for the Fund, but for trade unions, governments, everyone. I appreciate the work that has been done, and I can anticipate that we will agree with the actuarial assumptions, but going forward we always have to remind ourselves about the need for being cautious and prudent, and not for a short-term situation be over-optimistic.

Mr. Ducrocq remarked that that particular issue kept coming back almost at every meeting. It would be appropriate that the staff or management indicated at which point we could have a thorough discussion on this issue, so that we can have the committee updated, fully aware of the issues at stake, and have a clearer view on the way forward.

Ms. Alonso-Gamo made the following statement:

> I am happy to support the proposals. There are a couple of issues I wanted to bring up. One was the issue raised by the Staff Association in its written comments about linking the separation rate assumptions to future HR policies that are yet undecided. It would be more prudent to actually wait to see what those policies are and then calculate what would be the impact of the separation rate. I am not sure that we can know what the impact on the separation rate is going to be of some policy when we do not even know what it is.
>
> Second, I want to pick up this issue of the separation at the Rule of 50, because there are two issues here. One is financial and one is a matter of principle, because I think that there is a matter of presentation, I can understand what Directors are saying. But, if it is matter of financial impact, the fact is that given the discount rates that are applied it is cheaper for the plan the earlier a person retires. Everything else being equal, it is cheaper for the plan for someone to retire at 50 then at 55 or 60, for any grade or for anything. It is important to look at it from both angles and say what is the issue in terms of reputation? But if it is the financial impact that worries us, then that is not a problem.

Mr. Prader could support the staff representative on the issue of separation at selected ages by up to 5 percent, and further queried whether the Fund had a target of getting rid of people in certain groups, something that could be seen as a “killing rate” for the Fund.

Mr. Petri made the following statement:

> I also support the proposed amendments. With respect to the question posed by SAC, it would be useful if staff could explain how much of the proposed changes are due to the actual experience versus expected changes. I think that might be useful for a better understanding of the proposed changes.
>
> Also, I would like to take up the comment made before and support Ms. Alonso-Gamo on the point that one should separate the reputational risk from the financial situation. The question for the financial situation is whether it is actuarially fair for people to retire early, and if that is the case, then the plan does not really lose if there is early retirement. At the same time, the Board in the past has often recommended more staff turnover. In terms of message, it is hard to argue for more turnover and at the same time say that we do not want people to go into early retirement. The two are contradictory.

Mr. Prader made the following statement:

> In this context, since I am used to the frequently shifting positions of the Board, what is the current mantra? Are we in favor of more mobility or not? I know that at the time when some shareholders were starting to think about how to reduce or dismantle the Fund, then they believed in mobility, and also parts of the staff who were interested in accelerating their careers were interested in higher mobility.
>
> But, now, I think we are in a different mode. Member countries have been actually approached by IEO on the question of the tension between the Fund as a confidential advisor and the publication of Fund papers and documents. It is very clear that member countries have very often a different view on mobility of staff. Inside the Fund, there may be people who are interested for career rules in high mobility. But, member countries are interested in continuity of staff, in particular in difficult times like now.

Mr. Ducrocq remarked that in the context of human capital management, and judging by the situation in certain departments of the Fund, there was a human capital problem caused by the departure of experienced staff. It would be worth revisiting the issue, including from that perspective to ensure continuity and availability of sufficiently experienced staff.

The Acting Chair (Mr. Portugal) made the following statement:

> These issues of mobility are broader and have several dimensions in relation to what we are discussing here. I think what applies to the discussion

here, which is the pension fund discussion, is more mobility from the Fund to other organizations, or from other organizations to the Fund itself. It is not the internal mobility from one type of job to another type of job, which I understand is what Mr. Prader is mentioning, because this is certainly not affected by the pension rules. So, I would differentiate and separate that aspect which Mr. Prader mentioned, which is important, but not affected by what we are discussing here.

In terms of mobility, in and out of the Fund, our human resource policies is still to maintain as the mainstay of the Fund labor force, a situation of lifetime employment, for the majority of our staff, who enters here, as young professionals, and stays here their whole career. That would still continue to be the most important part of the labor force. But, we want, also, to introduce some mobility so that people can not only be here, but also go out, gain experience outside and then come back, be that experience both in the public sector and in the private sector, but we also want to have people who have more shorter careers here in the Fund because of skills and several other aspects. That is not going to change.

There will be probably a shift toward more shorter-term careers, but which would still be a minority in terms of the overall share of the labor force. But maybe Mr. Rodlauer, who is also responsible for human resources in addition to pension issues here, will address those points when he speaks as well.

The Deputy Director of the Human Resources Department (Mr. Rodlauer), in response to comments and questions from Executive Directors, made the following statement:

First, I would like to address the question on whether the foreseen depletion of reserves in 2032 is acceptable. Clearly, if it were to happen, it would be cause for concern. However, it is noteworthy that the way these projections are made, they are very conservative. In the past, we have always seen that because of the way the assumptions are set up there is a trend at the end for these required contributions to rise to 30-40 percent; however, we have also seen experience gains every year which lower the required contributions, so we are really not overly concerned that 20-25 years out the current projections indicate a depletion of the reserves. So, the short answer is, yes, I think this projection is acceptable and indicates a very sound basis for the plan, and as we said before, the results are substantially improved from the earlier situation when these reforms were first seen and approved by the Board.

That links to Mr. Prader's question of whether these assumptions are too optimistic overall. The actuary can speak to that. They certainly compare very well and conservatively with the assumptions used in the industry. We believe that overall they are appropriately conservative assumptions and not too optimistic. In fact, again, as I said, every year we have experience gains in the plan which show that the assumptions are appropriately conservative.

On the question of the Rule of 85, it is worthwhile to step back and recognize that it is part of the retirement plan's intention to reflect the organization's employment philosophy and employment objectives. The SRP task force, which has been there for three to four years working on these issues, looked very carefully at the SRP's early retirement provisions as part of the first phase of the comprehensive reform it was asked by the Board and by management to undertake in 2008. There was not just a long look motivated by the immediate concern of the downsizing, but it was more fundamentally a long look at, how do the early retirement provisions match up with the emerging employment and HR management strategy, and the business needs of the Fund.

Based on the results of this first phase of the review, management recommended and the Board approved that the Rule of 50 be introduced as a way of meeting the key—partly new—objectives, to ease early retirement out of the Fund, to enhance mobility and portability of pension benefits, and to attract mid-career and shorter-term service hires into the Fund, with the expectation that after a shorter period of service they could retire with a reasonable pension. At that point it was carefully considered whether to increase early retirement penalties in the plan. Those were not suggested, because they would run counter to the key objectives that I mentioned earlier.

The Rule of 50 was therefore introduced to increase the early retirement mobility at younger ages. At the other end of the spectrum, the Rule of 85 and normal retirement provision (which is that one can retire with an unreduced pension at the age of 62) were designed with two objectives in mind, first to provide appropriate and meaningful retirement benefits to staff who retire from the Fund, who in many cases have lost their contacts with national security schemes and labor markets and for whom, therefore, the pension from the Fund provides the only income after retirement.

The normal retirement age, 62, is an age-based approach that recognizes when a normal retirement should take place, while the Rule of 85 is a service-based approach that recognizes that a full career generally is between 30-35 years which, combined with age, is the right time for a person to retire. Increasing the eligibility for a penalty-free pension, currently available under the Rule of 85, would likely result in participants remaining in service at the Fund for a longer period of time. Taking these considerations into account, the task force, the Board and management did not consider at that time to provide less generous early retirement provisions.

It was not necessary, nor advisable, for the reasons that I have just stated which can be summarized again as follows. Participants, if those penalties were introduced, would likely stay longer at the Fund to accrue higher benefits, which would then in a financial way, as Ms. Alonso-Gamo has indicated, offset the financial gains that could be made by having a Rule of 85 or Rule of 50. On a net basis, the financials of the plan would not change, perhaps even worsen slightly.

It is very advantageous for the Fund, as for most companies, to promote mobility, particularly for the Fund, which has currently a very high share of staff on so-called permanent contracts (over 95 percent). Management's intention clearly is to create greater mobility in and out of the Fund to reduce the share of these permanent-contract staff somewhat, while maintaining the basic career model of a long-serving civil servant in the Fund as the core of the Fund. But, at the margin, we do believe we need more flexibility in the staff in terms of staff moving in and out of the Fund. That does not mean we believe the too rapid shift among desks is not an issue, and we need to monitor it carefully and make sure we have adequate mobility in internal assignments.

The early retirement provision of the SRP is an indicator of the Fund's competitiveness. At an earlier time in the task force, we provided a table comparing the early retirement provisions of the Fund with other international organizations. The Fund is very much in the middle. Of the 12 other international organizations with defined benefit plans, many have similar retirement provisions.

Finally, the SRP is well funded and has a financially sound position. From that point of view, it was not considered necessary to change the Rule of 85.

So, those are the main considerations that were behind the task force's conclusions and recommendations not to change at this point the Rule of 85 provisions.

There was a question about SAC's comments—why do we not include the impact of future policies on the assumptions, particularly the withdrawal assumptions? One follow-up question was whether the change in assumption reflects past experience or future policies. While the change in employment policies may not have been fully agreed upon yet, clearly the hiring trends in recent years as seen in the actual withdrawal and mobility practice compared to the assumptions, has already been such that we are giving greater emphasis to mobility in and out of the Fund. These intentions, as well as the experience, were behind the changes that the Board is now approving to the parameters of the plan such as improved withdrawal benefits, and all the other changes that we are making in the interest of mobility.

So, the changes in the SRP are being made in support and anticipation of the Fund's human resource strategy and work objectives. Based on these, as well as past experience, we believe it is fully appropriate to reflect this ongoing and continuing change in behavior in the withdrawal assumptions of the plan.

Mr. Ducrocq made the following statement:

It is useful to hear a little bit of history, but this financial neutrality argument is one thing. Another thing is, as we discussed earlier, there are other concerns at stake. This does not tell the whole story behind this debate on the Rule of 85.

Similarly, the SRP task force concluded it would not be advisable to change that. This is one thing. But, it is another thing to hear the Board's view on this. If I remember correctly, the last Pension Committee meeting that the Managing Director chaired, or was it the budget committee that the Managing Director chaired, one year ago, in spring 2009, there were several comments from Executive Directors on this. It was not only Mr. Fayolle and Mr. Kiekens. There was a clear request to have a discussion on this.

I would like to reiterate my question. Can we at some point have a discussion on this to see where the Board stands? It can be an informal discussion by the committee, or an informal Board briefing, so that everybody is on the same page on this, has the full knowledge of the issues, and can have a thorough analysis of all the dimensions that are relevant for this debate, not only the financial neutrality but also the HR policy, the reputational concerns, et cetera, et cetera.

Mr. Daïri enquired on ways to ensure that the incentives for greater mobility outside the Fund would not alter the main purpose, as outlined by the Acting Chair, of mainly relying on long-term employment. Furthermore, he enquired on ways to prevent the objectives and underlying policies from interfering with each other. While he could support the assumption regarding the increase of salaries, he did not associate himself with any policy implications in that regard, and considered that there was no link between the two. More flexibility on deciding the sizes of salary increases—that were more generous than what had been the case—might be desirable, but the two issues were separate.

Mr. Prader made the following statement:

> On the issue of mobility, in and out of the Fund, I wonder whether we are still starting from the same assumption that was formulated at the end of the period when there were questions about the viability and sustainability of the Fund, or whether now that the situation has changed. Under the impression of the period since November 2008, our view of mobility has also changed.
>
> I fully accept the explanation given by Mr. Rodlauer about the underlying motivation for the Rule of 50 and the Rule of 85. But, having been here and having seen three different visions and strategies over ten years, any official presentation of employment policies and also of pension policies is only valid for a certain Managing Director. I understand that the current Managing Director is fully behind this Rule of 50 and the Rule of 85. But, staff needs to be aware that a new Managing Director can change his mind under the pressure of the public. And then the whole presentation that we see today can also shift and everybody will take it as the last and most sophisticated conventional wisdom.
>
> I do not know how to deal exactly with the Rule of 50 and the Rule of 85, what kind of format of discussions there should be, but every general staff of an army has contingency plans and it is the task of professionals in human resources to think about the situation when the public would say that we have Greek pension plans in the Fund and that this is not any longer tolerable in the eyes of the international community.

Ms. Alonso-Gamo made the following statement:

> I think we have to put things in perspective, and realize first that the Rule of 50, which was agreed a couple of years ago under certain circumstances is not the same as the Rule of 85 that has been with us for about 30 years. So, I think that to say that it is something that has been changed and

is not true, this is going for a really long time, as well as the plan has been around for a long time.

But, we also have to see what it is that is underlying, which is, is the plan financially viable and are the actuarial assumptions correct? If we have a sound pension plan with sound actuarial assumptions and we have a certain provision, can we discuss the provisions in terms of does it make sense and is it consistent with our employment policy and employment objectives which is a valid question, but we have to separate it from the financial viability aspect, because it is financially viable, the way that it has been actuarially designed. So it cannot be compared with a pension plan outside that is not fully funded and not financially viable and has early retirement plans that have no actuarial penalties, and may not be financially viable. This is not the case. It is actually the opposite. The way the plan is designed, it has been designed in which the earlier one retires, the more financially viable the overall plan becomes because the penalties are such that one is getting so much less than is actuarially equivalent. That is one thing.

To discuss the overall employment policy and the pension plan, that is valid, in how the whole things fit. The one point I want to make, the Pension Committee should be looking at long-term trends and long-term issues for the pension plan, we cannot have a situation in which every two years we are revisiting the provisions and tinkering with them, because people take long-term employment decisions and have long-term plans on the basis of certain things that should be changed from time to time according to circumstances, but not too often. I do not see the rationale to keep on reviewing the plan.

There was an overall review of the plan which took several years, with a committee, and in fact at the committee meeting that Mr. Ducrocq mentioned taking place in April 2009, the Board endorsed that these were the changes that would be taken following that review and that in fact there would be no issue of revisiting these issues for a while. That was the conclusion of the Board. There were certain Executive Directors who wanted to look at the financial aspects, and that was when we could go back to the minutes and I recall exactly what Mr. Fayolle said. Mr. Kiekens was more looking at the financial viability of the plan and what some of these new measures were. But the fact is that the Board endorsed a number of changes following the review of the plan, and the agreement was that these were the changes that would be made and the agreement was that for the time being, this was it in terms of fundamental reviews of the plan.

Mr. Ducrocq made the following statement:

I do not wish to prolong this, but I would still like staff to indicate what we can do in terms of the process. However, on the meeting that Ms. Alonso-Gamo referred to, I have a different recollection. I think the Board endorsed the recommendations, but several Executive Directors noted that these recommendations were fine, and that they were technical adjustments mainly to the plan.

These were also adjustments that were meant to support HR policies and that was fine. But noting that it was not the end of the discussion on how the plan should be designed, and there were other concerns raised, as I said previously, in terms of reputational aspects and so on.

What Ms. Alonso-Gamo said was broadly correct, but Executive Directors did not say only that they were amenable to the recommendations: they also voiced some concerns and some requests to come back to these issues and have a thorough discussion in the months ahead. So, I think it is time that we had a long look at this.

Mr. Petri made the following statement:

A lot of the concerns of the Executive Directors at the time were due to the financial aspect of the plan, which was much less secure in the midst of the financial crisis than it is now. In fact, several Executive Directors said specifically that the financial viability needed to be reviewed in light of future experience.

Now, one year later, the financial viability is much improved, and I think, therefore, a lot of these concerns are less valid now. That does not mean that some other concerns are not still valid. It is very important to keep in mind that the system as it stands now appears to be financially viable for a very long time, and it is sustainable, whereas the Greek system clearly was not. In fact, I would say that if the Fund were to examine a country with a pension system that was in as good shape as the one we have now, we would think that no change would need to be made.

Therefore, it is important also for the public discussion to stress the fact that the systems are not comparable. We have unsustainable systems in some countries, and we have a system here that—under quite conservative assumptions—appears to be viable for over 20 years.

The Deputy Director of the Human Resources Department (Mr. Rodlauer), in response to further comments and questions from Executive Directors, made the following additional statement:

> I would just like to address the question of external experience and mobility, whether this is a short-term issue that came up before the crisis and should now be discarded.
>
> I think we need to always be very careful in looking at it year by year, but we, from HRD and management, are quite confident that in a situation where we have a staff that is composed of 95 or 98 percent of staff on 'permanent' contracts, it is the right policy to think of bringing in more external experience into the building. That is a view that we hear from member countries all the time, that they would like our staff to see not just inside grooming, brought up inside the Fund, but they want to see external experience both from being involved in member country policies or from other private sector experience. So that responds to member demands.
>
> It also responds to our view of the qualities of senior leadership in the Fund. We feel that our leaders, starting with division chief and mission chief, but even more importantly B3, B4, and B5s need to have external experience before they can credibly lead internal staff and interact with member countries' leaders. Therefore, we have recently introduced a requirement for our B3s and above that they have to have external experience as a condition for promotion. Given those kinds of incentives to have more cross-country experience, to be able to do the kind of multilateral comparative surveillance that we increasingly do, it is a 'no-brainer' in our view that we need to emphasize at the margin increasing external experience, from within and outside the Fund. That does not mean we want to go to 60 percent, 50 percent, 40 percent of long-term staff. As we said, the core model would remain long-serving staff, but we need the increased fertilization from external experience and we are quite confident on that.
>
> The broader issue is that we need to clearly define in a long-term view the workforce plan of the Fund, and the HR strategy of the Fund. We have done that quite clearly. We have published it, management has seen it, has approved it. While it is again an evolving strategy that is always adapted, I think this is one of the key parameters that will not change. It did not change as we went into the crisis, and it will not change as we get out of the crisis.

Mr. Meyer made the following statement:

> I wanted strongly to support Mr. Prader and Mr. Ducrocq's comments, at least from a chair that did not support the Board decision in April 2010. We had financial concerns about long-term financial viability, but those concerns were rooted in the structure of the staff retirement plan, and encompassed a broader range of concerns there. I join them in having that discussion—and it has been six months—and we have not had the opportunity to do that. This is important, as it is linked to a broader discussion of where we see the Fund going. I understand Mr. Rodlauer's point that we have an HR strategy—a goal of having the core of Fund staff spending the bulk of their career at the Fund. However, 95 percent is not the core. Ninety-five percent is an overwhelming majority, thus in terms of looking at the benefits, including the staff retirement plan; we still have some way to go. For that reason, it is very important that we do have that conversation, and I think as Mr. Prader and Mr. Ducrocq said, we do have a reputational issue here.
>
> Yes, there are unsustainable and sustainable pension programs, but I would recall, to which Mr. Prader alluded, that many of those pension programs, whether in the public or private sectors that were viewed as sustainable five years ago, ten years ago or 15 years ago, have subsequently been proven not to have been sustainable. It behooves us as the IMF to look at things from this perspective, to give careful attention to that. For that reason, I really hope to have that discussion. We would like to see it as part of a broader review of benefits more generally, but I think that we, at least, felt that the changes agreed earlier this year were more of a technical nature. They were not as far-reaching as we had hoped to come out of a comprehensive review. I understand that there are different views. But that is at least where we would like to come down on firmly.

Mr. Chetwin echoed the points made by Mr. Meyer, Mr. Ducrocq and Mr. Prader about the need for a review of the design of the plan and for a long look at its fundamentals. The concerns raised at the meeting earlier in the year were not simply about the financial position at the time, but were more fundamental and were attached to questions about reputation and the effect on plan design.

Mr. Sidi Bouna remarked that the grossing-up formula overstated pensionable gross remuneration for many years and wondered whether a more regular review of the formula was expected, especially considering that the Pension Committee favored an annual review. Furthermore, the UN mortality tables that were used dated back to the early 1980s. This raised the question of how often were the tables updated by the UN and whether the Fund was considering to review them more regularly also, such as every five or ten years.

Mr. Yakusha made the following statement:

We can in general support the proposed set of decisions. We note that some of those changes and assumptions are more conservative, while some of those changes suggest the same as what we are doing now, such as the inflation assumption. Frankly speaking, I would not be very surprised if there are different views about long-term inflation potential within the Fund, so we need to be careful here, also.

But, in general, because others do follow the same projections, and pension funds in member countries of our constituency do the same, we can support that. We would also like to support human resources as this trend toward flexibility would be definitely endorsed and we disagree with staff here that flexibility is not yet a policy. It is a policy. That is why we see that maybe we have some conservative assumptions about the future growth of salaries of SRP participants. What we do not understand for sure is whether we have the right assumption on the size of the Fund, which may definitely affect the financial viability of the pension scheme. So, on that, we are more cautious and we would like to be associated with Mr. Prader and Mr. Meyer and others on their concerns. It is not 100 percent sure that we have a full proof system that would be easy to present to the outside world as the pension system that has no reputational risk whatsoever.

So, in that sense, we also express concerns on the previous occasions that in a way we are missing one opportunity after another in implementing meaningful pension reform for the Fund, comparable to what we are urging our member countries to do.

Mr. Daïri made the following statement:

The Fund should not embark on annual comprehensive reviews of its pension system. This will not be credible with our staff, and if we want to keep the staff motivated and involved and interested in this institution, we should not change the rule of the game every year, or give the impression that they would be changed every year. The SRP's position has improved, and basically, the review has led to a recommendation and the Board in its majority has approved these changes, and does not call for a comprehensive review of anything in the immediate future. We need to give time to look at how things are evolving, and it is not right to compare the SRP in the Fund with some countries where they have excess employment and excess protection. This is not the case in this institution. Maybe not everybody agreed with the conclusions of the discussions, but in my view, the majority accepted the recommendation and took them and did not call them into question. We all want to improve the system, but it does not mean necessarily that we have to have a comprehensive review every year. This would not be optimal.

Also, as a point of clarification on the incentives for short-term hiring, I hope there is no attempt to try to settle the issue of diversity through this short-term window, because if it is done, it would be very regrettable. There should be complete separation of the two objectives, and we should not try to use one to serve the other, otherwise we are not transparent.

Mr. Prader made the following statement:

Mr. Daïri has a point that we should not have constant comprehensive reviews. We all know the bad experience of the years from 2004 to 2008 where the Fund was completely inward looking and was locked in a very bitter, resentful battle for a comprehensive review of benefits. But, nevertheless, we have to strike a balance, because the fact is, I appreciate the trust of staff in the Fund that the Fund will protect everything but the Fund actually is a cosmopolitan institution, it is an international institution, and it goes with the flow of international opinion. So, viability of the pension fund and everything is a function of the support of the shareholders. If the shareholders think they have to spend the pension fund for debt relief, they will do it. We have to be aware of that. So, viability is a thing that is a function of the level of support of the shareholders. Not of any calculation.

But, we have to walk a fine balance here. And, when I say that there should be studies of alternatives or contingency plans, I also want to be consistent, because we should not always ask for new things from human resources, and I know that Human Resources Department is being stripped of staff. So, it has to be viable and when we ask for something, in one form or another, be it for discussion in the Board, informal or not, or just contingency plans, it is up to management to decide. But, Human Resources should have to do that which is required to do the necessary work, for the infrastructure of the Fund. And, infrastructure of the Fund is human resources, pension plans, employment plans, so on. Mr. Portugal has a lot of experience in national administration and in the Fund. I am sure he will find a way to support the Human Resources Department.

Mr. Elder made the following statement:

I must confess to being new to the job, and therefore pretty new to the pension scheme. When I arrived, the worry I had was that in an organization like this, one would probably find a pension scheme that was unnecessarily generous and probably one that was overfunded. But if I was in the staff, that is what I would want. When I listen to the arguments, I worry a bit that there is a conflict in people being worried about a pension being correctly funded. The pension does need to be correctly funded, but if the staff captures the pension, it will be excessively funded to make sure staff benefits are covered in the future. The fact that a pension scheme is well funded does not necessarily mean it is a good thing. It could be a bad thing.

I struggle a bit to understand what we are discussing right now, but I understand that in the past, a significant number of Executive Directors have expressed concerns about whether the pension is too generous, and I think it would be. As far as our country is concerned, we are concerned about pay back in the United Kingdom, we are in a situation where lots of civil servants are taking pay freezes for a number of years and where pensions are being reviewed very aggressively. A lot of countries are going through that experience. It is perhaps not good enough for the Fund to say, fair enough, that may be happening in our member countries, but we do not need to go through that sort of issue ourselves.

I see an argument for reviewing how generous the pension is. In order to do that, I would suggest we get some people from outside to consider that. In my opinion, it is quite difficult for either the Board or the staff to judge how generous a pension should be. When I hear that 95 percent of the IMF staff are long-standing, that suggests to me the package must be very generous. By that I mean, the total package, not just the pension package. I would be interested in hearing what an external consultant might think of the general package that is being offered here and how comparable that is with competitive employers. We should ask the question about the total package being offered, not just the pension. It is very difficult to separate out just one aspect of the package, but if there is interest in the Board for such a discussion, that would be a good idea, because I certainly think in the United Kingdom, we have had to think hard about how we reward civil servants, and we cannot escape that question at the moment.

The Acting Chair (Mr. Portugal) made the following statement:

As Mr. Elder pointed out, he is new to these discussions. We had an overall review of the package of compensation and benefits in 2006. There was one aspect of that that was to be reviewed later, which was the pension. There was a task force that was chaired by me, and we considered three types of issues. First, is whether the plan is sustainable, because if it is not sustainable, we have to change it. Second, is it incompatible with the human resource strategy that we have and want to implement, and if that is the case, then we have to change it. We also examined this question of reputational risk. So, all these issues have been discussed for a year.

We came to some conclusions. These conclusions have been approved by the Executive Board. Some Executive Directors continued to raise some aspects, especially the aspect of financial viability, because we had not yet updated the mortality tables—we had assumptions that were still based on the 1993 mortality tables of the UN in which people would die earlier. Fortunately, people are living longer. So, it is going to be more expensive. This is being recognized in the next paper that is going to be discussed where we are in fact creating more conservative, and therefore more stressful assumptions in a number of areas, reducing the expected rate of return on assets, and increasing longevity and some other things. So we are completing that path to address the financial viability aspects here.

There is the other issue of whether it is a hindrance to our human resource policy. We thought some aspects of it could be, and then we decided to change these aspects. These changes have been approved by the Executive Board, and now they are going to be implemented. We have not tested them yet. It is to increase the withdrawal benefit to allow people to leave early, this Rule of 50, and all these other things. We do not know what the result of that would be. The pension is not the only issue which makes our staff stay longer here. One of the issues, because there are several issues outside the pension one, for instance, is when a staff member comes here with a G-4 visa, he or she will need to leave the country when he or she leaves the Fund. It is not possible for them to find employment elsewhere. People tend to have houses here, and families who grew up here with kids that consider themselves Americans. These are factors that perhaps are as important or more important than just the pension to keep people here.

But 95 percent, I agree totally with Mr. Meyer, is much more than what could be considered as the core. We want to reduce the 95 percent. We do not know if these changes that will or will not be approved will achieve that result or not. But, at least we have to try and apply them and see the result, and if they do not work, then we do more. So, from the point of view of being a hindrance to our human resource policy, we do not have a reason to review this issue again as it is not a hindrance from the financial point of view.

There is the issue of reputational risk. As it has been mentioned here, there is quite a difference between the situation of funded plans and unfunded plans. And certainly, the staff does not decide the level of funding of this plan. It is the Board and the shareholders who decide. Second, there is also a difference between national pension funds and private pension funds, because they have quite different types of approaches. On a national pension scheme, it is very important that the employees remain in the workforce and remain employed, because they continue to accrue benefits even if they change from one employer to another employer. This is a situation which is different in respect to private pension plans or limited pension plans, which is our case here.

Another aspect is that when changes are made to national pension plans, the savings tend to materialize more quickly, because they are typically applied to total benefits as opposed only to future accrual. Here in the Fund any change that we would have done would not apply for existing staff but would only apply to new staff. The effect would take 30 years, maybe, to materialize.

With regard to the question of financial viability, we review these assumptions every five years. But the review of the plan itself was very thorough. We examined whether we should close the current defined benefit plan and go to a defined contribution plan, and examine several other aspects, and the conclusion of the task force, which was endorsed by the Board, was "no," so it is not our plan to reopen this discussion now because there is not sufficient time. We would probably come to the same conclusions, because nothing has changed, since then, and probably those who were not so inclined to agree with those opinions would express the same view that they have expressed before.

Mr. Elder enquired when the Board agreed on the decision not to go for a defined contribution pension scheme.

The Acting Chair (Mr. Portugal) responded that the decision was taken in April 2010.

Mr. Yakusha concurred with Mr. Prader with regard to the perception of resource constraints in human resources. The Fund, in comparison to its peers was behind in introducing a "second pillar" such as a supplementary scheme like the 401K in the United States. A decision had been taken to introduce a second pillar but implementation had been delayed. To achieve greater flexibility with regard to human resources, the Fund needed more agreements on portability of pension benefits with other international financial institutions. There had not been much progress in that respect over the years, and more resources should be devoted toward achieving that objective.

Mr. Prader remarked that as mentioned by the Acting Chair any changes in the rules would apply only to future staff, which was something that had been experienced by many European central banks where political pressure had led to the introduction of new retirement plans for new staff. I can tell you that a lot of European central banks were in the same situation because of public pressure, they had to introduce for new staff, new plans. A delay would only bring about more public relations problems. At the central bank where he used to work at, there were five different pension plans, with each plan reflecting a new wave of public criticism. Thus the public relations aspect was something to consider, as the Fund may be forced to confront it at a later stage.

The Deputy Director of the Human Resources Department (Mr. Rodlauer), in response to further comments and questions from Executive Directors, made the following additional statement:

> The grossing up formula has to be formally reviewed by this committee every five years, so it is a process agreed on by the Pension Committee. In between we look at it annually to see if there are large deviations that need to be corrected. With regard to the mortality tables, we are now quite confident that because we are introducing dynamic tables that forecast continuing improvements we will not have to review it for a while and when we do it in the future, there will not be a large correction needed.
>
> On the question of how the future size of the Fund might influence the viability of these projections, it is perhaps useful to clarify that the actuarial assumptions and the valuation of the plan and the financial projections are based on a methodology that is called the aggregate cost method as explained in the paper, which basically only looks at the viability of the plan based on current participants irrespective of a future increase or reduction of the size of the Fund. It basically looks at the liabilities going forward: future salary increases, retirement, and so on, and then allocates the cost over the current and future salaries of those participants, so there is no impact of the future size of the Fund. Again this is a conservative method.

> When I said 95 percent of our staff are long-standing employees, this may have created a misunderstanding. What I should have said is that 95 percent or actually more of our staff are what we call regular staff appointments, which are different from limited-term appointments, when it is specified clearly that they are only here for two, three or four years, or contractual appointments, which again have a maximum of four years. With regard to the question of the tenure of staff, as addressed in the previous paper, we have looked at every cohort of the Fund over the last 20 years, and found it is not that bad. About 50 percent of our staff here has had a tenure of ten years or less. And when cohorts joined the Fund, it is clear that about half of them leave within the first ten years. So, there is significant mobility.
>
> The fact that 95 percent are on regular contracts is an issue, and we want to increase the contractuals and limited terms a bit more. At the margin, also, particularly for senior levels such as the managers, the division chiefs, the mission chiefs, the senior advisors and so on, many of us are actually long-term staff and have not had a lot of external experience and that needs to be changed. Again, it is a directional change and not a wholesale change of the model.

Ms. Alonso-Gamo remarked that it was important to put things into perspective, because the staff had been incredibly cooperative in all kinds of things in terms of all the revisions being discussed. What the committee was approving would lead to a reduction of 7 percent on average in the staff's pensionable gross and the staff had been cooperative and understanding that this was something that made sense on technical grounds. It was possible to revise long-term policies all the time and the process of regular revisions was already in place. As pointed out by Mr. Daïri, there was a pace for doing those things and the process had been followed. Similar conclusions would be reached even if the process was started too early.

The Acting Chair (Mr. Portugal) noted that members of the committee approved the decision on page 10 of RP/CP/10/9, and that with that approval, the Pension Committee had endorsed the proposed amendments to the plan. The paper would be issued for approval by the Executive Board on a lapse-of-time basis. The committee then was asked to consider the second document brought for discussion pertaining to the change in the actuarial assumptions and methods of the plan, especially with regard to the new mortality table.

Mr. Meyer reiterated his recommendation to reduce the inflation rate from 4 percent to 3 percent, though even that might still be overstating inflation given past averages and near-term expectations. He also reiterated his recommendation to change the average rate of salary increase down to 6 percent from 7.8 percent. Looking at the table provided by the staff, he wondered whether there was an effort to narrow the gap without actually getting the level down to what prevailing economic conditions implied, and as to the reason why the reduction were not more aggressive. The assumptions for inflation expectations and salary increases were generous in comparison to the assumptions made by the U.S. authorities, even though the Fund's assumptions had been moving in the right direction.

The Deputy Director of the Human Resources Department (Mr. Rodlauer), in response to further comments and questions from Executive Directors, made the following additional statement:

> On inflation assumptions, we were aware that for this year and next year, 3 percent is overly optimistic. However we double checked carefully with industry projections as well as with our internal Western Hemisphere Department, and both agreed this is a reasonable long-term assumption to make.
>
> For the plan itself, financially it does not have a lot of impact. It washes out more or less. What really matters are the real assumptions on salaries and returns because the 3 percent inflation is carried through to the nominal return and to the salary assumptions, so it does not really have a lot of impact in terms of the actuarily required contribution that comes out of these projections. But we feel that, and the Western Hemisphere Department confirms that, while being on the high side in the next couple years, it is a good long-term assumption for the plan.
>
> On salaries, that is an important assumption, because the lower the salary projections are, the more financially advantageous for the plan. Because, on a net basis, even though future contributions to the plan are increased by having higher salaries, the eventual pension is even higher because it is based on the last three salaries. It leverages the salary increase into the liability. The reduction of the salary is beneficial to the plan. That is why we have a bias to be a bit more conservative here. Looking at the industry again, we have carried in the 3 percent inflation rate being a 1 percent reduction and we saw the .8 percent reduction in the salary assumption as being reasonable. Given what we have seen in the recent past and going forward, we did not want to go further again in the interest of being conservative and consistent with industry projections.

The Actuary for the Staff Retirement Plan (Mr. Nearpass) made the following statement:

> Relative to the inflation assumption we did check with internal sources here at the Fund and looked at projections from the Federal Reserve and what

they were looking at and clearly they are anticipating over the next ten years or so, inflation would be lower than perhaps the 3 percent, somewhere in the 2.5 percent range is what we typically see, but we are projecting these assumptions out 50 and 60 years relative to current plan participants from the period of employment all the way through retirement, and it affects salaries, return on investments and also the cost of living increases provided by the plan. So, we think it is a conservative assumption that is reasonable. We do modeling for asset liability studies which we use an outside source for. Looking at projections of inflation based on current conditions, those studies are showing that the 3 percent range is a reasonable longer term assumption as we go out beyond the ten years and are looking more at the 30 to 40 year range. We thought it was totally appropriate.

The second point on the salary increase assumption, that is a bit of a balancing act, again, because we do want an assumption that is conservative and reasonable. 6 percent in today's environment is conservative, relative to some of the comments made before, with salary freezes in the short term and very low salary increases, but we are trying to be conservative with this keeping in mind that the salary increase assumption will apply for 30 or more years in the future. To make sure that the pension plan is adequately funded, the lower we go, as Mr. Rodlauer said, the lower the projected benefits are. The lower the benefits are, the lower the liabilities, and one of the dynamics is that the value of the benefits is greater as one gets older, the value of the benefits accruing is more significant than the value of the contributions being made by the participant at that time so we do not want to understate the liabilities. So we are trying to strike a conservative balance, yet a reasonable balance, which is clearly our goal here, too.

Mr. Elder queried what would happen to the money that accrued if the assumptions were too conservative, or more generally, what were the risks entailed by being too conservative on not sufficiently conservative. In the United Kingdom, the assumptions used were not sufficiently conservative, which in the long term forced the system to adopt less generous terms. Conservative assumptions might sound good, but they were not necessarily a good thing.

The Deputy Director of the Human Resources Department (Mr. Rodlauer) responded that the immediate impact of being too conservative was that the plan would have experienced gains, which would then be reflected in the subsequent valuation, and if there were no change in the funding mechanism, it would lead to excessive accrual of reserves. That would then create an impetus to reduce the Fund's contribution to the plan. It would also be useful to note that the salary increase assumption had no implications for the Board, as it referred to the individual salaries of individuals from when they started to work until the end of their career at the Fund.

The Acting Chair (Mr. Portugal) noted that the committee approved the recommendations of the actuary on pages 3 to 5 of RP/CP/10/8 and that the Executive Board would be informed accordingly.

The meeting concluded at 3:56 p.m.

APPROVAL: April 6, 2011