

PERSONAL EQUITY AND RETIREMENT ACCOUNT

Transforming the Vision into Reality

I. Policy Objectives:

Republic Act (R.A.) No. 9505, otherwise known as “The Personal Equity and Retirement Account (PERA) Act of 2008”, sought to create a savings investment vehicle which serves the following objectives:

- A. Institute a first step towards pension reform by establishing a multi-pillar retirement income structure.

Filipinos generally rely on their GSIS and SSS pension for their retirement. However, these retirement benefits need to be supplemented in order to afford the retirees a decent and comfortable level of living. The PERA establishes the needed supplementary retirement benefits for the working population. PERA are generally distributable when the Contributor reaches 55 years old.

State-sponsored retirement programs are defined-benefits program which create an implicit debt on the national government. By empowering an individual to manage his retirement benefits, concerns regarding the actuarial fund life and viability of SSS and GSIS will be mitigated. The establishment of another retirement pillar reduces pressure on government coffers and promotes long-term fiscal sustainability.

- B. Develop the domestic capital market by giving incentives to long-term investment and creating more institutional investors

Considering the required holding period for PERA, PERA can be ideally invested in long-term products needed for the development of the domestic capital market.

Moreover, this structure creates more institutional investors as these entities can pool the contributions (i.e. PERA administrators).

II. Mechanics:

- A. *A contributor may establish a PERA with a maximum annual contribution of P100,000.00. In case of married individual, each spouse shall be entitled to make a maximum annual contribution of P100,000.00, notwithstanding the absolute community of property governing the property relations between them. An Overseas Filipino Worker can make a maximum annual contribution of P200,000.00. The annual contribution made shall be entitled to a tax credit of 5%, provided that the same do not exceed the maximum annual contribution.*

A Contributor may make contributions in excess of the annual maximum contributions but any contribution in excess of the maximum annual contribution no longer enjoys the tax incentives attendant with PERA.

A tax credit was adopted to level the impact of the tax privilege given to the Contributors. The tax impact of a deduction would depend on the tax bracket of the taxpayer. A tax deduction would give higher tax benefits to the higher income group considering that they belong to a higher tax bracket.

The Secretary of Finance may, in the future, adjust the amount of annual contribution to reflect the present value of the maximum annual contribution.

B. Private employers may contribute to its employee's PERA to the extent of the amount allowable to the Contributor.

The employer contribution to an employee's PERA should be in addition to the mandatory Social Security System (SSS) contribution and retirement pay under the Labor Code of the Philippines. The employer's contribution to the PERA is deductible from the employer's income for tax purposes. The contributor retains the prerogative to make investment decisions pertaining to his PERA.

C. The Contributor shall make all investment decisions pertaining to his PERA.

The Contributor shall generally make all investment decisions pertaining to his PERA and the Administrator merely executes the Contributor's decisions.

The Contributor may appoint an Investment Manager who can make the investment decisions for and on his behalf. The same entity may act as both Administrator and Investment manager, provided that the entity has a trust license. The additional requirement of a trust license is imposed to assure that the entity exercise the highest level of prudence and care, considering the possible conflict of interest in assuming both roles.

D. The Contributor may establish 5 PERA with only one Administrator but has the option to change said Administrator.

To achieve administrative simplicity in the grant of tax incentives, a Contributor must designate only one administrator for all his PERA accounts. Notwithstanding that an individual has only one Administrator, the individual can still enjoy flexibility in his investment. An administrator is obliged to present all available product offerings, with emphasis on the products suited to the Contributor.

E. A PERA may be constituted under either an agency or trust arrangement.

In case of an agency arrangement, the contributor retains legal title to his investments. On the other hand, the contributor retains only beneficial title to his investments in case of a trust arrangement.

F. PERA investment products must be pre-qualified by the Regulatory Authorities.

Considering that PERA is available to the general public, the investment products offered under the PERA must be pre-approved by the Regulatory Authorities to promote consumer protection.

G. The assets under PERA shall be kept separate from the other assets of an Administrator/Custodian.

As an investor-protection measure, the PERA assets shall not be part of the general assets of the Administrator/Custodian for purposes of bankruptcy.

H. All income earned by PERA investment products are tax-exempt. Likewise, all distributions from the PERA are tax-exempt.

The intention is to exempt the investment income from tax and not merely defer imposition of tax.

I. Since the PERA is a pension/retirement account, the same should be long-term and must be distributed only when the contributor reaches 55 years old or upon his death.

The distribution to the contributor was limited to only two instances: (a) when the Contributor reaches the 55 years old, provided that the Contributor has made contributions to the PERA for at least 5 years; and (b) upon the death of the Contributor, irrespective of the age of the Contributor at the time of his death.

In case of the earlier instance mentioned, the distribution shall be made in either lump sum or pension for a definite period or lifetime pension, the choice of which shall be at the option of the Contributor. The Contributor, however, has the option to continue on with the account.

In case of the latter instance, there shall be complete distribution of the benefits.

J. Early withdrawals will generally be subject to penalty.

In order to ensure that contributions stay in the system on a long-term basis, any withdrawal shall be subject to an early withdrawal penalty. This will temper the tax incentives given to PERA investment products. Any premature withdrawal will be subject to a penalty. However, there are limited instances for which there will be no early withdrawal penalty:

1. For payment of accident or illness-related hospitalization in excess of 30 days; and
2. For payment to a Contributor who has been subsequently rendered permanently totally disabled as defined under the Employees Compensation Law, Social Security Law and Government Service Insurance System Law.

K. Rules and regulations on PERA, with the exception of the subject matter on tax incentives, shall be promulgated by the DOF, BIR and the Regulatory Authorities, with BSP as lead agency. The BIR will also be tasked to formulate rules and regulations on the grant of tax incentives.

To this end, the Regulatory Authorities and the DOF and BIR executed a memorandum of Agreement which provides a framework for (a) drafting the IRRs of the PERA Act of 2008; and (b) consultation and exchange of information among the Bangko Sentral ng Pilipinas, Securities and Exchange Commission, Insurance Commission, Department of Finance and the Bureau of Internal Revenue (BIR) relative to the implementation, administration and enforcement of the same law.

III. Consumer Protection Measures in the PERA-IRR

A. Qualification Requirements for PERA Market Participants or Players

1. Administrators

One major requirement for pre-qualification of an Administrator is the maintenance of net worth of at least One Hundred Million Pesos (P100,000,000.00) at all times. This is to ensure that Administrators who will participate in the PERA market have sufficient capitalization taking into consideration the nature of their duties. This also seeks to screen out fly-by-night entities from participating in the same market.

In determining the net worth of an Administrator, the following amounts shall be deducted from its combined capital accounts: (1) the one percent (1%) of the book value of the total volume of PERA assets administered and other capital adjustments as may be required by the concerned Regulatory Authority; (2) total outstanding unsecured direct or indirect credit accommodations extended to its directors, officers, stockholders and related interests (DOSRI); and (3) appraisal surplus or appreciation credit as a result of appreciation or an increase in the book value of its assets.

The other pre-qualification requirements focus on ensuring that the Administrator possesses adequate resources ranging from personnel equipped with the necessary expertise to perform the duties of PERA

administration to systems and technological capabilities required for the administration of PERA Investment Products.

An Administrator must have both a Qualification Certificate from the appropriate Regulatory Authority and the Accreditation Certificate from the Bureau of Internal Revenue

2. Investment Manager

Investment managers are initially limited to the juridical entities. The accreditation requirements for Investment Managers focus on ensuring that they possess sufficient experience and supervision and control procedures for the conduct of investment management functions.

3. Third Party Custodian

The Cash Custodian shall be primarily responsible for receiving and disposing all funds in connection with the PERA in accordance with the instruction of the Administrator. The Securities Custodian, on the other hand, shall be responsible for maintaining custody of all securities, evidence of deposits or other evidence of investment and disposing of the same in accordance with the instruction of the Administrator.

Only banks and trust entities may act as custodians. They shall observe the requirements imposed by the Manual of Regulations for Banks (MORB) on capitalization and capital adequacy, management, earnings, liquidity and sensitivity to market risk (CAMEL) composite rating.

B. Requirement of Posting Security for Faithful Performance by PERA Administrators

Considering the central role played by the Administrators in the PERA, Administrators must establish a security for the faithful performance of its duties. This shall consist of government securities, equivalent to one percent (1%) of the book value of the total volume of PERA assets administered and these are to be earmarked in favor of the concerned Regulatory Authority. The securities shall not be withdrawn, transferred or replaced by the Administrator without the prior written instruction of the concerned Regulatory Authority. The security for the faithful performance of Administrator functions shall be in addition to and shall be treated separately from the capital, surplus and undivided profits of the Administrator. Should an Administrator incur a deficiency in the security deposit, it is required to replenish the same within one week from the end each quarter. Failure to do so shall subject the same to appropriate sanctions.

This IRR provides the mechanism by which this security can be tapped by an aggrieved party. The Administrator shall issue an authorization in favor of the respective Regulatory Authority to withdraw, dispose and disburse the proceeds thereof to settle any claims arising from the breach of its duties as evidenced by a final and executory court order.

C. Profiling of PERA Contributors by Administrators and Investment Managers

The IRR requires the Administrator to observe certain procedures relating to the establishment of a PERA. These procedures include the following:

- Adoption of a pre-disclosure policy aimed at inculcating in the Contributors knowledge about the nature of, privileges and conditions of establishment of a PERA, categories of PERA Investment Products available to a Contributor and the risks associated with the same and obligations and responsibilities of the Administrator
- Account opening process which includes the conduct of Client Suitability Assessment and formulation of investment policy statement
- Documentation to formally establish the relationship between the Administrator and the Contributor
- Provision of risk disclosure statement to the Contributor, containing, among others, provisions on the general risks associated with each category of PERA Investment Product and cautionary statement on the aforementioned general risks
- Provision of information to the Contributor on the full range of PERA Investment Products with emphasis on the specific category of products corresponding to the risk profile classification of the Contributor. The Administrator shall also provide a process for allowing Contributors to invest in PERA Investment Products not falling within his risk profile classification, provided that this shall be allowed only upon prior written instruction of the Contributor

D. Duties of the Administrator, Investment Manager or Custodian in the Event of Suspension or Revocation of their Accreditation

The IRR sets out the procedure to be observed by the Administrator, Investment Manager or Custodian in the event of suspension or revocation of their accreditation. Their primary responsibility consists of advising the Contributor of the fact of suspension or revocation of their accreditation. The advice is aimed at ensuring that the Contributor is given time to take the necessary steps concerning his/her PERA in view of the suspension or

revocation of the accreditation of his/her Administrator, Investment Manager or Custodian.

Should a Contributor opt to transfer his/her entire PERA assets within a period of two (2) working days to another Administrator in view of the suspension or revocation of the Administrator's qualification, the IRR provides that such transfer or withdrawal shall not be considered as an early withdrawal and shall not be subject to penalties thereon. If the transfer of the entire PERA assets is made beyond the mandatory period by reason of the fault of the Administrator, the latter shall be personally liable for the early withdrawal penalties on such account.

E. Disclosure Requirements

Administrators and Investment Managers are required to provide the Contributors who engage their services minimum information on the nature and risks of each category of PERA Investment Products (General Risk Disclosure Statement). They shall also provide the Contributors a Specific Risk Disclosure Statement on a particular PERA Investment Product where the Contributors may wish to invest in. The aforementioned statements shall form part of the Administrator's files.

The Administrators are required to classify individual PERA products according to the risk profile classification of the Contributors which could be conservative, moderate or aggressive. This classification takes into consideration the risks and returns associated to investment products.

The PERA Investment Products shall be valued in accordance with the valuation methodology, standards and requirements as may be prescribed by the concerned Regulatory Authority provided that such valuation methods and standards are in accordance with the internationally accepted accounting and valuation standards.