

Regulating and Supervising Occupational DB Pension Schemes

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Theoretical Basis for Regulation and Supervision

- **Address Market Imperfections and Failures**
- **Overcome Asymmetrical Information**
- **Control Moral Hazard**
- **Compensate for Consumer Myopia**
- **Enhance Competition and Efficiency**

Supervision and regulation of voluntary pension schemes

- **Essential to consolidate reliable private pension schemes**
- **Main issues:**
 - **Specificities of different voluntary pension systems (DC,DC, occupational, individual)**
 - **Supervision approach:**
 1. **Compliance based vs. risk based**
 2. **Proactive vs. reactive**
 3. **Draconian vs. prudential**
- **Stage of development of private pensions**

Common Forms Of Complementary Pension Systems

- **Occupational Schemes**
 - Company Sponsored (DB or Collective Investment)
 - Multiple Employer – Trade Union
- **Mutual Benefit Society/Professional Associations**
- **Individual/Retail Contractual Savings**
 - Investment Products
 - Life Insurance/Annuity Products

Main Categories of Risks For Pension Systems

- **Systemic**
- **Portfolio**
- **Agency**
- **Principal**

Systemic and Portfolio Risks

- **General decline in assets due to broader economic problems**
- **Failure of sponsoring employers and financial institutions leading to default on pension promises**
- **Volatility of market value of assets leading to inability to fund cash flow of benefits**
- **Risk profile of investments inappropriate to needs of pension system – both too high or conservative investments leading to low benefit levels**

Agency and Principal Risks

- **Competence and quality of decision making by responsible parties**
- **Funding flow inadequate to support benefit levels**
- **Self investment in sponsoring entities causing inefficient risk/return or inability to liquidate assets to pay benefits**
- **Theft or embezzlement of assets**
- **Payment of excessive fees and expenses**
- **Asset skimming through transactions with related parties**
- **Lack of knowledge or ability to enforce property rights by members**
- **Limited or no capacity to mitigate systemic risks**

Particular Risks of Occupational Defined Benefit Systems

- **Funding flows are insufficient to meet future benefit obligations**
- **Benefits increases awarded to older workers to restructure workforce leaving inadequate funds**
- **Senior employees award themselves large benefit increases prior to retirement or failure of business**
- **Assets are illiquid and cannot pay cash flow requirements**

Control of Risks Through Regulation & Supervision

- **Regulation:**
 - Legal Foundations and System of Rules and Regulations Governing the Structure and Operation of Pension Funds
 - Establish form of system and “empower” various parties to perform functions or protect interests
- **Supervision:**
 - Oversight and Enforcement of Compliance With The Rules
 - Collection of information and monitoring of system to support review and analysis

Main Elements in the Regulation of Pension Funds

- **Licensing and Entry Requirements**
- **Standards for Quality of Governance**
- **Rules for Permissible Investments**
- **Qualifications and Standards of Conduct for Responsible Parties**
- **Prohibitions on Conflicts of Interest and Transactions with Related Parties**
- **Minimum Funding Standards**
- **Limits on Fees and Expenses**

Supervision of Occupational Pension Funds

- **Monitoring of funds activities through regular reporting and data collection**
- **On and off-site information collection on routine basis to deter abuses and when indications of problems are found**
- **Impositions of sanctions and penalties**
- **Venue of processing of complaints and assistance to members**
- **Education and training of responsible parties to facilitate compliance with standards**

Regulation and Supervision of Occupational Funds in Pakistan

- **Create comprehensive legal framework for establishment of occupational funds with explicit linkages to access to preferential tax treatment**
- **Establish and enforce minimum funding standards for occupational DB schemes**
- **Impose investment and portfolio restriction to limit financial risks**
- **Create regular reporting and disclosure requirements**
- **Give members clear rights and mechanism to pursue grievances**
- **Assign supervisory authority and establish monitoring mechanism**

Supervisory Authority

- **Clear mandate and accountability for results**
- **Defined authority and process for development and interpretation of rules**
- **Specific authority for sanctions, penalties and other actions**
- **Access to books and records or to require production of information**
- **Reliable funding source and adequate staff with required financial and legal skills**
- **Program of regular reviews and in response to specific indications of problems**
- **Explicit coordination of legal authority with other financial services regulators**
- **Process for receiving and responding to complaints by members**
- **Outreach and education to sponsors and industry**