CONSUMER PROTECTION IN PENSIONS SYSTEMS

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What is different about consumer protection for pensions?

- **Complex, difficult products:**
  - **several decisions -not a one-off purchase -joining a plan/ picking contribution levels/ selecting investment portfolios/ switching/ selecting a type of annuity purchased rarely and individuals -typically locked in for a long time + implications of decisions clear only after time lag**
  - **long term savings, a small difference in charge levels may have a significant impact of final outcome**
  - **concept of '*suitability*' - how apply in situations where no choice? Regulation?**

- **Role of employer / trustee**

- **Mandatory – extra protection for vulnerable individuals**
- **No / limited choice**
- **Competition within pension markets does not work well**

- **Range from personal voluntary DC (like other financial products) to DB occupational fund (different beast) – latter not really consumers but members still need protection**

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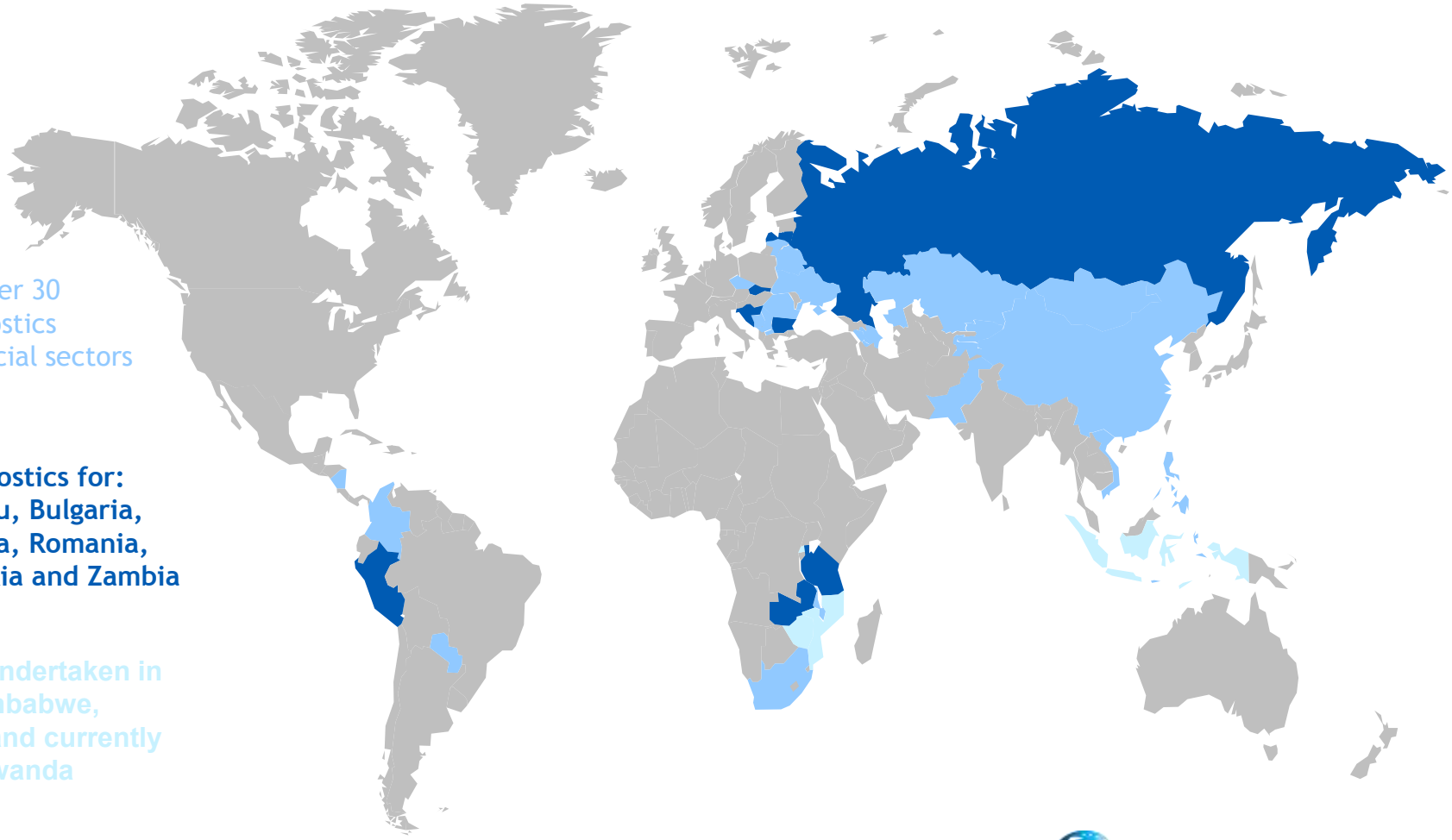
World Bank Good Practices for Financial Consumer Protection

Diagnostic tool – compatible with OECD High Level Principles on Financial Consumer Protection



Undertaken over 30 country diagnostics covering financial sectors in detail

Pension diagnostics for: Tanzania, Peru, Bulgaria, Croatia, Latvia, Romania, Russia, Slovakia and Zambia

+ personally undertaken in Indonesia, Zimbabwe, Mozambique and currently working on Rwanda

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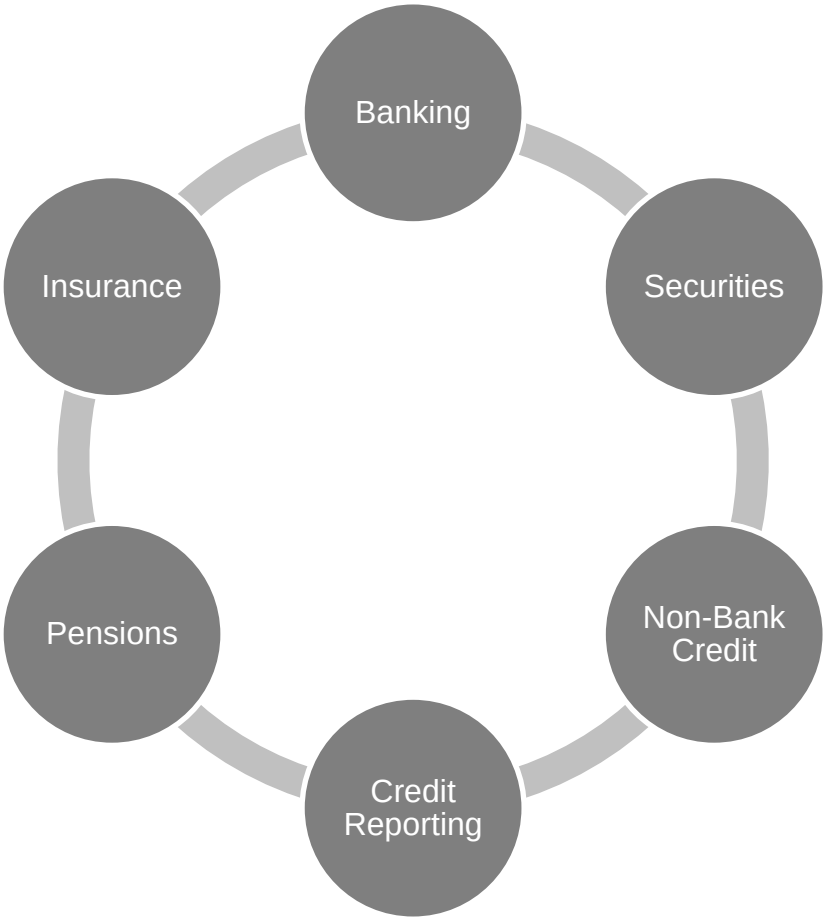
World Bank Good Practices for Financial Consumer Protection

For each segment, the World Bank's Good Practices cover:

1. ***Legal, regulatory and institutional framework***
2. ***Consumer disclosure***
3. ***Business practices***
4. ***Dispute resolution mechanisms***
5. ***Financial literacy***



GPs – including for pensions - currently under revision:

- ***to incorporate new international CPFL developments as well as new research on CPFL;***
- ***to reflect lessons learned from the past 30+ CPFL diagnostic reviews and policymaker feedback;***
- ***to draw from a broader range of country e.g. given the rapid increase across the globe in policymakers working on or interested in CPFL;***
- ***to address emerging CPFL issues with respect to topics such as digital finance and innovations in consumer financial products and services, delivery systems + providers.***

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Main Findings from Diagnostics

- ***Institutional capacity*** **- lack of institutional capacity / resources to supervise consumer protection / market conducts laws relevant to the pensions sector**

- ***Suitability*** **- limited laws relating to advice on suitability of pensions products (if choice exists)**

- ***Key Fact Documents*** **–less standard for pensions than for other sectors + not widely used**

- ***Dispute mechanisms*** **–not generally included in pension legislation / regulation application less clear than for other financial sectors**

Main Findings from Diagnostics

- ***Codes of Conduct* – again less widespread than other sectors / can be useful tool for raising awareness of consumer protection issues + raising industry standards**

- ***Training* – lack of formal requirements for or provision of training of employer HR / intermediaries and also trustees**

- ***Confidential Information* – though not generally a problem in the pension sector, this is not always explicitly covered in pension legislation/ regulation**

- ***Non-remittance of employee contributions* – one of the biggest abuses of pension fund members in some countries is employers deducting but not remitting employee contributions to the pension fund**

Leading Practices - Information

Leading practices – being more fully incorporated into the revised pensions section of the new Good Practices

- ***Supervisory comparative information***
  - transparent cost comparisons (Mexico)
  - synthetic cost indicators (Hong Kong, Hungary, Italy, Turkey)
  - payout information (SCOMP Chile – UK)

- ***Costs***
  - hidden costs (e.g. mutual funds in the pension fund portfolio) have to be disclosed or management fee duplications are explicitly prohibited (Italy).
  - Present fees in absolute currency not percentages (Mexico)

- ***Key Fact Documents***
  - (EIOPA/OPSG - Basic Information Document (BID)
    - name of the pension scheme
    - nature and main features of the pension scheme
    - brief indication of whether loss of capital is possible
    - indication of the consequences of an early exit
    - risk and reward profile of the pension scheme
    - contributions to be paid by the member
    - all costs and charges
    - past performance
    - not legally binding projections of possible retirement benefits

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Leading Practices - Information

- Combined statements (Netherlands)
- Modular approaches – front web page + links (Australia)
- Information via phone (Tanzania)
- Simple and understandable information provision, emphasize simple language and recommend the use of graphs (NEST UK)

X	√	Explain
Diversification	*The spread of your money across a range of different investments*	*You don't put all your eggs in one basket*
Annuity	*Retirement income*	*Regular income stream for the rest of your life*
Accumulation	*Building your retirement pot*	
Trivial commutation	*Taking your retirement pot as cash*	*If your NEST retirement pot is worth less than £2,000 or your total retirement savings are less than £18,000 you might be able to take this money as a cash lump sum instead of buying a retirement income*

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Leading Practices – Role of Employer

- **Pension administrators should send a timely warning to the employee (and preferably also to the authorities) if contributions do not arrive properly**
- **Personnel departments have an important role in information provision about possibilities related to pension accumulation. They should also be prepared to become the first point of contact for dispute resolution**
- **Supervisors should support personnel departments in their role to help employees**
- **Russia – sales force can contact HR but not employees directly**
- **Mozambique – provider good practice training HR department / make part of recommendations**
- **Where disputes cannot be settled by the HR department, the pension fund management company's client relationship representative or the pension supervisory authority, formal, independent, third-party mechanisms should be available – such as a financial sector ombudsman (international good practice for the operation of these bodies should also apply to the pension sector)**

Leading Practices - Sales

- **Suitability = age risk appetite, income, family situation, tax position and net worth**
- **Consumers warned if providers lack sufficient information (Australia, Colombia, Costa Rica, Israel, Mexico and Thailand)**
- **Sales may not go ahead (Hong Kong, India, Pakistan)**
- **Consumer's circumstances and the advice given be put in writing and retained (Australia, Hong Kong)**
- **Based on complaints and compliance testing, suitability checks may be supervised (Colombia, Israel, Slovakia)**
- **Regulators may assist service providers with annual regulatory seminars where responsibilities to clients get emphasized (South Africa)**

Leading Practices – Statements

- **Personal statements should focus on outcome (final pensions) more than simple return figures and past performance**
- **Statement should include a well-developed, simple to understand projection of future pension income and should demonstrate the potential impact of increased (and continuous) contributions and the postponement of retirement**
- **Projected monthly income, which is the most important figure for the consumer, should be highlighted, whereas projected fund values at retirement are secondary (but also to be included)**
- **Supervisory authority should provide assumptions for the projections, supplying the range in which the estimates may vary**

What needs to be combined with consumer protection?

- **International experience has shown has that competition in pension markets does not work well – however empowered consumers are, individuals remain unengaged and uninterested (recent UK survey found that people spend more time planning their annual holiday than their retirement…..)**

- **Additional mechanisms drawing on lessons from behavioural economics are being utilized to provide consumers with additional assistance:**
  - **Defaults**
    - **well designed / lifecycle**
    - **floor/ cap annuity levels**
  - **Framing and limiting number of decisions**
  - **Auto-enrolment**
  - **Limited sales force? Blind accounts**