

Structure and Governance of Pension Supervisory Authorities

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Structure of IOPS Members

Table 2. Structure of Pension Supervision in Selected OECD + IOPS Member Countries

Specialized Pensions Supervisor	Semi-integrated Supervision	Integrated Supervision
	<i>At least pensions + insurance</i>	<i>Pensions, insurance, securities and possibly banks</i>
Chile	Belgium	Australia
Costa Rica	Finland	Austria
Hong Kong	France	Bulgaria
India	Jordan	Canada
Ireland	Luxembourg	Croatia
Italy	Portugal	Czech Republic
Japan	Spain	Denmark
Kenya	Turkey	Germany
Mexico	Zambia	Hungary
Nigeria		Iceland
United Kingdom		Israel
United States		Jamaica
		Kazakhstan
		Kosovo
		Korea
		Mauritius
		Namibia
		Netherlands
		Norway
		Pakistan
		Poland
		Slovak Republic
		South Africa
		Thailand
		Trinidad + Tobago

Case for Integration

- Argument for financial integration in general:
 - Better suited to financial conglomerates
 - Economies of scale
 - Less likelihood of regulatory arbitrage
 - Better defined set of objectives (avoiding the Christmas tree effect)
 - Lower probability of “agency capture” by the industry
 - Improvement in the quantity and quality of information flows between departments
 - Better transparency and accountability

Case against Integration

- Agency becomes so big and powerful that it can potentially become divorced from the industry it oversees (Bureaucratic Leviathan)
- Moral hazard problem if the public develops the false impression that every financial instrument has the same risk or is supported by the same financial safety net
- Major differences in the core businesses of the different financial sectors remain (accountability for certain financial products can be blurred within a single integrated agency)
- Single agency might lose focus on the objectives of regulation and supervision for each different product and business
- There is no guarantee that supervisors within the same organization will communicate more efficiently and closely
- Risk of monopolist regulator – diversity of regulation may be good
- Economies of scale vs. suboptimal resource allocation
- Single agency may be easier to ‘capture’ (by industry/ politics) than several
- Transparency + accountability only increased if there is political will (if there is - may not be need to restructure)

Case against Integration – Unique Nature Pensions

- Long-term contracts involved + incentives/ compulsion to encourage long-term saving
- Coverage of a wide social and economic range of the population (particularly where compulsion) i.e. vulnerable consumers, low income and education levels
- Hence low risk tolerance – pensions can be subsistence rather than discretionary savings (social as well as financial role of pensions)
- Complexity of products (tax issues, salary assumptions , longevity, difficulties, asset valuations etc.) –hence asymmetrical information in favour providers / intermediaries
- Involvement of employers , sponsors unions – supervisors have to oversee them to (contribution payment etc.)
- Large number of funds in some countries
- Non-profit nature of pension funds in some countries
- Potential impact of pension assets on financial market and economic stability given their increasing size relative to financial markets (>100% GDP some countries)

Table 3. Efficiency and Efficacy of the Integrated and Specialized Approaches to Supervision in Meeting the Core Goals of Financial Regulation in Latin America

Issues	Objectives	Integrated Banking, Insurance and Securities		Integrated Banking, Insurance, Securities, and Pensions	
		Efficacy	Efficiency	Efficacy	Efficiency
Less Risk of Moral Hazard	Consumer Protection	+/-		+/-	
	Systemic Stability	+		+	
	Financial System Efficiency				
Less Chance of Regulatory Capture	Consumer Protection	+	+	+	+
	Systemic Stability				
	Financial System Efficiency				
Absence of 'Christmas Tree' Effect	Consumer Protection	+		+	
	Systemic Stability				
	Financial System Efficiency				
Less chance of a Bureaucratic Leviathan	Consumer Protection				
	Systemic Stability				
	Financial System Efficiency	+/-	+/-	-	-
Achieving Economies of Scale and Scope	Consumer Protection				
	Systemic Stability				
	Financial System Efficiency	+	+	+	+
Treatment of Financial Conglomerates	Consumer Protection	+	+	+	+
	Systemic Stability	+	+/-	+	+/-
	Financial System Efficiency	+	+	+	+
Greater Competitive Neutrality	Consumer Protection	+	+	+	+
	Systemic Stability	+/-	+	+/-	+
	Financial System Efficiency	+		+	
Greater Transparency and Accountability	Consumer Protection	+	+		
	Systemic Stability	+	+		
	Financial System Efficiency	+	+		

Source: Demaestri and Ferro (2004)

Depends on Context

- Other ways to characterize pension systems:
 - *Government + policy driven model* – specialist agency best suited
 - *Employer-driven model* – specialist agency best suited
 - *Commercially-driven pension fund model* – integrated agency best suited
- Integrated structure may be better suited to smaller / developing countries where it may be more difficult to find sufficient personnel with the necessary skill set to staff multiple agencies - but integration alone is not a sufficient condition for effective and efficient supervision

Conclusions

- Structure doesn't matter:
 - Benefits of specialization may be achieved via an integrated authority (through having a specialist pensions division within the agency)
 - Likewise many of the benefits of integration may still be achieved by a specialist pension authority if strong communication links with other supervisory institutions are established.
- No best answer as it depends on the context

Governance of Supervisory Authorities

- Establishing and maintaining of good governance settings of public agencies, and pension supervisory agencies, in particular, and measuring the effectiveness of their activities are increasingly important task for majority of jurisdictions around the world
- The IOPS has undertaken a major study on this topic, released last year, devoted to Governance and Performance Measurement of Pension Supervisory Authorities (Working Paper N°10)

4 Key Pillars of Strong and Good Governance of pension supervisory authorities

- **Independence:** requiring operation without undue influence, transparent processes for appointing/dismissal of senior management, ability to secure adequate resources and sufficient powers to take effective actions, which can be only over-ruled by judicial process
- **Accountability:** involving external audits, suitable internal scrutiny and review process and measuring performance;

4 Key Pillars of Strong and Good Governance of pension supervisory authorities

- **Transparency:** ensuring that authority is transparent about its objectives, strategies, actions and their results and achieves their understanding, through extensive consulting process with stakeholders;
- **Integrity:** requiring codes of conduct, discretion to apply powers, internal controls and competent staff.

Independence

- Clarity of the authority's responsibilities, mandate and powers, which provide for operational independence.
 - ½ IOPS members 'quasi-independent'
 - Almost all have clearly stated objectives and assigned mission statements (embedding objectives in legislation helps to foster transparency / accountability)
 - All sufficient powers
 - Some guidance from governments but day to day independence
- Processes for the appointment, composition, remuneration and expertise of the governing board (or senior management team if there is no board) that minimise the scope for undue influence
 - Most countries have open procedures + suitable requirements
 - Most authority heads appointed by government / have qualifications/ most are appointed for fixed term
 - Usually authorities have governing board
 - Senior officials tend to be appointed on civil service terms

Independence (continued)

- Ability to secure appropriate resources without being subject to undue influence
 - Budget generally set by government / mixed public funds + fees
 - 1/2 public commitment to fund adequately
 - Most outsource

Accountability

- External audit and accountability to stakeholders
 - All accountable to public body/ public at large
 - Mandated audits + internal reviews
 - Ombudsman for most
- Due process in the operation of the organisation, including clarity and division of responsibilities and the exercise of delegation
 - Division of responsibilities between board and operational management with clear authorization processes
 - Clear division of responsibilities inside authority (particularly with respect to enforcement actions/ sanctions)
- The measurement and reporting of performance
 - Internal evaluations (See separate slides)

Transparency

- Ensuring understanding of the authority's objectives, rules, responsibilities, and procedures along with its achievements.
 - Communication via websites/ annual reports/ media/ appearances at legislative body
- An educative and consultative relationship with stakeholders.
 - Dynamic interaction with supervised entities through regular communication and information sharing
 - Feedback from stakeholders (surveys / consultations)

Integrity

- Codes of conduct for board members and operational staff, including processes relating to conflicts of interest and confidentiality
 - Most governance codes + codes of conduct (ethical behaviour /conflicts of interest/ gifts / complaints procedure)
- The integrity of supervisory responses is assured through having the ability to apply appropriate discretion in exercising powers, without being constrained by the threat of litigation
 - All have internal rules for use of powers
 - Most guaranteed indemnity from prosecution

Integrity (continued)

- Internal controls aimed at securing consistency and transparency of decision making, effective risk management and efficiency and propriety in the use of resources
 - Most internal audit / some risk management unit / +external audit
 - Some internal risk models
- The provision and assessment of staff competence and expertise, deployed within the organisation and brought in from outside
 - Qualifications
 - Results-based performance measurement for staff
 - Training

Performance Measurement

- Difficult to measure due to counter-factual (i.e. what did not happen) + external factors play an important role
- Good system of performance information should be:
 - *Focused on the organisation's aims and objectives;*
 - *Appropriate to, and useful for, the stakeholders who are likely to use it;*
 - *Balanced, giving a picture of what the organisation is doing, covering all significant areas of work;*
 - *Robust in order to withstand organisational changes or individuals leaving;*
 - *Integrated into the organisation, being part of the business planning and management processes; and*
 - *Cost Effective, balancing the benefits of the information against the costs.*

Performance Measurement

- Supervisory authorities could establish a range of measures looking at the following categories
 - ***Effectiveness measures:*** looking at outcomes against the authority's high level objectives;
 - ***Efficiency measures:*** using the supervisor's credibility or reputation with its key stakeholders as a proxy or performance pledges;
 - ***Economy measures:*** which could take the form of cost per inspection or cost of overheads relative to operational activities