



Kenya Approach to Risk Based Supervision

IOPS CARIBBEAN REGIONAL
WORKSHOP ON PRIVATE
PENSION SUPERVISION



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RETIREMENT BENEFITS AUTHORITY, KENYA

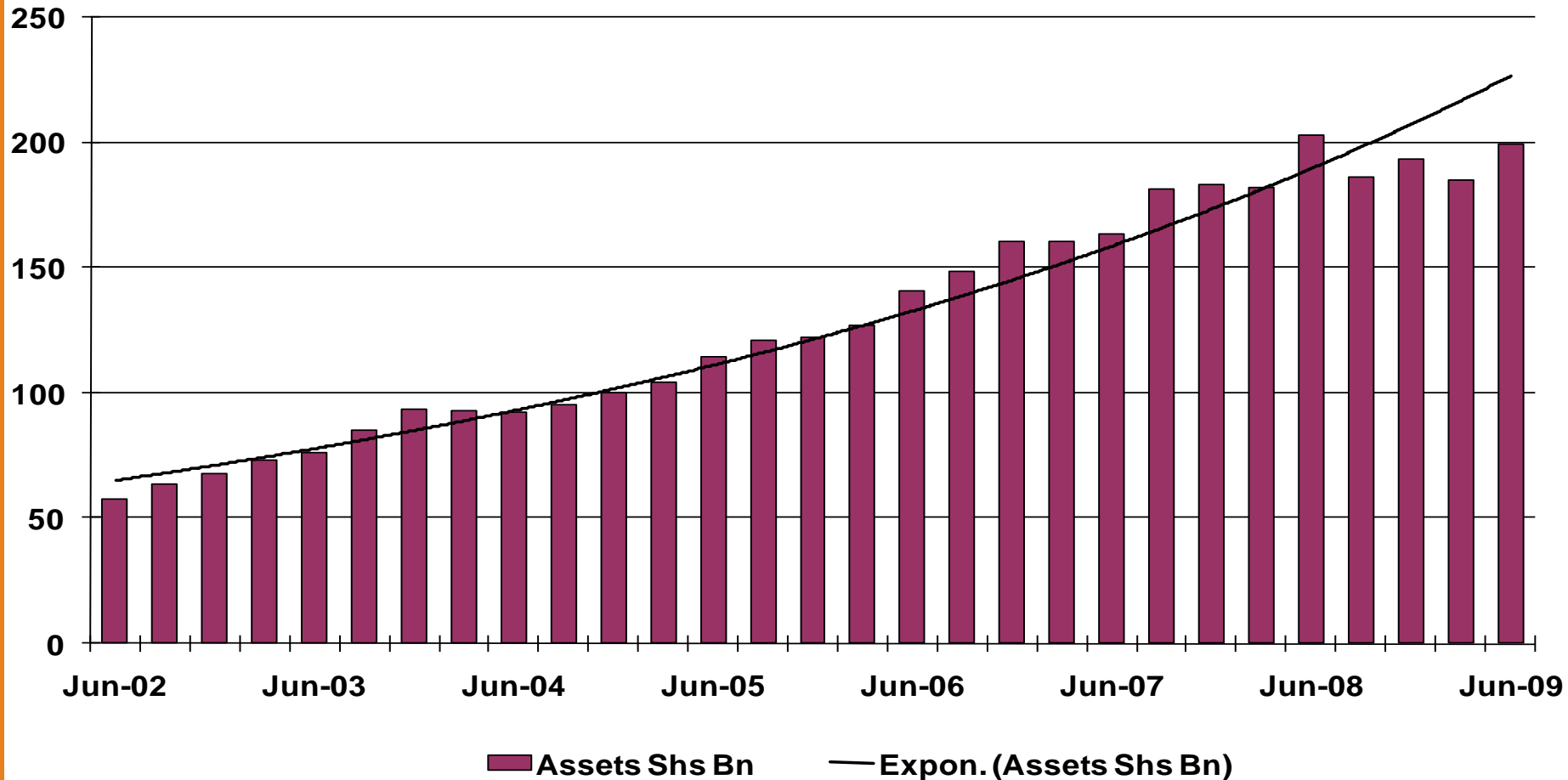
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- Overview of Risk Based Supervision Model in Kenya using IOPS RBS Toolkit Framework
- Challenges in Implementing Risk Based Supervision Model in Kenya

Kenyan Retirement Benefits Industry

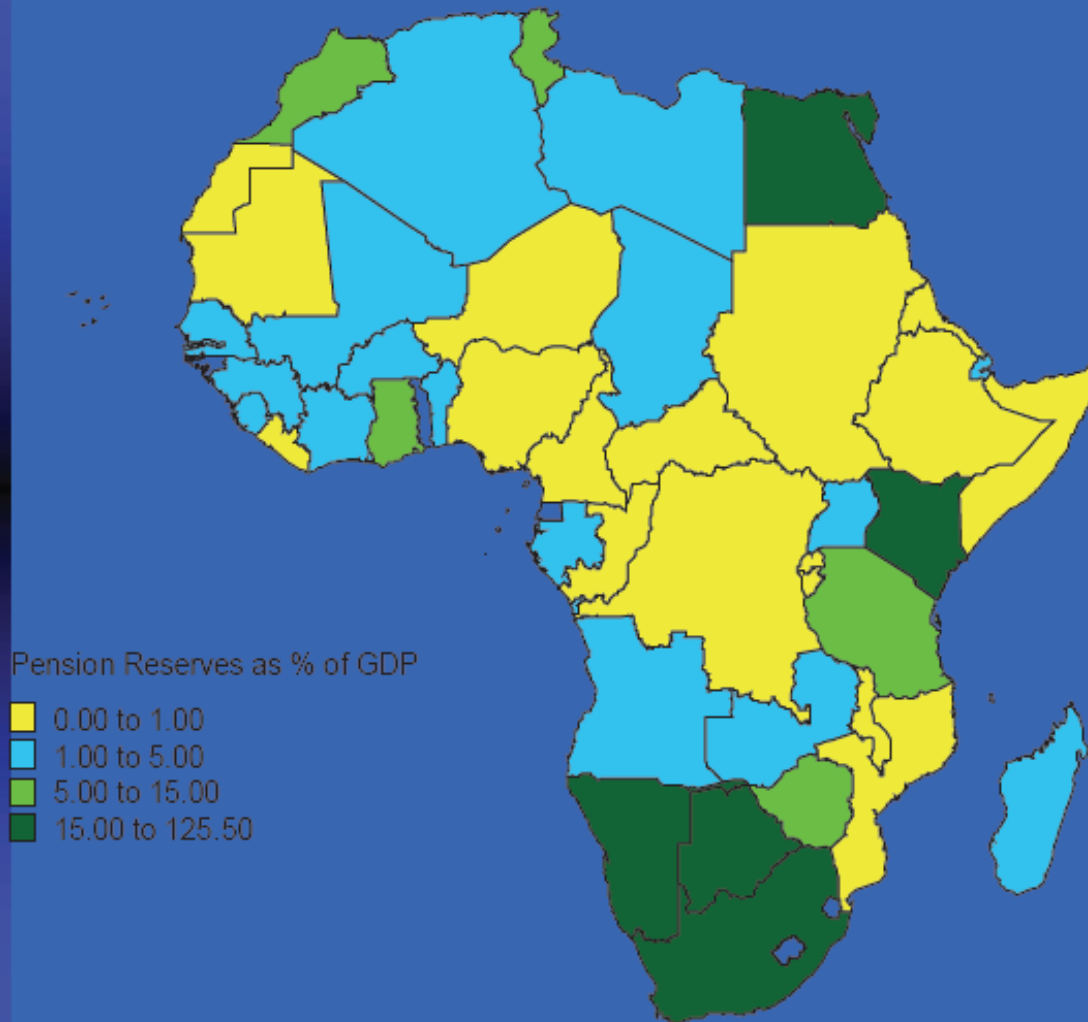
	Civil Service Scheme	National Social Security Fund	Occupational Schemes	Individual Schemes
Legal Structure	Act of Parliament	Act of Parliament	Trust Deed	Trust Deed
Membership	all civil servants	formal sector workers in companies with 5+	formal sector workers in companies that have schemes	individuals formal/informal sector join voluntarily
Funding	Non-funded	funded	funded	funded
Regulation	Exempt from RBA	Subject to RBA	Subject to RBA	Subject to RBA
Assets March 2009	nil	US\$ 1.0 billion	US\$ 2.5 billion	US\$ 40 million

Growth of Retirement Industry Assets



Note: Excluding NSSF, June 2009 provisional

Comparison with African Countries

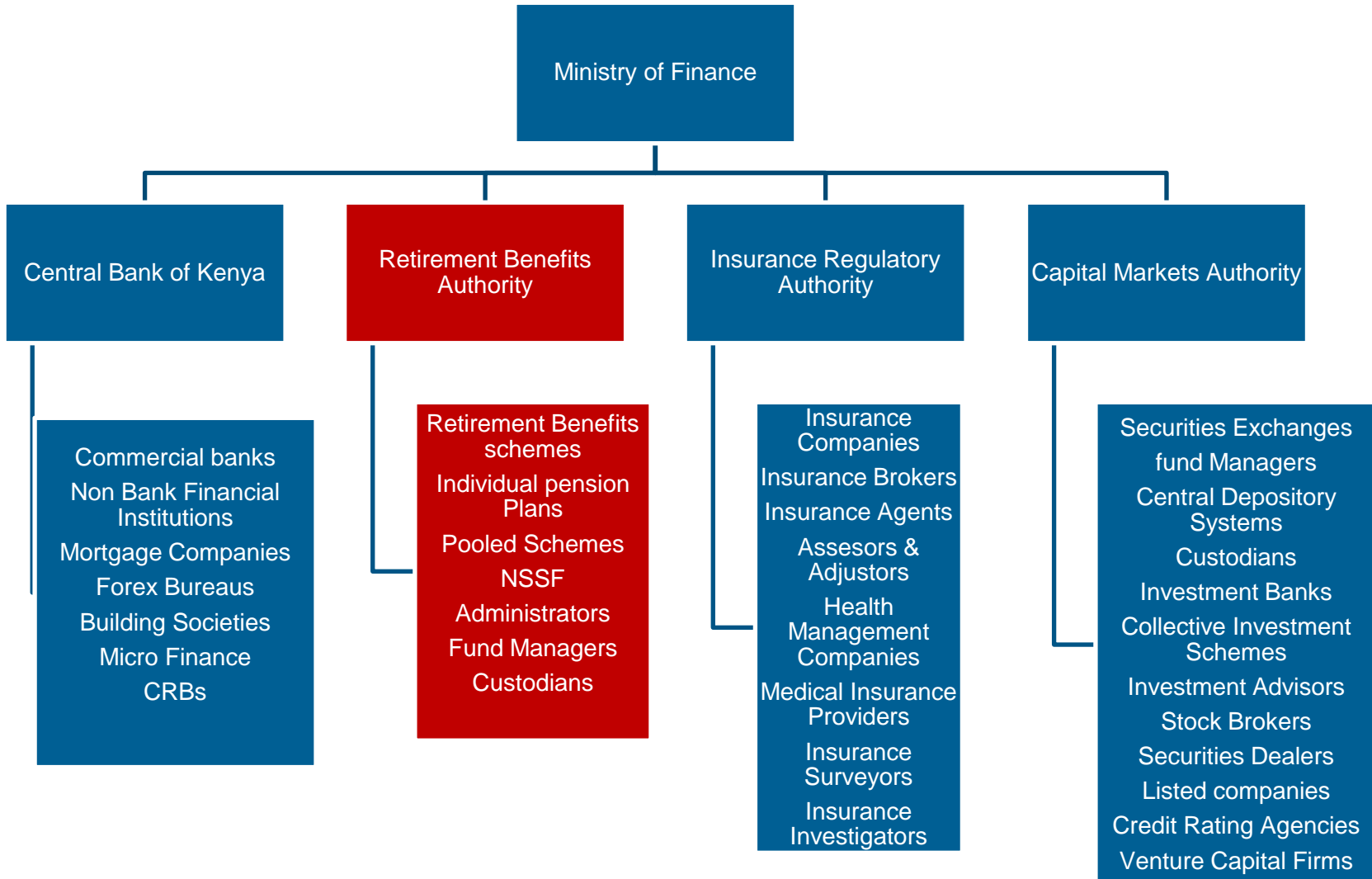


Financial Sector in Kenya



■ Banks ■ Stock Market ■ Pensions ■ Insurance

Regulatory Structure



RBA Statutory Objectives

**Retirement
Benefits
Authority**

- ❖ **Regulate and supervise establishment and management of retirement benefits schemes.**
- ❖ **Protect the interest of members and sponsors of retirement benefits schemes.**
- ❖ **Promote the development of the retirement benefits industry.**
- ❖ **Advise the Minister for Finance on the national policy to be followed with regard to the retirement benefits industry.**
- ❖ **Implement all government policies relating to the retirement benefits industry**

Risk Based Supervision - Introduction

- RBA has formally adopted Risk Based Supervision as its model of supervision for the retirement benefits industry.
- Previously RBA placed more attention on compliance status of retirement benefits schemes with little regard to potential risks
- Risk based supervision marks a shift to a more proactive approach as opposed to the previous reactive approach
- In implementing RBS, RBA received technical assistance from the World Bank as well as input from a consultant funded by the Government of Kenya and the World Bank.

Why did RBA adopt RBS?

- Gain a better understanding of the quality of management, the characteristics and risks in a scheme and apply consistency in supervision and in assessing compliance
- Schemes will benefit from the improved focus of supervision and understand why particular supervisory tools are used
- Improved governance, transparency and efficiency in schemes
- Higher returns at lower risk resulting in reduction in scheme failures
- Allocation of RBA resources more efficiently
- Greater development , innovation and confidence in the industry

Pre Conditions for RBS – Module 1

Legislative

- Governing law was amended in 2008 to allow RBA to issue practice notes
- **Proposed removal of most quantitative investment restrictions – pending**

Supervisory Readiness

- RBS implementation committee formed
- Trained staff in RBS
- **New IT system to be implemented**

Industry Skills and Readiness

- Supporting professionals are present in market
- **Pension funds risk management systems weak**
- **Capital markets lack full range of investment grade securities**

Obtaining Information– Module 2

Sources of Information

- Mandatory exception reports – whistle blowing required
- Periodic Scheme Returns
 - Annual Accounts
 - Investment returns – six months
 - Contribution returns – quarterly
 - Actuarial Valuations Tri - annual for DB Schemes only
- On site inspections
- Third Party reports – Interim administrators
- **Interrogatories and scheme self risk assessment - pending**

Quantitative Assessment of Risk – Module 3

Regulatory Requirements for DB Plans supporting QAR

- DB scheme actuarial valuations every three years. Law amended in 2008 to allow RBA in consultation with Actuarial profession to prescribe minimum basis for valuations through practice notes
- Minimum funding Level for DB schemes raised from 80% to 100% in 2009

Regulatory Requirements for DC Plans supporting QAR

- Schemes mandated to use independent fund manager and custodian registered by RBA
- Quantitative asset restrictions – Broad Maximums – on investments

Techniques of Quantitative Assessment of Risk

	DB	DC	Comment
Comparison of assumptions	✓	NA	
Sources of earnings	✓	NA	
Roll forward calculations	✗	NA	
Duration analysis	✗	✗	
Sensitivity testing	✓	✗	Required by regulation
Deterministic stress tests	✓	✗	Done in collaboration with IMF FSAP mission
Stochastic stress tests	✗	✗	
Value at Risk Calculations	✗	✗	

Risk Scoring– Module 4

Risk	Inherent risk	Management and control	Capital support
Weight	30%	35%	35%
Indicator	<ol style="list-style-type: none"> 1. Investment risk <ul style="list-style-type: none"> • Investment Policy • Investment returns • Risk Measures 2. Insurance risk <ul style="list-style-type: none"> • insurance risk insured • capacity to handle non-insured risk 3. Non-financial risk <ul style="list-style-type: none"> • simple plan provisions and procedures • transparent outsourcing • capacity to handle greater complexity 	<ol style="list-style-type: none"> 1. Trustee oversight <ul style="list-style-type: none"> • self-assessment • fit and proper criteria • lines of responsibility 2. Operations and Control <ul style="list-style-type: none"> • Interrogatories • filing & contribution record • Number & resolution of complaints • expenses 3. Independent review <ul style="list-style-type: none"> • use of independent professionals • reports without qualifications 	<ol style="list-style-type: none"> 1. The Fund <ul style="list-style-type: none"> •Funding / solvency ratio •Deficit recovery plan •Actuarial basis •Rates of return 2. The Employer <ul style="list-style-type: none"> • Timely remittances • DB actuarial assumptions • DC communication to members • Industry shape

Overall Risk Scoring

- For each indicator a score of zero is given if the outcome is satisfactory and a score between 0.25 and 1 for an unsatisfactory outcome depending on the indicator and the degree of the breach.
- The total score from each of the risk indicators for each of the three risk categories are aggregated .
- The aggregate score per risk category is weighted (30: 35: 35) so as to establish the overall risk score for every scheme.

Supervisory Response– Module 5

Overall Score	Classification	Supervisory Response
Less than 0.5	Green	No Action
0.5 – 1.5	Light Amber	Monitoring
1.5 – 2.5	Dark Amber	Intensive Monitoring
2.5 – 3.5	Red	Recovery Plan
3.5 – 4	Ultra Red	Intervention

Implementation Challenges

- Systemic issues arising from historical problems in some schemes and the impact of the global financial crisis which means many schemes may yield adverse risk scores.
- Lack of available data for a number of schemes which makes it impossible to score them.
- Difficulty in identifying and financing a suitable IT system in line with the new system as well as challenge of shifting industry towards electronic filling of returns in suitable format.
- Educating scheme trustees and service providers on the new system and enabling them to complete interrogatories satisfactorily.

Thank You

Asante

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