SUPERVISION OF PENSIONS - KENYAN EXPERIENCE

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Chief Executive – Retirement Benefits Authority

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## The Structure of Kenya’s Retirement Benefits Industry

<table>
<thead>
<tr>
<th>Legal Structure</th>
<th>Civil Service Scheme</th>
<th>National Social Security Fund</th>
<th>Occupational Schemes</th>
<th>Individual Schemes</th>
</tr>
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<tbody>
<tr>
<td>Act of Parliament</td>
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<td>Trust Deed</td>
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<th>Membership</th>
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<tbody>
<tr>
<td>all civil servants and teachers</td>
<td>-formal sector workers in companies</td>
<td>formal sector workers in companies that have schemes</td>
<td>individuals formal/informal sector join voluntarily</td>
<td></td>
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<tr>
<th>Funding</th>
<th>Civil Service Scheme</th>
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<td>Non-funded</td>
<td>funded</td>
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<td>Exempt from RBA</td>
<td>Subject to RBA</td>
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RETIREMENT BENEFITS INDUSTRY IN KENYA - ASSETS - US$ 4bn

- Civil Service Pension Scheme: 0%
- Individual Retirement Benefits Schemes, shs 2bn: 1%
- National Social Security Fund, shs 81bn: 30%
- Occupational Retirement Benefits Schemes, shs 181bn: 69%
GROWTH IN RETIREMENT BENEFITS ASSETS SINCE REFORM

Excluding NSSF
Prior to enactment of Retirement Benefits Act in 1997, schemes were not supervised and regulated and they faced the following problems:

- Lack of harmonized legislation
- Dominance by sponsors and misappropriation of scheme funds
- Members not involved
- Lack of transparency and information disclosure
- Poor record keeping
- Poor investments decisions
- Lack of professional input
- Funding problems
- Delays in benefits payments
REGULATION OF PENSION SCHEMES

- Establishment of a scheme is voluntary
- Registration is mandatory
- Establishment is under a written law or trust
- Rules to protect the member and the sponsor
- Schemes to be fully funded and separated from the sponsor
- Trustees must develop a prudent investment policy
PENSION SCHEME ADMINISTRATION

- Administration duties vested in trustees
- Trustees may appoint administrators to carry out their administration duties
- Trustees fully liable to members and supervisor
- Scheme rules must make provision for inter alia
  - Membership eligibility
  - Retirement age
  - Vesting and benefits formula
  - Dissolution of and winding up of scheme
  - Contribution rates etc.
PENSION SCHEME FUNDING - I

- Minimum funding level - 80% DB schemes, 100% DC schemes
- Schemes proper records must be kept
- Audited Financial statements - to be published
- Statement of contributions remitted and benefits payout
- Data of each member - membership statements issued
- Scheme rules and the amendments thereof
- Disclose information about the scheme
- Hold Annual General Meetings
Trustees to engage services of experts who have no relationship with the scheme. These include:

- Auditors
- Fund Managers
- Custodians
- Administrators
- Actuaries

- Defined Benefits schemes required to carry actuarial valuations every three years
RETURNS TO THE SUPERVISOR

- Annual audited scheme accounts
- Actuarial valuations for DB schemes
- Quarterly investment and custodian reports
- Quarterly record of contributions
- Any other information as may be required by the supervising Authority
INSPECTION OF SCHEMES

- Supervisor empowered to carry out inspection on scheme, fund manager and custodian

- Inspection reports may lead to imposition of sanctions against the guilty or appointment of interim administrator

- Obstruction of inspection or refusal to co-operate is a criminal offence

- Introduction of risk based supervision (to identify and reduce risks) will assist in identifying schemes to be inspected
SCHEMES INVESTMENTS
Trustees required:

- To have clear understanding of purpose, objectives and goals of the scheme (investments options to meet the scheme objectives)
- To formulate written policy on investment with help of investment advisor
- To revise investment policy every three years
- To ensure policy complies with statutory guidelines
- To appoint and monitor the investment manager
- To ensure strategic allocation of scheme funds diversified across and within assets
EXPERIENCE IN REGULATED ENVIRONMENT

- Improved Investments – diversified pool of assets
- Increased professionalism
- Increased member confidence – more people now desire to save for retirement
- Increased member participation and involvement
- Improved record keeping
  - Member statements issued
  - Scheme accounts summaries issued
- Scheme transparency and disclosure increased – Audited Accounts received by RBA and regularly analyzed
SHIFT TO RISK BASED SUPERVISION (RBS)

- Previous supervision based on off-site reviews and on-site inspections not tied to scheme specific risk
- Authority has shifted from a compliance based to more pro-active risk based approach.
- Approach concentrates on identifying pension risks using defined criteria, monitoring risks and dealing with any identified risk early enough before they become unmanageable and too costly to resolve
- RBS focuses on the aspects of scheme which pose high risk to the security and delivery of benefits
- Authority has implemented 75% of Risk Based Supervision based on implementation manual developed from international best practice
KEY RISKS ADDRESSED IN RBS APPROACH

- **Counterparty Default Risk**: Risk of loss from the failures of a counterparty to meet its obligations
- **Balance Sheet and Market Risk**: Risk of losses due to movements in interest rates and other market prices
- **Operational Risk**: The risk of losses resulting from inadequate internal processes, people and systems – whether these are internal to the regulated entity or in a service provider
- **Liquidity Risk**: The risk that an institution will not be able to meet its payment obligations as they fall due without excessive cost
- **Legal and Regulatory Risk**: The likelihood of adverse consequences arising from the failure to comply with all relevant laws and regulations
- **Strategic Risk**: Risks to the continued viability of an entity as a result of change in the operating environment, including internally driven change such as merger or introduction of new product line
- **Contagion and Related Party Risk**: Risk to an entity’s business as a result of close association with another entity – the risks may be direct through financial exposure or indirect through reputation damage
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<td>1. National laws should assign clear and explicit objectives to pension supervisory authorities</td>
<td>Objectives clearly spelt out in Retirement Benefits Act</td>
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<td>2. Pension supervisory authorities should have operational independence</td>
<td>Independent Board but Minister retains powers to appoint and fire Board</td>
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<td>3. Pension supervisory authorities require adequate financial, human and other resources</td>
<td>Authority funded through levy on schemes</td>
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<td>4. Pension supervisory authorities should be endowed with the necessary investigatory and enforcement powers to fulfill their functions and achieve their objectives</td>
<td>Authority has powers to sanction and directly prosecute offenders under the Act</td>
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<td>5. Pension supervision should seek to mitigate the greatest potential risks to the pension system</td>
<td>Implementation of risk based supervision</td>
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*Pension supervisory authorities should ensure that investigatory and enforcement requirements are proportional to the risks being mitigated and that their actions are consistent* | Authority has taken a flexible approach taking cognisance of historical factors that may mitigate against immediate compliance |
| 7  
*Pension supervisory authorities should consult with the bodies they are overseeing and cooperate with other supervisory authorities* | Constant consultation with industry. Financial sector regulators forum in place.                                                             |
| 8  
*Pension supervisory authorities should treat confidential information appropriately* | Scheme information kept confidential                                                                                                       |
| 9  
*Pension supervisory authorities should conduct their operations in a transparent manner* | Periodic updates to industry. Annual accounts and audit report circulated to industry                                                      |
| 10 
*The supervisory authority should adhere to its own governance code and should be accountable* | Authority operates an ISO 9001: 2000 certified quality management system                                                                      |
FUTURE CHALLENGES

- Bringing schemes to full compliance
- Ways of Increasing coverage
- Adequacy of retirement benefits savings
- Increased longevity of life
- Uncertainty of investment returns from the capital markets (market volatility)
- The increasing costs of providing promised benefits by Defined Benefits Schemes (most employers considering to shift DC schemes)
Ahsante

www.rba.go.ke