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standard of living for every  
Kenyan worker after their  
retirement”**

# **THE CHALLENGES OF ADOPTING RISK BASED SUPERVISION**

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# AGENDA

- **Introduction and Background**
- **Implementation of Risk Based Supervision**
- **Challenges Faced in Adoption of Risk Based Supervision**
- **Conclusion**

# INTRODUCTION AND BACKGROUND

# Introduction and Background I



- The Retirement Benefits Authority was established by an Act of Parliament in 1997 with one of its key objectives being “to regulate and supervise the establishment and management of retirement benefits schemes”.
- The World Bank Institute facilitated training of the Retirement Benefits Authority (“the Authority”) technical staff on Pension Supervision in February 2004 effectively introduced the concept of Risk Based Supervision (RBS) for pension funds.
- The Management of the Authority considered issues arising from this training and agreed on the importance of shifting, in a timely manner, from compliance reviews as the main tool of supervision to RBS.

## Introduction and Background II

- In consequence, a working committee was set up consisting of representatives from the Departments of the Authority involved in compliance to prepare the groundwork for the introduction of RBS.
- The terms of reference of the committee included:
  1. Assessing the risks faced by retirement benefits schemes in Kenya in a comprehensive manner.
  2. Assessing whether the regulatory framework was able to cope with the identified risks and to recommend improvements.
  3. Review system functionality and process flows to assist in:
    - a) Developing a quantitative and computerized risk assessment criteria.
    - b) Setting up control structures that would promptly register and record the risks (early warning systems).
- The result was a report completed in August 2007 giving the basic framework for the introduction of RBS for pension funds in Kenya.

# **IMPLEMENTATION OF RISK BASED SUPERVISION**



## Rationale and Objective of RBS

- For the Authority, the rationale behind introduction of RBS is to improve the regulatory process and make more effective use of its resources.
- As a result, the RBS approach conceptualized by the Authority has three (3) main objectives:
  1. To identify cases requiring closer supervision on a timely basis;
  2. To focus limited resources on review of those cases identified as requiring closer supervision; and
  3. To ensure timely corrective action.



## Overview of the RBS Approach

- In measuring the overall risks of schemes, the Authority weights risks according to the type of fund – amongst other parameters, greater weight is placed on solvency risk for defined benefit schemes and investment risk for defined contribution schemes.
- The schemes are weighted against a set list of risk parameters and the rating of a scheme is derived from considering in addition a number of risk mitigants which the scheme could have in place.
- On identifying and evaluating the risks and then giving the scheme a rating, the Authority is then able to assess the nature, extent and timeliness of intervention for implementation of remedial measures.



## Progress of Implementation of RBS

- Progress has been made in the implementation of the new supervisory model. The gains achieved include:
  - i) Adoption of the model proposed by the working committee in its final report through management commitment;
  - ii) Continuous sensitization of technical staff on the development of the model;
  - iii) Development and application of a Compliance Visit Manual and On-site Inspection Guidelines;
  - iv) Substantial progress in carrying out an initial risk assessment audit of all registered schemes through on and off site measures;
  - v) Engagement of consultants to assist in developing a system toolkit and to propose a Management Information System (MIS) interface for application of the toolkit.

# **CHALLENGES FACED IN ADOPTION OF RISK BASED SUPERVISION**



## Challenges Faced in Development of RBS

- The technical staff of the Authority has had to learn a considerable amount about the supervisory model in a global environment where this mode of supervision is still in its initial stages of implementation for the pensions industry. This has been time consuming and has required considerable resources.
- International RBS models have taken very different approaches to stress testing and value at risk measurement based on pension system peculiarities – limited historical data on the success of these models made development of the Kenyan model more challenging.



## Challenges Faced in Implementation of RBS I

- The first of the key challenges to implementation of RBS has been dealing with legislative weaknesses in the regulatory framework which do not support its implementation.
- Another significant challenge, on the part of the Authority, has been limited expertise in development of system toolkits and Information Technology (IT) interfaces to assist in risk scoring and red-flagging.
- The categorization of risks has also been a challenge as this may be considered to be subjective and therefore the reliability of the risk assessment exercise queried by stakeholders. Similarly, responsiveness of the categorization to a dynamic economic and political environment is a significant challenge.

## Challenges Faced in Implementation of RBS II

- Capacity development of the staff of the Authority involved in supervision is also a challenge as the new supervisory model requires a paradigm shift which involves a change both in culture and skills utilization.
- As expected, the stakeholders involved in the management of schemes, particularly the trustees, fund managers, custodians, administrators and auditors are concerned with the additional prudence, possible liability and sanctions that come with a shift in the supervisory model.
- Another challenge that is under consideration is the way in which the Authority shall measure the result of adopting the risk based approach to supervision, particularly to the extent that different stakeholders expect different outcomes and measures.

# CONCLUSION



## CONCLUSION

- The Authority is continually addressing the above and other challenges.
- Anticipation of stakeholder concerns and ways of alleviating these concerns proactively is key to successful implementation of RBS.
- The outlook for the pensions industry in Kenya is positive but gains must be safeguarded – risk based supervision shall be a crucial tool in so doing.



**Thank You**

**Asante**

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