

Competencia, Regulación y Supervisión de los Beneficios del Sistema de Pensiones

Seminario Internacional AIOS/ASSAL
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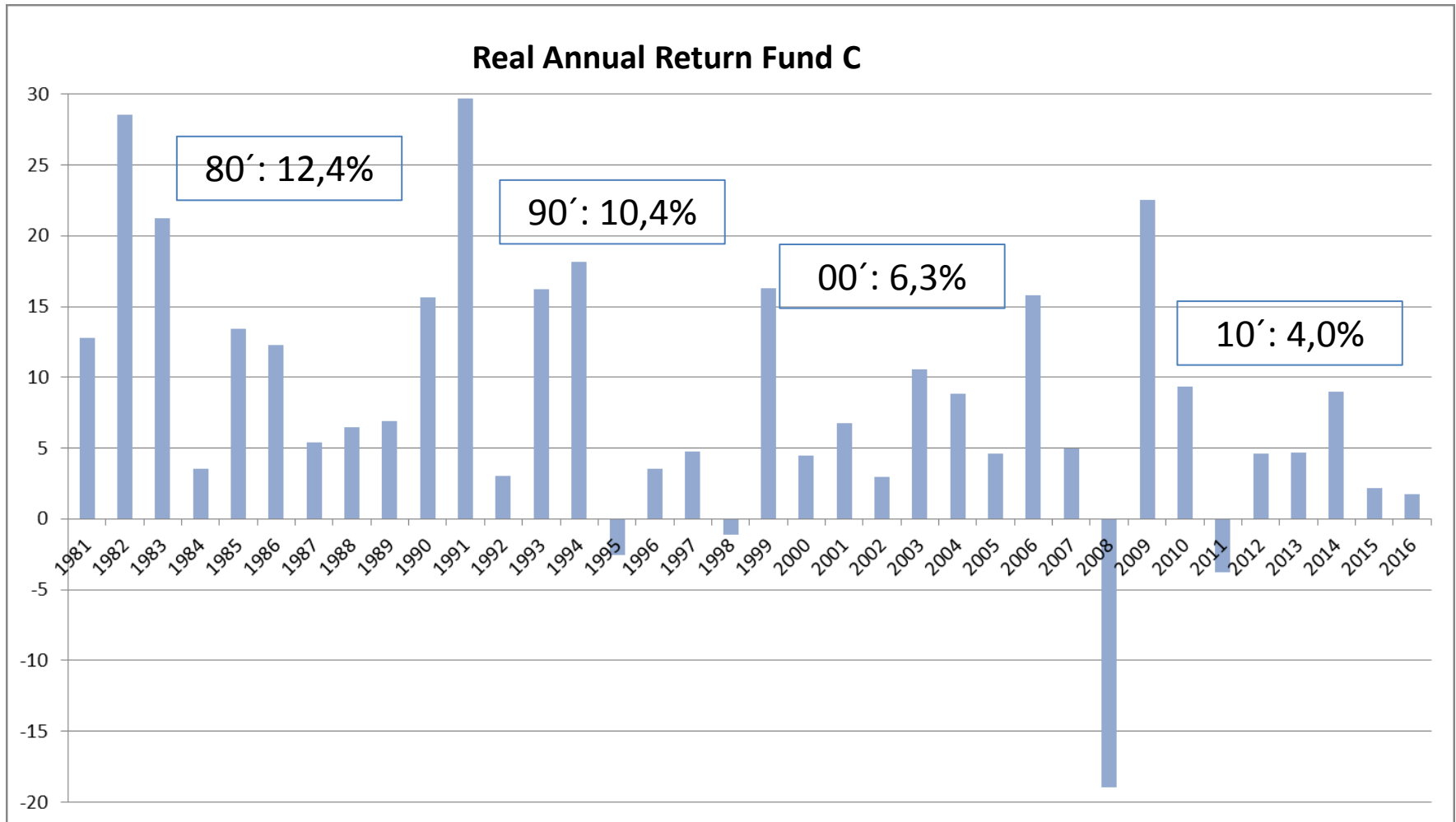
Olga Fuentes
Intendente de Regulación
Superintendencia de Pensiones
Vice-Presidente IOPS

Superintendencia de Pensiones

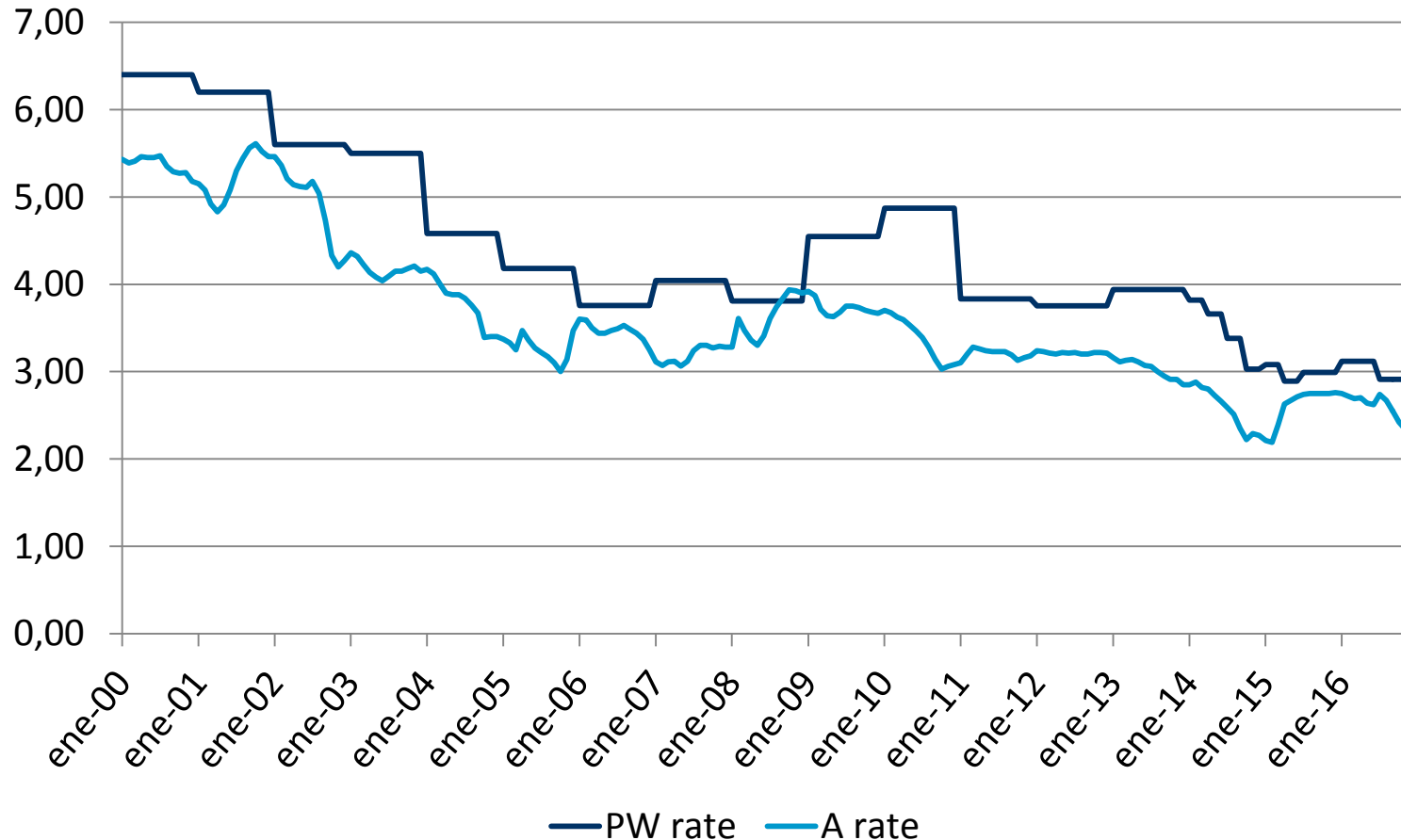
- Motivation
- Pension Types and Products
- Pensioner Profile for Programmed Withdrawal and Annuities
- Selection of Pension Products: Evolution
- Regulatory Framework and Parameters
- International Good Practices and Experience
- Conclusions and Challenges

- Main goal/challenge: pension adequacy without risking sustainability in an environment of higher life expectancy and lower interest rates
- Relevant risks for pension funds globally needs to consider:
 - Investment risk
 - Longevity risk
 - Human capital/labor risk
- Increased longevity and decreasing evolution of interest rates globally
- Latin America, including Chile, is in transition from the demographic dividend phase to a major aging period
- Public policies design and implementation requires technical expertise, a long term view, and continuous evaluation to introduce the necessary adjustments on time.



■ Real Returns



- Annuity rates and PW interest rates



- Life expectancy at retirement age

	1985		2015
	81,65	3,59 años →	85,24
	84,32	5,99 años →	90,31

- Benefits in the Chilean pension system consider:
 - Contributory pillar
 - Non-contributory benefits of the solidarity pillar
 - Subsidies (bonus per child)
 - Possibility of inheritance and take lump sums (restricted)
- Types of Pension
 - Age – legal
 - Age – early retirement
 - Disability – partial or total
 - Survivorship
- Pension Products:
 - Programmed Withdrawal
 - Annuity
 - Temporary Income with Deferred Annuity
 - Programmed Withdrawal with Immediate Annuity

PENSION PRODUCTS: MAIN DIFFERENCES

Characteristic	Programmed withdrawal (PW)	Life Annuity (A)	Temporary Income (TI) with Deferred annuity (DA)	PW +A
Administration	PFA	Insurance company	PFA/Insurance company	PFA/Insurance company
Possibility to switch	Yes	No	Yes: Temporary Income	Yes: PW
Ownership	Affiliate	Insurance company	TI: Affiliate; DA: Insurance company	PW: Affiliate; A: Insurance company
Financial market and longevity risk	Affiliate	Insurance company	TI: Affiliate; DA: Insurance company	PW: Affiliate; A: Insurance company
Pension value	Variable	Constant	Variable --> Constant	Variable + Constant
Inheritance	Yes	No	Temporary Income	PW
Access to the Solidarity Pillar	Yes	Yes	Yes	Yes

- Members whose balance does not finance the value of the Basic Solidarity Pension do not have the option to choose an annuity.
- They are candidates to receive benefits from the solidarity pillar or being able to adjust their pension to this value until the balance is exhausted.



Programmed Withdrawal

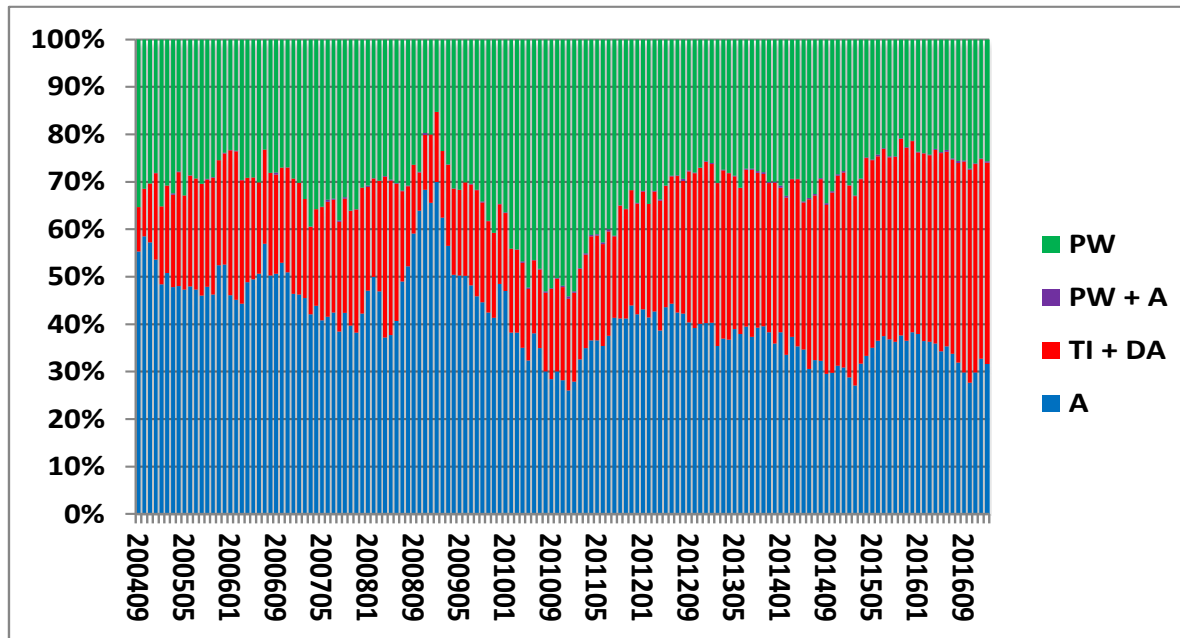
- Low life expectancy
- Low degree of risk aversion
- Higher return associated with higher volatility
- Bequest motive
- Complementary savings
- Longevity and market risks: affiliate

Life Annuity

- High life expectancy
- High degree of risk aversion and preference for a constant pension
- Early retirement
- Longevity and market risks: insurance company

Depending on individual characteristics, a combination of products can arise as an optimal decision.

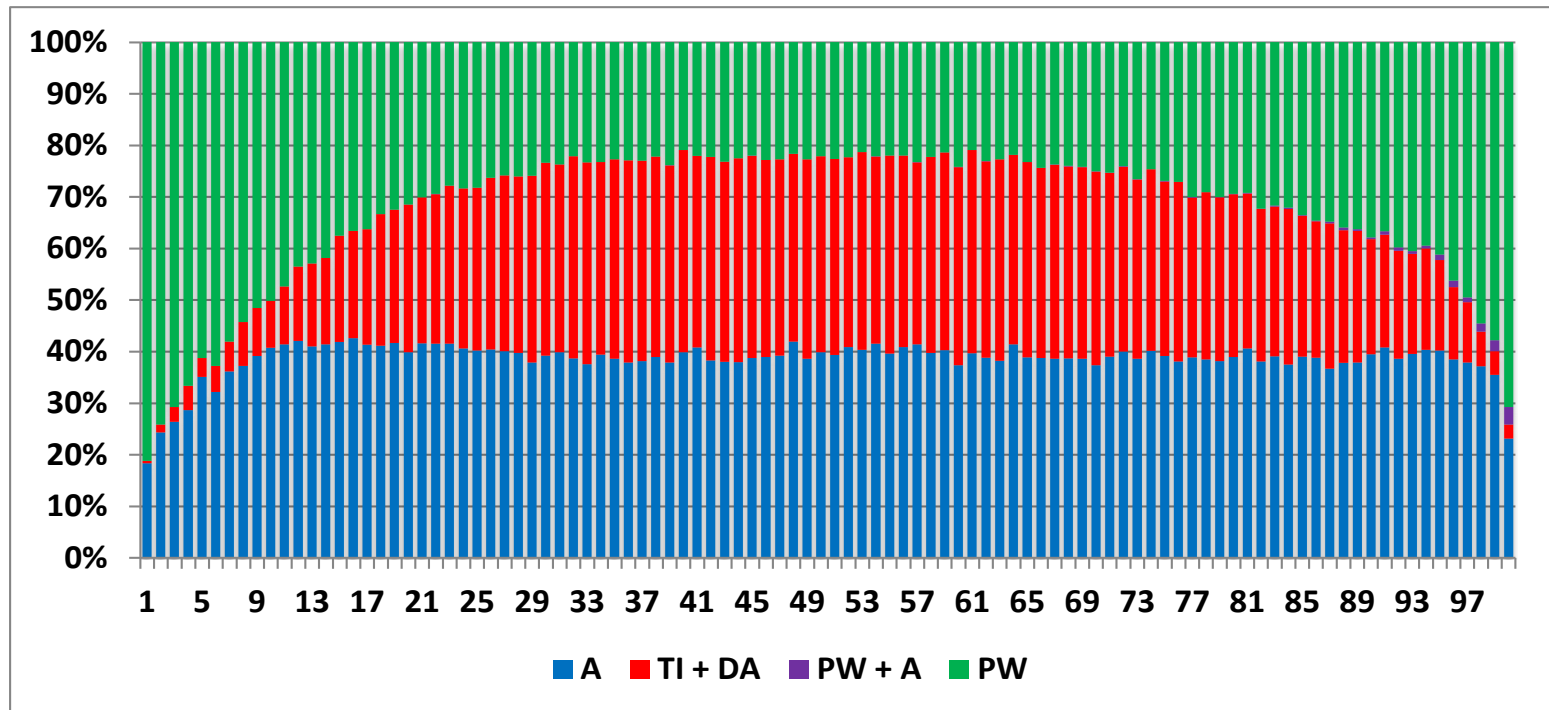
Pension claims in SCOMP (2004-2016)



Currently (4T2016),
the largest shares
are obtained by
TI + DA: 44%
Life annuity: 30%
PW: 26%

- The contribution of Programmed Withdrawal and Life annuity has varied over time
- Temporary Income with Deferred Annuity (TI + DA) has shown a sustained growth since 2011 (satisfy short term liquidity needs + a stable pension afterwards).
 - TI/DA = 2 in almost all selections
 - Deferral: between 1 and 2 years (75% of times), average = 20 months
- The flexibility offered by this modality could be enhanced to increase the deferral period and to consider other TI/DA ratios

PENSION PRODUCT SELECTION WITH RESPECT TO PERCENTILE OF CUMMULATIVE SAVINGS (2004-2016)



- Temporary Income + Deferred Annuity: higher in medium balances
Life annuity: Stable participation except for the more extreme percentiles
- Program Withdrawal: greater importance for balances of the 5% higher or lower of the distribution

- **SCOMP Electronic market quotation was introduced in 2004 to bring higher competition and information.**
- **Mortality tables are periodically updated**
 - Prevents pension resources from being exhausted in advance
 - Allows insurance companies to properly provision their reserves
- **Partial protection against longevity risk by introducing an adjustment factor into programmed withdrawal.**
- **Role of the solidarity pillar**
 - Risk buffering effect given by the solidarity complement (reduce the volatility of the pension distribution)
 - Solidarity pillar protects against longevity risk

- MT are jointly established by the Superintendence of Pensions (SP) and the Superintendence of Securities and Insurance (SVS).
- By law, the adequacy of these tables need to be assessed periodically
- **Last updating process: 2014-2016**
 - Data validation & Proposal of new tables
 - Discussion with the market (3 months)
 - Definition of new tables: end of 2015, valid from: July 1st, 2016
- The updating process received the technical assistance of the OECD
- **Key: Mortality tables incorporate future mortality improvements and adopted approach is within the best practices among OECD countries.**

- ✓ **International Best Practices and Guidelines (OECD, IOPS)**
- **Design for the Payout phase**
 - Balance between flexibility and protection (depends on the context of each country)
 - Protection against longevity risk is relevant
 - Default options are recommended.
- **Information and education**
 - Improve the education and financial awareness of individuals.
 - Efforts and responsibility include all: Governments, private sector, investors, members
- **Regulatory parameters**
 - Permanent update of mortality tables
 - Include stochastic projections of future improvements in life expectancy
 - Update them frequently

INTERNANTIONAL EXPERIENCE: PENSION PRODUCTS AND DEFAULT OPTIONS

Jurisdiction	Mandatory product			Possibility to choose between products					
	LS	PW	A	LS	PW	A	Other	Combinations	Default
Armenia (mandatory personal)									
Australia (mandatory, voluntary, occup., personal)									
Bulgaria (mandatory personal universal funds)									
Bulgaria (mandatory professional funds)									
Chile (mandatory personal)									
Dominican Republic (mandatory occupational)									PW
Hungary (mandatory personal)									A
Hong Kong, China (Mandatory Provident Fund)									
Iceland (mandatory occupational)									
Iceland (mandatory personal)									
Israel (mandatory personal)									
Kenya (mandatory occupational)									PW
Korea (mandatory occupational)									
Macedonia (mandatory personal)									PW
Mauritius (mandatory National Savings Fund DC)									
Netherlands (mandatory/voluntary, occupational)									
Nigeria (mandatory occupational)									PW
Panama (mandatory occupational pub. sector)									
Peru (mandatory personal)									
Poland (mandatory personal)									
Tanzania (mandatory)									

- **Pension Freedoms**
 - Regulation went from obligation to buy annuities to a wide range of options, allowing to take part or all as a lump sum.
 - Purpose of the reform was to give people freedom to make their own financial decisions. The role of advisers was reinforced.
 - The results (August 2016): Although RV purchases have decreased, there has not been a massive withdrawal of funds in the form of lump sum.
- **At the same time, UK NEST scheme of voluntary occupational pensions has been very successful**
 - Automatic enrollment has managed to reverse the downward trend in pension savings.
- **Considerations for the analysis**
 - Detrimental for income sufficiency, effect on work incentives, myopic behavior, insufficient financial literacy, consistency of the regulatory framework

- **Currently in the international discussion:** life expectancies vary according to the socio-economic situation of individuals.
- The magnitude of the differences and their evolution have important implications, since the calculations of pensions and non-contributory benefits are based on average life expectancies.
- **Evidence**
 - International evidence seems robust
 - In the literature, significant differences in mortality have been found using 3 types of socio-economic variables: education, income and occupation.
 - The magnitude of the differences according to preliminary evidence for OECD countries indicate that these differences on average (at retirement age) are approximately of 2 to 3 years, with maximum close to 6-7 years.
- Move forward in the analysis of variables other than gender and age seems to be relevant for the assessment of life expectancies

- The pension that a member receives, is the result of the whole set of decisions made during the his/her lifetime, including the choice of pension product
- **In this context, the key elements are:**
 - Promote financial education and awareness
 - Information to facilitate the good decision-making at the right time
 - Coherence between the policies related to the accumulation and the des-accumulation phase.
 - Pension product choice needs to be the one that best represent members preferences
 - Improve the affiliate/pension product match by evaluating and improving the information provided to members (scomp), the competition in the provision of pension products and their design.
 - Regulatory parameters (mortality tables, among others) need to be updated frequently.

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