FINANCIAL SERVICES COMMISSION

"The Occupational Pension Benefits Act - OPBA"

Presented by

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Investment Policy Review for Pension Plans Conference

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Management & Staff of Eckler Ltd; specially invited guests; ladies and gentlemen – Good Morning

The Financial Services Commission (FSC) is always pleased to be part of any event that promotes knowledge transfer in the area of occupational pensions. This pension investment conference, I believe, presents yet another opportunity for appropriately structured discussion on the pension sector, which of course, is dare to all of us.

This morning I would like to focus specifically on the Occupational Pension Benefits Act, now better known as the OPBA. My intention is to present a status update on the ongoing registration of pension plans, the transition from registration to reporting and regulation, and finally the regulatory focus on the statement of investment policies and goals.

OVERVIEW OF THE OPBA (PENSIONS)

As we know, before the enactment of the OPBA, the Inland Revenue Department held full responsibility for the approval of new occupational pension schemes and amendments, by virtue of the Income Tax Act – Cap.73. However, the Income Tax Act in its present form was never intended to monitor the occupational pension sector in the same manner that the OPBA has now set out. Since February 2011, the regulator, pension plan sponsors, stakeholders, and service providers have been coming to terms with the requirements under this new legislation.

The first task was to provide a registration framework to facilitate the submission of applications and registration of occupational pension plans under the new Act. The newness of the registration process meant that all parties had to learn on the job as we progressed. This, of course brought a measure of uncertainty of the process; steep learning curves; a need to create more awareness among plan sponsors and trustees about their responsibilities; very long nights for service providers and regulators alike; a certain level of frustration, and even an amount of hair pulling.

During the process FSC received in excess of 300 applications for registration. In addition, the regulatory ambitions of the OPBA required plan administrators to submit application packages that included highly technical actuarial valuations, certified trust deeds, plan text in compliance with the new Act, and copies of service agreements.

The registration effort is still ongoing; however, the process has progressed significantly thanks principally to the dedication and skill of all stakeholders involved. I take this opportunity to publically thank the plan administrators, plan sponsors and service providers who have supported the enactment and implementation of the OPBA. I also thank the Ministry of Finance and Economic Affairs for its support in the process, particularly when we needed to extend the registration deadline. In addition, very special thanks to my staff at FSC, particularly those in the Pensions Division, who have worked tirelessly through this ongoing process and put up with my neurotic behaviour on reviewing applications.

I am now happy to report that as at today’s date, FSC has fully registered 222 of the 300 applications we have received. We intend to have the remaining plans fully registered during 2016.

STATISTICS & DEFINITIONS

If I may turn specifically to the statistical breakdown of the plans registered, we have seen 138 or 62% being registered as Defined Contribution (DC) plans; 66 or 30% registered as Defined Benefit (DB) plan; and 18 or 8% being a combination of DC and DB structures. The information submitted from the registered plans thus far approximates the number of employee covered at 28,000 with assets under management of approximately BDS$1.4 Billion and all indications are that the final figure will be higher.

I also want to state here that it is evident the pension sector is a material portion of the financial system in Barbados, as the assets under management are approximately 10% of the size of the full system. In addition, pension plans often have demand for long-term and productive assets to support the long-tail position of pension annuities and so a vibrant pension sector also increases the demand for the long-term assets in the country.

Beyond the economic impact of pension plans, we also have to consider the social impact, as a pension plan by definition is a deferred income and these plans will at some point provide financial support for people in retirement, or supplement NIS or other funding sources to provide income for retired individuals in their twilight age. The OPBA, therefore, is a vital piece of legislation as it provides oversight of the administration of these plans.

As we transition our focus from registration to regulations, FSC is utilising a risk based-assessment framework to regulate the occupational pension sector. The risk-based framework allows FSC to evaluate the key inherent risk of each pension plan, rank those risks accordingly, and treat to those plans with the comparatively higher inherent risk, in an order of priority.

In order to effectively do this, FSC requires a consistent flow of statutory returns and the OPBA provides for statutory submissions of annual returns and financial statements by pension plan administrators. Once this data is received in a timely manner we intend to complete our supervision activities in line with the stated regulations.

On the topic of statutory submissions, I turn attention to the **Statement of Investment Policy and Goals**, more familiarly known as the **SIPG**. The OPBA provides for plan administrators to submit this written statement which describes the investment policies and procedures in respect of the plan's portfolio of investments and loans. The SIPG is statutorily required to be submitted to FSC within 60 days of establishment of an occupational pension plan. The rationale behind the use of the SIPG within the context of the OPBA was not to be a rule-based system; but rather, an indicator to allow plan administrators to consider their inherent risk appetites as they relate to the demographics of the pension plan when making investment decisions. This was felt to be a very important decision within the context of pension planning and so the legislation sought, through the use of the SIPG, to ensure that those responsible for the investment decisions of the pension plan gave appropriate thought and evaluation to the investment decisions.

FSC, as the regulator, will review the following, which should be contained in each SIPG:

- ***Type of pension plan, how benefits accrue and are paid*** … the variation in the accrual of liabilities in a DC plan are materially different from those in a DB plan; therefore, it is important to identify the plans.

- ***Restrictions or prohibitions applicable in respect of investments*** … the administrators need to establish the categories of assets in which they are comfortable investing and more importantly, the category of assets in which they do not want to invest, or limits beyond which they do not want to go. This is essentially referred to as the risk-tolerance level of the pension plan administrators. The investment guidelines in the OPBA give maximum limits on certain categories of assets, but this is the top-end guide and plan administrators may choose lower limits if they so wish. However, it is important for plan administrators to utilise this section to establish your risk tolerance.

- ***The cash flow needs of the plan (i.e. when the liabilities must be paid)*** … funds accumulate while people are working and contributing and are paid out when they retire from the pension plan. Therefore, it is important to estimate when workers will retire and create a cash demand on the plan.

- ***Liquidity of investments*** … having established the cash flow timeline, the maturity of the assets and the ability to convert those assets into cash as needed is important so that liquid cash is available to pay the pension of retirees as they come due.

- ***Diversification of the investment portfolio, including aggregate and individual investment limits***

- ***Asset mix and the rate of return expectations*** … these two sections, in collaboration, provide some form of support for the expected returns being utilised. If you expect high returns but your asset mix is low risk and low return you will end up with a mismatch.

These sections, therefore, allow plan administrators to better plan their investment decisions.

- ***The retention or delegation of voting rights acquired through plan investments*** … at times, with investment in shares, also comes voting rights. This section allows the plan administrator to detail how the voting rights will be dealt with because plan members do not own the shares directly so voting representation has to be established and agreed.

- ***The method and basis of valuation of investments that are not regularly traded publicly*** … this is not prescriptive, but it is important as the valuations will impact the statement asset size available to pay pensions. Where we cannot rely on a true market value, the method of calculating values is imperative.

- ***Related party transactions and the criteria to be used to establish whether a transaction is nominal or immaterial to the plan*** … this is a governance issue and whereas not prescriptive, we again would want to see the plan administrators detailing some methodology to appropriately deal with actual or perceived conflict of interest in investment decisions of the plan.

The use of a SIPG offers a number of benefits to pension plans:

1. It is a clear demonstration of fiduciaries' due diligence relating to investment decisions.
2. It is a communication tool for conveying investment goals and priorities which ensures that the investment mentality is transparent to members of pension plans.
3. It strengthens the internal controls of the pension fund as it offers a stated guide for investment decisions.

Plan administrators and trustees must recognise the importance of keeping investment choices consistent with the plan's current and expected future liabilities. This asset-liability management must be central to the SIPG and the plan administrator must ensure that the plan is consistent with the stated risk tolerances.

The SIPG is, however, not set in stone and should not be seen as a static document. In fact, what FSC expects is that the plan administrators will review the plans' demographic changes on a periodic basis, which could be annually or every two years depending on the level of risk. They should then make decisions with respect to maintaining the current investment strategy or amending the strategy in line with changes to the internal and external environment of the pension plan such as plan demographics, investment environment, interest rates, salary changes, and the like.

CONCLUSION

In closing, I want to reinforce is that FSC ideally wants to see pension plan representatives giving serious thought to the investment decision for the fund. There is no magic to a pension fund; it is not a case of making contributions, saying abracadabra, and then poof – there is enough funding available to pay appropriate pensions now and into the future. The SIPG is a document we see established by the OPBA to ensure that appropriate investment decisions are being made and we want to encourage all to pay enough attention to these decisions; not so much to be investment advisors, but more so, to understand the relationships inherent in pension plan investment and payment of funds out of a pension plan, and document same.

Given the theme for this conference, and given your registration, I can tell that I am preaching to the choir in this regard; but FSC is pleased that you have shown such level of interest in this topic and we trust that your interactions during this conference will produce well placed SIPGs in the future and of course, wise investment decisions for your pension plans.

I thank you for your kind attention.