

Investment Regulation

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Old Regulation 28

- Prescriptive set of maxima
- No guidance to boards
- Inappropriate (but compliant) strategies can be adopted
- Widespread exploitation of loopholes

New draft regulation

- Establish investment strategy
- Monitor performance
- Review strategy
- Report compliance
- Individual choice constraints
- Reduced prudential limits

Where are we?

- National Treasury considering draft
- Major study under way with regard to prudential regulation
- Publication may wait for completion

Through a crystal ball, darkly!

Drafting a new Act,
trying to anticipate future needs

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Through a crystal ball, darkly!

- What benefits can a fund provide?
- Who must belong?
- What types of fund should be allowed?
- Major trends giving rise, perhaps, to new “open” funds
- What should the role of the Regulator be?

What benefits can a fund provide? Pension fund organization

means –

(a) any association of persons established with the object of providing annuities or lump sum payments for members or former members of such association upon their reaching retirement dates, or for the dependants of such members or former members upon the death of such members or former members; or

Pension fund organization cont.

- (b) any business carried on under a scheme or arrangement established with the object of providing annuities or lump sum payments for persons who belong or belonged to the class of persons for whose benefit that scheme or arrangement has been established, when they reach their retirement dates or for dependants of such persons upon the death of those persons, and includes any such association or business which in addition to carrying on business in connection with any of the objects specified in paragraph (a) or (b) also carries on business in connection with any of the objects for which a friendly society may be established,

Questions

- An annuity?
- Everything in cash?
- Death of the member v death of other family members?
- Disability, resignation, retrenchment?
- Access during membership?

Are there benefits funds shouldn't provide?

- Pensions from DC funds?
- Benefits that have to be insured for the fund to be financially sound?

Types of fund

“New” DC with individual choice

- Fixed contributions: x% savings / y% expenses
 - Individual investment choice
 - Maybe some flexibility on contribution rate
- Frequently offered through umbrella funds

Look to the future!

The Future

- Package approach to remuneration
- International trend of individual accountability
- Employer contribution vests immediately

The Future

- Retirement Fund Tax Review
 - “One fund” possibility
 - Combined limit on contribution deductibility
- Taylor Commission
 - Compulsion
 - Minimum benefits/contributions
- Choice softens compulsion

A new type of fund

- Member elects participation (No employer / employee relationship required)
- No employer contribution (Full vesting in the employee)

A new type of fund

- Member has choice: investment, contribution, risk levels
BUT
- Choice = complexity of administration
= expensive systems

The Open Fund

The Open Fund

- Member has direct relationship with fund
 - Choice: contribution rate, investment, risk, vendor
 - Communication: administrator - member
 - Transfer: member option
- Employer may facilitate communication but has no other role

The Open Fund

- Governance:
 - Member representation
 - Board monitors communication, record keeping, investment choices, benefit payment
- Member level intermediation
- Substantial size (because of complex administration)

**If there are such “open” funds, is there a need
for umbrella funds with special rules per
employer?**

**Governance and financial management
Governance and financial management rules**

- Board manages a fund
 - Independent
 - Empowered
 - Composition balances stakeholder interests
 - Reports to stakeholders at least once a year
- Audited
- Actuarially valued

BUT!

- Onerous (responsibilities, training, time)
- Member elected trustees “subordinate”
- “Constituency representation”
- No provision for independent board members
- Small stakeholder groups excluded
- Ongoing dispute about payments / expenses

Weaknesses

- No definition in law of fiduciary duties
- Ineffective enforcement:
 - Fund only
- Need ability to punish:
 - Board members, as individuals
 - Consultants / administrators

Reasonably effective in

- single employer relationships
- industry-wide funds with common benefit / contribution structure

Impractical for umbrella funds with special rules per employer

- No member representivity in management

- Not independent of administrator
- Poor financial reporting at participating employer level
- Participating employer makes choices without member representation
- No protection at participating employer level (“sub funds”)

Economies

- Some economies of scale
 - Special rules short / general rules standard
 - No employer level board meetings
- Financial reporting / audit at overall fund level

We must seriously explore umbrella fund definition in a new dispensation

Regulation

A referee not a player!

- Make the rules
 - Fair treatment of consumer
 - Standards for service providers
 - Standards for rules
 - Equity on transfer / surplus apportionment
 - Effective dispute resolution mechanism
 - Financial soundness

A referee not a player cont.!

- Enforce the rules
- Ombud to mediate where there are no rules

Current practice

- Licence administrators
- Approve
 - Rules, amendments, transfers, surplus apportionments, liquidation distribution, variation of investment limits
 - Appointment of valuers, auditors, liquidators

BUT

- Limited powers of intervention, discipline
- Forum shopping for dispute resolution

Is this appropriate?

- FSB:
 - Heavy workload
 - Inexperienced staff
- Industry:
 - Business is run by specialists

BUT many flaws

Proposal (in terms of rules / amendments):

- Regulator delegates approval
 - Licenced specialists
 - “Rules”
- Compliance checked:
 - Compliance Officer at specialist
 - On-site visits
 - Heavy penalties for non-compliance

Retain approval when

- Stakeholders
 - compete
 - unequal access to advice
 - unequal bargaining positions
- Conversions, transfers, surplus apportionment, section 18 schemes

Appropriate relationship between the regulator and ombud

- Separate don't duplicate
- Avoid forum shopping
- Close relationship: ombud to advise on changes to the “rules” resulting from complaint investigation

Much consultation will be needed

How do we do this?

- Break the task up into bite-sized chunks
- Research alternatives
- Establish working groups
- Evaluate the alternative approaches in these groups
- Drafting team coordinates inputs from all the working groups

Thank you