



## 2º SEMINÁRIO INTERNACIONAL DE PREVIDÊNCIA COMPLEMENTAR

O papel da Previdência Complementar em meio  
ao cenário atual de mudanças

# Improving the Pension Payout Phase

## William Price

### 22 November 2019

APOIO:



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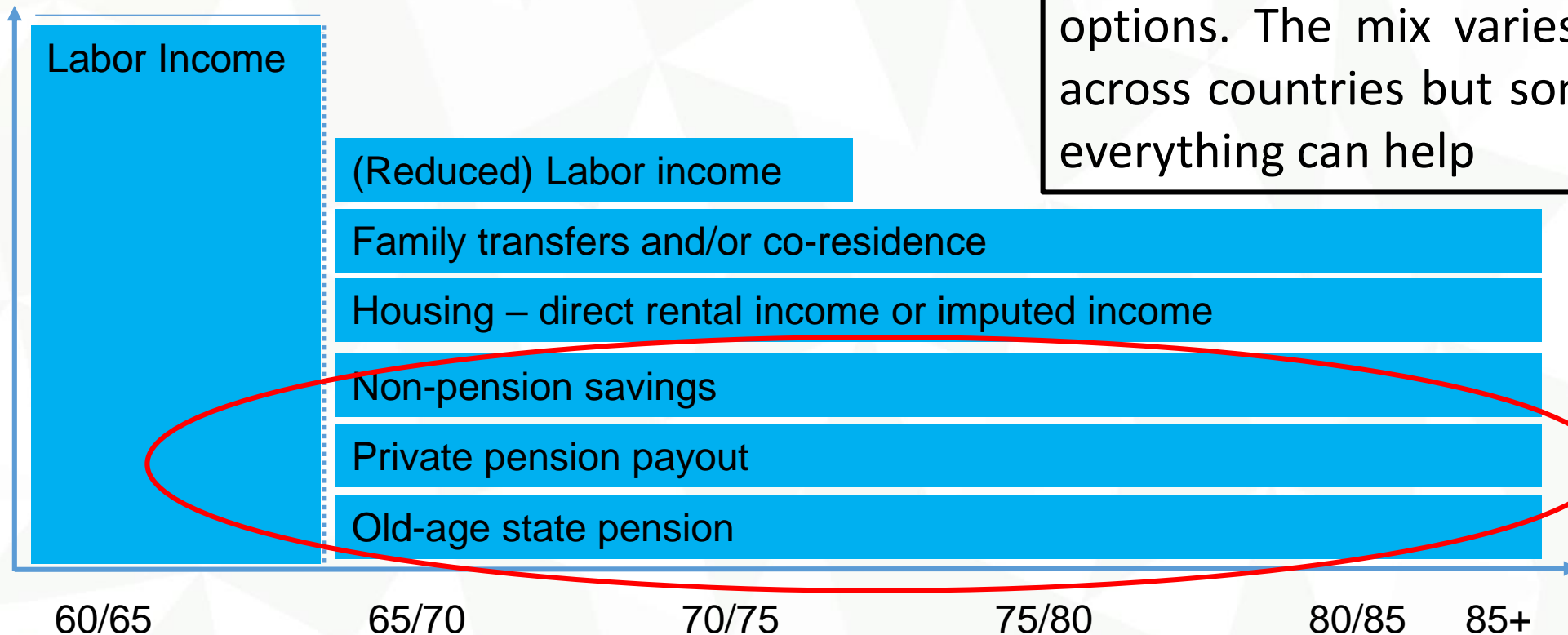
# Overview and summary of key messages

- **Why?** Using five key pension outcomes to guide decisions
- **How?** Creating a simple, low-cost and efficient value chain
- **Who?** Focus on providers with scale, expertise & governance
- **What?** Innovative ways to take account of 3rd and 4th ages
- **When?** Lots of good work and working examples now



# There are many ways in which people can receive income in retirement – pension and insurance products are only one way

Some (richer) people may have a mix of all elements – some may have few options. The mix varies significantly across countries but something from everything can help



# Why have a pension pillar or pension system?

- Ultimately to provide income in old age – and until death
- Other drivers and benefits – but income in old age central
- A pension system cannot be properly assessed without knowing the payout phase
  - **Coverage** – of contributors or recipients of pensions?
  - **Sustainability** – funding levels, size of contributions but also political stability
  - **Adequacy** – assets at 65? Decent replacement rate at 65 – or 75 or 85?
  - **Efficiency** – costs and returns during accumulation – but also during payout?
  - **Security** – is supervision during the accumulation phase integrated into decumulation phase, using the latest data, and supporting FinTech & SupTech?



# Specific and measurable targets exist for each outcome

Outcome	Potential indicators for the Payout Phase
<b>Efficiency</b>	<ul style="list-style-type: none"> <li>• Net of fee returns for phased withdrawals</li> <li>• Costs of pay-out product</li> <li>• Employment rates for older workers</li> </ul>
<b>Coverage</b>	<ul style="list-style-type: none"> <li>• Coverage of people contributing to a pension</li> <li>• Coverage of people receiving a pension (at 65/retirement age and 80)</li> <li>• Gender gap in coverage of pensions</li> <li>• Density of contributions by age and gender</li> </ul>
<b>Adequacy</b>	<ul style="list-style-type: none"> <li>• Initial income at (early) retirement versus income when 80 or 85</li> <li>• Gender differences in income level</li> <li>• Relative income from pensions compared to poverty and average earnings – from private pensions and from all pension sources</li> </ul>
<b>Sustainability</b>	<ul style="list-style-type: none"> <li>• Capital adequacy / solvency of insurance providers</li> <li>• Funding levels for Defined Benefit Pensions</li> <li>• Rate of change of longevity for men and women</li> <li>• Expected years of employment relative to expected retirement years</li> </ul>
<b>Security</b>	<ul style="list-style-type: none"> <li>• Number of international standards fully met</li> <li>• % of Occupational Defined Benefit assets legally separated from employer</li> <li>• % Governing boards meeting good governance requirements</li> </ul>



# **How to deliver payouts: create a simple, low-cost and efficient payout value chain that leverages scale**



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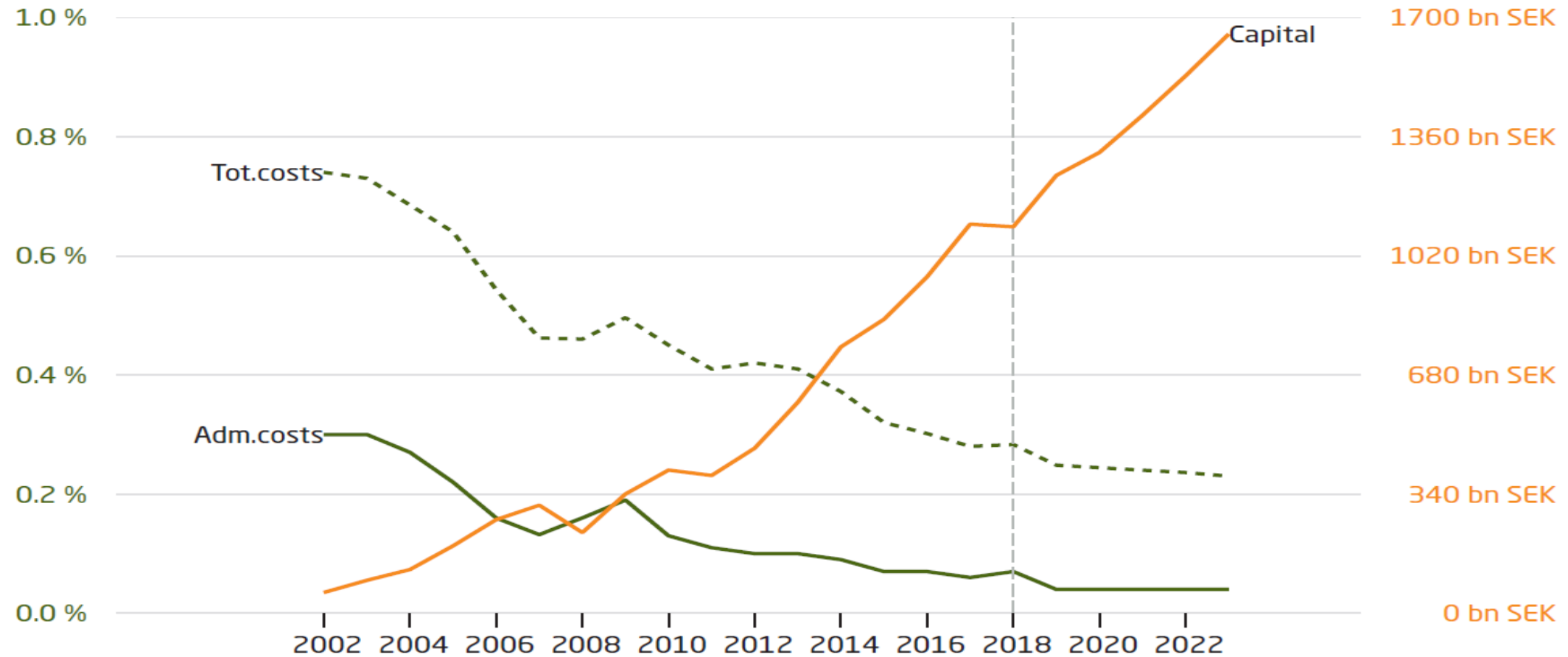
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# Falling unit costs of administration and investment management kick in very early and persist as assets rise

Figure 5.5 Premium pension costs and capital

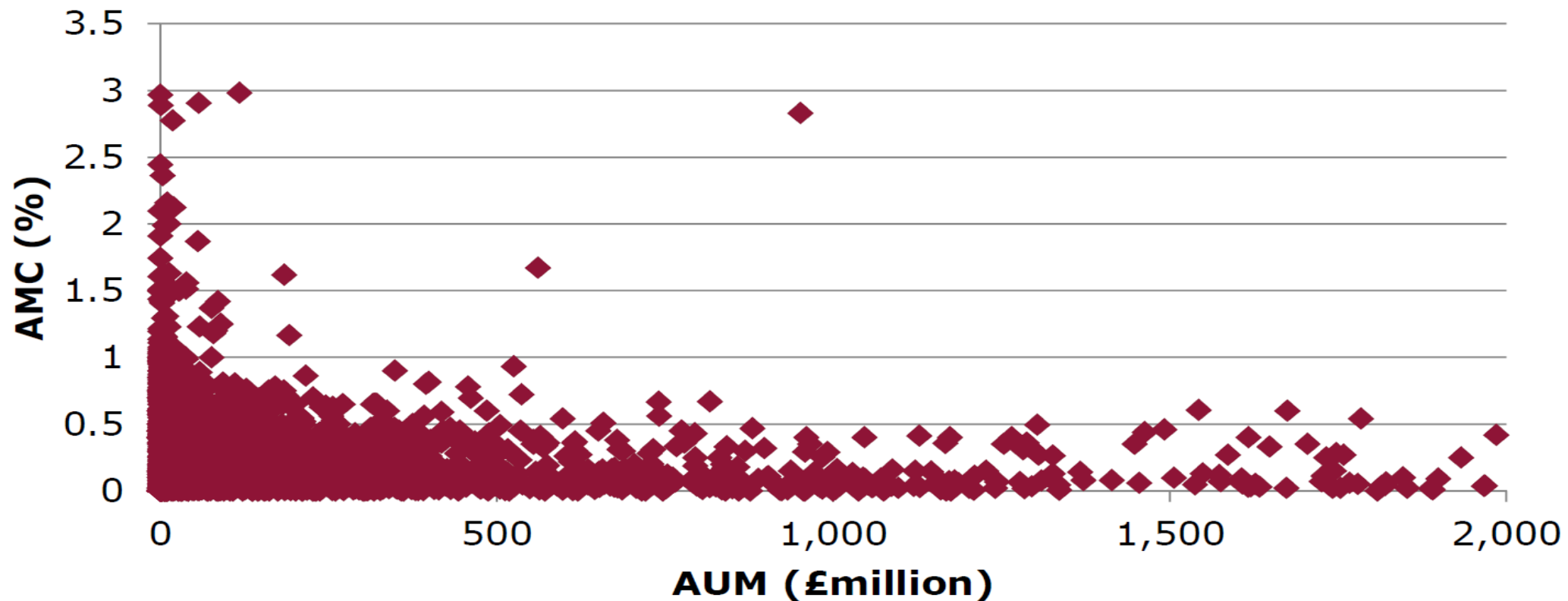


Tot.costs Costs of administration including capital management costs  
 Adm.costs Costs of administration  
 Capital Premium pension capital



# Scale economies exist across different asset owners – but not all get the same value

**Figure 1: The distribution of actual annual average management charge against AUM for mandates (2015)**



Source: Actual management charge and AUM data for segregated mandates, from a sample of asset managers across all asset classes



# The authorities should be seeking improvements at all stages of the value chain – and FinTech can potentially help

- Customer-specific “targeted” marketing
- Robo-advice, AI and chat-bots
- Internet sales and Price Comparison websites
- Social media and SMART phone/device channels for direct distribution

- Automated (including non-human) product service centres using robo-advice, chat-bots and AI
- Big Data enables ability to predict what customers want and need before they ask for it
- Continuous real-time customer communication and U/W

- Platform business models
- 360 degree view of customer for consultants
- Continuous real time data enabling focus on high value customers
- Unstructured data (e.g. voice) analysis and learning

Marketing,  
Sales and  
Distribution

Pricing and  
Underwriting

Product  
Management

Claims  
Handling

Customer  
Interactions

- Telematics – customers and insurers understand risk much better (wearables, IoT, SMART phones, apps)
- Big Data enabling more granular and accurate pricing and faster U/W
- Blockchain technologies to seamlessly manage and instantly verify data sources
- Peer-to-peer insurance models
- Granular, customer-specific product offerings including usual-based insurance

- Fraud detection using Big Data and Blockchain
- Blockchain facilitating trust-worthy and timely claims information
- AI and drones in assessing processes
- Claims cost efficiencies re online/SMART device claims lodgement, AI/automated assessing, optimised payouts, reduced labour costs
- Supply chain management efficiencies, vertically integrated claims processes

# In India the how and the who questions for pension payouts are linked - 5 companies offer up to 4 products via a central quotation portal. The full insurance market has nearly 30 life insurers with dozens of products



Central Recordkeeping Agency

## Annuity Quotes

Are you a:*	<input type="radio"/> Government Sector Subscriber <input checked="" type="radio"/> Private Sector Subscriber
Date of Birth:*	<input type="text" value="01/01/1959"/> (DD/MM/YYYY) Your age: 60 years
Gender:*	<input type="radio"/> Male <input type="radio"/> Female <input type="radio"/> Others
Marital Status:*	<input type="radio"/> Single <input type="radio"/> Married
J & K Resident:*	<input type="radio"/> Yes <input checked="" type="radio"/> No
NPS Corpus to be utilized for purchase of annuity: (in ₹)*	<input type="radio"/> <input type="text" value="0"/>
Annuity-Frequency*	<input type="text" value="Monthly"/>
Enter Captcha	4 9 + 3 = <input type="text"/>

SUBMIT

RESET



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# Chile's SCOMP annuity auction remains a good idea – despite the active debate on improving pensions generally



Entienda los pasos de su  
Proceso de Pensión SCOMP



Entienda su  
Certificado de Ofertas

ETAPA

1

¿QUÉ DEBO HACER PARA PENSIONARME?

ETAPA

2

SOLICITUD DE OFERTA

ETAPA

3

CERTIFICADO DE OFERTAS

ETAPA

4

TOMA DE DECISIÓN

ETAPA

5

OFERTA EXTERNA

ETAPA

6

SOLICITUD DE REMATE

ETAPA

7

ACEPTACIÓN DE LA OFERTA

ETAPA

8

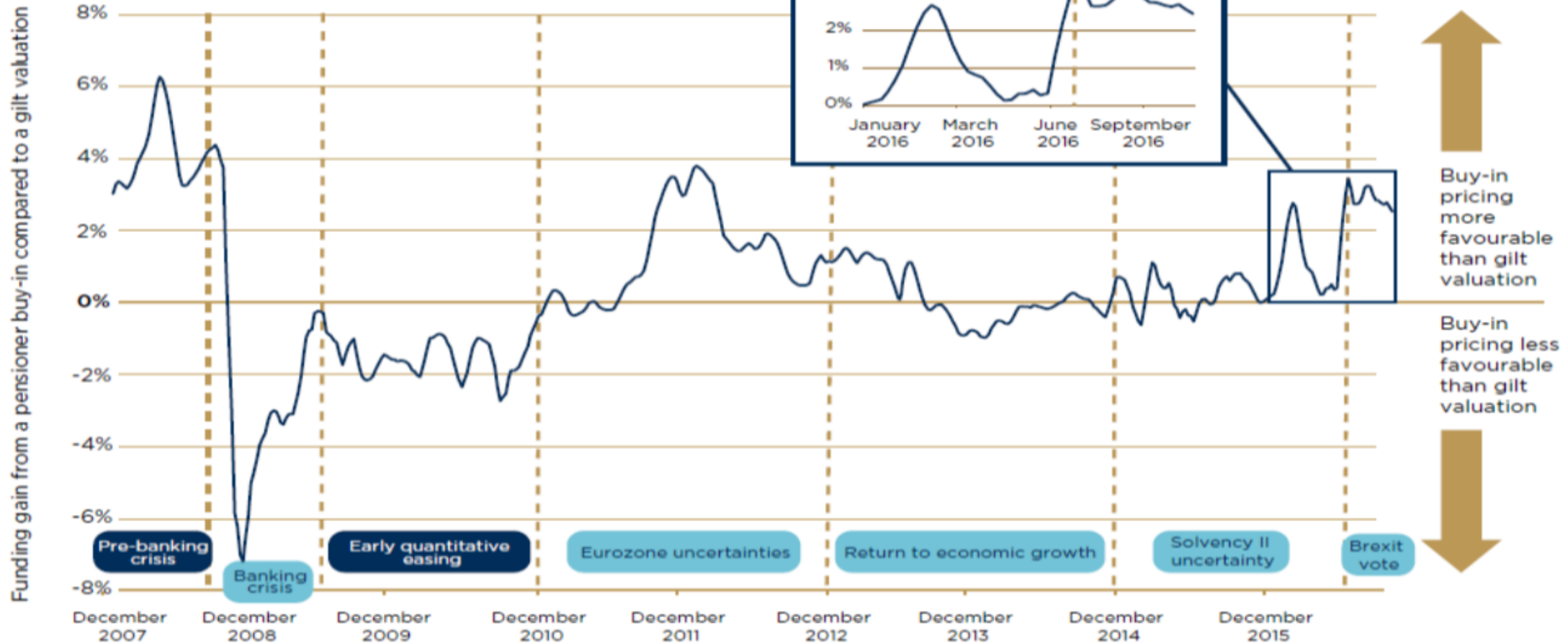
TÉRMINO DEL PROCESO

*“Overall, this paper finds that, after controlling for other regulatory changes and the main determinants of annuity rates, the new quotation system raised annuity payments by 15 percent” (Morales and Larrain, 2017)*



# Making bulk purchases at the best time can significantly increase incomes or reduce costs relative to each worker being a price taker

Interest rate variation in the UK  
2007-2015



Source: LCP analysis



# Who should operate in the payout phase?

- Regulators and supervisors should focus on institutions with scale, expertise and good governance
- Poor governance is at the route of most if not all failures
- Good governance leads to improved returns and better cost control
- All pension funds or insurance providers should have these qualities or the potential to develop them – but governance can be in short supply
- Even in small countries the benefits of (increased) scale is important
- Developing or improving a payout phase can involve building on good governance where it exists to benefit members and/or restrict participation in the payout phase to only the highest quality providers



# Poor Governance can play a big part in pension and insurance failures

Year	Country	Companies	Reasons
1787-1837	USA	26 new life insurers started but few survived	Start up competition
1857	USA	Ohio Life Insurance and Trust Company	Investments/Fraud
1869	UK	Albert Life Assurance Company European Assurance Society	High Expenses/Bonuses
1871-80			Competition
1920-30s			
1930 -1939			
1945-50			
1972			
1990			
1991			
1988-94			
1994			
1992-1994			
1996-99			
1997-2000			
1998-2002			
2000			
2001			
2002			
2003-04			
2007			
2008			
2009			
	USA	Continental Life Insurance Company	
	USA	Golden State Mutual Life Insurance	
2012	Taiwan	Kuo Hua Life	Investments
	USA	InterAmerican Insurance	Fraud/Investments

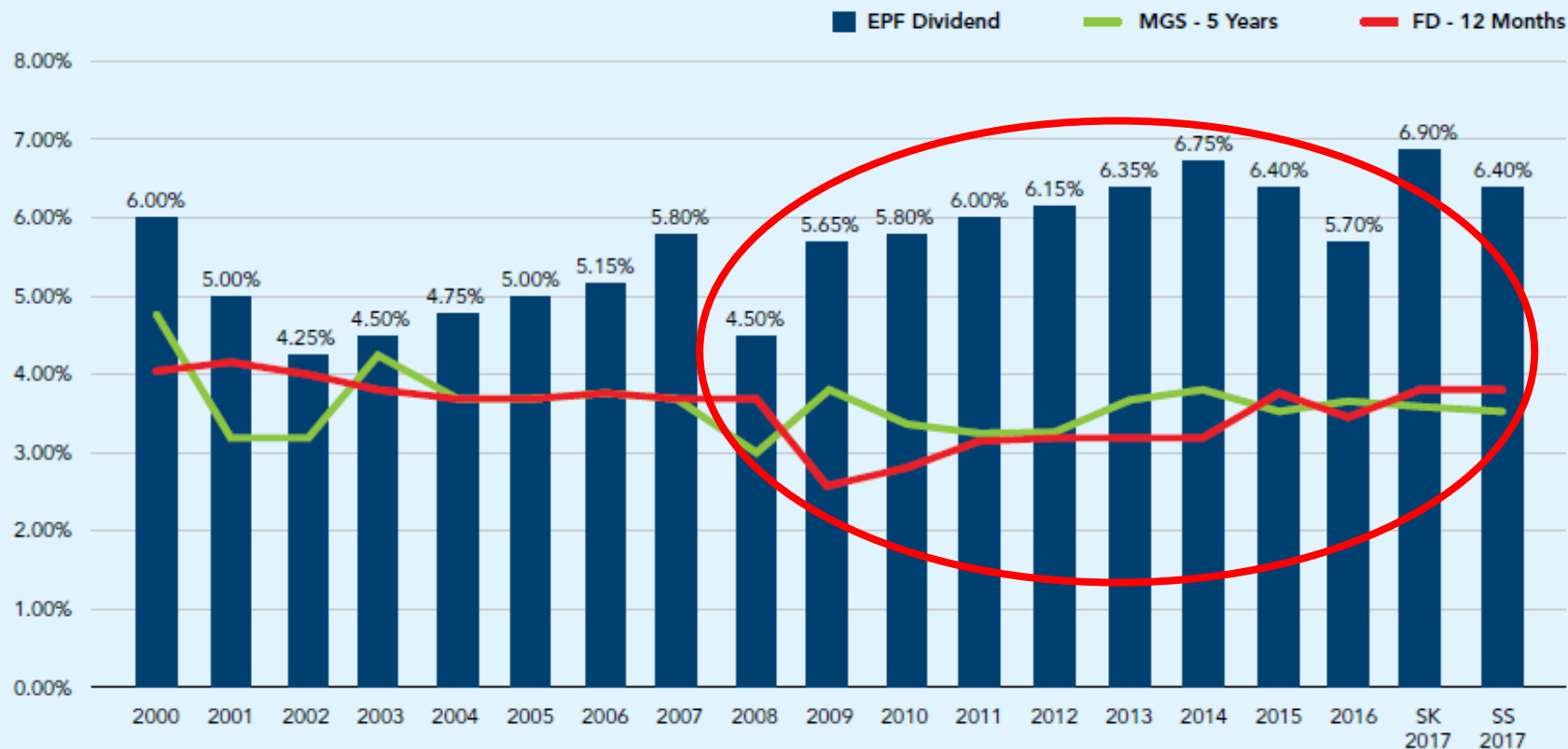
Brown and Balasingham reviewed insurance failures since 1787 to uncover five main features of bad governance

Hubris	Extreme pride or arrogance: desire to be “the best” led to new risk and approaches outside of company expertise, an overestimation of one's own competence or capabilities, especially when the person exhibiting it is in a position of power.
Myopia	No real vision - Drinking the ‘Kool-Aid’: Blindly following market practice; Keeping up with the Joneses: Diverging from strategy so as to have the latest and best.
Abuse of power/ Lack of Courage	Using power and authority for personal interests at the cost of other stakeholders; Extreme pressure often led to poor decision making, and often less ethical practices.
Stuck in the past	Lack of desire to change or accept the need to change despite overwhelming evidence.
Cronyism	Blind trust – people put in senior roles and kept in roles even if wrong fit for the role or situation or their risk appetite was at odds with the organisation; no accountability.



# Good governance on the other hand can have major benefits

**FIGURE 1: EPF returns relative to Malaysian Government Bonds and 1-year fixed deposits**



## Clark and Urwin 2007

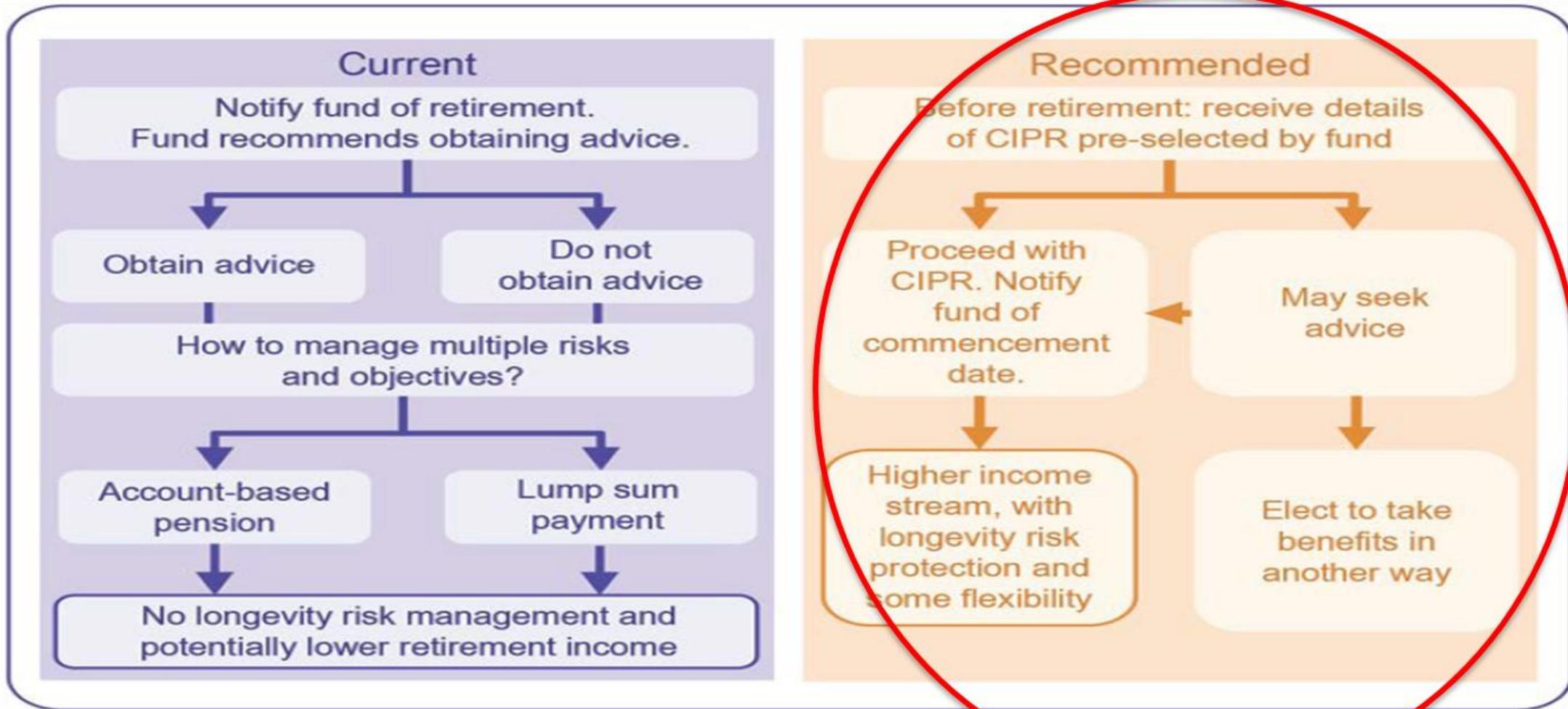
*“almost all of our best-practice funds had a performance margin 2% per annum or more over their benchmarks”*

## CEM Benchmarking and Ambachtsheer

*The benefits of the ‘Canadian Model’ of large, well-governed pension funds with expert investment and operations have added value equal to \$4.2 billion annually over the past 10 years relative to a comparable sample of 132 global funds.*



# Proposals in Australia aimed to use good governance from the accumulation phase to help members in the payout phase with a simple default alongside choice

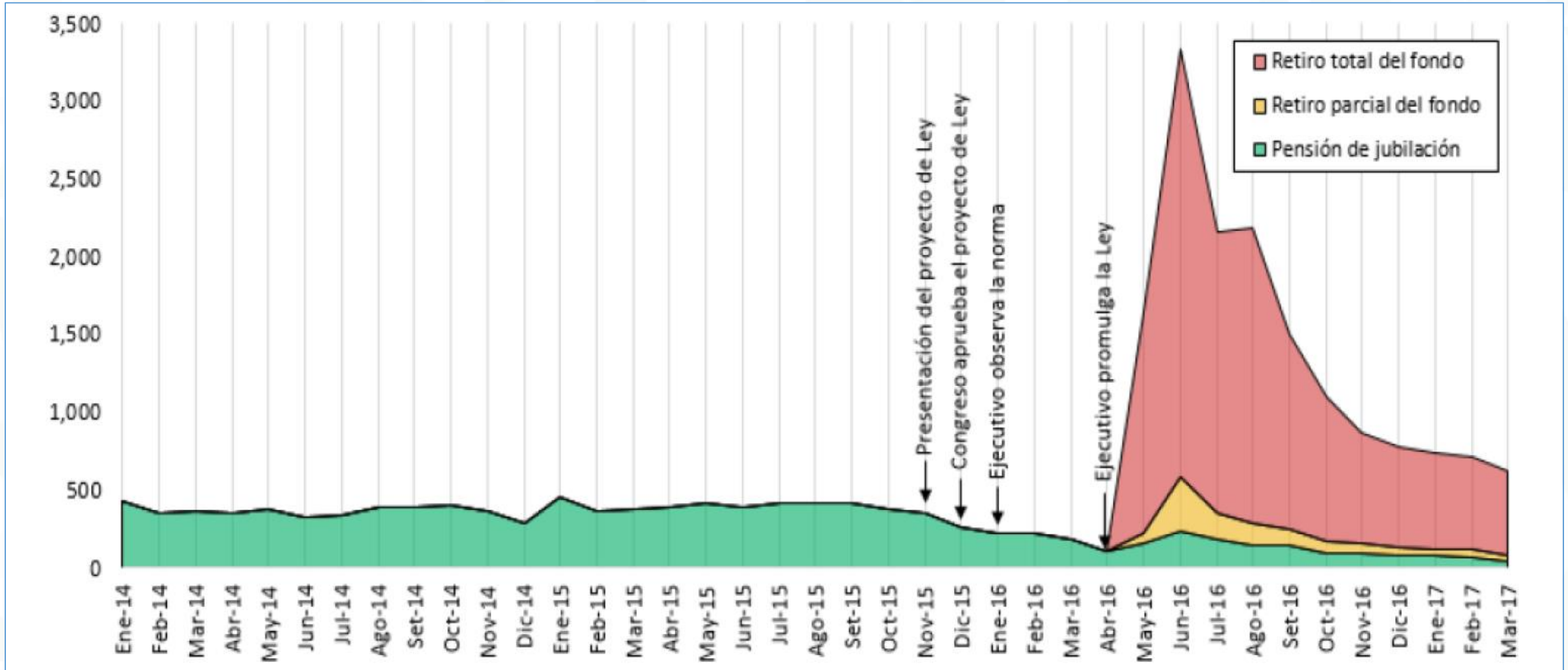


# What should be offered? Compare 5 broad options

- i. Lump-sum payouts
- ii. Integrating phased withdrawals into reformed public pension
- iii. Using a phased withdrawal with deferred annuities
- iv. Annuities
- v. Non-insured variable annuities



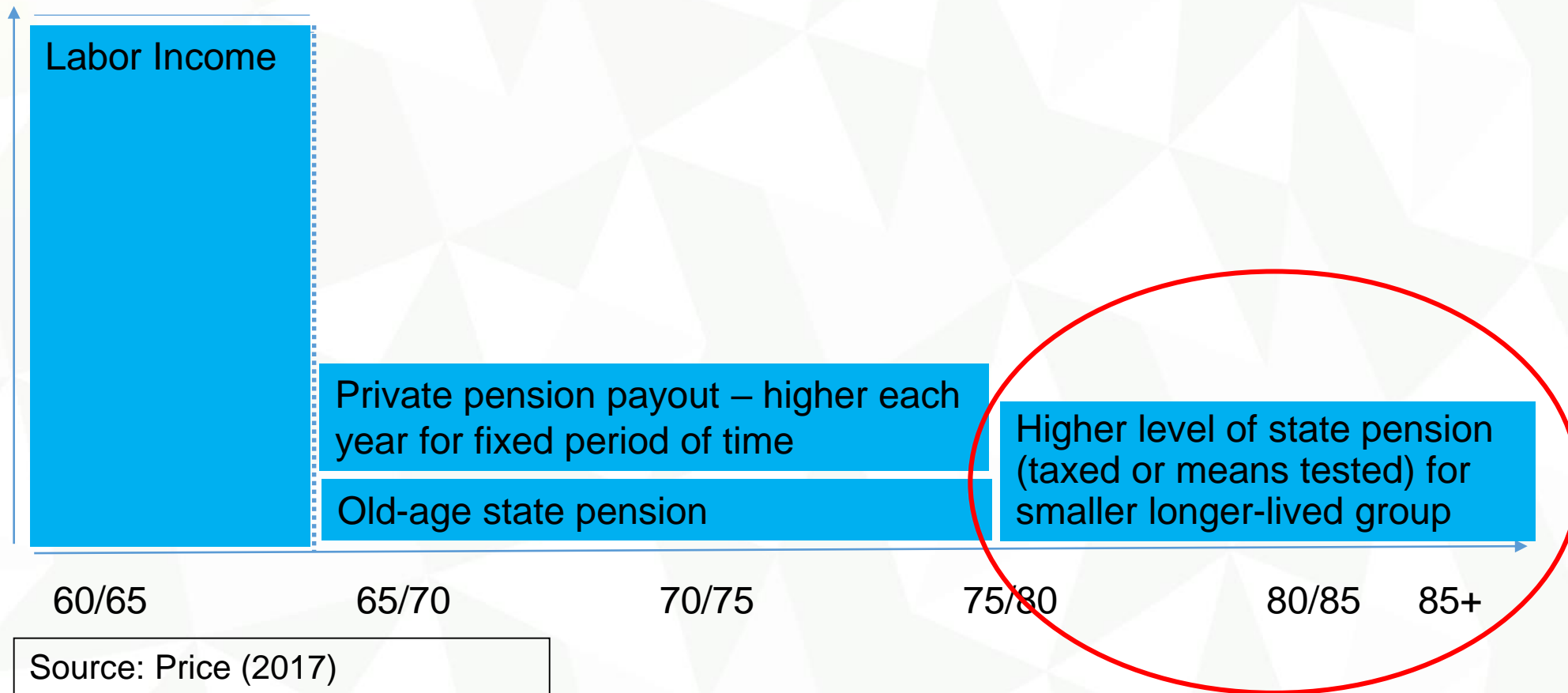
# Recent experience from Peru and the UK shows allowing unrestricted choice will lead to a dramatic shift from income products to lump-sums - increasing old-age poverty and lead to a failure to achieve good outcomes



Source: SBS - number of people Pension Products Chosen by AFP members 2014-2017



# One innovation is to increase state pension payment at very old ages so private savings (and some work income) only need to fill a specific window of time which is simpler to achieve

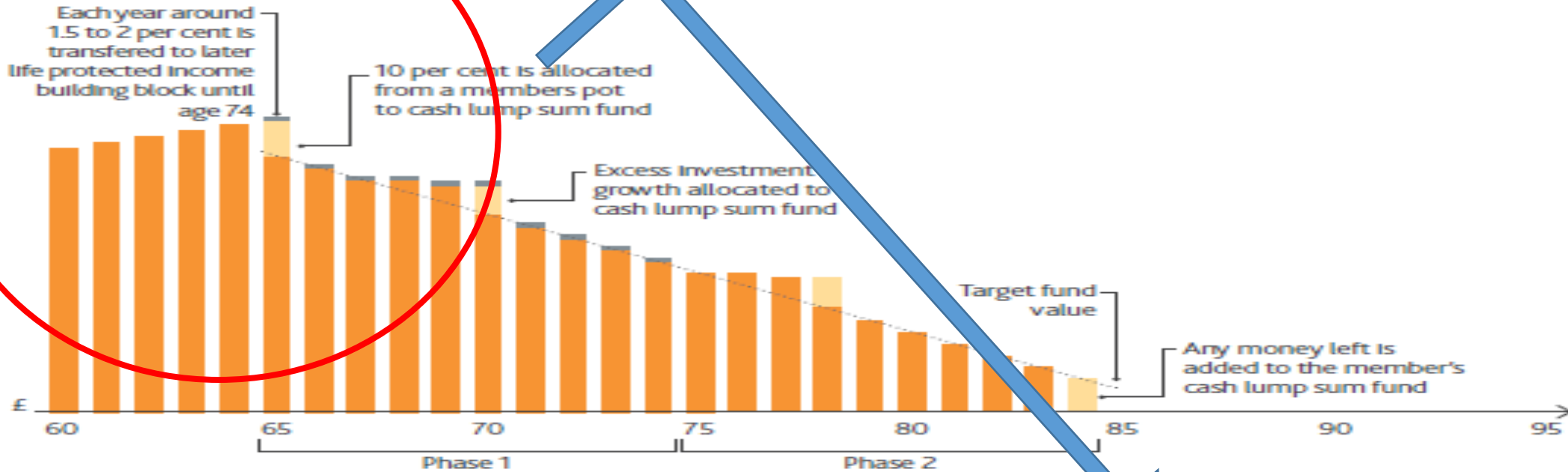




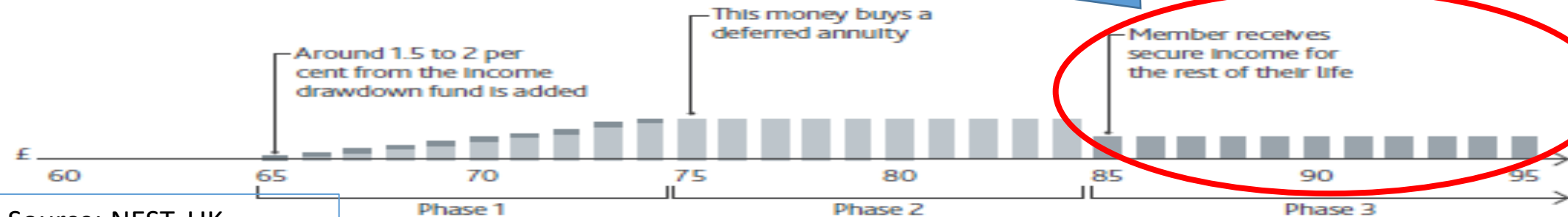
# For many countries a potentially powerful mix of phased withdrawal, some lump sum and a deferred annuity has the potential to provide solutions to the 3<sup>rd</sup> and 4<sup>th</sup> age of retirement

## How their income is generated

### Income drawdown fund



### Later-life protected income fund



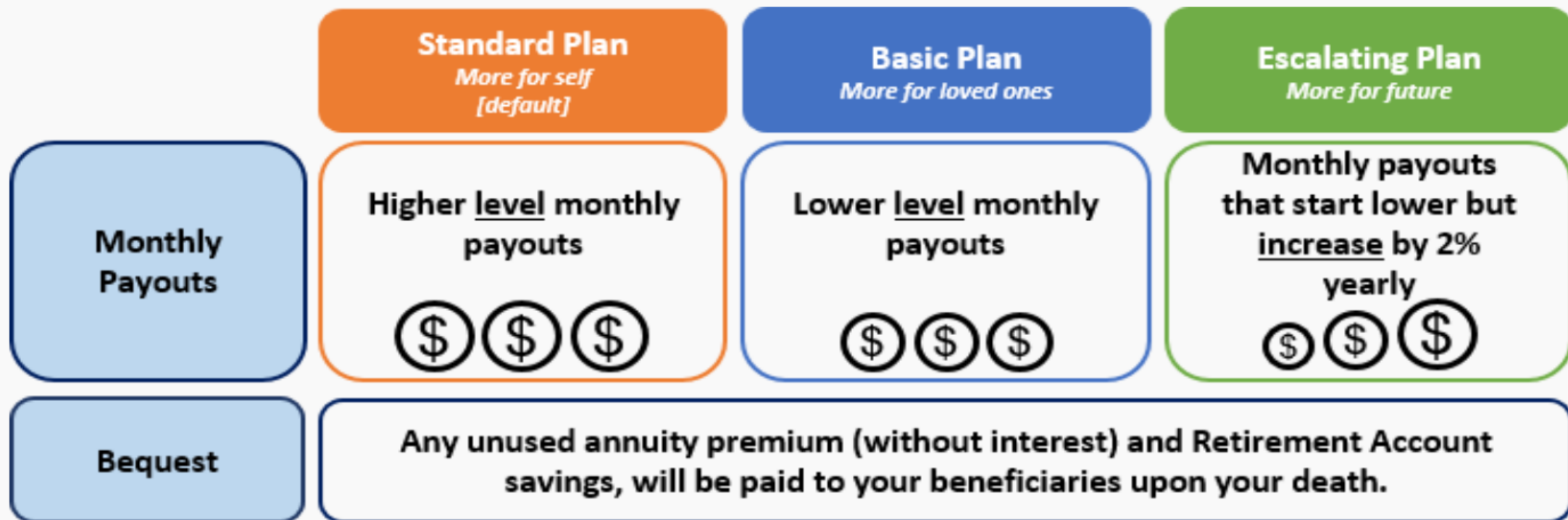
Source: NEST, UK

# The Central Provident Fund in Singapore now provides a form of variable life annuity that is a useful model to explore.

There are three CPF LIFE plans for you to choose from – the LIFE Standard Plan, the LIFE Basic Plan and the LIFE Escalating Plan.

The plans differ in terms of:

- the **monthly payout** <sup>?</sup> you would receive; and
- the amount you would leave (i.e. **bequest** <sup>?</sup>) to your beneficiaries.



Source: CPF, Singapore

# When? Never a better time than now ...

- **Interamerican Development Bank (IDB)** Best Practice Guidelines for the Payout Phase for the IDB Pensions in Latin America and the Caribbean network
- **D3P Society of Actuaries (SOA) Project** – creating the legislative, regulatory and technical models that can help implementation and delivery of new payout phases – moving from academic papers to day-to-day guide
- **NEST UK** Proposal for Phased Withdrawal linked to Deferred Annuity
- **Singapore Central Provident Fund and Sweden Pension Agency** – working examples of non-insured variable life annuities





# When?

## D3P Global Pension Consulting

### Contact Us <sup>+</sup>

D3P Global House  
3 Withdean Court  
Avenue  
Brighton BN1 6YF  
+44(0)20 7097 1773

[william.price@d3pglobal.com](mailto:william.price@d3pglobal.com)  
+44(0)7383 024303

[darren.ryder@d3pglobal.com](mailto:darren.ryder@d3pglobal.com)  
+44(0)7577 087780



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