



# **Joint Colloquium of the IACA, PBSS and IAAHS Sections of the International Actuarial Association**

**Westin Copley Place Hotel, Boston, U.S.A. – 4-7 May 2008**

## **Pension Reform in Jamaica within the context of the Pan Caribbean Region**

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## Layout of session

# **Pension Reform in Jamaica within the Context of the Pan Caribbean Countries**

- Background for reforms
  - Latin America region
  - Caribbean region
  - Case study – Jamaica
  - Implementation
  - Expected Impact v Actual Experience
  - Lessons learnt
- Consulting questions

# The Region



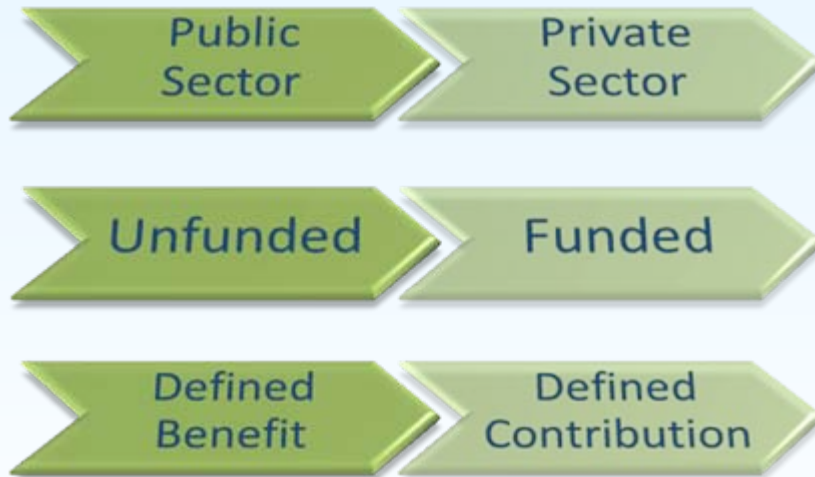
Scale 1:12,500,000  
Lambert Conformal Conic Projection,  
standard parallels 9°N and 17°N  
0 100 200 300 Kilometers  
0 100 200 300 Miles  
Boundary representation is not necessarily authoritative.

# Influences

- **Fiscal Deficits**
- **Financial Sector difficulties (particularly Jamaica)**
- **Social Reform**
- **Reduce Inefficiencies in the Public Sector**
- **Aging Population**
- **Improve Private Sector Participation**
- **Development of Capital Markets**

## Significant Pension Reform in the Region

- Shift responsibility and burden from



- The 1980s “the Lost Decade”
- The 1990s “a Decade of Hope”.

# Overview of Regional Pension Reform

- Legislation preceded reforms by several years in some cases
- Some included Parametric reforms
- Focused on:
  - ✓ Access
  - ✓ Adequacy
  - ✓ Funding

Country	Year	Reform Model
Chile	1981	Structural/Substitutive
Peru	1993	Structural/Parallel
Columbia	1994	Structural/Parallel
Argentina	1994	Structural/Mixed
Uruguay	1996	Structural/Mixed
Bolivia	1997	Structural/Substitutive
Mexico	1997	Structural/Substitutive
El Salvador	1998	Structural/Substitutive
Jamaica	1999	
Costa Rica	2001	Structural/Mixed
Barbados	2003	Parametric
Dominican Republic	2003	Structural/Substitutive
Brazil		Parametric
Guatemala		Parametric
Haiti		Parametric
Panama		Parametric

# Latin American Model

Mandatory Programme: defined contribution/funded

- Limited number of pension fund managers
- Any worker can select any manager
- Free to change manager anytime and move whole account
- Managers hold similar portfolios
  - Chile requires managers to offer portfolios with different proportions of equities
- Government collects and allocates contributions
  - Chile decentralized
- Managers responsible for maintaining account records
- At retirement drawdown facility or annuity purchase

# The Pillars - Chile

- The first pillar
  - a noncontributory public system providing welfare-based pensions
  - a contributory public system providing a State-guaranteed minimum pension (20 years of contributions)
  - public sector contributory systems closed by the new pension reform program;
  - pension systems for the armed forces

# The Pillars - Chile

- The second pillar
  - Obligatory
  - Contributory pension system for all new salaried workers in May 1981. (optional for self-employed workers.)
- The third pillar
  - voluntary,
  - operating on the basis of individually funded accounts.
  - tax benefits for its members.

# The Actuarial Model

- Completed assessments or diagnostics of costs, benefits and results.
- But model had difficulty predicting impact from small changes in costs or benefits
- Argentina and Bolivia introduced many changes to original reform proposed
  - costs skyrocketed, increasing transition costs and the fiscal deficit rather than reducing it.
- Solution: better model with sufficient variables and sound data

<b>Coverage Before and After the Reform (<i>percent of workforce</i>)</b>			
		<b>Coverage as of Dec. 2004</b>	
<b>Country and Year of Reform</b>	<b>Coverage Before Reform</b>	<b>Participants</b>	<b>Contributors</b>
Argentina (1994)	50	58	21
Bolivia (1997)	12	25	11
Chile (1981)	64	111 <sup>a</sup>	56
Colombia (1994)	32	28	11
Costa Rica (2001)	53	72	49
Dominican Republic (2003)	30	32	16
El Salvador (1998)	26	41	17
Mexico (1997)	37	77	30
Peru (1993)	31	29	12
Uruguay (1996)	73	43	22

a. The level of participation in Chile is skewed because it includes inactive members who have dropped out of the labor force.

Source: AIOS (2004); Mesa-Lago (2004).

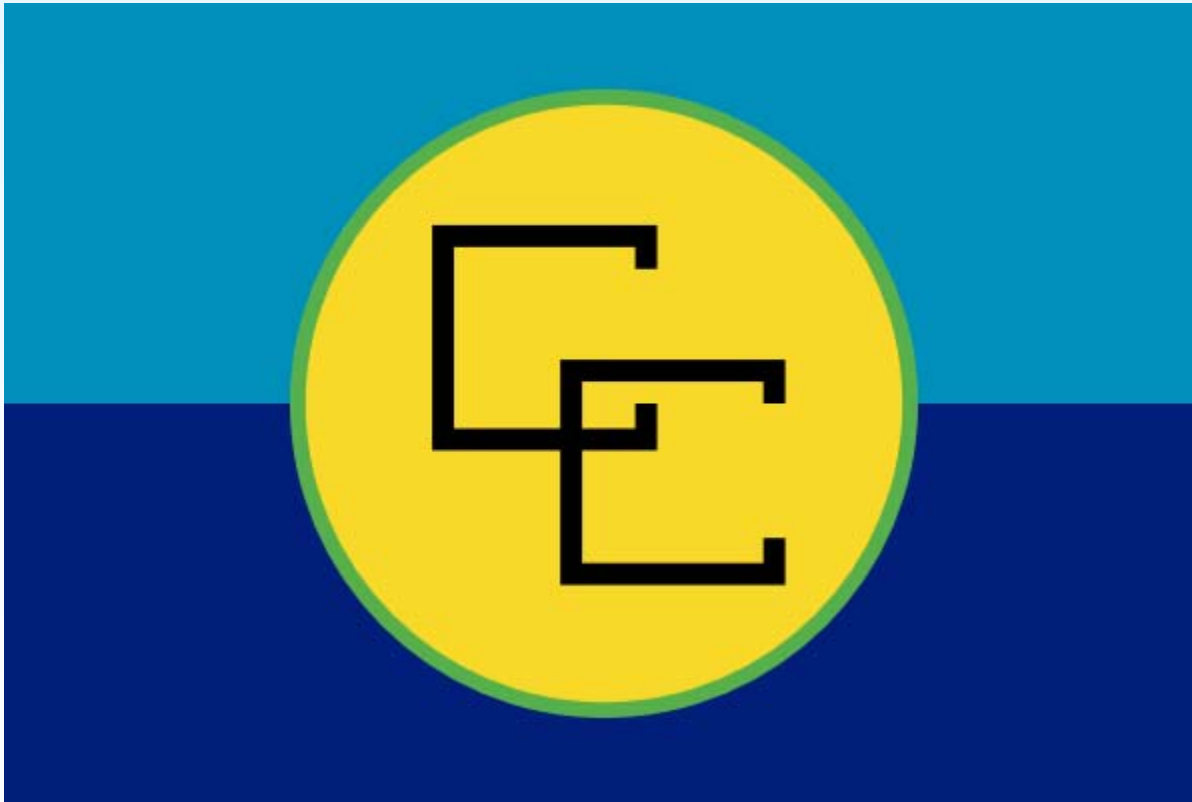
# The Outcomes of Reforms

- Structural reforms permitted the consolidation of disparate systems, making pension portability possible (Bolivia, Chile, Costa Rica, El Salvador, and Peru)
- Chile planned well for the rising costs of the transition
- Bolivia's transition costs caused rapid increase of fiscal deficit
- Growth in capital markets a benefit
- Elimination of the public monopoly and introduction of competition
- Increased efficiency in key areas such as record keeping and maintaining individual accounts

# The Outcomes of Reforms

- Management fees have declined but remain relatively high
- Decreases in operational costs only partially passed through to the consumers
- Limits on transfers (to discourage marketing and sales agents costs)
- Portfolio concentration caused by
  - Adoption of strict quantitative investment regulations
  - Underdeveloped domestic capital markets
  - Volatile macroeconomic environment
  - Lack of experienced fund managers

# CARICOM AND CSME



# CARICOM



**1. Antigua and Barbuda**



**2. The Bahamas – Community only**



**3. Barbados**



**4. Belize**



**5. Dominica**



**6. Grenada**



**7. Guyana**



**8. Haiti**



**9. Jamaica**



**10. Montserrat**



**11. St. Kitts and Nevis**



**12. Saint Lucia**



**13. St. Vincent and the Grenadines**



**14. Suriname**



**15. Trinidad and Tobago**

# CARICOM

- Caribbean Community
  - Established in July 1973
  - Treaty establishing the Caribbean Community and CARICOM Common Market
- 15 Full Member States
  - 14.8 million population
  - Categorized as less developed
- 5 Associate Member States and 7 Observer States
  - participating in areas of functional cooperation
- Primarily English speaking countries – English is the official language of CARICOM Secretariat

# Caribbean Economics

	<b>Population (in 000's)</b>	<b>GDP (Millions of US\$\$s)</b>	<b>Total Cont. Rate</b>	<b>Benefits as % of GDP</b>	<b>Reserves as % of GDP</b>
Anguilla	12	92	10.0%	1.7%	45.0%
Antigua-Barbuda	70	744	8.0%	1.7%	26.4%
Bahamas	320	5,257	8.8%	2.0%	23.3%
Barbados	270	2,702	17.3%	5.0%	30.7%
Belize	275	963	8.0%	1.7%	14.7%
British Virgin Is.	24	848	8.5%	0.5%	23.6%
Dominica	71	214	9.8%	4.3%	44.3%
Grenada	104	414	9.0%	1.6%	34.6%
Guyana	740	731	13.0%	3.3%	15.4%
Jamaica	2,640	7,353	5.0%	0.4%	5.7%
St. Kitts-Nevis	35	35	9.0%	1.6%	34.3%
St. Lucia	160	693	10.0%	1.5%	39.8%
St. Vincent	110	311	6.1%	1.6%	33.4%
Trinidad & Tobago	1,280	10,831	8.7%	0.6%	14.2%
Turks & Caicos Is.	21	251	8.0%	1.1%	22.05

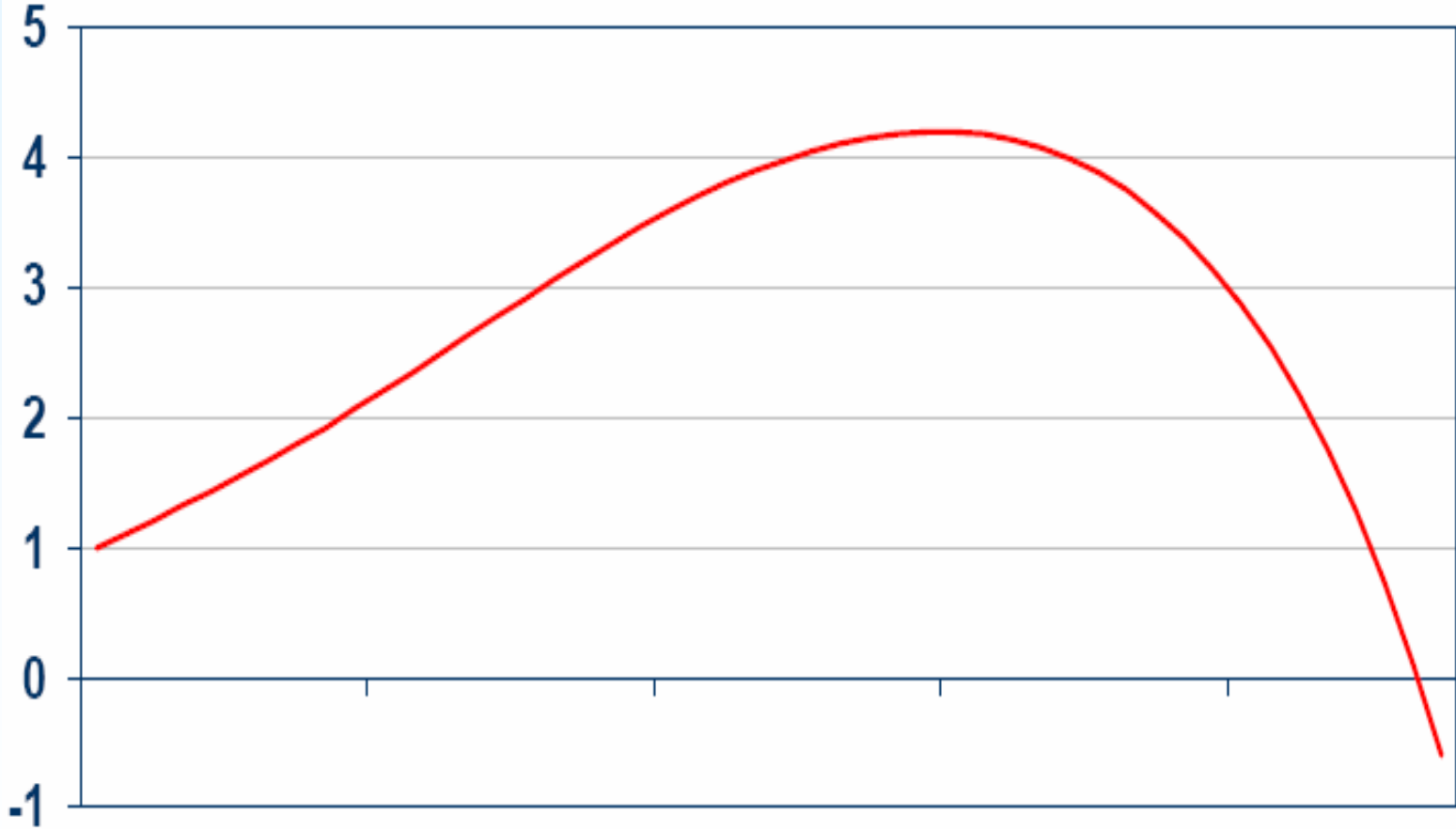
Note: SS Contribution rates – December 2005. All other data relate to 2003.

# Caribbean Demographics

- **Old Age Dependency Ratio increasing steeply**
  - **13 per 100 working population in 2010**
  - **18 per 100 working population by 2025**
  - **an Increase of 38.5%!**
- **Life Expectancy at Birth steadily Climbing**
  - **3.9 years improvement in 20 years**

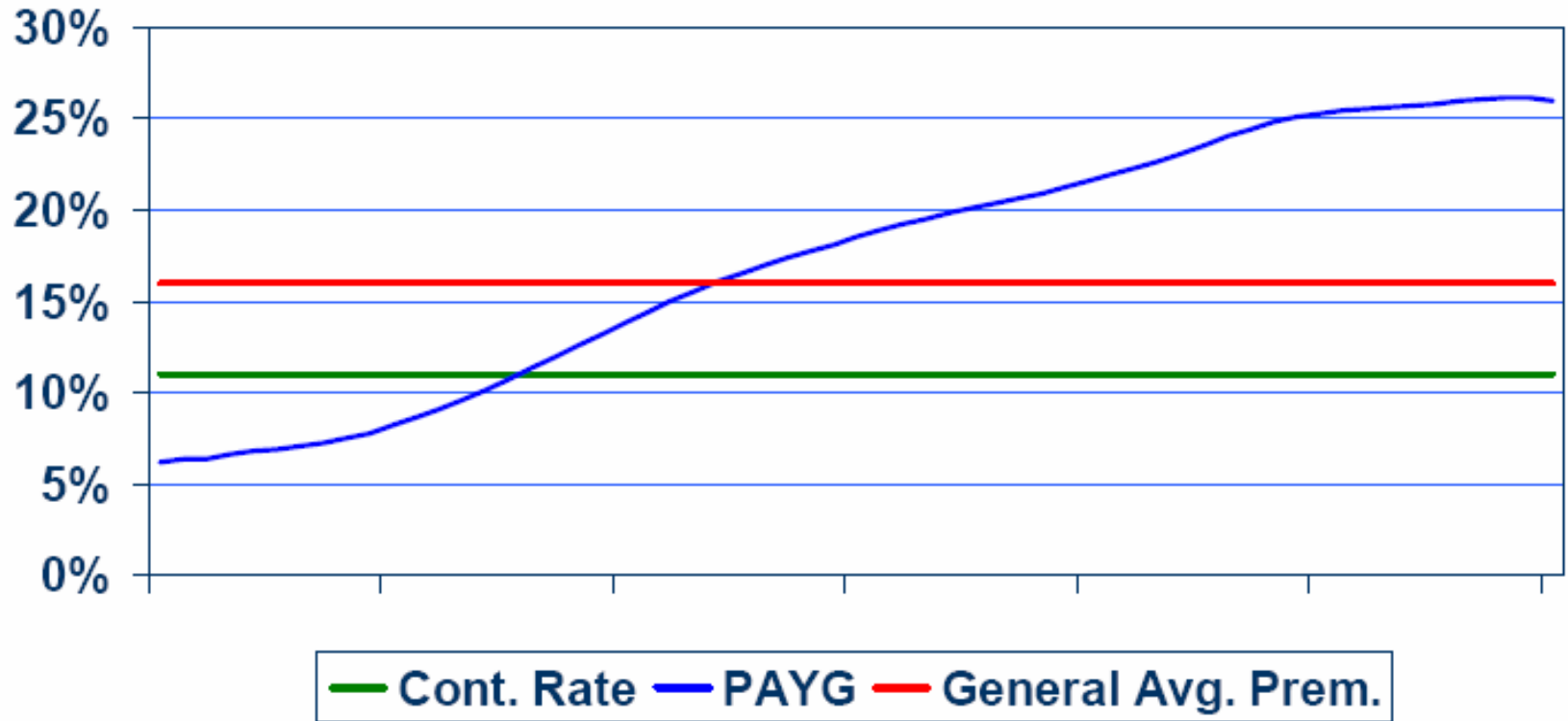
YEARS	LIFE EXPECTANCY (AT BIRTH)
2005 TO 2010	71.2
2010 TO 2015	72.4
2015 TO 2020	73.3
2020 TO 2025	74.1
2025 TO 2030	75.1

# PROJECTED SOCIAL SECURITY RESERVES



Source: CSME SS CAA 2006 – Derek Osborne

# CONTRIBUTION AND COST RATES



Source: CSME SS CAA 2006 – Derek Osborne

# Public Pension Programmes in the Region

## Benefits

### ❑ Short-term

- ❑ Sickness
- ❑ Maternity
- ❑ Funeral

### ❑ Long-term -Pensions

- ❑ Old-age/Retirement
- ❑ Invalidity
- ❑ Survivors

### ❑ Employment injury

- ❑ Injury
- ❑ Medical Care
- ❑ Disablement
- ❑ Death and Funeral.

- Primarily basic programmes
- Limited participation and consequently small portion of population benefits
- Experiencing shift away from extended family support structures to more financial independence of retired persons
- Complicated by more economic pressures so difficult for governments to respond
- PAYG and partial funding
- Reserves projected to decrease

# Private Pension Programmes

- General trend towards establishing private programmes
- Typically based on employment conditions which relies on formal employment
- No coverage of informal sector
- Heavy turnover with refund of own contributions the most favoured benefit
- Movement between countries with limited or no portability
- Limited Regulatory Framework

# Caribbean Single Market & Economy

- The CSM went into effect on January 1, 2006 and has 12 full members
- CSME should be fully operational between 2010 and 2015
- Harmonization of legislation
- Unrestricted movement of labour with intra-regional double taxation agreements
- Free Movement of Capital

# Pension Reform: Case Study of Jamaica



Market vendors – working Jamaicans who may not accumulate enough to provide adequate pensions  
photo BY RAY CHEN

# Jamaican Landscape Pre Reform

- 700 plans covering 80,000 persons
- US\$2 billion in assets
- Employer sponsored
  - Membership is compulsory
  - Employees typically contribute at least 5% of payroll
- Mostly DC, remaining DB's disappearing since introduction of IFRS
- Not reaching maximum replacement targets
  - Limited AVC uptake
- Poor Employer infrastructure and governance generally as understanding of pension in Jamaica is limited

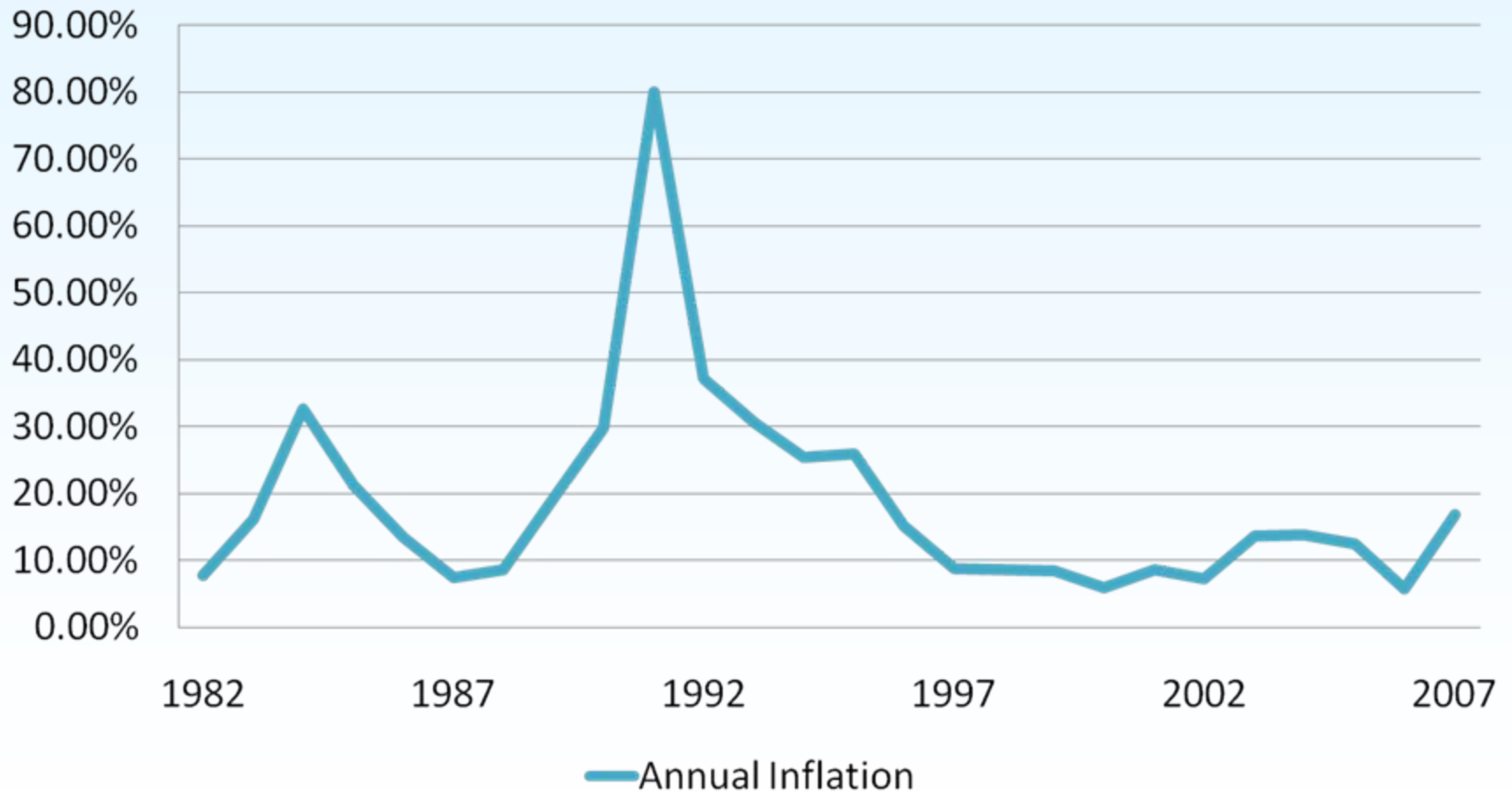
# Access

- Limited
- Only through employer sponsored arrangements
- Institutionally sponsored arrangements limited
- Coverage of private sector is about 10%
- Barriers
  - No critical mass (less than 30 employees)
  - Self-employed or on contract
  - Distrust of the arrangement (not perceived as value)
  - Part of the informal economy
  - Lack of financial education / awareness

# Jamaica - Adequacy

- Minimum wage is about US\$2,700 p.a.
- Large proportion of pensions below minimum wage
  - Inadequate accumulations due to frequent job changes or lack of means
  - Inflation (particularly bad for pre 93 retirees)
  - Weak savings practices
- Weak or no social safety net (Max payment US\$125 monthly)
- Extended family unit becoming less common

# Inflation Rates in Jamaica



# Jamaica - Objectives

- Adequacy and coverage
- Financial Independence for Retired Persons
- Social Awareness
- Access to all
- Effective Governance
- Minimum Benefit Standards
- Transparency
- Shifting from Pay-as-you-go to Fully funded for Public Sector Workers
- Improve contribution rates and benefits of NIS
- Widen coverage of NIS

# **Jamaica - The Pillars**

- 1. National Insurance Scheme**
  - Employed and self employed individuals
  - Limited medical and ancillary benefits
- 2. Public Service pensions**
- 3. Occupational Pension Funds (private groups)**
- 4. Approved Retirement Schemes (individuals)**

**Pillars 1 partially funded**

**Pillar 2 to move from PAYG to partial funding**

**Pillars 3 and 4 are funded**

**2005 reform affected Pillars 3 and 4**

# Process

- Formulate strategy
- Consultation
- Education
- Response
- Implementation

# Strategy/Consultation

- Established Regulators
  - Primarily from Canada
- Actuary to the Minister of Finance
  - Part of a team of three local actuaries who established the guiding framework for the pension reform
- Unions
  - To ensure “buy in”
- Pension Industry
  - Requests for feedback on draft documents
  - Invitations to discussions with the Regulator

# Established Regulators

## Outcomes of Consultation

- Not familiar with local circumstances/UK style pension trust law
- Not accustomed to scarce resources, scarce expertise and absence of economies of scale
- Resulted in mismatch of technical expertise and compliance requirements

## Commentary

- Focused on building a strong regulatory institution
- No perceived reference to a policy framework
- Co-ordination and co-operation of local expertise was needed
- Value should be in context of cost and resources

# Outcome of Consultation Unions

- Limited pension awareness
- Likely to use process to strengthen negotiating position
- Reluctance to give up cash refunds on exit from plan
- Member approval requirement for amendments provide opportunities for labour disruption or mischief
- “Member trustee” nomination and election process complex but actually reduces control of unions
- Locking-in/preservation of benefits delayed
  - in fact minimum benefit standards excluded because of difficulties in achieving consensus with unions

# **Outcome of Consultation Professionals**

- **The Actuaries**
- **The Attorneys**
- **The Accountants**
- **The Administrators and Investment Managers**
- **The Corporate Trustees**

# **Outcome of Consultation Pension Industry**

- Worked closely with government at the outset
  - Submitted papers
  - Made recommendations
  - Strongly supported reform (mandatory communication to members good)
- Provided strong feedback regarding draft legislation and regulatory approach
  - Initially feedback not effective as apparent rush to pass the Pensions Act
  - Expected registration and reporting costs exorbitant
  - The Senate picked up the problem areas in regulations and did not pass the draft as presented to them
  - Trustees objected to criminal sanctions

# Education

- FSC/Ministry of Finance
  - Seminars
  - Public Forums
  - Media publications
- Pension Industry
  - Employer sensitizations seminars
  - Written communications
  - Occasional employee programmes
- Educational Institutions
  - One institution created a course
  - Targeted at Trustees and Employer Administrators
  - Tax, New Regulations and HR Management

# Education by Regulator

- Viewed public education as a priority
- Focused on introduction to the new legislation targeting
  - Members of the public
  - Trustees and employers
  - Pension Industry players (though less so)
- Raised social awareness of pensions
- Focused on rights of pension plan members so there was low penetration in the understanding of pension provisions at the level of the ordinary man
- Low participation in pension arrangements is a concern

# Education by Pension Industry

- Majority of plans by (number) managed by Life Companies
- Education primarily through seminars
- Targeted primarily at employers who were expected to communicate to employees
- Resources stretched so diverting them for education is challenging

# Implementation



## THE PENSIONS (SUPERANNUATION FUNDS AND RETIREMENT SCHEMES) ACT, 2004

JAMAICA

No. 22-2004

I assent,



*H. J. Baile*  
Governor-General

*9<sup>th</sup> day of November, 2004*

AN ACT to Make provision for the management of superannuation funds and approved retirement schemes and for matters connected therewith and incidental thereto.

[ *The date notified by the Minister*  
*bringing the Act into operation* ]

BE IT ENACTED by The Queen's Most Excellent Majesty, by and with the advice and consent of the Senate and House of Representatives of Jamaica, and by the authority of the same, as follows:—

# Intended Impact of Reform

- Greater coverage
- Reduce public sector cost
- Increased private pension funds would enlarge investment market liquidity
- Could reduce dependency on foreign capital
- Create broader demand for equities and debt instruments, especially bonds
- Stimulate savings and investment (as per Chile).

# Pension Reform Implementation - Jamaica

- **1<sup>st</sup> ...surprise**
- Effective date of the Pensions Act backdated to 1 March 2005
- Regulations only released ONE year later
- Registration and Licensing requirements reduced but still onerous
- Registration a strain on resources
  - Trustees
  - Administrators and Investment Managers
  - Responsible Officers
  - Plans
- Just over two years later only 4 Plans approved

# Make transition Easier

- Devise a simple process how the two regulators will operate
- Use strengths of existing system
- Give TAAD more resources
- Allow FSC access to TAAD files
- Grandfather all TAAD approved funds and get on with business

# Expected Impact vs Actual Experience



# **Intended Impact of Reform on Private Pension Plans**

- **Registration of Plans, Trustees, Administrators, Investment Managers would provide official players in the market**
- **Collection of statistics**
- **Improve governance of plans**
- **Increases availability of pension provision to the working population**
- **Improve adequacy of pensions**

# Initial Expenses

	<b>Expected (US)</b>	<b>Experience ( US Estimated)</b>
Transition Activities	140,000	560,000
Trustee Expenses	140,000	700,000
Regulators Application Fees	90,000	90,000
Small Plan Wind Up Fees	420,000	1,680,000
Reporting Technology	50,000	50,000
Legal Fees	210,000	3,000,000
Employer Expenses	420,000	1,400,000
<b>Total Initial Cost</b>	<b>1,470,000</b>	<b>7,480,000</b>

# Ongoing Expenses

- True cost still to be determined
- Insurance Expenses are the only likely area of over estimation
- Could be an about turn:
  - ✓Results of implementation are hard to avoid
  - ✓Regulator does not have full jurisdiction due to approach taken

	Expected (US)
Regulators Fees	2,000,000
Administrator Expenses	550,000
Fund Manager Expenses	1,000,000
Legal Expenses	500,000
Actuarial Expenses	570,000
Accounting Expenses	1,400,000
Insurance Expenses	4,200,000
Total Initial Cost	10,620,000

# The Market after reform

- Plans suffered exorbitant registration costs
- Rationalization of plans – companies reduce number of plans in operation
- Discontinuance of plans
  - About 25% plans in existence
  - Winding up of weak plans
  - Winding up of small plans

# Actual Impact of Reform

- Costs to operate plans much higher at the expense of members' benefits.
- More emphasis on lawsuits and penalties for non-compliance rather than improving staff service skills and systems
- Reduced market is not large enough for all the players offering services to pension funds
- So far, not good verdict

# Lessons Learnt



## **Lessons Learnt - Jamaica**

- Failure to adequately assess and strengthen the capabilities of existing institutions to administer the reform
- In general did well in creating new institutions to regulate and supervise the new pension system.
- Licensing of Administrators and Investment Managers relies on competition to force minimum standards

## **Lessons Learnt - Jamaica**

- More thought needed for transition
- Role of the two regulators not clear
- More thought needed for simple effective implementation
- Registration will take years
  - More beneficial to have concentrated on individual arrangements and include self employed persons
- Fees charged to unregistered plans and plans that will never be registered
- Clear and comprehensive policy statement needed
- Better understanding of British style trust based pensions

# **Issues to Address**

## **Labour and Economic Issues**

- **Movement of labour**
- **Create agreements for pensions between countries**
- **More Multinationals operating in more than one territory in the region**
- **More DC Plans**
- **Control inflation to justify saving for retirement**
- **More developed capital markets needed**
  - **Access to overseas investments**

# **Issues to Address**

## **Funding and Access**

- Low income groups and women not covered
- Possibility for declining contributions
- Impact of administrative costs and commissions
- Critical analysis of the effect of pension reforms on the region's capital markets
- Need to liberalize investment options and exchange controls
- Work toward building confidence in the system.

# In the Future

- Caribbean will emerge into a single domestic space with complete freedom of movement within the region
- Single currency and regional stock exchange
- A Caribbean Court of Justice as the last court of appeal (away from the UK privy council)
- Harmonized legislation
- A Caribbean Monetary Authority accountable to a council of Ministers of Finance
- Challenges with countries having specific fiscal or political issues will eventually be overcome

# Impact on Pension Programmes (In a perfect world)

- Employees have comfort that pension accrual continuous when relocating
  - Cable and Wireless, Digicel, ADM
- An improvement of portability of pensions
- Economies of scale for regional employers
  - Less disruption due to migration within the region
  - One plan per regional company
- Reduction in complexity due to differences in legislation in each country
- Less risk associated with multiple currency
- Downside - at least 15 years away but urgent for pensions to be addressed today

# Expertise Useful to Government

- Know local conditions
- Refrain from adopting models wholesale from another country
- Listen to the local practitioners
- Identify the problem areas
- Develop home grown solutions
- Require adequate training
- Lawyers familiar with British style trust law

# Financial security in retirement?

- Restore confidence and trust?
- Widespread mistrust of governments in general
- Lack of confidence in financial institutions
- Skepticism about contributing to individual accounts
- Large Informal employment situation affects the coverage rates

# Discussion





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# **Discussion**

# References

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