

# Supervision of Public Pension Funds

## The Case of Costa Rica

Edgar A. Robles – Cordero, Ph.D.  
Intendent of Pensions

# Outline

- Overview: National Pension System
- Basic Statistics
- Supervision and Regulation
  - Legal Framework
    - The Superintendence of Pensions
    - Laws
- Operational Framework
  - Supervision model based on risk

# The Pension System in Costa Rica

Several regimens with its peculiarities

- Three types:
  - Defined contribution (New Law)
  - Defined benefit (Basic System)
  - Pay as you go financed by Government Budget

# Contribution for the Pension System

Percentage contribution from wages:

Institution	Employer	Worker	Government	Total
1st Pillar: CSSI	4.75%	2.50%	0.25%	<b>7.5%</b>
2nd Pillar: Private	1.75%	2.50%	---	<b>4.25%</b>
3rd Pillar:	---	Voluntary	---	---
4th Pillar			Full	

# Pension System ...

## Costa Rican Basic Pension System Basic Statistics December 2002

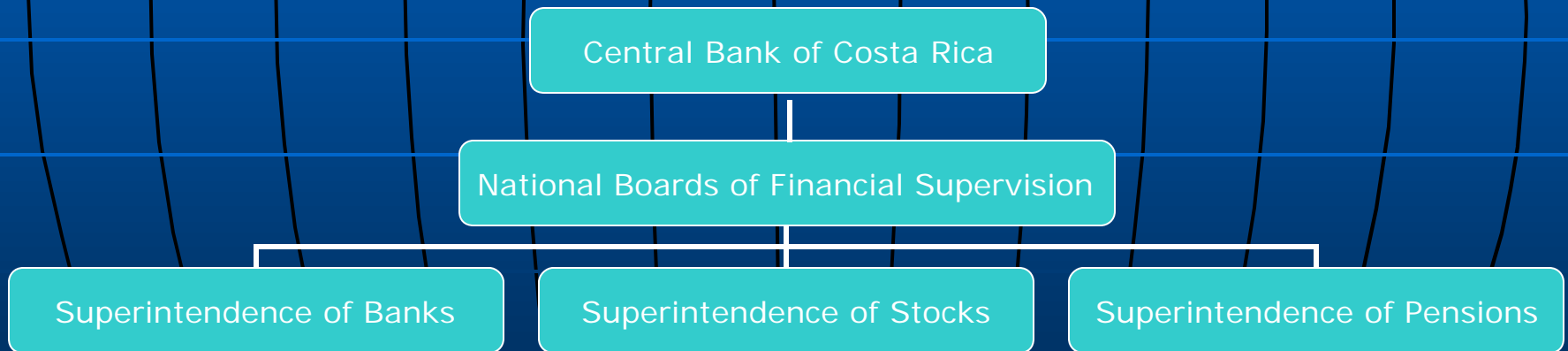
	Number of Contributors	% of Work Force	Number of Pensions	Fund's size Millions of US \$	% GDP
<b>BASIC SYSTEM: Defined benefit</b>				<b>1.492</b>	<b>6,6%</b>
<b>Basic Regimen</b>	<b>966.151</b>	<b>57,0%</b>	<b>209.594</b>	<b>1.487</b>	<b>6,6%</b>
CSSI	928.937	54,8%	207.667	1.307	5,8%
Teachers	37.214	2,2%	1.927	180	0,8%
<b>Complimentary Regimes</b>	<b>70.977</b>	<b>4,2%</b>	<b>7.787</b>	<b>5</b>	<b>0,0%</b>
<b>PRIVATE SYSTEM: Defined contribution</b>			<b>0</b>	<b>879</b>	<b>3,9%</b>
Voluntary Regime	225.400	13,3%	0	641	2,8%
Compulsory Regime	1.266.866	74,7%	0	238	1,1%
	Number of Contributors	% of Work Force	Number of Pensions	Annual Expense Millions of US \$	% GDP
<b>PAY AS YOU GO: Public Budget</b>	<b>16.964</b>	<b>1,0%</b>	<b>45.135</b>	<b>398</b>	<b>1,8%</b>



# Supervision and Regulation

# Superintendence of Pensions

Supervises and regulates. Defines benefit plans.



# Public Pension System

- Basic Regime:
  - Costa Rican Social Security Institution
- Substitutive Regimens:
  - Professors and teachers
  - Judicial Employees
- Public Servants
- Pay as you Go.

# General Risks of Public Systems

## Vices from the past

- Political Risk
- Poor financial performance.
- Fraud
  - No affiliation
  - Under declaration
  - Inadequate use of benefits

# General Measures to Improve performance and sustainability

- Supervision of Administrative performance
- Existence of Regulatory Bodies
- Supervision of Investments
- Monitor actuarial equilibrium
- Accountability Schemes

# Superintendence of Pensions

- Law: Regulator and Supervisor of all Pension Regimes, except CSSI (only Supervision)
- Produces all guidelines and rules governing the function of the pension system

# Concerning Public Regimes

- Watch for actuarial equilibrium.
- Supervises the investments, emits policies for composition and valuation of the portfolio.
- Proves the correct and timely imputation of contributions in the account of workers.
- Defines information requirements (contents, form and periodicity)

# Concerning Public Regimes

- Watch for the correct and timely concession of benefits.
- Resolves denounces by workers.
- Informs annually about financial situation of each regime
- Supervises the qualification system for inability.

# In the case of the Pay as you Go System

- Checks the legality and opportunity of resolutions
- Checks modifications and revaluations of pensions.

# In every case

- The Superintendence can qualify the financial irregularity of a fund based on:
  - Risk degree of fund's assets.
  - Liquidity risk degree.
  - Risk of interest rate movements
  - Exchange rate risk

# Supervision Model

Supervision based on risks

# Supervision based on Risk

## Four Critical Areas

- Minimum Standards of Administration.
- Evaluation of the Controlling Bodies.
- Performance of Operational Risk.
- Sustainability: Financial and actuarial Situation.

Objective: The supervisor will have a photograph of the administrator and how he manages the risk, so it is possible to do informed inspections with impact of the regime.

# Minimum Standards of Administration

- Structure of administrative costs.
- Ability to set rules:
  - Elaboration, approval and actualization of sets of rules.
  - Existence of basic rules for the administration of deposits and benefits of the funds.
  - Existence of limits to the ability to set rules.
- Accounting records standards.
- Informatics' systems and safety of data bases.

# Evaluation of Controlling Bodies and Performance of Operational Risk

- Sufficiency of internal control.
- Periodicity of external control.
- Independence of these bodies.
- Measures of operational risk.

# Sustainability of the system (Financial and actuarial)

## ■ Investment performance

- Minimum standards for the management of investments.
- Explicit investment limits.
- Custody of stocks.
- Financial risk follow-ups.
- Performance evaluation.

## ■ Actuarial equilibrium

- Frequency of studies
- Follow-up of results.

## ■ Independence and qualifications of actuaries.



# Pay as you Go Regime

- Same model but without financial module.
- Most of the risk comes from fraud and abusive benefits.
- Must project expenses in order to promote potential reforms.
- Need to control moral hazard:
  - Accountability
  - Periodical information:
    - Financial management
    - Mid-term sustainability

# Where do we want to go?

Make no difference between private and public regulation.

- Investment policies: locally and abroad, valuation of assets, investment limits, custody of assets, ...
- Daily supervision of funds and contributions
- State of the art informatics
- Accountability: regular reports of financial performance (at least monthly).



**THANK YOU**