Developments in the Operation and Supervision of the Pension System in Brazil

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Overview

- Brazil did not adopt the typical Latin-American approach to pension reform.
- Model similar to the U.K. And U.S.
- “Cosed system”: occupational pension plans.
- “Open system”: personal pensions and group personal pensions (GPP).

- Closed system: supervision by the Ministry for Social Security and Assistance (SPC).
- Open system: supervision by the Finance Ministry (SUSEP).
- National Monetary Council / Central Bank oversees investment regulations.

The New Legal Framework

- Law nº 109 of 29th May 2001.
- Law nº 108 – Occupational pensions plans sponsored by State owned companies.
- Changes apply almost entirely to the “closed system”.

Regulating the Closed System

- Perceived as a public finance risk.
- The real problem is the governance of State owned companies (SOC).
- Law nº 108 addresses the governance structure of pension funds sponsored by SOCs.
- Focus on evaluating the funding status of befined benefit plans.

- Most of the new legislation still needs further specification.
- First issue being deal is portability
- Lack of public policies stimulating the creation of occupational pension plans.
- The move towards participant directed CD plans is an important improvement.

Consequences

- Negative media coverage – loss of confidence in the system.
- Regulatory burdens and stiff penalties disencourage new sponsors.
- The closed system has stagnated.

Investment Regulation

- Does portfolio regulation withstand a cost-benefit analysis?

- The time for international diversification.

Regulating the Open System

- High market concentration.
- Major players are subsidiaries of universal banks.
- The market is competitive – falling commission rates and investment management fees.
- Growing presence of international players.

- Impressive growth rates over the last five years.
- A tendency of GPPs replacing occupational pension plans as the preferred vehicle of employer provided pension benefits.
- New plans are unit linked.
- SUSEP is studying some new plans offering certain investment guarantees.

Soundness of the Open System

- The overhaul of the banking system by the present government had a strong positive effect on the soundness of the open pension system.
- The risk of creating financial conglomerates that are simply too large to colapse.
- A caveat: the traditional “open system” plans that offered a guaranteed accrual rate of inflation plus 6% per anum.

Novelties

- Regulation of new products: the PGBL and the VGBL.
- Greater portability within the open systems and partially with the closed system.
- It is not current practice of “closed” CD plan participants to buy annuities in the market.

The Problem of Providing Annuities

- Current law establishes that mortality table and interest rate must be set when the pension plan is acquired.
- Annuities must also be inflation-linked.
- Lack of long term securities to hedge against risks.