Republic of Zambia

Pensions and Insurance Authority

Capacity Building Program

Consultants’ Report

Final Report
Revised June 23 2006

Lawrie Savage & Associates Inc.
Consultants: Don McIsaac, Mark Fowler, Yoseph Aseffa, Lawrie Savage
### Acronyms and Abbreviations

<table>
<thead>
<tr>
<th>Acronym</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>BOZ</td>
<td>Bank of Zambia</td>
</tr>
<tr>
<td>CIMA</td>
<td>Conférence Interafricaine des Marchés d'Assurances</td>
</tr>
<tr>
<td>COMESA</td>
<td>Common Market for Eastern and Southern Africa</td>
</tr>
<tr>
<td>FSAP</td>
<td>Financial Sector Assessment Program</td>
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<tr>
<td>FSDP</td>
<td>Financial Sector Development Plan</td>
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<tr>
<td>GOZ</td>
<td>Government of Zambia</td>
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<tr>
<td>IAIS</td>
<td>International Association of Insurance Supervisors</td>
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<tr>
<td>ICP</td>
<td>Insurance Core Principles</td>
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<tr>
<td>INPRS</td>
<td>International Network of Pension Regulators and Supervisors</td>
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<tr>
<td>LASF</td>
<td>Local Authority Superannuation Fund</td>
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<tr>
<td>MOL</td>
<td>Ministry of Labour</td>
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<tr>
<td>NAPSA</td>
<td>National Pension Scheme Authority</td>
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<tr>
<td>NPS</td>
<td>National Pension System</td>
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<tr>
<td>PIA</td>
<td>Pensions and Insurance Authority</td>
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<tr>
<td>PSPF</td>
<td>Public Service Pension Fund</td>
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<tr>
<td>PSRA</td>
<td>Pension Scheme Regulation Act</td>
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<tr>
<td>SADC</td>
<td>Southern African Development Community</td>
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<tr>
<td>ZRA</td>
<td>Zambia Revenue Authority</td>
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<tr>
<td>ZSIC</td>
<td>Zambia State Insurance Company</td>
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</table>
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Republic of Zambia

Pensions and Insurance Authority
Capacity Building Program

1. Mission

Through a contract awarded by the FIRST Initiative, Lawrie Savage & Associates was invited to send a team of experts to Zambia to work with the Pensions and Insurance Authority. The team was to focus in three key areas:

1. Pensions:
   a. Assess current situation for private pensions in Zambia
   b. Review of current and proposed legislation
   c. Review and assessment of current PIA supervisory policies and procedures in the pension area
   d. Assess feasibility of market development in private pensions and propose an appropriate policy framework

2. Insurance:
   a. Assess current situation for insurance industry
   b. Review Insurance Act and assess compliance with IAIS Core Principles
   c. Review current and proposed insurance legislation and recommend any required amendments
   d. Review and assess current PIA supervisory policies and procedures in the insurance area

3. Matters relating to PIA’s supervisory efficiency, effectiveness and capacity:
   a. Preliminary work on a sustainable and viable organizational strategy and business plan
   b. Review current information and reporting systems for insurance and pensions and make recommendations where necessary
   c. Assess training needs of staff
   d. Review proposed study tours for appropriate PIA staff
   e. Identify resources and financial needs over the next 3 to 5 years and make recommendations with regard to sources of required funding

We should mention that while our mandate is to suggest areas for improvement, we acknowledge the fact that PIA has made good progress over the past year or two in terms of laying the groundwork for modernization and the adoption of new approaches that will move the organization further towards best international practices.

Members of the team were Yoseph Aseffa, Mark Fowler and Don McIsaac. The members would like to express their appreciation to the Registrar and staff of PIA for the gracious courtesy, hospitality and cooperation that was extended to them.

While in Lusaka, the team members met with representatives of insurance companies and administrators of private pension plans; with representatives of the trade associations of insurance companies and brokers; with the Zambia Revenue Authority; Securities and Exchange Commission;
and with senior officials in the Bank of Zambia and in the Ministries of Finance and Labour. An enumeration of the major contacts made by the mission team during the visit, along with an outline of the topics discussed, appears in the Executive Summary of this report at item 2(b).

2. Executive Summary

(a) Priority Recommendations for PIA Action

We suggest three levels of priority for planning purposes. Category 1 items, the highest priority, focus on raising the basic level of financial and supervisory knowledge within the organization. This strengthening will put PIA in a position to move forward with what we have termed Category 2 actions. In this category we include basic measures designed to strengthen the organization as well as important actions to begin strengthening the supervisory framework. Category 3 is comprised of critical steps that are needed to more closely align PIA with international core principles and best practices. To a certain extent it may be feasible to undertake actions concurrently. More comments in this regard are detailed after the table that follows:

<table>
<thead>
<tr>
<th>Category</th>
<th>Recommended Action</th>
<th>Initiated by</th>
<th>Description</th>
<th>Responsible Institutions</th>
<th>Resources</th>
</tr>
</thead>
<tbody>
<tr>
<td>Category 1</td>
<td>Appointment of Resident Advisor</td>
<td>PIA</td>
<td>Recruit advisor to assist in development of laws; guidelines; procedures; may be necessary to have separate advisors for insurance and pensions</td>
<td>PIA in consultation with international donors;</td>
<td>Funding by international donors</td>
</tr>
<tr>
<td></td>
<td>Short-term training</td>
<td>PIA</td>
<td>Specialized series of workshops to be held in Lusaka over a 2-week period</td>
<td>International experts; Resident Advisor; invite participation from other interested parties such as MOL and insurance industry</td>
<td>Funding by international donors; costs as estimated in tables with report</td>
</tr>
<tr>
<td></td>
<td>Study Tours</td>
<td>PIA</td>
<td>Visit by key staff members to supervisory agencies in a number of countries</td>
<td>PIA; Resident Advisor; Cooperating foreign supervisory agencies</td>
<td>Funding by international donors; costs as estimated in tables with report</td>
</tr>
<tr>
<td></td>
<td>Training Program</td>
<td>PIA</td>
<td>Staff at all levels should be trained in best international practices of supervision; report lists many areas where training is needed; training must be continuous</td>
<td>PIA; Resident Advisor; Other supervisory agencies</td>
<td>Funding from international donors; costs as indicated in report</td>
</tr>
<tr>
<td></td>
<td>Issue Guidelines</td>
<td>PIA</td>
<td>Guidelines can in some cases be effective supervisory tools, in the absence of legislation</td>
<td>PIA with cooperation of industry; Resident Advisor</td>
<td>Costs to be partly borne in compensation of Resident Advisor</td>
</tr>
<tr>
<td></td>
<td>Develop an effective annual budgeting exercise</td>
<td>PIA</td>
<td>Choose factors and a basis for the levy system that is equitable for all participants</td>
<td>PIA; consultation with industries affected; Resident Advisor</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Develop budget</td>
<td>PIA</td>
<td>Budget should provide for adequate numbers of competent</td>
<td>PIA; MOF; insurance and</td>
<td></td>
</tr>
<tr>
<td>Category</td>
<td>Recommended Action</td>
<td>Initiated by</td>
<td>Description</td>
<td>Responsible Institutions</td>
<td>Resources</td>
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<tr>
<td>Category 1 Continued</td>
<td>Develop procedures manuals; guidelines; procedures and rules to govern financing of PIA</td>
<td>PIA</td>
<td>Some guidelines are required urgently in the absence of adequate legislation; procedures will cover both on-site inspection and desk analysis</td>
<td>PIA; consultation with Resident Advisor</td>
<td>Costs to be partly borne in compensation of Resident Advisor</td>
</tr>
<tr>
<td>Category 2</td>
<td>Develop IT strategy</td>
<td>PIA</td>
<td>Acquire equipment and software necessary to operate a modern supervisory agency; include inter-office systems for communication and data-sharing</td>
<td>PIA; Resident Advisor; funding in initial stages to come either from MOF or from international donors</td>
<td>Process will take up to 18 months; financial support from international donors</td>
</tr>
<tr>
<td>Category 2 Continued</td>
<td>Establish PIA as an independent and autonomous supervisory agency; Obtain authority to levy market players for cost of supervision</td>
<td>PIA</td>
<td>Complete the process of passage and adoption of proposed amendments to the Pension Schemes Regulation Act</td>
<td>PIA; MOF; MOJ; NBFI committee under FSDP;</td>
<td>Should be completed in 2006</td>
</tr>
<tr>
<td></td>
<td>Strengthen human resources at PIA</td>
<td>PIA</td>
<td>Establish employment conditions (salary and benefits) that are</td>
<td>PIA; consultation/comparison with</td>
<td>Salary increases to be absorbed through</td>
</tr>
<tr>
<td>Category</td>
<td>Recommended Action</td>
<td>Initiated by</td>
<td>Description</td>
<td>Responsible Institutions</td>
<td>Resources</td>
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<tr>
<td>Category 3</td>
<td>Adopt risk-based approach to supervision</td>
<td>PIA</td>
<td>Annual program of activities should reflect priorities derived through comprehensive analysis of data collected from insurance companies and pension plans commensurate with those in comparable agencies, sufficient to attract competent staff</td>
<td>BOZ and SEC; Resident Advisor</td>
<td>revenue from industry levies; process of recruitment will take up to 18 months</td>
</tr>
<tr>
<td></td>
<td>Reduce amounts of premiums in arrears</td>
<td>PIA</td>
<td>Enforcement of legislation; amend legislation to adopt “no premium, no cover” rule. <em>(PIA has introduced the National Insurance Credit Policy Guidelines, providing a helpful summary of legislative provisions and PIA expectations. While the Guidelines may be effective in remedying the credit problem, it will take time to determine whether or not this will be the case. In the meantime, PIA should not lessen its efforts to enforce the legislation and otherwise take steps to reduce arrears.)</em></td>
<td>PIA, with support of industry and brokers, MOJ</td>
<td>Medium-term results depend upon enforcement</td>
</tr>
<tr>
<td>Category 3</td>
<td>Reduce overdue pension contributions</td>
<td>PIA</td>
<td>Enforce timely remittance of contributions; require disclosure of unpaid accrued contributions; upgrade financial reporting standards</td>
<td>PIA, pension fund managers and trustees, auditors, employers and scheme sponsors</td>
<td>Costs to be partly borne in compensation of Resident Advisor</td>
</tr>
<tr>
<td></td>
<td>Investment guidelines</td>
<td>PIA</td>
<td>Guidelines should reflect prudent portfolio management; specific disclosure of related party investing; enhance disclosure of investment activities</td>
<td>PIA; Resident Advisor; insurance industry; pension fund managers and trustees, auditors, employers and scheme sponsors</td>
<td>Costs to be partly borne in compensation of Resident Advisor</td>
</tr>
<tr>
<td></td>
<td>Motor TPL Insurance</td>
<td>PIA</td>
<td>Develop uninsured motorist fund; special high-risk pool; set indemnity limits for injured parties</td>
<td>PIA; Resident advisor; international experts</td>
<td>Estimated costs for international advice US$25,000</td>
</tr>
<tr>
<td></td>
<td>Winding-up procedures</td>
<td>PIA</td>
<td>Clear procedures for dealing with companies involved in either voluntary or forced liquidation; need legislation to protect priority rights of policyholders</td>
<td>PIA; Resident Advisor; MOJ</td>
<td>Costs to be partly borne in compensation of Resident Advisor</td>
</tr>
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</table>

As mentioned above, by categorizing the items into three levels of priority it is not our intention to suggest that all items would have to be carried out in a serial manner. Indeed, within categories a number of action items may in be feasible on a concurrent basis. For example, if it were possible to appoint a Resident Advisor early on in the process, then that Advisor could play an important role in assisting with many of the other Category A items. As a further example it would be possible to work on developing an effective budgeting process while at the same time designing appropriate guidelines that PIA already has the authority to issue.

There may also be opportunities for simultaneously undertaking some items that are in different categories. For instance, it may be possible to commence the design of investment guidelines...
In other words the consultants intend the table and the relevant priority classifications as shown to serve as an overall planning guide rather than to be considered as being “carved in stone”.

(b) **Summary of Contact Meetings**

It was important to meet with various system stakeholders in Zambia so as to have their input into the overall process of assessing the current supervisory framework. The meetings were also important in providing the consultants with context and perspective in examining the issues that need to be addressed as PIA moves to adopt more efficient and effective supervisory approaches.

Key meetings and points arising from the discussions are summarized in the table below.

<table>
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<tr>
<th>Focal Point</th>
<th>Organization</th>
<th>Name</th>
<th>Remarks</th>
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<tbody>
<tr>
<td>Legislation /</td>
<td>Pensions &amp; Insurance Authority (PIA)</td>
<td>Mr. Chris Mapipo, his 2 deputies and all officers and inspectors</td>
<td>We held our first meeting to discuss our mission with the CEO and his</td>
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<td>Supervision</td>
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<td>senior officers on the morning of 12 September 2005. We were given</td>
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<td>files containing a number of working documents such as draft PIA</td>
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<td>report for 2002 and 2003, draft legislation submitted to parliament</td>
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<td>and subsequent discussions with interested parties and existing</td>
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<td></td>
<td>pensions and insurance acts. Discussions focused on PIA establishment,</td>
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<td>management, its limited resources to undertake adequate planning and</td>
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<td>supervision of the bodies operating under its authority. We were</td>
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<td>assured the support of PIA staff as the CEO was to be on leave for</td>
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<td>the initial 2 weeks of our stay in Zambia. During the ensuing weeks</td>
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<td>we were provided with additional information and materials; we had</td>
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<td>intensive discussions with the staff and visited various institutions</td>
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<td>mentioned below. We were accompanied by senior officers of PIA on a</td>
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<td>number of our visits. CEO returned after two weeks and we were able</td>
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<td>to discuss a number of issues with him including our draft report,</td>
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<td>reflecting our findings and recommendations for technical assistance</td>
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<td>to strengthen the PIA. The mission team delivered three training</td>
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<td>seminars that were attended by the CEO and virtually all professional</td>
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<td>staff of PIA. PIA organized the meeting in order to obtain further</td>
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<td>comments from industry and other interested parties on the pensions</td>
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<td>and insurance legislation amendments under review. We attended the</td>
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<td>meeting on a consultative capacity to give our opinions wherever</td>
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<td></td>
<td>Stakeholders Meeting</td>
<td>Insurers, Brokers, representatives of NAPSA and Revenue Authority</td>
<td>required.</td>
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<td>and Pension Fund Trustees</td>
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<td></td>
<td>Madison Insurance Company Zambia Ltd</td>
<td>Mr. Lawrence S. Sikutwa, Managing Director and CEO, Mr. Adivi</td>
<td>Discussed market conduct, relationships among insurers and brokers,</td>
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<td>Apparao, Company Actuary</td>
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<td>challenges facing the insurance industry such as uncollected</td>
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<td>premiums, competition on rates and possible solutions; relations with</td>
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<td>the PIA, and what the industry sees as the role of the PIA, legislative</td>
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<td>review issues, and levy on the industry.</td>
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<td>Insurance Industry</td>
<td>Zambia State Insurance Corp. (ZSIC)</td>
<td>Ms. Irene Muyenga, Managing Director and other officers: Yoram</td>
<td>Previously a monopoly insurer and presently the only government owned</td>
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<td>Chulu, Gilbert</td>
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<td>Discussed ZSIC’s transition challenges as private companies were set</td>
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<td>up, its financial difficulties due to its heavy investment in</td>
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<td>non-performing property; management problems past and present, its</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>potentials for survival and growth under a competitive market, and its</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>views of the market and the</td>
</tr>
<tr>
<td>Focal Point</td>
<td>Organization</td>
<td>Name</td>
<td>Remarks</td>
</tr>
<tr>
<td>------------</td>
<td>--------------</td>
<td>------</td>
<td>---------</td>
</tr>
<tr>
<td></td>
<td>Sikazweh, Grace Mulendema, Emanuel Chimuka and Chibamba Kanyama</td>
<td>Supervisory authority, its efforts to reduce operating expenses, successfully reducing employee count from approximately 3,000 to under 400.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>African Life Assurance Company</td>
<td>Mr. S. P Williams, Chief Executive Officer and current Chair of Insurance Companies Assn</td>
<td>Discussed the Life insurance industry in Zambia, the legislative provisions, the regulatory environment, relationships with brokers, taxation, the practice of fronting, etc. African Life is a subsidiary of the South African company that pioneered the simplified issue life policies offered to extended family groups using payroll deduction for premium payment.</td>
</tr>
<tr>
<td></td>
<td>Professional Insurance Corp. of Zambia Ltd.</td>
<td>Mr. Ashok K. Chawla, Managing Director and Mr. T. K Ramanaathan, Financial Controller</td>
<td>Discussed the insurance industry, relationships with supervisory authority and brokers, the insurance law amendments under review and the proposed financing of the PIA through levy.</td>
</tr>
<tr>
<td></td>
<td>ZIGI Insurance Company Ltd</td>
<td>Mr. Saviour H. Konie, Chairman/CEO</td>
<td>Discussed the state of the insurance industry, market conduct, relations with brokers and the supervisory authority, the proposed amendments of the insurance act, uncollected premiums, and the special challenges for a young private insurer such as ZIGI</td>
</tr>
<tr>
<td></td>
<td>Cavmont Capital</td>
<td>Mr. Shadreck Lungu, manager, Asset Management</td>
<td>Cavmont is interested in developing its life insurance portfolio using modern products borrowed from the South African market. This is the newest company to be licensed in Zambia</td>
</tr>
<tr>
<td></td>
<td>Brokers Insurance Brokers Association of Zambia</td>
<td>Mr. Hastings E. Chiti, Executive Director</td>
<td>Discussed broker related issues, brokers’ relationships with industry and the supervisory authority as well as market issues such as premium collection and responsibility of brokers. We also sought brokers’ position on the insurance act amendments under review</td>
</tr>
<tr>
<td></td>
<td>AON Zambia Limited</td>
<td>Mr. Vincent Witt, Managing Director</td>
<td>Discussed the organization and relationships among brokers in the market, their relations with the insurance industry and the supervisory authority; legislative provisions on the business of brokers and the issue of code of conduct and uncollected premiums</td>
</tr>
<tr>
<td></td>
<td>Savanna Insurance Brokers Ltd</td>
<td>Mr. Mark C. Nidilla, Managing Director</td>
<td>Discussed the role and challenges of brokers in the market, insurance supervision and legal issues</td>
</tr>
<tr>
<td></td>
<td>Pensions Industry</td>
<td>Muna Hantuba, Chief Executive of Zambia</td>
<td>Discussion of the pension industry, legislative proposals, prospects for industry growth, challenges it faces, taxation issues, investment opportunities and lack of capacity for markets to absorb fund growth, role perceived for PIA as principal advisor to government on pension policy, PIA seen as policeman rather than facilitator, PIA lacks proper information management systems, flaws in current legislation, pending investment proposals may conflict with prudent portfolio management, contribution remittance arrears, government’s management of the pension industry, fears that NPS may displace private pension industry, inadequacy of tax support for private pensions, NPS and NAPSA situation, need for capital market development, administration problems of pension schemes and roles of trustees, problems with multiple employer trust system, recovery of supervisory costs, management of insolvent schemes, and recent representations of private pension fund managers.</td>
</tr>
<tr>
<td></td>
<td>Zambia State Life Insurance</td>
<td>Yoram Chulu, Director – Life and Pensions</td>
<td>In-depth discussion of the private pensions market, current issues retarding its growth, inadequate contribution deductibility, benefit taxation, investment portfolio development and overweighting of</td>
</tr>
<tr>
<td>Organization</td>
<td>Name</td>
<td>Remarks</td>
<td></td>
</tr>
<tr>
<td>--------------</td>
<td>------</td>
<td>---------</td>
<td></td>
</tr>
<tr>
<td>Company (ZSIC)</td>
<td>Zambia State Life Insurance</td>
<td>mortgages, lack of depth in financial instruments, lack of consistent real rate performance, marketing and costs, movement to convert to self-administered trusts by larger employers, pursuit of unpaid contributions, annuity conversion bases for defined contribution schemes, insolvent schemes and issues related to PIA effectiveness.</td>
<td></td>
</tr>
<tr>
<td>National Pension Scheme Authority (NAPSA)</td>
<td>Musonda S. Cheta, Director – Corporate Planning and Development Yolland Kachinda, Manager Actuarial and Research</td>
<td>Discussed the roles of NAPSA and PIA, issues and challenges facing PIA, prospects for the growth of the private pensions market, administrative issues facing private schemes, collection of contributions and remittance problems, need for administrative coordination between PIA and NAPSA, e.g. portability requirements and related standards, pending legislation and cost recovery for PIA and certain technical issues regarding the valuation of the NPS’s financial condition.</td>
<td></td>
</tr>
<tr>
<td>QED Actuaries &amp; Consultants South Africa</td>
<td>Mr. Colin Hendriks, Director</td>
<td>Discussed the state of private pensions industry, technical actuarial matters re. Methodologies and assumptions used in the financial reporting for private defined benefit schemes, insolvent schemes and potential for remediation.</td>
<td></td>
</tr>
<tr>
<td>PIA, ZRA, ZSIC, IBAZ, MOF&amp;NP, DFID, Grant Thornton</td>
<td>various</td>
<td>The pensions expert participated in several of these meetings as there were overlaps with certain issues, e.g., role and funding of PIA, legislation, structure of financial sector and related initiatives, product marketing etc. See remarks above.</td>
<td></td>
</tr>
<tr>
<td>Government Agencies</td>
<td>Ministry of Finance and National Planning</td>
<td>Ms. Petronella N. Mwnagala, Permanent Secretary</td>
<td>Discussed government objectives in setting up the PIA, government expectations and what support will continue to be provided. The case for a unified regulatory system for the financial sector, FSDP/SIDA assistance and how it will assist PIA, the legislative review underway. The PS indicated that there was some risk the draft bill to amend the Pensions Act might be withdrawn. Problems of authorizing cost recovery systems in Zambia were discussed including issues related to PIA and state enterprise pension schemes.</td>
</tr>
<tr>
<td>Ministry of Labour</td>
<td>Ms. Edna Mudenda, Director – NBFI Dept., Mr. Visscher Bbuku, and Mr. Lameck Zimba, Asst. Directors, Mr. Moses Chatulika, Senior Inspector, Bank Supervision, Mr. M. J. Phiri, Inspector - Financial Analysis, NBFI Supervision Department</td>
<td>Discussed the historical supervision of Insurance by the Central Bank, pre-PIA, the current activities of the Bank and possible relationships in the future between the Bank and PIA. The Central Bank also acts as the FSDP secretariat. Ms Mudenda has agreed to ensure that PIA representatives are present at periodic meetings of the NBFI committee organized under the FSD plan.</td>
<td></td>
</tr>
<tr>
<td>Ministry of Labour</td>
<td>Unfortunately those present did not provide business cards and we inadvertently omitted to make</td>
<td>MOL lacks the capacity to supervise NAPSA and the other public pension schemes – sees itself as a partner with PIA. While the Minister of Finance has a responsibility to audit various state bodies, such as NPS, the only supervision presently in place occurs through internal audit system at NAPSA. Changes to certain laws respecting state pensions require change to the constitution. MOL</td>
<td></td>
</tr>
<tr>
<td>Organization</td>
<td>Name</td>
<td>Remarks</td>
<td></td>
</tr>
<tr>
<td>--------------</td>
<td>------</td>
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<td></td>
</tr>
<tr>
<td>Securities and Exchange Commission</td>
<td>Mr. Clement Sichembe, Secretary &amp; CEO, Ms. N. Hamanyanga, Mr. Michael M. Liweleya</td>
<td>Reviewed developments in securities markets; discussed SEC’s success in striving for financial independence through a levy on market participants; Registrar of PIA has consulted frequently with head of SEC</td>
<td></td>
</tr>
<tr>
<td>Zambia Revenue Authority</td>
<td>Mr. Kabaye Mwale, Deputy Commissioner – Central Direct Taxes Division</td>
<td>Discussed taxation of insurance and pension benefits and contributions; examined exemptions available to contributors and policyholders; reviewed taxation of insurance companies as corporations</td>
<td></td>
</tr>
<tr>
<td>International Organizations</td>
<td>DFID (Department for International Development of the UK) Lusaka office</td>
<td>Met with DFID officers because DFID/SIDA funding to the restructuring program of the Zambia Financial Sector is mentioned in the World Bank FSAP Report and the TOR. We were advised that DFID works closely with the Ministry of Finance and the Central Bank. Discussed if there has been any specific plan for the coordination of supervisory bodies within the Zambia financial sector leading to the possibility of a unified supervisory body as in the UK. Our objective was to determine what possible assistance could flow to PIA in its current strategy.</td>
<td></td>
</tr>
<tr>
<td>Others</td>
<td>Grant Thornton</td>
<td>Discussed the accountants profession, their perception of the insurance and pensions industry, the varying levels of detail published in the reports of different insurance companies, internal control systems and good governance in the industry, the role of the supervisory authority, financial reporting for pension schemes and the treatment of contributions due but not received etc.</td>
<td></td>
</tr>
<tr>
<td>QED Actuaries &amp; Consultants, South Africa</td>
<td>Mr. Craig Falconer, Director and Mr. R. Patel, Sen. Actuarial Consultant</td>
<td>Discussed the state of the insurance industry, its appreciation of the role of actuaries, the services of QED to the insurance industry and the pension funds in Zambia.</td>
<td></td>
</tr>
</tbody>
</table>

**Organizational strategy and business plan**

The functional plan proposed by PIA in its management retreat (shown as Appendix Twelve to the report) has many positive features. We believe that, given certain safeguards, it could be a useful model for the development of PIA.

1. The expertise required for such an organization “by function” is not currently available within PIA. Having met with virtually all of the incumbent professional staff, the consultants believe that a move to this structure would be risky if an attempt is made to simply transfer existing staff from their present positions into the positions listed on this organization chart. We would propose the following plan of action:
a. The Resident Advisor, once appointed, would draft the Position Descriptions for all the professional positions. Note: The post of Registrar will not be part of this process.

b. All other positions would then be offered, through a competitive process, to those persons possessing the necessary professional and other credentials specified in the Position Descriptions.

2. It should be possible to staff all the positions in a reasonable period of time, even though it can be expected that some of the appointees will come from outside PIA. The training of appointees, both incumbent staff of PIA and newcomers, in the functions of a competent financial sector supervisory team will take a longer time – possibly a period of years.

3. In order to ensure that the required supervision is applied in all areas, it will be necessary to specify that one of the two posts of “senior inspector” be assigned exclusively to the work of insurance companies and the other to working with pension plans.

4. The position of Director – Policy, Research and Market Development is critical to this organization. We believe that this position, or one subordinate to it, would have to supply all technical expertise to PIA, including actuarial advice. At present, PIA has no one on staff who could perform these functions.

5. The Director-Finance& Corporate Affairs will have the responsibility to plan, organize and carry out the process of determining assessments to be paid by licensed institutions and of collecting those levies.

6. It is likely that in the initial period, PIA will not be in a position to recruit a qualified actuary for the work of Policy and research as well as technical advice to the inspection teams. Appointees with strong mathematical skills could be given special training in actuarial topics as an interim measure.

7. Compensation arrangements for these professional positions must be reviewed in light of what is available for other comparable positions in Lusaka, particularly in BOZ and SEC and salaries adjusted accordingly.

8. Obviously the capacity to gather revenue through the levy on licensed institutions is also critical. Where such levies are inadequate, the government should commit to supplement the budget of PIA as required.

3. PIA: Financing and Budget

<table>
<thead>
<tr>
<th>Possible Budget for PIA</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Item</strong></td>
</tr>
<tr>
<td>Resident Advisor</td>
</tr>
<tr>
<td>Long term education and</td>
</tr>
<tr>
<td>training</td>
</tr>
<tr>
<td>Study Tours</td>
</tr>
</tbody>
</table>
The broad developmental process outlined above would enable PIA to complete its transformation into a modern supervisory regime. The salary figures we have used are assuming that levels are commensurate with those at the Central Bank and the Securities Commission. We do not have any information on actual salary levels currently in force at PIA.

It may be that the system of levies on supervised institutions will not be sufficient to cover the costs of developing the organization in the short term, in which case it may be necessary to arrange some type of temporary backstop from the Government of Zambia. (We have made this point with officials at the Zambian Securities Commission.) Nevertheless we see any funding that may have to be provided over the short term as being a worthwhile investment that will bear significant dividends later on in terms of helping to strengthen the economy and providing the population with the social benefits that are a part of an insurance and pension regime.

<table>
<thead>
<tr>
<th>Possible Budget for PIA</th>
</tr>
</thead>
<tbody>
<tr>
<td>offices of other insurance supervisory agencies, for periods of 2 weeks each. Cost estimate is $4,000 per person</td>
</tr>
<tr>
<td>Short term training workshops</td>
</tr>
<tr>
<td>Short term training workshops</td>
</tr>
<tr>
<td>Acquisition of info systems and software and related training of staff</td>
</tr>
<tr>
<td>Preparation of Directives, manuals, Terms of Reference</td>
</tr>
<tr>
<td>Legislative Review</td>
</tr>
<tr>
<td>Legislative Review</td>
</tr>
</tbody>
</table>

Total 625,700
4. **Assessment of Situation and Principal Findings**

(a) **Prospects for the Pensions and Insurance Authority (PIA)**

Our mandate was to review the operations, resources and activities of PIA in order to identify any areas where we might recommend technical assistance to strengthen its capacity to do its job. Upon arrival we learned that new legislation is under consideration that will make important changes to PIA and the way it is financed. Draft amendments to the Pension Scheme Regulation Act will clarify the status of PIA as an independent government agency with its own Board. While it would have been preferable to have the legislature adopt a special Act establishing PIA as an autonomous body, the changes proposed should have the desired effect.

Of equal importance, PIA will also be granted the power to assess levies on supervised entities, both insurance companies and private pension plans. These levies should provide sufficient revenue to enable PIA to acquire all the resources, both human and technical, that it needs if it is to operate as a modern supervisory agency applying best international practices. The amendments drafted do not fix all the shortcomings that have been identified in the regulatory system in Zambia (see our later comments on legislation), but the changes to PIA itself represent an important watershed.

(b) **PIA as a Supervisory Agency in September 2005**

The investigations conducted by the mission team have identified three major areas where PIA must be strengthened if it is to function as, and to be respected as, a modern, efficient, effective supervisory agency. The first and most obvious shortcoming relates to the resources made available to PIA. Its budget has, until now, been provided through special allocations from the Ministry of Finance and National Planning. Resources made available have not been sufficient to enable it to hire the full “establishment” of staff called for in its operating plan. Most of the staff have been with the agency only a very short time and few have any experience in the insurance or pensions fields. Beginning this year, PIA has managed to procure enough computers to ensure that each professional staff member has a desktop. However, there are no laptops for use in field work and the local area network that links the staff computers has only limited functionality. PIA has not been able to create effective databases that it could use in performing analysis of the conditions in the markets it is supposed to supervise.

Pension Scheme Regulation Act, 1996 and Insurance Companies Act, 1997 provide the legislative basis for the work of licensing, monitoring, supervising and sanctioning of licensed entities in Zambia. These two pieces of legislation are more modern than those which exist in some other African countries. However, they suffer from serious shortcomings when examined in the light of emerging international standards for financial sector supervision. For example, the laws do not include requirements for corporate governance and the expected behaviour of Directors (or trustees in the case of pension plans) in establishing appropriate corporate policies; monitoring management’s adherence to those policies; and taking remedial action when those policies are violated.
Of greater practical significance at this time is the fact that Regulations necessary to give effect to some of the important provisions of the Acts have not been promulgated. In a few cases, companies have been advised to continue using Regulations made under the authority of older legislation (dating from the 1960’s) where those Regulations are not in conflict with provisions of the current legislation. The existing legislation provides authority to the Minister to issue regulations and to prescribe certain rules. In addition, the Registrar is empowered to issue binding guidelines in a number of important areas. However, many of the necessary regulations, rules and guidelines have yet to be issued.

The supervision of pension schemes is an important part of the mandate of PIA. Owing to the importance attached to pension plans as part of the total compensation package for workers, the Ministry of Labour has a direct and continuing interest in the supervision of pension plans as well. This interest is further enhanced by the fact that PIA has oversight responsibilities with respect to two large public schemes, LASF and PSPF, while the Social Security Dept of the Ministry of Labour is responsible for the national scheme, NAPSA. In recognition of the convergence of interests of Ministry of Labour with those of PIA, the Pension Scheme Regulation Act makes the appointment of the Registrar by the Minister of Finance, subject to the concurrence of the Minister of Labour. In practice, PIA’s operations are subject to a dual reporting relationship, to Labour as well as to Finance.

Within the last year, PIA has begun to play a more active role as supervisor. For example, a program of on-site inspections of insurance companies and pension schemes has been launched. New procedures of many types are being tested. It will be important that PIA develop written procedures for all important functions (inspections, analysis, dealing with auditors and actuaries) and that staff be thoroughly schooled in these functions. Working paper standards would also be a helpful device to make the inspection processes more effective. The documentation of these procedures, training of staff, and development of working papers will all demand that PIA be provided with additional technical assistance and funding.

5. Other Considerations that might Impact on PIA

An important initiative of the Government of Zambia is the Financial Sector Development Program (FSDP). This is a comprehensive program that seeks to strengthen the financial sector in the country and to promote its further growth. FSDP will harmonize the regulatory systems for the various players in the sector (banks, insurance companies, pension plans) and seeks to ensure that all segments are properly supervised. In some circles there have been suggestions that it might be advisable to create a single supervisory agency (as in UK or South Africa). No final decision has been taken on this latter point and the mission’s inquiries have led to the conclusion that it may be several years before any initiative to integrate supervisory organizations takes place, if at all.

Information has also come to light to suggest that the countries of the COMESA zone are giving serious consideration to the creation of a harmonized system of laws, across the member countries, to help ensure the smooth flow of trade in services. Such a program would follow the model of the European Union or perhaps of the CIMA Code that applies in the franc zone of West Africa. Under such a harmonized model, Zambia would have to ensure that its regulatory system was consistent with that which applies in Egypt and Kenya and Tanzania, for example.

These other initiatives create some uncertainty for the directions that PIA should take in re-engineering its supervisory system. However, since the measures being considered under these
various initiatives should not have any impact on the Zambian insurance market for several years, the team holds the view that the best course of action for PIA is to take whatever steps are necessary to strengthen its capacity as an insurance supervisor within the present framework. Having in mind the growing acceptance of international standards, modern approaches adopted by PIA are likely to be similar to the measures being adopted in other African countries.

A proposed Strategic Action Plan for PIA’s development in the short term appears as section 9 of this paper. This is supported by item 9(k) where a plan for training of staff is described and by item 9(o) where a budget provides estimated costs for the plan of action and the training described.

6. The Insurance Industry and its Supervision

(a) Industry Statistics

There are currently 8 private insurance companies licensed and operating in Zambia and one state-owned company. One of the private companies does only life insurance business and another (ZimRe, subsidiary of Zimbabwe Reinsurance Company) confines its activities to the business of reinsurance. All are incorporated in Zambia. Foreign companies may enter Zambia only by establishment of a subsidiary. The market is small and premium income for the entire industry during 2003 was 271 billion kwacha (US$ 57 million). This represents approximately 1.2% of the GDP of Zambia. The following table contrasts insurance in Zambia with that of other African countries:

<table>
<thead>
<tr>
<th></th>
<th>Life Insurance %GDP</th>
<th>Per capita</th>
<th>General Insurance %GDP</th>
<th>Per capita</th>
<th>Total %GDP</th>
<th>Per capita</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mauritius</td>
<td>2.78</td>
<td>119.1</td>
<td>1.81</td>
<td>77.4</td>
<td>4.59</td>
<td>196.5</td>
</tr>
<tr>
<td>Zimbabwe</td>
<td>2.40</td>
<td>21.4</td>
<td>1.77</td>
<td>15.8</td>
<td>4.17</td>
<td>37.2</td>
</tr>
<tr>
<td>Kenya</td>
<td>0.78</td>
<td>3.4</td>
<td>2.20</td>
<td>9.5</td>
<td>2.98</td>
<td>12.9</td>
</tr>
<tr>
<td>Ethiopia</td>
<td>0.05</td>
<td>0.04</td>
<td>0.89</td>
<td>0.85</td>
<td>0.94</td>
<td>0.89</td>
</tr>
<tr>
<td>Nigeria</td>
<td>0.14</td>
<td>0.6</td>
<td>0.63</td>
<td>2.5</td>
<td>0.77</td>
<td>3.0</td>
</tr>
<tr>
<td>ZAMBIA</td>
<td>0.21</td>
<td>0.93</td>
<td>1.01</td>
<td>4.37</td>
<td>1.22</td>
<td>5.30</td>
</tr>
</tbody>
</table>

Table shows insurance penetration (premiums as % GDP) and insurance density (premiums per capita in US dollars).

(i) Results of Non-Life Operations for 2003

The following table provides an indication of the operating results for insurance companies in Zambia for the year 2003. Figures are for non-life business only.
### 2003 Non-Life Insurance Results (ZMK millions)

<table>
<thead>
<tr>
<th>Income Statement</th>
<th>ZimRe</th>
<th>Goldman</th>
<th>Madison</th>
<th>Cavmont</th>
<th>Zigi</th>
<th>Nico</th>
<th>Zsic</th>
<th>Picz</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross Premiums</td>
<td>3,230</td>
<td>17,318</td>
<td>55,189</td>
<td>783</td>
<td>11,586</td>
<td>20,586</td>
<td>50,413</td>
<td>67,764</td>
<td>226,869</td>
</tr>
<tr>
<td>Net Premium</td>
<td>1,938</td>
<td>7,275</td>
<td>38,311</td>
<td>295</td>
<td>9,315</td>
<td>8,997</td>
<td>40,720</td>
<td>40,678</td>
<td>147,529</td>
</tr>
<tr>
<td>Change in Unearned Premiums</td>
<td>-62</td>
<td>290</td>
<td>-4,728</td>
<td>-260</td>
<td>-851</td>
<td>-27</td>
<td>-2,077</td>
<td>-3,843</td>
<td>-11,558</td>
</tr>
<tr>
<td><strong>Net Earned Premium</strong></td>
<td>1,876</td>
<td>7,565</td>
<td>33,583</td>
<td>35</td>
<td>8,464</td>
<td>8,970</td>
<td>38,643</td>
<td>36,835</td>
<td>135,971</td>
</tr>
<tr>
<td>Management Expenses</td>
<td>-1,452</td>
<td>-3,821</td>
<td>-10,709</td>
<td>-1,189</td>
<td>-1,575</td>
<td>-5,560</td>
<td>-20,539</td>
<td>-8,109</td>
<td>-52,954</td>
</tr>
<tr>
<td><strong>Underwriting Results</strong></td>
<td>-80</td>
<td>572</td>
<td>1,412</td>
<td>-1,092</td>
<td>4,322</td>
<td>-64</td>
<td>4,888</td>
<td>12,753</td>
<td>22,511</td>
</tr>
<tr>
<td>Other Management Expenses</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>-4,109</td>
<td>1,000</td>
<td>-3,109</td>
</tr>
<tr>
<td>Investment Income</td>
<td>81</td>
<td>1,102</td>
<td>2,953</td>
<td>221</td>
<td>182</td>
<td>965</td>
<td>820</td>
<td>2,364</td>
<td>8,688</td>
</tr>
<tr>
<td>Other Income/(Outgo)</td>
<td>261</td>
<td>-768</td>
<td>891</td>
<td>345</td>
<td>-4,776</td>
<td>-30</td>
<td>7,207</td>
<td>-7,498</td>
<td>-4,368</td>
</tr>
<tr>
<td><strong>Profit/(loss) before tax</strong></td>
<td>262</td>
<td>906</td>
<td>5,256</td>
<td>-526</td>
<td>-272</td>
<td>871</td>
<td>8,606</td>
<td>8,619</td>
<td>23,722</td>
</tr>
</tbody>
</table>

### Balance Sheet

| Current Assets                            | 3,437 | 9,567  | 28,416  | 2,371  | 6,394  | 7,332  | 64,428  | 22,858  | 144,803  |
| **Net Current Assets**                    | 110   | 5,561  | 3,949   | 1,830  | -93   | 4,653  | 23,384  | 17,301  | 56,695   |
| Long Term Assets                          | 1392  | 1096   | 3760    | 221    | 612   | 1863  | 23552   | 10620   | 43,116   |
| Long Term Liabilities                     | 0     | 0      | -147    | 0      | -2,919| -20,398| -17,370  | -40,834 |          |
| **Total Net Assets**                      | 1,502 | 6,657  | 7,562   | 2,051  | 519   | 3,597  | 26,538  | 10,551  | 58,977   |
| Capital + RE+Reserves                     | 1,502 | 6,657  | 7,562   | 2,051  | 519   | 3,597  | 26,538  | 10,551  | 58,977   |
7. Deficiencies in the Regulatory System

As noted above, since the Insurance Act was adopted in 1997, the supervisory authority has not managed to issue all the regulations and guidelines that would be required to give full effect to the provisions of the Insurance Act. The incumbent Registrar is taking steps to correct this situation. In the absence of the desired regulations, there are, in Zambia, no specific requirements that govern the valuation of assets and the valuation of liabilities. In addition the rules governing the measurement of the adequacy of capital and surplus (solvency) do not reflect the size and nature of risks assumed by the companies. Without these fundamental tools, effective supervision is difficult.

Minimum capital requirements specified in the legislation to start a company are insignificant (equivalent of US$ 225,000.).

Fortunately the legislation does provide authority for the Minister to make regulations that will help deal with some of these problems and there is wide power given to the Registrar to issue binding Guidelines (section 99 of the Insurance Act). If these powers are used in a considered and appropriate fashion, it should be possible to improve the regulatory system applicable to insurance companies in a reasonable period of time, without having to wait many years for the next “round” of revisions to the legislation.

The Insurance Act defines what types of assets would not be admitted for the solvency test, but the legislation does not impose quantitative limits on the investment portfolio of an insurance company. There are companies operating in the marketplace that have very little liquidity in their assets. In some cases, the combination of property investments (land and buildings) plus amounts owed to the company by policyholders (outstanding premium) will together constitute as much as 80% of the assets on a company’s balance sheet. Companies in such an illiquid situation will find themselves unable to pay claims in the medium and longer term. The problem of excessive amounts of “premiums receivable” plagues all the players in the market, with substantial amounts that are more than 6 months overdue. The Registrar is planning a concerted effort, with support from the industry, aimed at correcting this situation.

(a) Assessment against IAIS Core Principles

PIA was not found to be fully observant of any of the Core Principles of the IAIS, although it could be said to have “largely observed” the principle on licensing. Most of the others were judged to be only partly observed although a few, such as “corporate governance” were rated as “not observed”.

A detailed summary of the findings of the Core Principles assessment is contained in Appendix Ten. It should perhaps be noted that it would not be the practice of the World Bank/IMF teams to prepare a full assessment of PIA’s insurance regulatory/supervisory system against Core Principles, having regard for the relatively immature nature of the insurance sector in Zambia. However the findings were developed as part of an assisted self-assessment conducted together with members of the PIA insurance inspection team. A sample of the ICP findings follows herewith:

CP 3 Supervisory Authority

ICP 3 requires the supervisory authority to have “clear rules for appointment and removal of the head of the supervisory authority. These should be publicly disclosed.” While the appointment and dismissal
of the Registrar may be provided for by contract, as far as we were able to determine, the details of the contract are not publicly disclosed. ICP 3 also requires that “the supervisory authority should be operationally independent from external political and commercial interference in the exercise of its functions and powers.” At the time of the visit, PIA did not have full legal authority as an independent entity. PIA has not had sufficient resources to hire its full “establishment” of staff and this is worrisome since it is believed that additional staff will be needed to discharge all the responsibilities that will devolve upon PIA under new legislation. Funding for essential training has not been provided. Information systems need to be upgraded but PIA lacks the resources.

CP 7 Suitability of Persons

At present the Insurance Act in Zambia applies a fit and proper test only to the CEO of an insurance company although the Minister can extend the rules to other officers. There are no conflict of interest rules specified for actuaries; auditors; Directors and senior managers.

CP 8 Change of Control

There is no evidence that the Registrar has any influence over changes in control. Applicants seeking to acquire control of an insurance company should be obliged to satisfy similar criteria to those applicable to new licenses.

CP 9 Corporate Governance

The Insurance Act is silent on corporate governance, for all practical purposes. There are no references to a company’s Board of Directors. While there are occasional references to Directors, the “fit and proper” provisions do not apply to Directors. Insurance companies are incorporated in accordance with the Companies Act, which dates from 1985 and hence does not reflect current practices in corporate governance. For example, Boards need have only 2 Directors; there is no requirement under the Companies Act for an Audit Cttee; nor does there seem to be any reference to the need for independent directors. It is worth noting that there are relevant sections in the Banking and Financial Services Act. For example, the majority of the members of a bank’s Board of Directors must be persons who are neither officers nor employees of the bank.

CP 10 Internal Controls

There is no formal authority through the Insurance Act that compels the Board to monitor a system of internal controls. In Zambia, some of the audit firms are forthright in reviewing and demanding strong internal controls from their insurance company clients, although we understand that this is not always the case. We were advised that PIA inspectors have made the review of internal controls a basic component of their on site work. However, in the absence of effective corporate governance requirements, the Boards of Directors of insurance companies in Zambia can not be expected to be discharging the functions that a proper internal control system would expect of them.

CP 18 Risk Assessment and Management

PIA has not issued any instructions to insurers with respect to risk assessment and management. Inspection procedures have not been established in a formal way but it appears that a review of a
company’s risk management policies and risk control systems is not yet a part of the inspection function, although this is an expectation under the core principles.

CP 23 Capital Adequacy and Solvency

In the absence of specific rules regarding valuation of assets and liabilities, the solvency test in the Insurance Act has little effect. Solvency test does not consider issues of liquidity, matching of assets and liabilities, and suitable forms of capital. Capital adequacy requirements are fixed and not sensitive to the size, complexity and riskiness of the company’s operations. Solvency control levels have not been established.

(b) Zambia State Insurance Company

Zambia State is still owned by the Government of Zambia, despite repeated attempts to privatize it through the sale of shares. Since the market was opened to new players, this company’s total market share has slipped to the point where it now ranks third by total premium income. The company is still the major writer of motor insurance in Zambia, issuing most of the policies for those persons who elect to acquire only the minimum amount of protection required by the Road Safety Act. Zambia State is responsible for administering the “yellow card” program in Zambia. This is the reciprocal system that enables Zambian drivers to operate their vehicles on the roads of other participating countries and vice versa.

Management of the company has completed a major down-sizing of the company’s operations. The work force has been reduced from over 3,000 to approximately 350. Claim payments have been brought up-to-date, a considerable improvement over the situation prevailing only a few years ago.

The company has a disproportionate amount of real estate in its investment portfolio – an inheritance from its early history. While there is still some hope that the company will one day be privatized, there are important roadblocks in the way of any potential purchaser.

8. Private Pensions and their Supervision

(a) Industry Overview

The PIA supervises some 215 schemes at present, of which 30 or 15% are defined benefit schemes. The number of supervised schemes has been increasing in recent years being some 142 in 2001, 159 in 2002 and 170 in 2003.

However, the distribution is extremely skewed as the number of active members of defined benefit schemes currently represents approximately 80% of total active members of all supervised schemes and the number of retired members of such schemes represents about 76% of total retired members of all schemes. The skewing effect is mostly attributable to the inclusion of the PSPF and LASF, both of which are defined benefit schemes.

The vast proportion of supervised schemes are participants in multi-scheme, multi-employer trusts that are created by 8 fund management companies, most of which are, in turn, wholly-owned
subsidiaries of licensed insurers. (The relationships of insurers and other financial institutions and the presence or absence of holding company structures was not investigated in this connection.) The ZSIC Pension Trust Fund manages over 100 schemes. There were 18 single-employer trusts as at the end of 2003, and there is evidence of efforts of some employers wishing to withdraw from the multi-scheme, multi-employer trusts. Individual employers participate in these arrangements by virtue of their executing “adherence agreements” which oblige them to respect the terms and conditions of the governing trust deed and scheme rules.

Invested assets of supervised schemes as at December 31, 2003 totalled some ZK 803B. The PSPF reported ZK 129B or 15% of the total while the LASF reported nil.

Invested assets of supervised schemes have increased from ZK 325B in 2000 a growth rate of approximately 25.3% pa. This is highly unusual but is largely attributable to the high rates of return on investments. If deflated, the growth rate is a more reasonable 3-4% pa.

The following table provides additional statistics on pension schemes supervised by PIA

<table>
<thead>
<tr>
<th>Data Item</th>
<th>Year 2003</th>
<th>Year 2002</th>
<th>Year 2001</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of schemes supervised</td>
<td>170</td>
<td>159</td>
<td>142</td>
</tr>
<tr>
<td>Number of members:</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Actives</td>
<td>164535</td>
<td>142280</td>
<td>134016</td>
</tr>
<tr>
<td>Deferred</td>
<td>18514</td>
<td>21006</td>
<td>3090</td>
</tr>
<tr>
<td>Retired</td>
<td>58484</td>
<td>53955</td>
<td>56344</td>
</tr>
<tr>
<td>Contributions (ZK B)</td>
<td>269.2</td>
<td>165.3</td>
<td>142.7</td>
</tr>
<tr>
<td>Investment Income (ZK B)</td>
<td>104.2</td>
<td>135.0</td>
<td>70.4</td>
</tr>
<tr>
<td>Benefits (ZK B)</td>
<td>164.1</td>
<td>118.2</td>
<td>95.0</td>
</tr>
<tr>
<td>Expenses (ZK B)</td>
<td>44.2</td>
<td>33.4</td>
<td>27.8</td>
</tr>
<tr>
<td>Net (C+I-B-E) (ZK B)</td>
<td>165.1</td>
<td>148.7</td>
<td>90.3</td>
</tr>
<tr>
<td>Assets (ZK B)</td>
<td>802.9</td>
<td>624.5</td>
<td>464.6</td>
</tr>
<tr>
<td>Net Rate of Return %</td>
<td>13.6%</td>
<td>22.1%</td>
<td>16.4%</td>
</tr>
</tbody>
</table>

Further information on the pension industry appears in Appendix One. Appendix Four contains an outline of demographic, economic and actuarial factors that are relevant to a study of pensions in Zambia.

(b) INPRS Core Principles ~ Assessment

The core principles of the International Pension Regulators and Supervisors and PIA’s compliance status were reviewed during intensive on-site discussions with the Pension Department and PIA’s legal counsel. Appendix Five reports on the status of observance of all 15 principles. The following is a synopsis of the results of this assessment exercise.

CP 1 Effective regulation and supervision.

There is partial compliance with this core principle. In two specific areas where the system does not substantially comply, the pending amendments will accomplish that objective. However, in regard to the specification related to accounting standards (sub-item 1.5), the existing practice of non-disclosure in the audited financial statements of accrued contributions due but not remitted implies
that substantial compliance is not achieved. (PIA does receive regular information from trustees regarding contribution arrears but that data does not appear to be audited.)

CP 2 Establishment of pension plans, pension funds, and pension fund managing companies.

There is substantial compliance with most items. However, the compliance with sub-item 2.6 (required capital for fund managing companies) has not been resolved although the pending legislation will grant PIA the power to mandate minimum capital for service provider agents including fund managers.

CP 3 Governance

There is lack of substantial compliance with several sub-items which will be removed with the adoption of the proposed amendments. However, the issue of whether, and under what conditions, the actuary and auditor will be required to act as ‘whistle-blowers’ is unresolved although it is contemplated that these will be required by way of regulations to be passed following the adoption of the amendments to the PSRA.

CP 4 Pension Fund liabilities, funding rules, winding up and insurance.

There is no compliance. The pending provisions will enable PIA to effect compliance by way of regulations that have been drafted for adoption once the legislation has been amended. These deal with the reporting of actuarial liabilities and the funding of unfunded liabilities and deficits although these do not appear to involve specific maximum amortization periods as part of the funding rules.

CP 5 Asset Management

There is substantial non-compliance. This will be remedied by the pending legislation. There is no plan to regulate the use of derivatives for purposes of risk hedging. This should be given further consideration in light of the possible increased access of foreign investments under the proposed investment guidelines.

CP 6 Rights of Beneficiaries and Adequacy of Benefits

It is unclear that there is substantial compliance with this principle. The legal provisions concerning non-discriminatory access (eligibility conditions are not regulated by the PSRA) should be ascertained by further research. Also the definition of ‘accrued benefits’ should be investigated to ensure that it means full and unconditional vesting irrespective of members’ age and service.

CP 7 Disclosure and Education

The compliance picture is mixed. It is unclear that there is substantial compliance with item 7.1 as respects members being promptly informed about any material changes in the fund and with item 7.3 as respects members being provided with adequate information necessary to make sound decisions regarding investment and forms of distribution.

CP 8 Supervision

There is substantial non-compliance with provisions respecting the operational independence of the supervisor, the availability of proper resources and staff, the supervisor’s authority to impose fit-and-
proper tests of trustees and others, and the power to reject a proposed trustee or other person in a governance role.

(c) Overdue Contributions

PIA needs to take a long-term approach to addressing the problem of overdue contributions to pension funds in addition to its current effort to have these amounts computed (on an unaudited basis) by the fund managers for reporting and remediation. While the pending legislation will assist in that it will require accrual of interest and payment of penalties, this is not a long-term solution. (Note that this will, in any case, require the audit of the calculation of the accrued interest by PIA if it is not done by another auditor.) Implementation will certainly involve effecting changes in auditing practice but should also target strengthening the legislative requirements. At the next opportunity the legislation is opened for substantive changes, the feasibility of creating deemed trusts for due and unpaid contributions should be investigated. This will permit PIA to instruct employers to keep such amounts in trust accounts separate from their other accounts during the permitted delay in remittance period (which should be subject to strict limits). PIA would also be able to advise employers that their failure to comply with the deemed trust provision would expose the directors and officers to indictment for breach of trust.

Investment Concerns

Guidelines that seek to impose maximum and/or minimum portfolio limits on a pension fund should be subjugated to the practice of prudent portfolio management. Thus the guidelines should emphasize that trustees retain the duty to ensure that the portfolio is at all times maintained in a condition that is appropriate to the fund’s circumstances. This means, for example, that a minimum portfolio limit may be quite out of order in respect of some asset classes in the event the fund’s wind-up is apprehended. Similarly, a maximum limit on an asset class may be quite improper in terms of the fund’s obligation to manage risk in accordance with the needs or capacities of members. Where members in a scheme wish to minimize their risk (and their returns) this could conflict with one or more of the stated limits.

Another concern is the potential impact of an acceleration of the funding of the deficits in the PSPF and the LASF on the local capital markets. In order to avoid an unfortunate shock to asset prices, it may be necessary for the GOZ to invest such funds offshore and repatriate them as the demand for capital in Zambia grows.

The proposed amendments do not affect the provision authorizing the making of secured loans to affiliated employers provided these do not exceed 5% of the total assets of the fund. This policy will have to be amplified to ensure that such limit includes all secured loans to all related employers in order to limit the risk exposure to the failure of a group of connected companies or entities. Also, there will need to be elaboration of the nature of the eligible securities; presumably these will be restricted to GOZ issues.

Another matter concerns the need for and application of the so-called ‘10% limit’ which is a portfolio risk control that prevents excess exposure to the failure of a single entity (the total investment of the fund in any shares, debt securities or loans to a single entity should not exceed 10% of the portfolio). This issue assumes increased importance in view of the intention to allow up to 5% of the fund to be loaned to the employer. The application of the 10% limit in such a case
would restrict the investment of the fund in the shares of the employer (assuming it is listed) to 5% of the fund.

PIA should require specific disclosure of all related-party investing, including mortgage loans to members, in its quarterly returns and this information should be published in its annual report.

(d) Conversion of Multi-employer plans

PIA should research existing trust deeds to ascertain what provisions exist that would either facilitate or impede the withdrawal of the funds of affiliated schemes from the multi-employer trusts. Following that research, strategies for removing impediments should be devised and evaluated by PIA legal counsel having due regard for Trust Law in Zambia and any applicable precedent. If strategies that are efficient cannot be envisaged, a legislative resolution should be crafted for consideration at the earliest opportunity for presenting amendments. One possibility would be for the legislation to mandate resolution by binding arbitration with the PIA Board acting as arbitrator. However, consideration should also be given to the possibility of PIA making a regulation mandating such binding arbitration once the pending legislative amendments are passed. The framework for such an arbitration process is beyond the scope of this report. It must also be recalled that, irrespective of any such initiative, any outcome of an arbitration process could be appealed through the Courts.

(e) NPS and NAPSA

Although the consideration of the status of the NPS and NAPSA lies beyond the scope of the consultancy, the issue of placing the NPS and NAPSA under the supervision of PIA was raised during on-site discussions on several occasions. For example, it was mentioned by officials at the Ministry of Labour that the International Monetary Fund has offered such advice, although the details in that regard were not disclosed. It was also mentioned that the International Social Security Association was requested to provide an opinion on the subject; the details of that consultation were not disclosed.

It would seem that a useful discussion of such a recommendation would require some sort of agreement of what scope is intended by the proposed supervision of the NPS and NAPSA by PIA. PIA does not have the powers of Parliament, i.e. its capacities to effect change are limited in comparison. It is not obvious that the undisclosed expectations inherent in the proposal could be fulfilled by PIA in its current or proposed incarnations, particularly having regard for the significant number of international core supervisory principles in both pensions and insurance which, as previously mentioned, PIA is not currently in a position to meet.

In any case, the proposal would appear to require passing a special Act by the Parliament of Zambia that would amend relevant provisions of the National Pension Scheme Act and, concomitantly, amend the PSRA 1996 to repeal the current exemption and provide for the framework of that supervision, which might well need to be different from that currently contemplated by the PSRA 1996 for pension schemes.

However unlikely that may appear to be feasible in the near term, for the sake of further analysis, it is assumed that this approach could be pursued. Thus the question reduces to a consideration of what
ameliorative measures could be achieved by authorizing PIA to supervise the administration of the NPS by NAPSA in some fashion.

To address this issue would require a detailed comparison of the governance requirements currently applicable to the NPS and NAPSA and the authorities of the Board of NPS to address problems, with the provisions of the PSRA 1996, in order to ascertain what additional measures, if any, would be available to strengthen the administration of the NPS and/or improve its financial condition. While this is beyond the scope of this report, it is useful to note that the PSRA 1996 contemplates the de-registration of a pension scheme in the event it does not comply with the provisions of the legislation, and a scheme is not permitted to be managed if it has been de-registered, i.e. it must be terminated and wound-up. This general approach would not appear feasible in regard to the NPS which, as a national program, should probably only be terminated by elected persons, i.e. not by appointed persons.

It is recommended that PIA seek funding for a special investigation to be made by an international expert that would include a comprehensive feasibility study of the issues that would have to be addressed, and the options that should be evaluated, in order to permit a useful, value-added migration of the supervision of the NPS and NAPSA from the Ministry of Labour to PIA.

9. **Proposed Organisational Strategy & Business Plan**

To be an effective supervisor, PIA needs to embark on a number of actions aimed at building adequate and functional supervisory capacity. These actions may be categorized as follows:

(a) **Organisation**

- PIA has been operating as a semi-autonomous agency under the umbrella of the Ministry of Finance and National Planning. As discussed below, legislation currently under discussion is intended to clarify its independent status. At the same time, it appears that consideration is being given in some quarters to creating a new supervisory regime for Zambia that would integrate all aspects of financial sector supervision in a single agency. At the present time, the Bank of Zambia is responsible for the supervision of banks and certain non-bank financial institutions. One approach to achieve integration might be to transfer responsibility for supervision of private pension plans and insurance companies to the Bank of Zambia. This has been done with some success in other jurisdictions.

- At this stage, we have not been informed of the intention of the government and the Minister in respect of the plans for integrated supervision. **Accordingly, our deliberations have started from a presumption that there will not be a move to integrated supervision but and that PIA will become a truly independent supervisory authority.**

- At present, PIA is organized along institutional lines. In other words, separate teams of inspectors are engaged for (a) the supervision of private pension plans and (b) supervision of insurance companies. A copy of the current organisation chart is attached as Appendix Eleven.
One of the first steps undertaken by the current Registrar, shortly following his nomination, was to hold an off-site strategic planning session with senior staff of PIA. As a result of this strategic planning exercise, PIA has been giving consideration to a re-structuring along functional lines. In other words, while there would be a number of specialist positions, such as that of research actuary and IT specialist, the inspection staff would be a single team, with responsibility for all types of institution supervised by PIA. A copy of a proposed organisation chart that would give effect to this new structure is attached as Appendix Twelve.

PIA should frame a strategy for managing its supervision of the insurance and pensions industries in such a way that it maximizes its engagement of the key stakeholders. This may well pose a challenge in terms of its intention to structure its affairs along functional lines rather than by industry. The management of the communications process (which essentially includes all directives, guidelines, advisory committees, web-site postings, newspaper insertions, brochures, publications and the annual report) should be a high priority and will require the involvement of staffers that are knowledgeable and experienced in matters relating to pension schemes and insurance companies. Thus, PIA will have to have a clear delineation of how its communications will be structured. The same sorts of comments will apply to other functions – most will have industry-specific components that will require specialist support in order for them to be efficiently and effectively carried out.

PIA’s Business Plan should be based on the outputs of the risk-based assessment of the supervised entities. This is where PIA must clearly establish its priorities and focus on increased numbers of inspections supported by comprehensive analyses of its data. Also to be given priority is increased training of staff, especially in the technical areas of analysis and inspection. The training effort should parallel the preparation of industry-specific reference and operational procedures manuals. These activities must be supported by the issue of regulations, industry guidelines, and directives that will serve as sets of minimum standards for the supervised entities. The revision and re-structuring of the annual report will also support the achievement of the Business Plan objectives as it will feature regular progress reports in that regard in addition to the other new material to be brought to the attention of stakeholders.

The Business Plan should be multi-year with specific milestones and completion dates defined for each of the priorities.

(b) Legal Instruments

Proposed amendments to the current pensions legislation seek to establish the status of PIA as an independent and autonomous supervisory agency, although the amendments proposed are less effective in this regard than would a special Act of Parliament enacted for the express purpose of the creation of PIA. In addition, PIA will be able to levy assessments on the insurance companies and private pension plans that it supervises. This is expected to provide all the resources it will need to perform its duties.

The current legislation equips PIA with an impressive list of supervisory powers that it may employ in discharging its mandate. However the Authority has not taken advantage of all the powers available to it.

Legislation authorizes the Minister to make regulations or to prescribe rules in a number of key areas, such as valuation of assets and valuation of liabilities. Likewise, the Registrar has authority
to issue guidelines in a number of areas. **However, many of the statutory instruments that are in common use by supervisory authorities have yet to be created.**

- In order to function as an effective supervisory organisation, PIA must take whatever steps are necessary to put in place a complete regulatory system that gives full effect to the powers, regulations and guidelines just mentioned. PIA will need assistance in developing these supervisory tools for the Zambian markets, and **staff will need instruction and coaching in their effective application.**

(c) **Human Resources**

- PIA should be empowered to have an adequate number of supervisory staff and key professionals in the various areas of its responsibilities. This would mean providing it with the required budget to hire and equip them through a sustained program of education and training; and remunerating them at par with their counterparts in other supervisory agencies in the financial sector and indeed the supervised markets. Otherwise, it would be difficult for PIA to retain key staff who may otherwise be attracted to other institutions.

- Specialist positions will be required in the area of research actuary and information technology. While there is a scarcity of actuaries in Zambia, it should be possible for PIA to recruit mathematics graduates and to encourage them to pursue studies in actuarial science.

- Supervisory personnel for insurance inspections and analysis work should have qualifications such as the FIIC. Students can be encouraged to pursue this designation. Likewise, suitable pension administration credentials should also be sought.

(d) **Computerization**

- Development of an IT strategy. PIA will likely want to ensure that all of its personnel have access to the latest technology. There should be tools for inter-office communication and it is expected that plans would call for an integrated database of information on supervised institutions to which all would have access. PIA will need advice on the construction of an appropriate strategy. In many cases, they will be able to purchase off-the-shelf software.

- Computers, servers and laptops necessary to support the system designed will have to be acquired.

- IT Training will have to be provided to existing and new staff as circumstances dictate.

(e) **Education and training**

- PIA should secure membership in both the IAIS and INPRS at the earliest possible opportunity. This will provide access to a rich collection of information and training material.

- Budget of PIA must be designed so as to ensure appropriate training can be delivered. See later section with details on training along following lines:
  - Long term education strategy
  - Regular short period workshops
  - Participation at various relevant international conferences and meetings
- Overseas visits and attachments

(f) Developing Operations Manuals

- PIA will need to develop procedures manuals in many areas in order to ensure consistent and effective application of supervisory activities.

- Procedures Manuals for such fundamental activities as licensing, inspection and desk analysis are needed forthwith.

- Inspection work would be facilitated and consistency ensured if a “working paper” approach were adopted in order to facilitate the conduct and documentation of inspection findings.

- PIA should consider the development of guidelines for policy research and market development.

- In the new structure, PIA will be a revenue-gathering agency and will be responsible for collecting levies and controlling funds. PIA will be obliged to develop financial regulations for PIA finance and corporate services.

(g) Guidelines and Directives for the Industry

- PIA will be obliged to develop and implement directives for key issues covered in the legislation.

- One important example will be the production of guidelines for market conduct and cooperation issues.

- Develop discussion forum with industry

(h) Advertising: Education and Public Image

- PIA could consider enhancing the public image of the private contractual savings industries through a public relations campaign.

- In one example, the supervisor in another country achieved this objective by persuading private companies to allocate a portion of their budget to finance the cost of an advertising and public education campaign.

- Develop education and information programs

- Promote public image of contractual savings institutions and their social responsibility

(i) Financing through Levy on Industry

- Under proposed legislation, PIA will be able to cover its costs of operation by assessing a levy on supervised entities.

- In order to ensure that such a system functions effectively, PIA will have to develop an effective annual budgeting exercise. This will involve the preparation of a budget in advance of the start of the fiscal year, and its approval at some level – certainly by the PIA Board but perhaps also by
the Minister.

- In each subsequent year, PIA will be obliged to present a statement of accounts for the year just concluded, indicating among other things any significant departure from budget. These accounts should be available for review by trade representatives of the supervised institutions or their trade associations.

- Annual levy for any year should be based on the budget estimates.

- PIA will be expected to devise methods of distribution of the costs reflected in the budget among the 3 types of entities that it supervises – insurance companies, pension funds and brokers.

- PIA will have to choose factors and a basis for the levy system that is, and is perceived to be, equitable for all participants in the target group

- System of levies will need to approved by the Board of PIA.

(j) **Appointment of Resident Advisor(s)**

The challenges facing PIA are significant and the work plan outlined above is considerable. A review of the present style of operation of the Authority suggests that staff are obliged to devote time to various non-supervisory activities that take time away from the work of supervising companies. To the extent possible, PIA should take steps to minimize time spent on non-supervisory activities. Priority should be assigned to the work of supervision such that, for example, each insurance company would be the object of an on-site inspection each year.

In order to re-focus the efforts of staff and to ensure that priorities are assigned and strictly observed, it is proposed that one or two resident advisors be retained for PIA. It may be necessary to have one such advisor for each of the principal units – private pension funds and insurance companies. However if a person could be located who could provide appropriate guidance and leadership in both fields that would be a more effective solution. The individual(s) chosen should have a through knowledge of the industries concerned and of the issues involved when supervising them. He/she would provide leadership in developing all the work tools described elsewhere in this paper as well as advising the staff in best practices of supervision, both on-site and off-site. Terms of Reference follow.

(i) **Terms of reference for Resident Advisor:**

**Republic of Zambia**

**FIRST INITIATIVE**

PENSIONS AND INSURANCE AUTHORITY; PROFESSIONAL ADVISOR

FIRST Support to Strengthening of Supervisory Capacity of PIA

1. Under the terms of a Financial Sector Development Program (FSDP), Zambia is seeking to reform and strengthen the regulatory/supervisory system for financial institutions. FIRST has agreed
to provide financial assistance to help PIA to carry out the reforms that it must undertake in order to ensure that the supervision of insurance and pensions is brought into conformity with international standards and best practices.

Background

2. According to the FSDP, there is a need for harmonization of the various pieces of legislation that govern the pensions and insurance industry in Zambia. The insurance legislation is inadequate and does not conform to the expectations of the core principles of the International Association of Insurance Supervisors. The Contractual Savings Working Group of FSDP also identified a need for capacity-building at PIA.

3. There are 9 insurance companies operating in Zambia, 8 of which are privately owned and the other is state-owned, Zambia State Insurance Corporation. The industry is small with total premiums of US$ 57 million for 2003. This volume of premium represents only 1.2% of GDP, a fairly low rate of insurance penetration, even for an African country.

4. PIA supervises 215 pension schemes, of which 30 are defined benefit schemes. The DB schemes are very important and 80% of active members of pension schemes are in DB plans. Pension assets amounted to approximately US$ 170 million at the end of 2003.

6. PIA has been operating since 1997. However some aspects of its supervisory system have not yet been fully developed. Although it has begun to conduct on-site inspections of insurance companies and pension plans, it has not yet put into place the review and analysis mechanisms that are essential to effective supervision. While most of the insurance companies are visited at least once per year, resources permit the inspection of only a small fraction of the private pension plans each year. The staff members involved with the work of supervision are young and enthusiastic, yet they lack experience in supervision and most have no experience in the operations of financial institutions.

7. PIA lacks the resources that it requires if it is to perform all the functions that are expected of an effective modern supervisory agency under prevailing international standards. It also lacks autonomy and is effectively an agency of the Ministry of Finance. Legislation currently being considered by Parliament will, if adopted, provide PIA with a considerable level of autonomy and will also enable it to obtain financing for its operations through a levy or assessment collected from all licensed institutions.

Objective

8. The objective of this technical assistance is to assist PIA to carry out the reforms that it requires and to help to put into place a comprehensive supervisory system that conforms to international standards. It is expected that the role of the advisor will be that of guide as the staff of PIA design and carry out the necessary reforms themselves.

Activities

9. The consultant will provide close support to the Registrar and staff of PIA and will provide assistance in implementation of the FSDP. The following specific activities are contemplated:
• Organize and deliver a special intensive training program. The plan contemplates a two-week concentrated course that will provide all members of the supervisory team with a better understanding of their responsibilities as financial sector supervisors, as well as a more complete understanding of risk based supervision.

• Assist with the development of a system of levies or assessments to be paid by licensed institutions. The process will require the development of a budgeting process as well as a program for determining, collecting and accounting for the contribution to be made by each licensed institution.

• Organize study tours for key personnel who will visit other important supervisory agencies in the region. The consultant will assist the Registrar in identifying the suitable candidates to take part in these tours. The objective should be a “train the trainers” approach.

• Develop supervisory guidelines to be applied to all licensed institutions. The present legislation does not include all the necessary regulatory and supervisory requirements that are necessary in order to conform to best international practices. Since it is unlikely that legislative changes can be achieved in the near future, guidelines will be prepared and circulated as an intermediate step and companies will be expected to comply.

• The consultant will assist with the preparation of procedures manuals for such supervisory activities as on-site inspection; desk analysis and review of actuarial reports. The consultant will work with the staff in the development of these procedures and the manuals that document them and will conduct training sessions to ensure their proper implementation.

• The consultant will assist with the development of position descriptions for all professional positions within PIA. There would also be advantages to having the consultant assist with the actual recruiting, in terms or providing input to the PIA Board and senior management, thus enabling PIA to benefit from the consultant’s significant experience in this area.

Schedules

7. This technical assistance is estimated to require 30 staff weeks, and should be completed by December 31, 2006. It is expected that the consultant would be on-site in the offices of PIA for an initial period of up to 2 months and that subsequent work would involve monthly visits of short duration. An important milestone will be the passage of the amendments to the legislation that are currently under discussion. If passed, these amendments will provide PIA with the status of an autonomous institution with authority to raise its own financing through a system of levies.

Outputs

8. The following outputs are expected:

• Deliver intensive two-week training course.

• Organize and deliver study tours for selected staff members
• Develop supervisory procedures and produce manuals to document them
• Draft guidelines to which licensed institutions must conform
• System of budgeting and assessment established and operating
• Revised organization chart and position descriptions

(k) Training

(i) Long-term education and training strategy

Select professional bodies, specialist centres, certification courses.

Budget: attached

(ii) Attachments and Study Tours

Much progress has been made by supervisors in the region from whom PIA executives could learn and share experience. Countries such as South Africa, Kenya, Mauritius, etc. have provided training for senior staff of other supervisory authorities and should be considered for this purpose.

Budget: attached

(iii) Short-term training Strategy

We propose a specialized series of workshops for PIA during which sessions on Insurance and Pensions would be presented on-site in Lusaka over 2 weeks on selected topics that focus on key areas where a high level of mastery of the topics will enhance the performance of PIA in planning and implementation of a functional supervisory regime.

Owing to the continuing interest of the Ministry of Labour in the work of supervision being performed by PIA, it is the opinion of the Registrar that participation in these on-site training courses should be made available to designated members of the staff within MOL. The ideal candidates might be those persons with responsibility for monitoring social security programs.

PIA could also extend a goodwill gesture by inviting appropriate industry executives to participate in the training workshop. Industry executives that have the same level of understanding of key supervisory issues will be appreciative of and cooperative with PIA in its supervisory tasks which aim at the following three tasks.

(1) ensuring enforcement of the insurance and other national laws,
(2) verifying that the industry is adequately meeting its contractual obligations to clients, and
(3) ensuring that the industry is functioning in harmony with a high standard of competition and good governance that enable it to achieve stability and growth.

The following workshop topics have been suggested for the consideration of PIA, and other topics may be added:
- IAIS core principles
- On-site inspection
- Insurers’ technical accounts: (solvency, reserving, reinsurance, etc.)
- Effective financial reporting
- Corporate governance multi-tier - PIA, industry, intermediaries
- Reading financial statements of insurance companies

Occupational Pension Schemes: the following are examples of sessions that could be provided:

- INPRS Core Principles
- Governance of Occupational Pension Schemes and Service Providers
- Defined Benefit Pension Scheme Funding: Concepts, Practice & Regulation
- Actuarial Topics related to Pension Scheme Funding and Solvency: a series of training sessions intended to familiarize participants with the technical essentials of the actuarial aspects of pension scheme operations
- Defined Contribution Pension Scheme Issues and Supervision
- Pension Scheme Financial Reporting
- Analysis of Pension Scheme Auditors’ Reports
- Analysis of Pension Scheme Actuarial Reports
- Risk Based Supervision of Pension Schemes
- Structure and Conduct of Pension Scheme Inspection
- Supervisory Strategies for Dealing with Non-Compliant Schemes, Fines and Other Sanctions
- Portability and Annuitization of Retirement Benefits
- Termination and Wind-Up of Pension Schemes

Budget: attached

(I) Information Systems

PIA needs software and training to gather and process information to enable it to produce reports and monitor performance of the supervised entities. Computerisation strategy for PIA could be divided into the following headings:

1. Computerising the day to day administrative, inspection and secretarial activities with off the shelf Microsoft Office. These could also be used to generate follow up.
2. Computerising the accounting activities of PIA using basic accounting packages handling general ledger and receivables management. This would be important to administer PIA budget, levy, and operating accounts. These cost around $3000 including installation and training.
3. Custom designed software to process and consolidate the statutory technical and financial accounts that supervised institutions submit in prescribed format at periodic intervals as well as through their audited accounts. Software packages of this type are usually expensive (Upwards of $50,000). Alternatively, PIA could retain local consultants to assist it in developing in-house tools. This approach would make use of readily available programs such as Access and EXCEL and we estimate the additional cost for the work of the local consultants at around $10,000. The same software could likely also be used to devise various tools of analysis including alerts on the market place.

Budget: attached
(m) **Directives/Manuals/TOR**

Assuming that PIA is empowered through a budget that would enable it to recruit, equip and maintain an optimum number of professionals, it would need to develop directives, manuals and terms of reference that would make its services transparent and effective. These tools should be supported by the laws and practices in place as well as by understandings among the different interest groups, i.e. the consumers, the players and the public interest.

These supervisory tools require a thorough understanding of the laws of the land and mastery of the market place, and PIA may require external consultancy assistance in formulating a number of these tools. A brief description of these tools is given below.

**Insurance Sector:**

1. Best practices in Corporate Governance
2. IAIS core principles methodology
3. On-site inspection Manuals
4. Guidelines on desk Analysis and follow ups
5. Report forms for statutory returns
6. Risk based Supervision
7. Analysis of Financial Statements
8. Investment Analysis
9. Co-insurance
10. Uncollected Premiums/ Credit Policy
11. Reinsurance
12. Broker-Insurers Relations
13. Administration of Fidelity Bond
15. Associations: Self-regulation and Code of Conduct
16. Arbitration Committee
17. Premium trust accounts
18. Break up of composite insurers
19. Minimum Continuing Capital Surplus
20. Claims Reserves: o/s claims, IBNR, Special Reserves, Statutory Reserves
21. Premium Reserves: Unearned Premiums
22. Solvency calculations
23. Companies in difficulty and insolvencies
24. Motor guarantee fund
25. Valuation of Assets
26. Insurance levy
27. Internal documents (Job descriptions, Financial Regulations, etc)
Looking specifically at Pensions:

Items 1-8, 14, 25, 27 above and the following:
Trustee performance guidelines
Pension scheme administration functions
Liquidity analysis
Administrative controls
Approval of constituting documents
Approval of amendments
Meetings of members, due process issues
Contribution holidays
Surplus refunds
Member complaints and inquiries

Budget: attached

(n) Training Sessions delivered during mission

- Three training sessions of approximately 2.5 hours duration each were conducted on site during the mission:

Theme 1: Regulation and the Insurance Industry - an overview

Theme 2: Insurance Companies (Introduction to Risk-Based Supervision; process of on-site supervision; the concept of the Regulatory Ladder)

Theme 3: Private Pension Plans (Introduction to Risk-Based Supervision; corporate governance; financial reporting; special topics)

- Core Principles Assessment: Interactive training sessions were held to assist PIA with self-assessment of its observance of the Core Principles of IAIS and INPRS. Mission members worked with the inspection teams for each of the Pensions and Insurance units. These programs were delivered over a period of approximately 1.5 days each.

(o) Budget for technical assistance projects

(i) Education and Training Budget in US dollars

<table>
<thead>
<tr>
<th>Main header</th>
<th>Sub-header</th>
<th>Specific Programme</th>
<th>Provider</th>
<th>Number</th>
<th>Unit Cost</th>
<th>Duration</th>
<th>Total Cost</th>
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<tbody>
<tr>
<td>10.1 Long-term Education and Training</td>
<td>Long distance education</td>
<td>Private pensions supervision</td>
<td>WB USA</td>
<td>2</td>
<td>7,000</td>
<td>1 week</td>
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<td></td>
<td>Long distance</td>
<td>Associate, IA</td>
<td>IA UK</td>
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<td>22,200</td>
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<tr>
<td></td>
<td>Long distance</td>
<td>Associate, PMI UK</td>
<td>3</td>
<td>22,200</td>
<td>4 years</td>
<td>66,600</td>
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<tr>
<td>Main header</td>
<td>Sub-header</td>
<td>Specific Programme</td>
<td>Provider</td>
<td>Number</td>
<td>Unit Cost</td>
<td>Duration</td>
<td>Total Cost</td>
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</tr>
<tr>
<td>Long distance</td>
<td>PMI</td>
<td>Associate, CII</td>
<td>IISA, RSA</td>
<td>3</td>
<td>10,000</td>
<td>4 years</td>
<td>30,000</td>
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<tr>
<td>Short courses</td>
<td>Auditing</td>
<td>IISA, RSA</td>
<td>Esami ZM</td>
<td>2</td>
<td>10,000</td>
<td>4 weeks</td>
<td>20,000</td>
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<tr>
<td>Short course</td>
<td>Access, Office Management</td>
<td>Mauritius, S. Africa, Kenya, etc</td>
<td>Esami ZM</td>
<td>2</td>
<td>10,000</td>
<td>4 weeks</td>
<td>20,000</td>
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<tr>
<td>10.2 Study Tours</td>
<td>Up to 2 weeks per supervisor</td>
<td>Attachments to supervisory offices</td>
<td>Mauritius, S. Africa, Kenya, etc</td>
<td>5</td>
<td>4,000</td>
<td></td>
<td>20,000</td>
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<td>10.3 Short-term Training Workshop</td>
<td>Specialised workshops</td>
<td>6 topics on Insurance</td>
<td>2 speakers</td>
<td>10,000</td>
<td>2 weeks</td>
<td></td>
<td>20,000</td>
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<td></td>
<td>Specialised workshops</td>
<td>10 topics on Pensions</td>
<td>various</td>
<td>2</td>
<td>15,000</td>
<td>3 weeks</td>
<td>30,000</td>
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<td>10.4 Resident Consultants</td>
<td>Fixed-term Advisors</td>
<td>1 in Pensions, 1 in Insurance</td>
<td>Various</td>
<td>2</td>
<td>10,000</td>
<td>9 months</td>
<td>180,000</td>
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<td>10.5 Toronto Centre</td>
<td>Leadership Course for Supervisors</td>
<td>Intended for heads of supervision</td>
<td>Toronto Centre</td>
<td>1</td>
<td>10,000</td>
<td>1 week</td>
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(ii) Information Systems Budget in US dollars

<table>
<thead>
<tr>
<th>Main header</th>
<th>Sub-header</th>
<th>Specific Programme</th>
<th>Provider</th>
<th>Description</th>
<th>Unit Cost</th>
<th>Duration</th>
<th>Total Cost</th>
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<tr>
<td>Information Systems</td>
<td>Administrative</td>
<td>Training of existing clerical and secretarial staff</td>
<td>Local</td>
<td>5 people</td>
<td>500</td>
<td>3 months</td>
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<td></td>
<td></td>
<td>Acquisition of general ledger with receivables management</td>
<td>ACPAC or Microsof</td>
<td>5 user suite</td>
<td>5,000</td>
<td></td>
<td>5,000</td>
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<tr>
<td>Accounting</td>
<td></td>
<td>Training of 3 users and &amp; 3 inquirers</td>
<td>Internat. tender</td>
<td>7 User</td>
<td>75,000</td>
<td></td>
<td>75,000</td>
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<tr>
<td>Insurance Supervision</td>
<td>Acquisition &amp; installation of Insurance supervision pack</td>
<td>Internat. tender</td>
<td>7 User</td>
<td>75,000</td>
<td>75,000</td>
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<td></td>
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<tr>
<td></td>
<td></td>
<td>Training on Insurance pack</td>
<td>Internat. tender</td>
<td>7 User</td>
<td>15,000</td>
<td></td>
<td>15,000</td>
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<tr>
<td>Pensions Supervision</td>
<td>Acquisition &amp; installation of Pensions supervision pack</td>
<td>Internat. tender</td>
<td>7 User</td>
<td>75,000</td>
<td>75,000</td>
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<td></td>
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<tr>
<td></td>
<td></td>
<td>Training on Pensions pack</td>
<td>Internat. tender</td>
<td>7 User</td>
<td>15,000</td>
<td></td>
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<tr>
<td>Hardware</td>
<td>Network Server with Backup</td>
<td>HP/IBM</td>
<td>8,500</td>
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<td></td>
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<td>8,500</td>
</tr>
<tr>
<td></td>
<td>Laptop/Workstations</td>
<td>HP/IBM</td>
<td>6</td>
<td>1,500</td>
<td></td>
<td></td>
<td>9,000</td>
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**Total:** 477,200

**Total:** 208,500
## (iii) Legislative Review
### Budget in US dollars

<table>
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<tr>
<th>Main header</th>
<th>Sub-header</th>
<th>Specific Programme</th>
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<th>Description</th>
<th>Unit Cost</th>
<th>Duration</th>
<th>Total Cost</th>
<th>To be completed</th>
</tr>
</thead>
<tbody>
<tr>
<td>10.3 Insurance</td>
<td>Directive, Manuals and Terms of reference</td>
<td>Review legislative provisions and PIA needs, draft documents and discuss and finalize each document; conduct training on application of DMT’s</td>
<td>International Consultant</td>
<td>27 documents</td>
<td>2,500</td>
<td>3 months</td>
<td>67,500</td>
<td>Mid 2006</td>
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<tr>
<td>10.3 Pensions</td>
<td>Directive, Manuals and Terms of reference</td>
<td>Review legislative provisions and PIA needs, draft documents and discuss and finalize each document; conduct training on application of DMT’s</td>
<td>International Consultant</td>
<td>25 documents</td>
<td>2,500</td>
<td>3 months</td>
<td>62,500</td>
<td>Mid 2006</td>
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<tr>
<td>10.4 Legislative Review</td>
<td>Pensions</td>
<td>Full review of the Pensions Act, harmonize with other acts in the financial sector and also with Pensions acts in the sub-region, especially COMESA</td>
<td>Zambian Legal Consultant</td>
<td>Draft Bill with related directives</td>
<td>20,000</td>
<td>3 months</td>
<td>20,00</td>
<td>2 – 3 years</td>
</tr>
<tr>
<td>10.4 Legislative Review</td>
<td>Insurance</td>
<td>Full review of the Insurance Act, harmonize with other acts in the financial sector and also with Insurance legislation in the sub-region, especially COMESA</td>
<td>Zambian Legal Consultant</td>
<td>Draft Bill with related directives</td>
<td>20,000</td>
<td>3 months</td>
<td>20,00</td>
<td>2 – 3 years</td>
</tr>
<tr>
<td>10.4 Legislative Review</td>
<td>PIA Act</td>
<td>Draft a separate act for PIA as an autonomous institution, with comparable rights and responsibilities with other agencies in the financial sector</td>
<td>Zambian Legal Consultant</td>
<td>Draft Bill with levy details</td>
<td>5,000</td>
<td>1 month</td>
<td>5,000</td>
<td>2 – 3 years</td>
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</table>

**Total:** 175,000
10. Proposed Sequence for Follow-Up Actions

Recommendations contained in this report cover many topics. In order to provide a focus for follow-up action, the following sequence of actions is proposed:

(a) Retention of Resident Advisor(s).

The present staff of PIA are obliged to cope with numerous inquiries from government officials, brokers and the public. In addition, most professional staff members serve on one or more of the various sub-committees established under the FSDP. While this is important work and should not be neglected, all of these activities will get in the way of the discharge of the basic duty to supervise the contractual savings institutions.

We hope that a Resident Advisor would serve as a catalyst to mobilize the efforts needed to make all the necessary reforms facing PIA. While the advisor will be expected to contribute in a hands-on way to the drafting of documents and work instruments and to the training of staff in best practices of supervision, the advisor can also play a critical role in setting a schedule for the work of reform and for ensuring that the timetable is maintained.

(b) Amendments to Legislation.

While the draft bills now being considered by Parliament do not provide for all the amendments that are needed to bring the standard of supervision up to date with best international practices, they do represent two very important steps forward. The drafts will, first, establish PIA as an independent agency with legal standing, and second, provide the authority for a levy on the supervised entities. The revenue from this levy should enable PIA to acquire the resources, both human and technical, that it lacks. It should be possible, over time, to gradually improve the compensation of staff to competitive levels in order to ensure retention of the most desirable people. Resources should be adequate to provide the training needs of PIA in the medium and longer term. (Short term training requirements should be sought from other sources, such as FIRST.)

As a matter of early priority, the Resident Advisor could assist PIA in establishing the proper base for assessment and by proposing an acceptable rate of assessment. The work will require collaboration with industry players and the design of appropriate procedures and documentation for determining the assessments and then collecting them.

PIA should secure membership in both INPRS and IAIS.

(c) Strengthening the regulatory system.

In the near term, following the amendments to the legislation that are currently under discussion, it is unlikely that any further progress can be made in revising legislation. Parliament’s appetite for insurance and pensions legislation is likely to cool, especially in light of the general elections expected for 2006.

PIA, under the leadership of the Registrar, and with the assistance of the Resident Advisor, should begin to fill the regulatory gaps by issuing the various Regulations, prescribed rules and directives that are authorized by the current legislation but have never been promulgated. For example, insurance supervision is not likely to be effective in the absence of a practical
system for solvency measurement. To continue with the insurance example, regulations must be issued that provide rules for valuation of assets, valuation of liabilities, and the formula for calculating the solvency margin. Important matters for pension supervision relate to the conversion of multi-employer plans and the problem of outstanding contributions that many schemes are facing today.

Much of this can be accomplished within the powers available to the Minister and the Registrar under the existing legislation. The report lists other areas where improvements may be required.

(d) Training.

Arrangements can be made to begin the training of supervisory staff. The report includes the following proposal “We propose a specialized series of workshops for PIA during which sessions on Insurance and Pensions would be presented on-site in Lusaka over 2 weeks on selected topics that focus on key areas where a high level of mastery of the topics will enhance the performance of PIA in planning and implementation of a functional supervisory regime.” This would be an excellent first initiative to launch the training program.

Attachments and study tours to offices of other supervisors in the region would be another measure to introduce at this stage.

(e) Information Systems.

The upgrading of information systems at PIA will have to be accomplished over the medium term (one or two years). While it is a straightforward matter to purchase additional equipment and publicly available software, the introduction of new requirements for financial reporting and general data gathering will have to be coordinated with the supervised industries as they will be expected to adjust their systems in order to produce the required information. At the same time, development of actual supervisory tools and test ratios as well as training of PIA staff in their use will also take some time.

An essential part of this undertaking will be the development of new reporting forms for use by supervised entities. This effort should be directed by the Resident Advisor.

(f) Corporate Governance.

The improvement of corporate governance requirements and practices in Zambia is a significant concern of the FSDP. Adoption of modern best practices in this area will require changes to many pieces of legislation as well as publication of guidelines by organizations such as BOZ and PIA along with the adoption of codes of good conduct by industry trade associations. PIA has the power under its existing legislation to issue guidelines of all kinds. It could use this power to begin to move the industries that it supervises in the direction of improved corporate governance. However final results in this regard can not be expected to be achieved in the short term.

(g) Compulsory Motor TPL Insurance.

Consultants should be retained to assist PIA in developing an uninsured motorist fund to help indemnify persons injured in an accident where the guilty driver is either not insured or can
not be identified. It may also be helpful to establish a special pool for the insurance of high risk drivers whose safety record causes most companies to deny them coverage. Another legislative amendment that could be of assistance in Zambia would be the creation of a set of indemnity limits through the legislation that would specify the amount of benefit that would be paid to an injured party depending on the nature of the injury.

(h) Preparation of amendments to legislation.

In the medium term it is to be expected that PIA will have another opportunity to introduce the changes that are required to bring the pensions and insurance legislation into line with international best practices. Once PIA has developed the guidelines and directives discussed earlier it should have the raw material to begin drafting the necessary changes to the legislation. The work of drafting and consultation could begin as soon as possible to make use of the advice of the Resident Advisor and to ensure that affected parties (insurance companies, pension funds, brokers) will have ample time to make their views known before any new bills enter the parliamentary process.

(i) Plans for the Supervision of NAPSA.

There are many references in the FSDP report to the need for regulation/supervision of the NPS system by an independent authority. Since PIA has been made responsible for the supervision of private pension plans and also, apparently, the LASF and PSPF schemes, some observers have presumed that PIA is the logical candidate for supervision of NAPSA. Such a perception loses sight of the nature of supervision of private pension plans, not to mention the very limited resources of PIA. In the supervision of private plans, PIA or any pension plan supervisory agency, grants a license to a pension plan so long as it meets certain criteria. In the event the plan fails or ceases to meet the conditions, PIA is authorized to withdraw the license. In such a case the plan is terminated and arrangements are made for protecting the accrued rights of plan members that were acquired before the termination. It should be obvious that this process of disciplining the plan (and indirectly its sponsors) would be neither appropriate nor workable for a national scheme, such as NAPSA, where participation is mandatory and where the government stands behind the funding of the scheme, prepared to cover any deficits.

Supervision or oversight of national pension schemes has been accomplished in a variety of ways in other countries. There are usually three parts:

- **Review of the adequacy of funding.** This is the responsibility of a qualified actuary. In some countries a senior public service position is created for the Chief Actuary who reports to Parliament on the condition of the plan.

- **Establishment and enforcement of investment guidelines.** One approach to achieving this objective is to establish an investment board for NAPSA. This board should be made up of competent business representatives and be independent of government. The board would be responsible for developing an investment policy for the NAPSA assets and for ensuring that the persons who manage these investments adhere to the policy. Reports of the Board would also be public, likely tabled with Parliament.

- **Internal controls over the administration of NAPSA.** National schemes must employ substantial staff in order to administer their operations, especially in light of the need...
to serve employers and workers in all parts of the country. The auditor general could be charged with the responsibility for oversight of the efficient and effective operations of an organization like NAPSA. One important aspect of controls relates to overseeing the collection of contributions by employers and their prompt remission to NAPSA. Delinquent employers should perhaps be reported in the media.

- The FSDP report recommends that a feasibility study be authorized into the possible ways that Zambia can obtain the degree of assurance that it needs over the operations of NAPSA. Any such feasibility study should recommend an approach that Zambia may adopt in order to meet the expectations with respect to supervision of NAPSA. The report also makes the point that it would likely be preferable that the solution that is ultimately adopted for supervision of NAPSA be applied equally to LASF and PSPF.

(j) The Pensions and Insurance Authority

(i) 4.1 Statutory Authority

The office of the Registrar of Pensions and Insurance was established by the Pension Scheme Regulation Act no.28 of 1996. The Insurance Act no. 27 of 1997 makes no mention of the supervisory authority. The Pensions and Insurance Authority was not established with distinct legal personality as is the case with the Bank of Zambia. Based on section 4 of the Pensions Act, the Minister of Finance appointed the first Registrar of Pensions and Insurance in April 1997. Through custom and practice, the office has come to be identified as the Pensions and Insurance Authority (PIA). No documentation was found on the change of name or the creation of PIA.

Section 104 of the Insurance Act 1997 authorized the Minister to establish an Insurance Advisory Council; likewise Section 106 of the Insurance Act 1997 authorized the Minister to establish a Policy Holder Protection Board. Until the appointment of the incumbent Registrar, neither the Council nor the Board was established. Within the last year, the Advisory Council has been named and it has met on a number of occasions. The Registrar had arranged for a special industry task force, called the Advisory Task Force on Premium Rates, to make recommendations regarding minimum standards for pricing of insurance products. The report on this topic is currently being considered by the Advisory Council. Nominees have been identified for the Policy Holder Protection Board but the board has not yet been convened.

PIA began reviewing and partially enforcing the two Acts on Pensions and Insurance in 1998 with the aim of achieving internationally accepted best practices in supervision. It is the conclusion of the mission that PIA has not been provided with adequate means, human and financial, to carry out its mission. The Government of Zambia seems to be appreciative of the various shortcomings in the provisions of the two Acts in force, as the state of insurance and pensions regulation and supervision has been a key point for discussion and consideration under the following initiatives:

- The 2002 Financial Sector Assessment Program (Report of the World Bank/IMF),
- The 2004 Financial Sector Development Plan of the Government of Zambia,
- The DFID/SIDA Project.
- The draft bills currently in Parliament amending the above-mentioned 2 Acts.
(ii) Organisation

(1) Board of Directors:

Although the office of the Registrar was created under the Pensions Schemes Regulation Act No. 28 of 1996 (PSRA 1996), no board was created to oversee the administration and operation of the office. This seems to be an oversight by the body that drafted the Act, and provision has been inserted in the proposed pensions amendment of 2005, section 6 creating a board that does not specify representation of the pensions and insurance industry, while naming other institutions. Two unspecified members are to be named by the Minister of Finance, and for the sake of transparency, it would be worthwhile to specify representation of the pensions and insurance sector.

(2) Management:

The PSRA 1996 provided for a Registrar assisted by 2 deputies, one each for pensions and insurance. Reporting to each deputy is one senior inspector and 2 inspectors. Other functions cover legal, finance and administration.

(3) Human Resources

As a result of the limited resources of PIA, it is understaffed. Staff remuneration does not compare well with that offered by other regulatory bodies. Although significant improvements were made within the past year, the situation is such that there has been high staff turnover. For PIA to function satisfactorily, it needs to be empowered with an adequate budget that would allow it to hire and retain key professional staff.

This would mean affording it the required budget to hire and equip them through a sustained program of education and training; and remunerating them at par with their counterparts in other supervisory agencies in the financial sector and indeed the supervised markets. Otherwise, it would be difficult for PIA to retain key staff who may otherwise be attracted to other institutions.

(4) Funding

The proposed Pension Scheme Regulation (Amendment) Act 2005, section 24, provides for a levy on pension funds and insurance companies, the level and rate of the levy to be determined by the Board. It is a generally agreed principle world-wide that the budget of authorities that supervise financial institutions be funded by contributions from the supervised entities. In countries that have adopted such an approach, contributions are usually arrived at after taking into consideration the budgetary needs of the supervisory authority as well as the financial means of the industry and other factors, e.g. inflation. In this regard, the supervisory authority would design the realistic budget it requires to administer its statutory tasks, and submit this budget to its Board for approval. Good governance requires that public agencies be accountable to the bodies funding their expenses; and that the funding bodies be represented on the Board deciding on the income, expenditure and work plan.

The stakeholder meeting held on September 29, 2005 discussed the plans for operation of the levy system in Zambia. There was general consensus in favour of PIA being financed in this manner but strong views were expressed to the effect that the structure should include a cap on the levy formula that would put a ceiling on the rate (e.g. in respect of pension funds, the ‘x’% applied to net assets – there seemed to be a consensus that this would be a suitable base – could not exceed some fixed %,
say ‘k’ %, irrespective of operational requirements or other considerations), and subject to a further limit expressed as say, ‘c’ ZK per member.

It should be noted that there was no mention made of any arbitrary cap on the levy being considered in respect of the insurance supervision program. In most countries, the levy on insurance companies is expressed as a percentage of premiums and such a model will likely function in Zambia.

Secondly, it should be recalled that PIA’s pension supervision program is in the nature of a public safety program and it would be most unusual for it to be subjected to arbitrary limitation. Thirdly, the inevitability of inflation, especially at rates currently experienced in Zambia, would make any fixed “per member” ceiling completely inappropriate.

It is recommended that PIA resist the imposition of any cap or ceiling. The budget of PIA will be set in a transparent manner and will be controlled by a Board that includes industry representation. This oversight pre-empts the need for any arbitrary cap or ceiling.

(5) Training Needs

Having acquired the requisite professionals, PIA needs to go through a continuing education and training program to empower its staff to perform adequately and discharge their supervisory duties satisfactorily. Insurance and Pensions are specialized fields where academic excellence alone will not suffice. Exchange of expertise and experiences with well established and mature supervisory bodies, custom tailored workshops and seminars on key areas where PIA seems to be lacking in specific skills, participation in international bodies whose objectives are the enhancement of supervisory capacity, etc. are all indispensable. Our recommendations are contained under item 9(k) of this report.

(6) Information Systems

Presently, PIA has a few networked computers with Microsoft Office suite that help it to run routine administrative, accounting and secretarial activities. It uses Microsoft Access to compile information returns from the supervised entities. To function adequately and discharge its duties, PIA needs software and training to gather and process information to enable it to produce reports and monitor performance of the supervised entities. Our recommendation on Computerisation strategy for PIA is contained separately under item 9 (d) of this report.

11. The Insurance Industry

(a) Industry Overview

The following overview is based on information contained in the PIA report, adjusted where necessary using the published accounts of individual companies in those cases where we have not been able to confirm the application of acceptable prudential accounting standards.

(b) Composition of the Industry
Based on the Registrar’s Report 2003, the Insurance industry comprises the following players: 8 insurers (4 of which are composite), 1 reinsurer, 38 brokers, 41 agents and 15 motor assessors, loss adjusters and claims agents.

(c) Underwriting Results

The result of the industry in total has been positive for the 3 years under review, 2001 – 2003 registering an underwriting surplus of 10% and 7% in 2002 and 2003 respectively. Five companies have registered underwriting surpluses during the period under review, if they can be given full credit for the high volume of uncollected premiums in each of these cases. Two companies have recorded a net loss for the year; and this becomes problematic when considered in light of the high level of uncollected premiums that are included in their net earned premium accounts.

(d) Management Expenses

Another cause for concern would be the level of management expenses which stand at an average of 49% of net earned premiums for the whole industry for 2003. This means that some companies, especially the smaller ones are at a level much higher than 50% and such companies would most likely be delinquent on claims payments as they would also have high levels of outstanding premiums.

(e) Claims ratio

The net claims incurred ratio for the whole market appears to be satisfactory, and stands at 37% and 36% for 2002 and 2003 respectively. However these ratios can only be relied upon when adequate provision has been made for outstanding claims. This has not been demonstrated.

(f) Commissions

For the insurance industry as a whole, commissions paid during 2002 and 2003 amounted to 11% and 8% of net premiums in 2002 and 2003 respectively. This would average around 15% on broker and agent generated businesses as some 35% of the total business is not commissionable.

(g) Composition of insurance business

Motor insurance, which is compulsory, constituted 67% of gross and 47% of net premiums. Fire insurance came second with 27.7% of gross and 12.8% of net premiums. All other classes of insurance contribute less than 25% of the industry’s income.

(h) Zambia State Insurance Corporation (ZSIC)

ZSIC was set up in 1967 as a state monopoly to transact all classes of insurance and private pensions; and this situation continued until 1991 when the government decided to liberalize the market. The Government tried to privatize ZSIC without success. With the establishment of privately owned insurance companies and privatization of a number of mines, industries and commercial companies previously owned by the State, ZSIC lost substantial market share and had to sell a number of properties. This led to a situation where its viability was in question for a number of years with severe accumulated losses and loss of substantial part of its portfolio to the newly created private
sector insurance companies. It regained profitability in 2002, but is stressed by its substantial investments in non-performing properties, the proposed amendment requiring separation of life and general business, as well as alteration of the multi-employer funds.

Zambia State continues to operate and is the leading underwriter of motor insurance in the country. When companies are ranked by total general insurance premiums, Zambia State has fallen to third place, behind Professional and Madison.

In order to improve its financial situation, the company has undertaken an aggressive downsizing program and has reduced its payroll in recent years from an estimated 3,500 employees to the present 350 – 380 range.

While it is still a candidate for privatization, the government does not appear to be actively seeking a buyer for the company at the present time.

(i) **Role of Brokers**

As brokers currently handle around two-thirds of the total insurance premium in Zambia, their role and contribution to the healthy development or otherwise of the insurance industry is indeed significant. However, there appear to be a number of problem areas in the relationships of brokers and insurers. The main problem areas include the role of brokers in administration of insurance contracts, responsibility of brokers in collecting premiums, providing up-to-date information on the status of outstanding premiums; rules on the prompt payment to insurers of premiums collected by brokers and on the transfer of clients from one insurer to another.

(j) **Outstanding Premium Arrears**

Outstanding premiums with insured clients and brokers currently stand at alarmingly high levels for the whole industry. Provisions in the Insurance Act suggest that a policy of general insurance will “cease to operate” if the premium is outstanding for 60 days or more. However, because of confusion over the role of brokers and extreme competition for business, companies have not been enforcing the 60 day rule. Proposed amendments to the Insurance Act that will reduce this time limit to 30 days might be helpful, but only if accompanied by the requisite directives from PIA to ensure due compliance. The ‘No Premium No Cover’ provision as exists in a number of emerging markets, and administered by the Insurers’ Association as an information clearing house, could be useful.

At the direction of the incumbent Registrar, a special industry task force has drafted a “National Insurance Credit Policy” that seeks to clarify the situations and relationships applicable to the payment of premiums and to any delay in payment. If fully implemented and adopted by all concerned, this policy will help to alleviate the problems with premium arrears.

(k) **Market Retention Capacity**

The industry has varying levels of retention for different types of general insurance. The following table shows the current market retention of different risk types. Motor insurance, the only compulsory insurance in Zambia, is retained substantially within Zambia (95%), whereas less than one-third of the Fire and Marine insurance premium is retained within the country.

The industry could aim at retaining higher amounts in Fire and Marine insurance. One way to do this would be through a market agreement monitored by PIA, with a commitment to ensure that no
facultative reinsurance be placed outside the country before local capacity is fully utilized. Initially, this could be arrived at through co-insurance of peak risks, with agreed rules on participation so that the lead underwriter’s business interests are not compromised. Examples of types of business where this might be useful include Fire treaty and any special risks that are currently placed abroad on facultative basis. However, Determination of company capacity would be a function of paid-up capital and free reserves to be determined on agreed rules and guarantee deposits for cash loss.

<table>
<thead>
<tr>
<th>Class of insurance</th>
<th>Gross Premiums</th>
<th>Reinsurance Premiums</th>
<th>Net Retention %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Motor</td>
<td>107,676</td>
<td>5,515</td>
<td>95%</td>
</tr>
<tr>
<td>Fire</td>
<td>62,846</td>
<td>43,239</td>
<td>31%</td>
</tr>
<tr>
<td>Accident</td>
<td>20,652</td>
<td>8,162</td>
<td>60%</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>13,793</td>
<td>6,086</td>
<td>56%</td>
</tr>
<tr>
<td>Marine</td>
<td>11,760</td>
<td>8,152</td>
<td>31%</td>
</tr>
<tr>
<td>Engineering</td>
<td>8,895</td>
<td>3,054</td>
<td>66%</td>
</tr>
<tr>
<td>Aviation</td>
<td>998</td>
<td>18</td>
<td>98%</td>
</tr>
<tr>
<td>Burglary</td>
<td>517</td>
<td>3</td>
<td>99%</td>
</tr>
<tr>
<td>Total</td>
<td>227,136</td>
<td>54,231</td>
<td></td>
</tr>
</tbody>
</table>

Note: Figures in Zambian kwacha

(I) Issuance of Personal Annuities

Despite the limited activities of Zambian insurers in the field of life insurance, it is interesting to note that there is a steady market for the purchase of life annuities. Pension schemes operating in Zambia permit retiring persons to commute a portion of their accumulated benefits when they reach retirement age. However a portion of the retirement benefits must be taken as a stream of income. (It is interesting to note that this income is not taxable to the recipient). Annuity products of life insurance companies are often used to deliver the stream of income, although anecdotal evidence suggests that some pension funds have been issuing annuities. In most countries, only life insurance companies are authorized to issue life annuities. In Zambia, the Insurance Act is silent on this question. A portion of the accumulated retirement savings of the individual is transferred to the insurance company by the pension fund as a single premium and the company issues a contract to the individual. There are no Zambian tables for mortality among annuitants. Actuaries who advise Zambian insurance companies (primarily residents of South Africa) have provided advice to companies seeking to establish prices and reserves for their obligations under these annuities. In practice they are using South African annuitant mortality tables and this provides a margin of conservatism owing to the fact of greater longevity among South Africans. Likewise, conservative estimates of future rates of investment return have been employed in making the calculations.
12. **Market Conduct Issues**

(a) **Relationships within the Industry**

PIA can do much to enhance transparency and cooperation between itself and the supervised entities by establishing clear channels of communication through guidelines and directives pertaining to various aspects of its supervisory duties. These should normally be commented upon by interested parties to ensure maximum support from them. In addition, efforts should be made on a consultative basis among the different parties to establish co-operation mechanisms that enhance the public image of the industry, improve customer protection and harmonize relationships among players. In the following paragraphs, we discuss some of the useful tools for such purposes.

(b) **Associations**

Industry associations should have clear and lawful constitution and by-laws, in harmony with the Insurance Act and supervisory directives, specify consultative and self-regulatory role, obligatory membership and sanctions. They can help to set up standards, monitor application of good market practice in business acquisition, customer education, improving public image of the industry, etc.

(c) **Arbitration Committee**

To resolve cross industry problems. The supervisory authority could assist by bringing together industry players.

(d) **Office of insurance ombudsman**

This is a useful body when established with appropriate terms of reference, and PIA could benefit from the existence of such a body to promote good corporate governance practices, improved customer care and protection.

(e) **No Premium No Cover**

This provision, as it appears in the insurance laws of other jurisdictions, specifies that insurance coverage does not begin until the insurance company has received the premium. Markets have often set up mechanisms monitored by their trade associations to enforce these rules; and where a customer goes from one insurer/broker to another without clearing its arrears, these bodies specify obligations of the subsequent insurer/broker as regards payment of arrears. The supervisory authority verifies that the arrangement is lawful and in the bona fide interest of the consumer. Of course premiums may not make their way to the insurer for two main reasons. First, the consumer has simply not paid, and this is the situation addressed by the rule just mentioned. A second reason for the premium not reaching the insurer can be that it is the intermediary rather than the consumer who is not remitting the premium. In this regard, a rule that can be beneficial to consumers is to provide that when a consumer is able to produce a bona fide receipt demonstrating that premium was handed to a broker or agent in respect of a particular insurer, the insurer is on the risk, that is to say “payment to the agent or broker constitutes payment to the insurer”. This places a strong onus on the insurer to be satisfied that it is dealing with reputable intermediaries and that it has appropriate controls to ensure that premiums are properly remitted, because if they are not, the insurer may find itself on risk regardless.
(f) Premium Trust Accounts

Brokers will be required to establish separate accounts for client funds, and file monthly statements. Need for total transparency and full report should be provided by brokers to the insurers, with copy to PIA.

(g) Local Capacity Limitations

These would lead to export of retainable premiums. The problem is insurers’ financial ability and/lack of confidence in their peers, and also lack of supervisory directives to motivate companies to work together and fill market retention capacity.

(h) Proposals for Improvement

- PIA should establish functional and well-equipped cooperation mechanisms including associations and committees mentioned above
- PIA should develop and implement formal guidelines dealing with such market issues as the code of conduct and self-regulation among industry players
- Enforcement of legislative provisions on o/s premiums, financial reporting, valuation of assets, broker-insurer relations

(i) Depth of Capital Markets

Investment opportunities for contractual savings institutions operating in Zambia have been quite limited. There is very little trading on the local stock markets and there is little secondary trading in debt securities. Once an institutional investor acquires a debt security, it tends to retain that security. The largest asset items on the balance sheets of the insurance companies are investments in land & buildings and amounts receivable, especially overdue premiums. Nevertheless the situation is improving. Shares of a number of corporations listed on the South African Stock Exchange have been cross-listed on the Zambia Stock Exchange. Government has now made available debt securities with durations of 3 and 5 years. These will be attractive to institutional investors. If measures described elsewhere lead to a reduction in the amount of outstanding premiums, the volume of investable assets will increase. Supervisory requirements should place a ceiling on the proportion of assets that may be held in the form of land & buildings. Gradual introduction of such restrictions would lead to a situation, over time, where the dependence on property investments is much reduced.

13. Insurance Regulatory System

(a) The Insurance Act No. 27 of 1997

Regulation and supervision of insurance in Zambia is governed by the Insurance Act of 1997. While this is a reasonably modern piece of insurance legislation, it has some major shortcomings. For example, while it grants to the supervisor the power to issue “cease and desist” orders, it does not impose any responsibilities on Boards of Directors. In fact the legislation does not contain the expression “Board of Directors”.
Under the provisions of the Insurance Act, the Minister is authorized to issue certain regulations and to prescribe certain rules. For his part, the Registrar is also authorized to issue guidelines in a wide variety of areas. As noted earlier, few of these regulatory instruments have been created. It has been said that officials recognized that there were fundamental shortcomings in the 1997 legislation when it was first passed and that amendments would have to be made to correct these. Hence the decision was taken to postpone issuing the relevant regulations, etc. until the legislation could be amended. For those matters where companies needed some minimum guidance in order to conduct their affairs, PIA decided to continue using existing regulations that had been issued under the authority of the 1968 Act, to the extent that they are not in conflict with the provisions of the 1997 Act.

To some extent, the supervision of companies has been compromised by the lack of these regulatory tools. For example, in the absence of clear rules for the measurement of solvency and without rules for minimum capital, it would be difficult for staff inspectors to be very aggressive in dealing with companies that do not appear to be in a sound financial condition. The objectives of supervision have not been clearly defined in the legislation nor do they appear to have been clearly communicated to staff members. It appears, for example, that dealing with issues arising from the activities of brokers and with inquiries from policyholders has taken a significant amount of staff time away from the business of supervision of insurance companies.

Amendments to legislation have been drafted and have received first reading in the legislature. It seems likely that these will be adopted before the end of 2005. However these amendments will not remedy all the shortcomings that are perceived to exist. Further discussion on specific topics follows.

(b) Valuation of Assets

By virtue of section 40 of the Insurance Act, the Registrar may take steps to verify the valuation of asset and liability items. Under present arrangements it appears that the valuation of assets is left to the discretion of the company working, we presume, in conjunction with its auditors. This is an unsatisfactory situation and the valuation rules should be specified by the regulatory system. In the ideal, the Minister should issue regulations prescribing the rules for valuation of the different types of assets. Proper valuation of assets is an indispensable ingredient to the development of a meaningful solvency standard.

Valuation rules would prescribe how appraisal values for holdings of land and buildings are to be determined. They would also specify that certain assets are disallowed for solvency purposes, such as premiums more than 60 days overdue.

(c) Sufficiency of Provisions

At present there are no guidelines and instructions in place in Zambia that would govern the computation of claim loss provisions. There is a requirement for IBNR and that is a good thing, but there is no control over the adequacy of the basic provisions established for claims reported. At the very minimum, PIA should develop a run-off style monitoring method to help it to identify those companies that may not be posting adequate provisions for claims. More sophisticated methods for testing accuracy could also be developed with the aid of a consultant who is expert in such matters.

(d) Solvency Standards

Once appropriate valuation has been secured for the assets and liabilities of the insurance companies, it will be possible to develop a meaningful solvency standard for application to Zambian companies.
The industry is too small and immature to adopt the sophisticated risk-based capital formulas that are seen in more developed countries. However, it would be quite simple to make regulations and require companies to perform a solvency test calculation using the formulas that were adopted in the initial stages of establishment of the common market for insurance by the countries of the European Union. This method was described in the FSAP and a copy of the relevant summary is included as an appendix to the FSAP report.

Once such a solvency standard is in place, supervision would proceed against this backdrop. PIA could establish guideposts (regulatory ladder) for taking different types of action toward the companies depending upon the degree of compliance with the required minimum amount of capital and surplus. For example, if a company passes the test by a very small margin, then the Registrar could write to its CEO and explain that the situation requires careful monitoring. If, on the other hand, a company’s resources fall below 100% of requirements, then the supervisor would demand immediate remedial action by the company. If that remedy was not produced forthwith, the supervisor could take steps to stop the company from issuing new policies.

(e) **Bank Overdrafts and borrowing**

Balance sheets filed by the licensed insurance companies indicate that insurance companies have been engaged in raising funds through borrowings. General insurance companies have balances outstanding in the form of bank overdrafts, loans from related companies and even shareholder loans. Life insurance balance sheets include amounts borrowed from credit institutions and from related companies. Such borrowings should be a cause for alarm. Companies can not avoid the occasional need for short-term borrowing to meet cash flow problems. However, no insurance company should be engaged in raising money by borrowing, as a regular practice. The Insurance Act should include a prohibition against borrowing or at least establish strict limits to such activity. If it became necessary to liquidate such a company, it would be important to have measures in place to ensure that any such obligations are subordinated to those of the policyholders and their beneficiaries.

(f) **Proposed Amendments to the Insurance Legislation**

The proposed 2005 amendments cover the following main areas:

- abolition of composite insurance companies
- introduction of premium trust accounts
- authorization of auditors by PIA

(g) **Matters not yet adequately addressed in Legislation and proposed amendments**

(i) **Establishment instrument of PIA**

It would be preferable if there was a separate piece of legislation that deals with the establishment of PIA. This is the approach taken in other countries and has been recommended by PIA. The recommendation was overridden for some reason by the Ministry of Justice and the amendments currently under consideration attempt to establish PIA formally through clauses in the Pension Schemes Regulation Act.
(ii) Creation of PIA supervisory board

We would recommend that representatives of the affected industries be included on the supervisory Board, with due regard to the risk of conflicts of interest.

(iii) Code of conduct

The legislation could authorize the Registrar to compel supervised bodies to implement self-regulation mechanisms through their associations, empowered to sanction non-compliance. For example, in some jurisdictions, the supervisor has delegated to the relevant trade association many of the routine functions relating to training, qualification, licensing and discipline of brokers and other intermediaries. These activities are currently demanding a great deal of time for PIA staff.

(iv) Qualifications and responsibilities of Directors

Modern regulations and supervision in the financial sector include significant reliance on Directors for monitoring and oversight of the activities of the management of an institution. Directors should be held accountable for this function. Boards should comprise individuals who act with integrity, skill and competence. Boards should include at least some minimum number of members who are independent of management and the employees of the company.

(v) Declaration (conflict) of interest

Such statements should routinely be required from company board and management as well as members of the supervisory board and committees.

(vi) Audit Committee

Board of Directors of each company should be required to set up this committee to ensure compliance with the laws and regulations as well as company rules. Majority of members should be independent. Audit committees are presently required of banking institutions operating in Zambia through the Bank and Financial Services Act. There is no such requirement in the Insurance Act and the inspectors have indicated that only a few companies have established such committees.

(vii) Arbitration Committee

To resolve cross industry problems. Alternate dispute resolution methods should be sought to reduce costs and delays that are associated with actions that proceed through the courts.

(viii) Office of insurance ombudsman

Many jurisdictions have found it convenient to establish an office of insurance ombudsman. This may be a government official or it may be someone appointed by the industry trade association. An ombudsman provides another convenient contract point, especially for consumers, and often helps facilitate the resolution of problems with insurance matters, without reference to courts and without taking the Registrar’s time away from the supervisory work.

(ix) Good Corporate governance requirements
In general, Boards should be obliged to assume accountability for establishing standards and objectives, for monitoring compliance with those standards and for taking remedial action where necessary. These measures are most important in areas such as internal controls; dealing with investment policy; dealing with the functions of risk management; and reviewing transactions with related parties.

(x) Motor Compulsory Insurance

Compulsory business is governed in large measure by the Road Traffic Act. At present there are no provisions for an uninsured motorist fund to help indemnify persons injured in an accident where the guilty driver is either not insured or can not be identified. It may also be helpful to establish a special pool for the insurance of high risk drivers whose safety record causes most companies to deny them coverage. Another legislative amendment that could be of assistance in Zambia would be the creation of a set of indemnity limits through the legislation that would specify the amount of benefit that would be paid to an injured party depending on the nature of the injury. Such limits have proved very helpful in other African countries and serve to reduce delays in settlement and also to minimize the number of claims that become the object of litigation.

(xi) No Premium No Cover

In an effort to reduce the volume of unpaid premiums that appears on the balance sheets of Zambian companies, the amendments to the legislation suggest that the time limit for premium payments be reduced to 30 days from the present 60. Strict implementation of the 30-day revised provision should help companies improve their balance sheets. Another potentially useful measure that has been adopted in other African countries is the “no premium no cover” approach. Under such an approach, the insurance company will not issue a policy to the broker for onward transmission to the insured party until the insurance company has actually received the premium. A supplementary approach mentioned above, is to provide that payment to an insurer’s intermediary constitutes payment to the insurer, thus giving insurers a strong incentive to make sure that their intermediaries are remitting premiums fully and on a timely basis.

(xii) Sources and uses of the fidelity fund

Insurance Act calls for the establishment of a fidelity fund by PIA. This fund is to receive all amounts paid to PIA in the form of fees, fines, etc. While the fund apparently exists, no procedures have been put into place to govern the use of the funds. The intention of the legislation is to employ these funds to help compensate persons who might otherwise suffer loss in the event of the failure of an insurer or by the actions of an insurer or broker. There is a need for clear, written instructions on the procedures that will be followed in dealing with the fund. Such rules would be issued by the Policy Holders’ Protection Board.

(xiii) Other Issues in the Regulatory System Requiring Attention

- Regulation of Insurance Products: Supervisory authorities need to know what products are being sold in the market. The same arguments apply for product authorization to guard against speculative and/or undesirable products being sold in their markets. The level of control on product authorization can be classified into ‘File and Use’ or ‘Prior Authorization’ as in the case of Reinsurance arrangements. Some supervisory agencies are now opting for an approach where they have power under the law to require policy terms to be revised where this is found by the supervisor to be necessary in the public interest. However rather than
having policies filed with the supervisor prior to their introduction to the market, problematic policy provisions are noted on the basis of public complaints or by spot check during on-site inspections. In this event the company can be subject to sanctions and required to change the policy terms. There are a number of supporting benefits to this approach: (1) the company and its board should be fully responsible for the details of all coverages that they are going to provide, (2) it is difficult for a supervisor to spot potential problems with new policies because of the technical nature of the policy terms and the lack of highly trained supervisory staff with appropriate levels of experience, (3) once policy forms have been filed and therefore seemingly “approved”, any subsequent problems that do become evident may be placed on the government’s doorstep because of the “approval” and (4) most policies will not have any problems so reviewing all the forms gives rise to a considerable volume of work, generally with little payback.

- **Composite insurers:** Define relations of linked companies, capitalization and cross investments, and directorships; draw realistic schedules and mechanisms to ensure smooth separation of existing composites. At all times, a separate management and capitalization will be required.

- **Insurance and Brokers associations:** Where the Insurance Act does not specify corporate governance, consultative and self-regulatory role, obligatory membership and sanctions as rights and responsibilities of these associations, the Supervisory Authority defines these roles and gives the associations the required authority via a directive. In effect, the associations would contribute to supervisory performance and in due course the Supervisory Authority can delegate a good part of its routine tasks, and maintain only oversight duties.

- **Capital Reserves:** Strong insurers lead to stable markets and increase national retention capacity. As is the case in many countries, legislation could establish a systematic procedure for strengthening the capital base of a company by applying part of the annual net profit after tax to a capital reserve account. This may be done on a long term basis and the following has been suggested as an example:

  - 25% of profit after tax up to 50% of paid up capital
  - 10% of profit from 51% to 100% of capital;
  - 5% thereafter

- **Companies in difficulty and Insolvencies:** Before companies reach insolvency, good supervision would identify the difficulties faced by an insurer, and recommend various courses of action, one of which is putting the company under management of a person appointed by the regulator, especially if the problem is bad management. The objective is to rehabilitate the company and give it the chance to recover and continue to remain in business. When a Supervisor identifies a company in difficulty it will undertake consultation with the Board and industry association and define supervisory courses of action and procedures for insolvency leading to supervisory take over, rehabilitation/reorganisation, and liquidation on failure.

- **Winding up:** The Supervisor should have a well defined procedure for winding up of companies that go into liquidation voluntarily or enter into compulsory liquidation. The objective is to make sure that the interests of the policyholders are adequately protected and that the insurance industry and the financial markets are not adversely affected. Often this
procedure entails working with different professions such as the auditors and actuaries, if any, and representatives of interest groups.

- **Share holding limits:** In those jurisdictions where capital requirements are very low, legislation will restrict the proportion of an insurance company’s shares that may be held by one person. A possible upper limit on this proportion would be 25% per person. One-person or family-held insurance companies should not be encouraged.

- **Fronting:** Special exemptions of PIA on a case by case basis, e.g. WB conditions on development finance or loans, major investments and other government commitments, inadequacy of local covers or capacity could lead the Supervisory to allow fronting or placement of local risks with foreign insurers and reinsurers without the usual participation of the local insurers. This is often done on a case by case basis, but the Supervisor keeps full record of the justification as well as the details of cover.

(h) **The PIA annual report:**

PIA is to be complimented on its success in producing an Annual Report for 2003 and the prior year. Although the Insurance Act calls for the preparation of a report to the Minister, the Minister has not yet tabled the reports in Parliament and hence they can not be circulated to the public. In any case, in order to satisfy the public’s need for a description of the work of supervision and to provide a satisfactory presentation of the performance of the pensions and insurance industry, there is need to improve the analysis of technical results and financial reporting that appears in the report in several aspects. Genuine progress in this direction will await the introduction of revised formats for prescribed returns to be completed and filed by the companies. The revised formats will call for information of a nature and in a style of presentation that is superior and more complete than that which now prevails. Directives on minimum required disclosures in insurers’ annual accounts could also be helpful in this exercise. An optimal report from PIA as a supervisor of insurance would include tabular information on the following:

- Accurate financials up to P&L and balance sheet
  - Ratios of key issues supervised:
    - Asset valuation basis
    - Capital adequacy
    - Solvency
  - Premium adequacy (management expenses, acquisition costs, claims)
  - Aging of uncollected premiums
  - Claims breakdown (paid, o/s, IBNR, special provisions, etc.)
  - Loss ratios by line of business
  - Reinsurance performance
    - Premium outgo, commissions, claims recoveries
  - Analysis of Management expenses, commissions, etc.
- Section on brokers

Text comments from the Registrar should include:
- Explanation of transactions regarding loans, linked companies, directors and management
- Description of PIA’s efforts towards a healthy market development and efforts towards corporate governance by all parties,
- Significant items arising in them course of the application of the relevant legislation, drafting and promulgation of regulations, guidelines and directives.
14. Private Pensions

(a) Pension ~ Industry Overview

The main components of the formal pension system in Zambia are the National Pension Scheme, the schemes created by statutes and private occupational pension schemes. Personal pensions are not a significant component at the present time but are expected to grow as the economy develops and employment opportunities in the private sector expand. The former components are discussed below.

(b) National Pension Scheme

This is a mandatory contributory defined benefit scheme covering all employees of employers and all self-employed persons. It is a statutory program and is the successor to the National Provident Fund which was converted from a defined contribution basis to a defined benefits structure. The NPS is subject to overview by an appointed Board which is chaired by the Principal Secretary to the Minister of Labour. The NPS is audited by outside auditors on a regular basis and is subject to triennial actuarial review. There are two components to the system; the original Provident Fund benefits and the more recent Defined Benefit scheme (fixed contributions and benefit accrual on the proportion of earnings indexed to average wages subject to minimum and maximum service credits). These components are maintained as separate schemes in terms of there being separate assets and accounts supporting the determination of benefits. The internal asset-liability structure and the financing of the NPS is beyond the scope of this work but is relevant to PIA in the event any decision to have PIA take on some measure of oversight.

The NPS has been criticized on several fronts, these relating primarily to lack of control over the collection of mandatory contributions from employers who are obliged to remit both employee payroll deductions as well as matching employer amounts. This is aggravated by the preparation of published financial statements on the basis of cash reporting of contributions which does not attempt to report contributions due to the fund but which have not yet been remitted.

The view has been expressed that this may be appropriate in order to avoid over-stating fund assets due to the expectation that many such contributions are unlikely to ever be remitted. The argument is also made that to show such contributions as an asset would compromise the validity of reporting of the financial condition of the fund, i.e. understating its deficit. This argument should be rejected. The more important issue is that the non-reporting of such amounts is conducive to laxity in the effort to enforce collection.

The NPS is not supervised by PIA although there are references in various documents that suggest that such might be a useful initiative. In addition to the question of the capacity of the government to submit itself to the authority of a body that it has created, there are a number of practical considerations that should be carefully evaluated in that regard. For example, the inspection of a system such as the NPS would clearly involve a massive deployment of resources that would be difficult to fund and even more difficult to manage by an entity to be structured in the manner anticipated for PIA in its oversight of private occupational schemes. The work of supervising the NPS would likely dominate the entire organization for some extended initial period given the existing problems of collection and administration. In that regard it is to be noted that the counterpart systems in the US and Canada are not supervised by the counterparts of PIA in those jurisdictions.
(c) Statutory Schemes

The PSRA applies to all pension schemes in Zambia except the NPS. This means that it applies to schemes that cover certain public sector employees. These schemes are the PSPF (Public Service employees) and the LASF (Local Authority employees). They have some 80,000 and 17,072 active members respectively and some 125,012 and 22,907 retired members respectively. Put in perspective, these two supervised schemes represent about 75% of the active membership, and about 73% of the retired membership, of supervised schemes. Both these schemes were established by statute.

As has been documented extensively in other reports, these schemes are not in acceptable financial condition. It appears that the GOZ is responsible as the employer directly for the financing of the PSPF and, indirectly, through the Ministry of Local Government, for the financing of the LASF (this latter scheme operates as a multi-employer scheme). These schemes also are afflicted by arrears of contributions although there is some effort being made by the GOZ to remedy the arrears situations. However, the deficit in the PSPF is currently and informally estimated to be some 3 trillion ZK and the funding of such an immense deficit relative to the Zambian economy in the context of conventional practice of funding occupational pension scheme deficits (a relatively rapid amortization over 10-15 years) raises very difficult questions.

The financial condition of these schemes (massive arrears and deficits) coupled with the relationship of PIA to the GOZ makes their effective supervision by PIA extremely conjectural. For example, how would it be equitable for PIA to rigorously enforce contribution remittance requirements on private scheme sponsors unless the GOZ were to become a model in that respect? The resolution of such issues is clearly beyond the scope of this report but they must be carefully analyzed by PIA management. It may be feasible for PIA to make a case for the amendment of the legislation that would further exempt the statutory schemes, should the GOZ so deem acceptable.

(d) Private Occupational Pension Schemes

There are some 200 such schemes currently on the records of PIA. Some are active, a few are dormant (no new benefits being accrued) and a few are empty (of members but not of assets). The detailed overview of these schemes is provided in the Appendices.

(e) Taxation

This is a critical factor in relation to pension schemes. Most jurisdictions support private provision of retirement savings by granting them favourable taxation treatment. The categorization of the various approaches to this is to classify the three main components of contributions, investment income of the funds and the benefits according as to whether they are ‘T’ or taxed as they accrue or ‘E’ or exempt. As an example, if in a jurisdiction contributions are made out of pre-tax income, if investment earnings are not taxed as they accrue and if benefits are taxed as they are paid, such a system would be referred to as EET. This would be the case in the US, Canada and Australia although there would be varying limits applicable to the amounts of contributions and the corresponding benefits granted this treatment.

The taxation of private occupational pension schemes is governed by the provisions of the Income Tax Act CAP 323 Schedule Four. It provides for the approval of funds that meet certain basic requirements. These include the general requirement that the establishment of the fund or scheme by or on behalf of the employer must be made under a set of rules. The approval of the fund or scheme is contingent on the rules being in conformity with those enumerated in the Schedule.
In Zambia, the rules governing the tax deduction entitlements related to pension schemes are contained in CAP 323 section 37 of the Income Tax Act. The principal features of the tax from the standpoint of the private occupational pension system are as follows.

(f) Contributions

There is a limit on the amounts that an employee may deduct as a contribution to the lesser of: 15% of earnings, or ZK 18 million. This implies that anyone contributing at the rate of 5% of earnings to a scheme and who earns less than ZK 3.6 million may deduct the full contribution while those earning more can only deduct an amount of ZK 180000 an amount that represents a declining % of earnings as the latter increase. Since most new entrant public servants contribute at the 5% rate to the NPS, the deduction limit will affect them if they earn over ZK 3.6 million. Public servants hired before 2002 contribute to the PSPF at 7.5%, and those who earn over ZK 2.483 million will be contributing non-deductible amounts. Typical public servants would earn about ZK 12 million and would be making considerable amounts of non tax-exempt contributions to either the PSPF or the NPS. The effect on other workers in industry or commerce would be commensurately greater. This is likely to be a significant impediment to the expansion of the private occupational pension system in Zambia.

Employer contributions to private occupational schemes that are granted favourable tax treatment are limited to 15% of payroll. This is in addition to their 5% mandatory contribution to the NPS. This is not subject to a fixed amount per employee maximum as is the case for employee contributions. This is likely to be a satisfactory limit for most employers except those that have to fund unfunded prior service liabilities or scheme deficits in addition to paying their share of the costs of current service benefits, in which case they may be faced with making contributions that they cannot deduct. It is recommended that PIA research this matter and, if any concerns are confirmed, they should be brought to the attention of the ZRA.

(g) Investment Income

Investment income earned on investments in Treasury Bills or Government Securities by pension funds are subject to withholding at the rate of 15% (final tax). The investment incomes on other investments, including realized and unrealized gains, is not subject to tax; although a special 1% medical levy is charged in all investment income.

(h) Benefits

Retirement pension benefits are tax free after retirement. Lump sum benefits on retirement representing employee contributions are tax free if less than ZK 10 million. We can thus classify the taxation system of private occupational pension schemes in Zambia as ‘Significantly T’, ‘Somewhat T’ and ‘Significantly E’.

See Appendix Two for further details.

15. Regulatory system for Pension Plans

(a) Legislation

Note: the following commentary excludes issues related to the provisions of the legislation related to the structure of PIA, the Board and the legal constitution of the regulatory system. The detailed comments and findings on these issues are dealt with in other sections of the Report to PIA.
(b) **The 1996 Pension Scheme Regulation Act**

This is the existing legislation that governs the private occupational schemes in Zambia. It extends to all pension schemes except the NPS (s. 2) and this has been deemed to oblige PIA to supervise the PSPF and the LASF. These latter schemes suffer from chronic and severe unfunded liabilities that appear to be, in large measure, due to unpaid contributions, although it is likely that significant proportions of the current amounts are due to experience losses due to the impact of inflation on salaries and wages.

The Act established PIA, defines the structure of the private occupational pension scheme fund system using multi-employer trusts, and provides for the registration of schemes. It further mandates conditions to be met by registered schemes, including preservation of rights and the protection of members, provision of annual benefit statements to members, the conduct of periodic actuarial investigations, that asset management is to target the maintenance of the real value of members’ benefits, and the provision of portable benefits as defined. It also provides for the duties and authorities of the Registrar, financial reporting, de-registration, rehabilitation, final distribution of funds, sanctions and appeals.

Further detailed discussion of the Act is provided in Appendix Nine.

(c) **Proposed Amendments to the 1996 Pension Scheme Regulation Act**

These amendments will:

- re-structure PIA through the establishment of a Board and the definition of its functions and duties,
- continue the functions and duties of the Registrar,
- provide for the registration of pension fund administrators and custodians as well as fund managers,
- mandate equal employer-member trustee representation,
- impose fit-and-proper criteria for trustees,
- provide for the establishment of single-employer trusts as well as multi-employer trusts,
- make certificates of registry of indefinite duration,
- impose a 25% maximum single person share-ownership limit on fund managers, scheme administrators or custodians,
- mandate experience and fit-and-proper requirements for the CEO of a fund manager, administrator or custodian,
- increase the frequency of actuarial investigations to triennial from quinquennial,
- impose various duties (now imposed on the manager) on the trustees,
- authorize the Board to levy the assets of, or contributions made to, pension schemes,
- allow the Minister to make regulations for the de-registration and wind-up of pension schemes,
- create employer’s liability for the payment of interest on overdue contributions and allow the Board to impose penalties for late remittance of contributions, and,
- create director and CEO liability for having consented to or connived in the commission of offences under the Act by a manager, administrator or custodian and exposure to penalties of fines or imprisonment.

Further detailed discussion of the proposed amendments is provided in Appendix Nine.

(d) **Assessment of the Supervisory System**
PIA has established a basic structure for discharging the duties and meeting the expectations of the legislation. It collects information regarding registered schemes, reviews the filings, performs some analysis, conducts a limited number of inspections which are characterized as either formal or spot, participates in stakeholder groups and prepares an annual report that it provides to the Minister for tabling in Parliament.

Sample reviews of internal reports indicate that these are of limited scope, contain inadequate analyses and do not appear to deliver sufficient information for making robust assessments of the risk situation of supervised schemes or for the support of regulatory action. While there has been evidence of serious issues involving pension schemes, PIA has not moved to address them by way of industry-wide directives or guidelines despite the apparently adequate scope in the existing Act in that regard. However, PIA has demonstrated its ability to take determined action in respect of individual pension plans that have demonstrated serious problems.

There are over 200 schemes and 8 fund managers to be supervised. The existing complement of staff, while capable and enthusiastic, does not appear adequately trained and resourced to permit their skills and productivity to grow. There is great need for the delivery of considerable specialized training in specific areas of pension scheme operations, administration, funding and solvency, investment of funds, risk management, financial analysis, roles of trustees, fund managers, administrators, auditors, investment managers and actuaries. Similarly, there is pressing need for information systems that will serve all PIA’s data base, analytical, reporting and administrative needs. PIA’s internal processes need complete review following which extensive documentation must be made and applied by staff subject to management oversight. Required reports should be reviewed and improved in order to serve the need for proper pension scheme administration and the objectives of risk-based supervision. PIA’s annual reports should be completely re-thought in the context of the need to disseminate information and knowledge to stakeholders and the capacities that should follow the information system and reporting reforms. Without those initiatives it is doubtful that effective and efficient supervision will be feasible with or without the implantation of risk-based methodology.

(e) Regulatory Strengthening

There are several initiatives that PIA could undertake immediately that would be useful first steps in securing a stronger better administered private occupational pension scheme sector. First, it could issue a guideline to all employers who have established schemes (whether funded through multi-employer or single employer trusts) reminding them of their duty to remit their required contributions to their respective trust funds without delay, as they are deemed in law to become trust property as soon as they are earned by reason of employees’ membership in the scheme. Subject to confirmation by PIA legal counsel, the directive should note that this is an obligation on the employer, its directors and officers imposed as a result of trust law, and that failure to treat such contributions as held in trust by way of separate accounts (that should be cleared by transfer to the trust fund forthwith) is an extremely serious matter.

PIA should enforce the provisions of sections 18, 28 and 30 of the PSRA and direct fund managers to ensure that the benefit statements of members are prepared in such a manner as to show the amounts of employee contributions accumulated on the basis of the amounts actually received by the trustees and audited by the fund auditors. It would be misrepresentation to base benefit accumulations disclosed in employee benefit statements amounts that include contributions held back by employers and not remitted to trustees in a timely manner as at the benefit statement date. This policy could be notified to employers, trustees and auditors without waiting for the passage of
the pending amendments. Alternatively, PIA could direct these parties to include a footnote to any benefit statement prepared on the basis of ignoring unpaid due and accrued contributions showing the amount of contributions due to have been remitted but withheld by the employer or sponsor as at the statement date.

Longer term initiatives of PIA should include, in order to complement the new authorities to be introduced by the pending amendments, obtaining the authority: to require actuarial valuations on an annual basis where the scheme is believed to be under-funded; to require solvency valuations on an annual basis where the scheme is likely to be insolvent should it terminate in the near future; to direct trustees to furnish such information to members and beneficiaries as PIA deems necessary; to replace trustees who fail to meet the fit-and-proper test on a continuing basis and to act in the place of a scheme member for purposes of instituting legal proceedings against a Board of Trustees or a person appointed by the Board to provide services to the scheme in the event of their contravening the Act, scheme rules or Regulations (the current PSRA section 27 is inadequate in that regard); to declare a scheme terminated in the event of non-payment of required or recommended contributions and to have it wound-up; and to engage independent professional advice regarding a general matter of policy or as respects a specific issue involving a particular scheme.

(f) Auditing and Delinquent Contributions

This is one of the most significant and urgent issues facing PIA in regard to its responsibilities for supervision of private occupational pension schemes. See Appendix Three for further discussion of the issue of due and unpaid contributions.

Auditing of pension schemes is a vital component of pension supervision. It is necessary for the supervisor to fully appreciate the nature of the pension scheme audit and to co-ordinate its activities with those of the auditor accordingly. Where auditors’ reports are qualified or are prepared on the basis of variations from IAS (International Accounting and Auditing Standards) the supervisor must take action to fill any gaps in order to ensure that the interests of pension scheme members and beneficiaries are appropriately safeguarded.

An on-site meeting held in Lusaka with representatives of the local auditing community indicated that there may be a serious gap in the financial reporting structure that needs the attention of PIA. The financial statements of pension schemes should, according to generally accepted accounting principles, be prepared on an accrual basis. This means that all non-ledger assets and liabilities are accrued from the end of the prior period to end of the current period and that the corresponding income or expense items are increased or decreased to effect the change in those items.

Of course, the primary income items in regard to the financial statements of a pension scheme are contributions and investment income. The accrual of these items typically give rise to asset items, these being the contributions due but not received by the scheme’s fund and the investment income due but not received. These two items would be disclosed as items in the assets of the financial statements.

In Zambia, it appears to be customary for the investment income due and accrued to be reported, as is normal and proper, but it is not customary for contributions due and accrued to be so reported.

This gives rise to an anomaly in that the financial statements are not prepared on a consistent basis.
More importantly, the assets of the scheme are systematically understated and the financial reports do not constitute a fair presentation of the scheme’s financial condition. Even more importantly, the financial statements do not enable the Supervisor to assess the degree to which contributions have not been properly remitted by the sponsor/employer to the trustees for deposit to the fund. In the event of financial difficulty leading to wind-up of a scheme, such an asset must be recovered and the identification of its quantum is essential. This is an issue that should be of great concern to PIA.

It is recommended that this matter receive immediate attention. PIA should take a strong public position to the effect that it does not sanction non-disclosure of unpaid accrued contributions and that it intends to secure appropriate authority to enforce the timely remittance of all scheme contributions and that it expects the full co-operation of all parties, trustees, fund managers, auditors and, most importantly, employers and scheme sponsors.

(g) **Orphaned Benefits**

Orphaned benefits are benefits for which pension schemes hold liabilities and which are never matured by reason of claims by members or beneficiaries. The most common type is retirement pension benefits but they can also involve death benefits or survivor benefits. Members who leave employment often retain rights to deferred pensions (to which death benefits may attach) but must normally apply for them once the relevant age and/or service conditions are met. The legislation and the proposed amendments are silent on the subject of the appropriate measures to minimize the risk that benefits are lost due to the inevitable oversight of benefit entitlement through the passage of time or other factors (incapacity, disability etc.). Also, there is no standardized prescription for trustees’ duties in trust deeds for the treatment of this subject.

A further exacerbating factor is the absence of a practice on the part of many pension schemes that would provide “exit statements” to departing members who have deferred entitlements to retirement benefits or whose survivors would also have benefit entitlements.

The recommended remedies are:

PIA should direct trustees to provide exit statements to terminating members that clearly indicate their rights to deferred benefits and their responsibilities to make claims and the conditions that must be fulfilled in order for their claim to be approved.

PIA should recommend to the Ministry of Labour and the NPS that they offer a service to trustees and administrators of occupational pension schemes that would permit trustees to notify them of persons who ought to have matured entitlements and who have not presented claims. The NPS could then attempt to contact such individuals and notify them that they have been advised that they may have benefit rights and that they should contact the pension scheme administrators for purposes of lodging their claim. The ZRA could also be invited to participate in this arrangement since they may have more up to date information regarding such individuals’ contact co-ordinates.

PIA should also clarify the treatment of funds that are never claimed despite all efforts to pursue claimants with matured entitlements. The disposition of such funds (e.g. in empty schemes with unclaimed assets) should be prescribed after study and analysis of practice in Zambia and neighbouring jurisdictions.

(h) **Portability of Pension Benefits – Transfer Values**
The PSRA mandates that benefits in respect of terminating members be granted portability, i.e. accrued rights must be transferred to another scheme if a member changes employment. The legislation requires the scheme rules to deal with the calculation of portability rights and that a member must be provided each year with a benefit statement showing the member’s actual benefits and the member’s accrued portable benefits.

The Act defines what is meant by portable benefits in the case of both types of scheme, but there is no prescribed structure for determining the mechanics governing the operation of this provision. In particular, the calculation of the present value of the member’s accrued benefit has been cited as a pressing issue. Concern has been expressed that fund managers are encountering practical difficulties in complying with these requirements.

It is clear that a case-by-case calculation of the present values could involve potentially significant expense depending on the agreed methodology.

PIA should, as part of its inspection procedures, ascertain and document the extent of these issues and any practices that may have been adopted for consolidated review and analysis. The results should be communicated to industry representatives, including auditors and actuaries, and a consensus view sought that could then be used to formulate a directive to all parties-at-interest.

(i) Funding Requirements and Current Practices

The PSRA delegates the design of the funding of defined benefit schemes to the scheme actuary and, interestingly, stipulates that the actuary shall not be bound to take directions from the manager, trustees or the employer (a rare mention of that entity). There are no specific funding requirements as they are generally understood in other jurisdictions, i.e. stipulations regarding the certifying of the normal cost (currently accruing benefits) and the recommended amortization of prior service liabilities or deficits in compliance with prescribed schedules subject to maximum periods etc.

PIA has not documented any survey it may have made of the funding methods, actuarial assumptions and amortization schedules that have been disclosed in reports actuarial reports on file.

PIA should conduct a review of previous filings and document the results. It would also be useful to inquire of regional pension scheme regulators if they have any comparable analyses and offer to exchange these for review (of course, privacy laws would have to be observed, to be advised by legal counsel to PIA). In similar vein, PIA should inform itself of any formal requirements in this regard in the legislation and regulations administered by its counterparts in neighbouring jurisdictions which could be consolidated and shared as well. This will assist in the development of policy for exposure to the industry.

(j) Marketing and Administration Expenses

These are a key issue affecting the successful performance of defined contribution pension schemes (the vast majority of schemes supervised by PIA). There is a general perception that these expenses are unacceptably high in Zambia. PIA should document the experience of schemes in this respect, extending the analysis to include several years’ data (it is assumed that it has been disclosed in quarterly filings for the last few years) and present it to the industry for comment and suggestions as to how efficiencies can be achieved. It is also recommended that these results be shared with pension scheme supervisors in neighbouring jurisdictions with invitations to share their experience with PIA.
See Appendix Eight for further discussion of means of controlling fees and costs for private pension schemes.

(k) Multi-Employer Schemes ~ Conversion to Single Employer Schemes

Section 7 of the PSRA obliges pension funds to be established in the form of multi-employer trusts. Alternatively a fund must be affiliated to such a fund by formal agreement. This arrangement ensures that there are a limited number of fund managers in the market, there being 8 at present. The proposed legislation would permit the establishment of single-employer trusts. This is undoubtedly a positive development and should facilitate the achievement of greater efficiency and reduced expenses of investment management and scheme administration for many employers. The issue of how an employer may terminate the participation by its pension scheme in the multi-employer fund that has been required to date in order to consolidate all funds in a new (yet to be established) single-employer trust is essentially a legal question that requires analysis of the specific constituting documents of the multi-employer trust.

It is recommended that PIA structure a review of such documents to ascertain the scope for withdrawal of participation and concomitant transfer of funds to a new single-employer trust (without termination of the pension scheme as such) that is provided in existing multi-employer trusts. In the event that it is concluded the scope is not adequate to permit the initiation of new arrangements implicit in the new authority legislated by the proposed amendments, the legislative proposals could be improved to mandate such outcomes. PIA could be awarded arbitration powers for purposes of securing agreements equitable to these trusts. This would be preferable to forcing trusts to seek remedies through court sanction.

(l) Monitoring of Pension Schemes

There is a generic process that may be defined for the supervision of private pension schemes in which is embedded the activities of registration, processing of returns, analysis of information for purposes of risk-based management often referred to as off-site review and analysis or desk analysis, on-site inspection, special event management, regulatory intervention and sanctions. Each of these activities has its own characteristics and is a subject for staff training and documentation of procedures by way of supervisory manuals.

(m) Off-Site Review and Analysis (Office Review of Filed and Related Material)

This component consists of data collection, storage and manipulation via information technology, and also includes partially structured activities such as analysis of auditors’ and actuaries’ reports and investment policies and portfolio analysis. It also includes the collection and deployment of intelligence data related to the economy, financial and Labour markets, bank and non-bank institutions, securities markets and investments as well as developments in the areas of new financial products, regulation of the financial sector and supervisory innovations and advances. Again, the structuring of this component generates its own training and documentation requirements.

(n) On-site Inspections

The ingredients of this component are the outputs of the off-site review and analysis process, together with the results of interviews with scheme fund managers, administrators, trustees, auditors and actuaries and officials of other agencies having oversight responsibilities involving pension schemes, as well as the analysis of such additional data and documentation as is secured by the on-
site activities themselves. This component has certain special features related to the management of
the inspection activity including protocols for scheduling, documentation, access to and protection of
information, and report construction and follow-up. It too involves dedicated staff training and
manual construction.

(o) **Review and Analysis of Liabilities for Defined Benefit Schemes**

Related to the matter of funding requirements, this should be an ongoing component of the
supervisory process in support of risk-based operations and inspections. There should be a formal
process for performing these reviews and analyses based on a standard matrix. The processes used by
counterpart regulators should be requested and considered for adoption where feasible. The results of
the process should form part of PIA’s pension scheme data base and given significant weight in the
risk rating structure. This item should be emphasized in the staff training program.

(p) **Solvency Rules for Defined Benefit Pension Schemes**

As an extension of the analysis of liabilities (which looks at the pension scheme as a going concern
entity) it is useful to have an opinion that the scheme would be expected to be solvent should it
terminate in the near future. A set of solvency rules achieves that objective and is of vital utility to
the pension scheme supervisor, sponsors, trustees and members and beneficiaries in cases where a
plan is poorly funded. PIA should carefully consider adopting solvency rules. An example of how
the system facilitates meaningful supervisory reporting to stakeholders is given by the Annual Report
of the Alberta Superintendent of Financial Institutions available at the following URL.
http://www.gov.ab.ca.treasury.

(q) **Information Systems Issues – Pensions**

These are essentially similar to those involving Insurance Supervision in terms of generic
information inputs and outputs that serve the supervisory process. PIA may have to give special
consideration to the needs of the Pension Department in terms of such issues as member access to
their scheme information, facilitation of communication with members with deferred benefits,
education and awareness needs of members and the general public regarding pension schemes and
pensions generally, and how those concerns may be addressed through appropriate web-site design.

(r) **Supervisory Fees ~ Pension Schemes**

The pending amendments to the PSRA provide that PIA may levy fees, and in the context of pension
schemes, may do so on the basis of levying contributions to schemes and/or the investment income
of pension schemes. This proposal appears to have caused some concern within the Finance Ministry
and the Pension Industry.
The Finance Ministry has noted that there have been several instances of regulatory or other public
service entities having been authorized to collect or levy fees that have ended in failure of one sort or
another. Thus there is the reasonable desire to avoid further such incidents.
The Pension Industry would be concerned that fees be subject to restraint and that they be deployed
strictly in the pursuit of the best interests of the private occupational pension system.

These concerns are deemed eminently reasonable and prompt the following recommendations.

1. PIA should request regulations be passed that ensure the fees are based on approved budgets
   with allowance for normal volatility in whatever base is selected for the purpose of
calculating the levy. That process should be essentially transparent and this condition would be met if the regulation is sufficiently detailed and the budget approval is also essentially a public exercise. Given the proposed constitution of the PIA Board (industry representation is ensured) the latter requirement should be satisfied.

2. The principle of cost recovery should be enshrined in the levy system. This is the approach followed in Canada where the federal government has passed regulations that are clear in that respect. The system works essentially on a running average basis so as to smooth out the effect of volatility.

3. The regulations should require PIA to publish a statement of the operations of the levy system for the pension schemes for the year under review. The statement should be based on income and expenditure amounts that are included in the consolidated statements for PIA. The suggested disclosure should relieve any anxieties that each industry is being levied on a self-supporting basis. PIA’s administration system should automatically generate the relevant data including all allocations of overhead in support of the transparency of the process.

4. The regulations should function on a continuing basis and output the revised levy for the succeeding fiscal year using as inputs approved budget and anticipated industry trend and economic data. The treatment of prior years’ over- or under-assessments should be transparent. The process should be essentially automated and there should be no need for annual issuance of Statutory Instruments, i.e. when the levy amount is changed.

The detail regarding the regulatory provisions for pension supervision fees based on the cost recovery principle, as adapted by the Government of Canada, is shown in Appendix Six.

(s) Registration of Service Providers (Custodians, Investment Advisors, Administrators and Fund Managers)

The pending amendments to the PSRA contemplate that PIA will register and supervise these entities. There are several issues to be considered in this regard.

First, with respect to Custodians, there would be little merit in allowing as a custodian any entity other than a bank or a wholly-owned subsidiary of a bank that has been registered and licensed by the BOZ. This should be a condition of PIA in granting a registration to a pension scheme.

However, it would be reasonable for PIA and the BOZ to reach a working understanding regarding their respective roles in relation to custodians, especially in regard to the BOZ’s registration and supervision of such entities. I.E. it is reasonable for PIA to appreciate how the BOZ exercises legal control over the provision of custodial services by banks, i.e. the BOZ requires banks to only offer such services through custodian subsidiaries of banks (on a wholly-owned or other basis) which are then actively supervised and inspected by BOZ officers, or BOZ takes the position that registration under the Bank Act automatically conveys authority to provide custodial services in which case such business is inspected by the BOZ in the normal course of its activities. It appears that the Securities regulator also licenses custodians. PIA should consider their acceptability as custodians for pension schemes.

With regard to registration of investment advisors (who only offer investment advice services) and scheme administrators, it may be that the approach contemplates these as being restricted to wholly owned subsidiaries of existing licensed insurers or other licensed financial institutions. In such cases, it would seem to suffice if PIA were to rely on the licensing of such institutions as sufficient for its purposes of supervision of pension schemes. There should be every effort made to avoid multiple registrations and licensing of existing financial institutions.
However, should other investment advisors or plan administrators become active in the market (i.e. entities not incorporated by licensed financial institutions in Zambia) PIA would have to carefully consider its proposed policy to subject them to licensing and supervision. The international experience does not appear to support the assumption of such activities on the part of the supervisor of private pension schemes in such instances, although it is acknowledged that no studies appear to have been made in that respect. Should PIA decide to undertake registration and supervision of such entities it will have to carefully consider the risk/reward structure of so doing and the associated costs. It is unclear that PIA should perform duties that should be properly discharged by the trustees of the pension schemes. It is their responsibility to engage and monitor the performance of service providers. **PIA should focus on monitoring the performance of the trustees and issuing directives and guidelines as necessary to protect pension scheme members and beneficiaries.**

See Appendix Seven for a specimen Code of Conduct for Service Providers.

Pension Scheme trustees in Zambia are currently obliged to engage service providers to their schemes who are known generically as Fund Managers. There are currently 8 such companies active, and they dominate the market. These firms provide both investment advisory, general administration and sundry services to the multi-employer trusts that they have executed in return for management fees. In many cases they are limited liability subsidiaries of Zambian supervised financial institutions.

The contributions of the multi-employer schemes of those Fund Managers and of the other employers who have affiliated with these trusts are paid to the Fund Managers in trust who then invest them in the name of their trust.

The Fund Manager is known as “manager” under the current PSRA (defined as a person who is licensed as a company or institution and is registered under the Act to establish or manage a pension scheme) and does not transact business with the public in the sense of a unit trust or a mutual fund.

The PSRA imposes duties on managers as a consequence of their being registered entities including, to ensure that the pension scheme is at all times managed in compliance with the Act, Regulations, plan rules and directions of the Registrar, to take reasonable care to ensure that the administration of pension funds is carried out in the best interests of members and that members are informed periodically in accordance with the provisions of the Act, to report any occurrences that could affect rights of members, to report any contributions that are more than one month in arrears and to report any mass dismissals in process or impending.

However, the Act does not require any special corporate governance provisions for Fund Managers nor does it impose any minimum capital standards on them.

The meaning of “manage a pension scheme” is not defined but the Act does have some specific duties that a manager must perform, such as appoint an auditor to audit the fund and an actuary to value the pension scheme, (these are to present their reports directly to the trustees and Registrar), prepare an audited annual report of its accounts and file them with the auditor’s report on the fund with the Registrar within 3 months of the end of the financial year. The Fund Manager shall also prepare quarterly returns in prescribed form and file them within 14 days of their preparation (an oversight to be corrected in the pending amendments).
It is to be noted that Fund Managers are not subject to incorporation under the PSRA and, as such, are subject only to the corporate governance standards generally applicable to limited liability companies in Zambia. However, sub-section 13(2) of the PSRA does empower the Registrar to include conditions in the certificate of registration of a Fund Manager “as the Registrar may determine”. (Sub-section 13(3) defines mandatory conditions that shall be included in the certificate.)

Subject to review by PIA legal counsel, it appears possible to mandate governance conditions for Fund Managers by way of registration conditions. This could, it would seem, include minimum capital requirements and other matters.

The question of what such requirements should or might be lies beyond the scope of this consultancy.


In compliance with the mission of the consultancy, this section addresses market development issues and proposals for a policy framework.

(a) Market Development Issues

The following significant impediments to the development of a vibrant, efficient market for private pensions have been identified. The feasibility of market development will be enhanced by way of making headway in removing these impediments.

(b) Government Policy in Specific Areas

The government support of occupational pensions has been inadequate in certain key respects.

(c) Tax Policy

First, there is the issue of taxation. While it is beyond the scope of this work to discuss in detail the alternatives to the current treatment of the taxation of contributions to, investment income accruing in, and benefits paid from, occupational pension schemes (a general discussion has been provided elsewhere in the report) and their advantages and disadvantages, it must be acknowledged that there is significant criticism within the pensions industry in Zambia of the relatively low level of contribution deductibility. This level makes it unattractive for the above-average earner to participate in private pension schemes. This feature, coupled with the exemption from taxation of capital gains, creates a bias toward informal retirement savings outside private occupational schemes.

It may be argued that this bias is overcome by the exemption from tax of benefit income streams at and after retirement. However, that feature may be seen to merely compensate for the fact that there is little possibility to index pensions which are subject to massive erosion after retirement. The absence of capital gains tax (actually the system can be regarded as one with a zero inclusion rate) may also be attributable to the persistently high rate of inflation (countries like Canada and the US have a non-zero inclusion rate).

(d) Economic Policy
Secondly, there is the issue of economic policy. As mentioned, the inflation rate is still extremely high in Zambia. Further, the evidence appears to suggest that it is difficult to earn a reasonable net real rate on investments at reasonable risk. This sort of environment is not conducive to the development of private pensions markets, whether occupational or personal. A low rate of formal employment (less than 10% of persons of employable age are in the formal employment sector) is not conducive to the development of a private pension system. It is through the formal sector that people generate the disposable income necessary for a nascent private pension system to flourish.

(e) Government Commitment to Pensions as an Employer

Thirdly there is evidence that the government has not been as diligent as might have been hoped for in discharging its responsibilities towards supporting the occupational pension schemes that were created by statute and in ensuring that the NPS is meeting its objectives in a satisfactory manner. This dilatory behaviour creates the impression, however mistaken that appearance may be, that government does not take the financing of occupational pension schemes seriously and is disinterested in demonstrating exemplary performance in this respect.

(f) Inadequate Supervision of Occupational Pension Schemes

Fourthly, there is the question of the effectiveness of the supervision of private pension schemes. While PIA is still a young and ambitious organization, it does not appear to have made a significant impact on the performance of Zambian Pension Funds. In particular, more effort needs to be applied to improve the reporting and collection of pension scheme contributions to due and accrued. No directives to the industry have been issued in this regard, nor has the accounting profession been formally engaged in efforts to develop and craft practical ameliorative strategies. In regard to defined benefit schemes with significant unfunded liabilities, PIA should perhaps require trustees and Pension Fund Managers to engage scheme sponsors and employers in discussions with the object of improving the funded status of these schemes and communicating the agreed strategy with members and beneficiaries. PIA faces a serious challenge in addressing the issue of pension scheme contribution arrears. While the incidence and severity of such arrears was not investigated, there is concern that the information that PIA acts on may be inaccurate. It receives reports of arrears situations from Fund Managers and attempts to ensure these are liquidated. The effectiveness of the PIA’s efforts in achieving success in the removal of arrears and in reducing their incidence was not investigated. PIA should maintain data in these respects and include appropriate information regarding its activities and results in its annual report.

(g) Expense of Investment Management and Scheme Administration

Fifthly, the expenses of pension scheme investment management and administration appear to be inimical to the realization of satisfactory net real rates of investment income, a generally accepted precondition for the promotion of retirement saving. In particular, financial reporting has been observed that masks the determination of net real rates of return on the trust funds, unjustifiably flattering the performance of the investment manager. It should be remembered that in regard to defined contribution schemes the investment performance of the funds must normally cover all investment and administration expenses making it critical that the scheme financial reporting disclose the net real rate of return on a proper basis (in the case of a defined benefit scheme it is arguable that the employer finances these expenses via the actuarial normal cost determination process).
(h) Public Knowledge of and Awareness of the Need for, Private Pensions

As is typical of developing jurisdictions, the level of public knowledge regarding the private pension system and awareness of the need for private pensions is inadequate and stands in the way of the system’s growth. Since literacy rates in Zambia are quite high and attendance through secondary school is compulsory, there is no excuse for not making efforts at all levels, public and private, to educate the public and encourage their increased access to the private pension market.

(i) Proposals for a Policy Framework

The following proposals are suggested for evaluation. Of course, some issues concern possible government administrative and economic policy reform. Others fall within PIA’s spheres of activity.

(j) Government Policy

(i) Tax Policy

The government should consider increasing the tax exempt room available for employee contributions to private pensions. Since a reasonable pension requires saving 15-20% of earnings over a working lifetime (assuming a retirement age of 60), and since government support should extend into a significant proportion of the population earning above the average private sector wage, it is suggested that the limit on deduction of employee contributions to private pension schemes be increased, on a phased-in basis, with a long-term target of a limit of the lesser of 7.5% of earnings and a fixed amount equal to 7.5% of 20% of the average wage in the private sector. To cushion the fiscal impact, the taxation of benefit payouts could be made subject to withholding tax at some modest rate, concomitant with the reduction in inflation rates and the corresponding increase in real rates of return. Appropriate accommodation should be made for the deductibility of contributions by self-employed persons.

(ii) Economic Policy

No specific proposals are suggested. Continued effort to reduce the inflation rate and increase real rates of return on securities and equities is seen as essential to the growth of the private pension system.

(iii) Government Commitment to Pension Administration

It is suggested that the government formulate a specific strategy and a high-priority action plan to accelerate the elimination of any contribution arrears that have accrued in the statutory schemes, improve the funded status of those schemes (review of contribution rates, benefit formulation, investment policy and administrative reform to reduce expenses) and improve its delivery of benefit communications to the members and beneficiaries of such schemes. The government should discharge its responsibilities at a level of diligence that it would seek to impose on private scheme sponsors, trustees and managers. Similarly, the government should mandate performance standards and targets for the administration of the NPS as part of a concerted overall effort to highlight its commitment to the pensions system.

(iv) Improved Supervision of Private Pension Schemes
This should be the sole preoccupation of PIA in the pension area.

There is urgent need for multi-front campaign targeting employers and sponsors, trustees, fund managers and the accounting profession to reform the financial reporting of pension schemes. The contribution arrears reporting and amortization issue must be resolved and a high standard set in accordance with international standards.

The solvency of defined benefits schemes that have significantly low funded ratios must be investigated and sponsors required to file specific action plans to remove solvency deficits within a reasonably short time frame.

Pension scheme financial reporting should be improved and a standard performance structure for reporting results of defined contribution schemes developed in consultation with the industry and professional advisors (fund managers, auditors and actuaries). Risk based supervision techniques should be adopted to ensure that PIA’s resources are efficiently utilized.

The publication of the PIA annual report on pension schemes must be expanded and re-focused to ensure that it is useful to all stakeholders, including government, industry, trustees and members and beneficiaries.

Development of internal procedures and policy manuals and staff training and development must receive high priority and be adequately resourced. Document, justify, and propose through due process all legislative and regulatory initiatives necessary to plug any identified gaps in its supervisory scope and/or authorities.

Formulate a long-term strategy for raising the level of knowledge of members and beneficiaries of their pension scheme’s administration, as well as that of the public in general, with targets, performance measures, budgets and consultative process. Press for other government departments and agencies to co-operate and provide resources. These initiatives will only be feasible if PIA obtains significant increases in its financial capacity through fees or levies which will fund the required equipment, technology and staff.
1. **Pension Industry Overview - Detail**

The pension industry in Zambia consists of - (1) the National Pension System “NPS” and – (2) the 200 or so employer-sponsored occupational trusteed pension schemes supervised by the Pensions and Insurance Authority “PIA”. Most of these are defined contribution schemes, but the majority of members are in defined benefit schemes. There are also two very large closed (to new entrants) funds, the PSPF for public servants and the LASF for local authority employees. These are also defined benefit schemes that are supervised by PIA. However, these two schemes were created by legislation or statutory instrument and, as such, are fundamentally different in character from other schemes supervised by PIA. It should be noted that in most jurisdictions, including the US and Canada, these sort of schemes would not lie within the ambit of the responsibility of the pension supervisory authority charged with supervising occupational schemes. There is no data to suggest that personal pensions of individuals in the nature of contractual savings with financial institutions or unit trusts are of significance.

**NPS**

This is a mandatory 2\textsuperscript{nd} tier contributory program that provides defined benefits based on covered earnings indexed to average wages and that requires all employed and workers and employers to contribute at the rate of 5\% of earnings (the self-employed contribute at 10\%). It is a continuation of the precedent National Provident Fund that was based on the defined contribution system, the benefits of which were significantly reduced as a result of hyperinflation. The program pays lump sum benefits on death and retirement and income benefits are available on retirement at age 55. The retirement benefits are computed according to a formula that determines credits for prior periods of contributions to the NPF and that uses a fixed accrual rate based on earnings for contributory periods after the conversion date. Positive cash flow is invested in the Zambian capital markets and in overseas markets, the latter being subject to a portfolio limit, currently 30\% (\?).

The NPS has its own complement of staff to pursue delinquent contributions as does the ZRA. There have been discussions to consider the possibility of delegating this responsibility to the ZRA as is done in other jurisdictions.

The NPS was established by statute and is directed by a Board that is chaired by the principal secretary to the Minister of Labour. Further issues that should be analyzed in regard to the NPS (not within the ambit of this consultancy) are:

- Practices to enforce contribution collection and the financial condition of the NPS.
- NPS practices regarding the provision of information to contributors.
- NPS practice in regard to attempts to locate contributors who are eligible for retirement benefits and thereby minimize the incidence of orphaned benefits.
- NPS investment policy.

The NPS may or may not be authorized to assist trustees/administrators of private occupational pension schemes in locating members whose co-ordinates are not known but who are eligible for retirement benefits by contacting such members at their last known address and advising them to contact the trustees/administrator. This issue should be raised in future discussions with the NPS, the Minister of Labour and the ZAPFM. There are counterpart arrangements in overseas jurisdictions, e.g. the administration of the Canada Pension Plan and the administration of OPRA in the UK. The most recent annual report on the NPS has been requested and will be reviewed if received and time on-site permits.
Private Trusteed Occupational Schemes

PIA supervises some 215 schemes at present, of which 30 or 15% are defined benefit schemes. The number of supervised schemes has been increasing in recent years being some 142 in 2001, 159 in 2002 and 170 in 2003.

However, the distribution is extremely skewed as the number of active members of such schemes currently represents approximately 80% of total active members of all supervised schemes and the number of retired members of such schemes represents about 76% of total retired members of all schemes.

The vast proportion of supervised schemes are participants in multi-scheme, multi-employer trusts that are created by 8 fund management companies that are, in turn, wholly-owned subsidiaries of licensed insurers. (The relationships of insurers and other financial institutions and the presence or absence of holding company structures was not investigated in this connection.) The ZSIC Pension Trust Fund manages over 100 schemes. There were 18 single-employer trusts as at the end of 2003, and there is evidence of efforts of some employers wishing to withdraw from the multi-scheme, multi-employer trusts. Individual employers participate in these arrangements by virtue of their executing “adherence agreements” which oblige them to respect the terms and conditions of the governing trust deed and scheme rules.

Invested assets of supervised schemes totalled some ZK 803B. The PSPF reported ZK 129B or 15% of the total while the LASF reported nil.

Invested assets of supervised schemes have increased from ZK 325B in 2000 a growth rate of approximately 25.3% pa. This is highly unusual but is largely attributable to the high rates of return on investments. If deflated, the growth rate is a more reasonable 3-4% pa.

The financial condition of supervised schemes is not disclosed in the published reports of PIA. However, it is clear from the published data summarized above that the solvency situations of the PSPF and the LASF must be greatly compromised. A file note based on a review of the 2003 financial statements for the PSPF suggests that the deficit in this scheme was almost ZK 2 trillion as at the end of 2002 and is likely to have grown considerably in the interim. It also appears clear that the government, as sponsor - either directly in the case of the PSPF or indirectly in the case of the LASF - has not been sufficiently aggressive in requiring that impediments to the prompt preparation of actuarial valuation reports on these two major schemes be removed.

The nominal rates of return on the invested assets of supervised schemes have been approximately 16.4% in 2001, 22.1% in 2002 and 13.6% in 2003. These estimates have been calculated based on the balance sheet and income/expenditure aggregated data shown in recent PIA Reports. Given that the rates of inflation in those years were 21.4%, 22.2% and 21.4% respectively, and that expenses have to be netted against such rates, it is clear that the net real rates earned on the invested assets were negative.

Contributions to supervised schemes have been increasing rapidly in recent years, the growth rate between 2001 and 2003 being about 88% in nominal terms or about 62% in real terms.

Private occupational pensions in Zambia do not appear to be indexed automatically but there is some evidence that they have been periodically upgraded following retirement in order to attempt to preserve their real value. Given the relatively high rates of inflation in Zambia in recent years it is
evident that pensions would be rapidly eroded in real value once they enter payment in the absence of any upgrading.

The conversion of defined contribution plan accumulations to pensions in Zambia generally involves the issue of life annuities by a licensed life insurer at retirement. These are usually issued by an insurer which is linked to the fund manager, i.e. a form of tied selling. The largest insurer, ZSIC, advises that it uses conversion rates supplied to it by its actuarial consultant and that these rates tend to stay in force for some time (the actual experience was not ascertained). This suggests that these rates are very conservative since interest rate risk is a function of time and, further, given the tied selling and the lack of a competitive market in which to auction sales.

2. Pension Schemes ~ Taxation

NPS - NAPSA
The national pension scheme features a mandatory participatory structure to which all employed, employers and self-employed persons must contribute. This is the National Pension Scheme administered by “NAPSA”. See Appendix III for details regarding this scheme.

Contributions
Employees contribute to the scheme at the rate of 5% in respect of all earnings and employers must contribute on the same basis in respect of their employees. Self-employed persons contribute the full 10% on all their earnings. These contributions are made on all earnings, i.e. are not subject to any maximum covered earnings.

Employers may deduct 100% of their contributions to the NPS from taxable income. However, employees may deduct only contributions that do not exceed the lesser of 15% of earnings, or ZK 15000 per month (or ZK 180000 per annum). Contributions in excess of such amounts are made out of after-tax income. In respect of employee contributions to the NPS, the limits imply that employees earning over ZK 180000/.05 or 3.6 million will not be able to deduct all their NPS contributions for income tax purposes. Most formal sector employees earn substantially in excess of that amount. Since the exempt limit is not indexed to the inflation rate (currently approximately 19% p.a.) the limit’s impact is growing with time.

In addition the effect is exacerbated where employees must also contribute to a private occupational scheme in addition to contributing to the NPS (unless the private scheme is integrated in recognition of the mandated first tier status of the NPS).
It is to be noted that over 50% of ‘direct’ taxes arise from the payment of personal income tax. Consequently the immediate removal of the ZK 180000 per annum ceiling on deductible contributions would have a significant impact on the Government’s revenue from direct taxation and on the fiscal position.

Investment Income
The NPS, being in part a continuation of the National Provident Fund, has a significant investment portfolio (in excess of K500 billion as of 2002) which includes Treasury Bills and Government Securities. The investment income on such assets is subject to a 15% withholding tax which is a final tax on those amounts. No other tax is paid on any income of the scheme by NAPSA.

Benefits
The scheme pays out lump sum benefits and income benefits. Lump sum benefits are available on death, disability or retirement. Income benefits are payable on disability or retirement. No survivor income benefits are paid.
Lump sum benefits paid on death are not taxed, they are treated as gratuities. Lump sum benefits paid on disability or retirement that do not exceed 10 million ZK are not taxed. The amount of any lump sum benefit in excess of 10 million ZK is taxed at the “concessionary” rate of 10%. (The personal income tax system in Zambia features progressive rates with a minimum rate of 10% and a maximum rate of 35%). Income benefits are not taxed.

Private Schemes

Occupational Schemes

These comprise some 200 schemes with funds in excess of K802 billion as at 2003 and covering about 45% of the formal sector workforce.

Subject to the following limit on employer contributions, the tax treatment of contributions to, investment income from Treasury Bills and Government Securities earned by their trusts, and benefits paid from private occupational schemes is the same as that applicable to the NPS.

The total of deductible employer contributions to all pension schemes - both mandatory (NPS) and voluntary (occupational scheme) - is limited to 20% of pensionable earnings. Where the employer is required to make contributions to an occupational scheme that, in addition to the obligatory and fully deductible contribution of 5% of pensionable earnings to the NPS, exceed 20% of pensionable earnings in order to fund the scheme in accordance with the recommendations of the scheme actuary, the contributions that exceed the limit would not be allowed as deductions from the corporation’s taxable income.

Personal Schemes

This area is seen to present significant opportunities for future development. According to industry experts, the nature of the products and their taxation is yet to be determined. (Note: it may well be that the tax treatment of endowment life insurance policies could be cited as a candidate model for that purpose. However the government may wish to encourage the development of specific products in that regard.)

3. **Accrual of Scheme Contributions – Due and Unpaid Contributions Asset**

While it may be argued that the recoverability of this asset of a pension scheme is not easily determinable since this requires assessment of the creditworthiness of the employer or scheme sponsor, that issue must not impair the construction of proper financial statements. Since the role of PIA is to protect scheme members’ interests, PIA should require that this asset be rigorously determined on an ongoing basis and that it not be discounted for recoverability. It must be evaluated and disclosed on the basis of presumed full collectability, coincident with the construction of the financial statements on a going concern basis. In addition, the asset should be accrued with investment income at the net rate of return earned by the investments of the pension fund during the period through which contributions were due but unpaid. The collectability issue is only material in the event of plan wind-up leading to the distribution of collectable assets. (In the case of an actuarial valuation constructed on the premise that the scheme were soon to terminate and wind-up there could be some justification to establish a reserve for doubtful receipt of contributions in order to disclose the solvency position of the scheme.)
International best practice requires that financial statements be based on generally accepted accounting and auditing principles as stipulated in International Accounting Standards which, in turn, normally require that accrual principles be respected. Thus pension benefit legislation typically relies on the soundness of those standards.

PIA should work with the ZICA and the ZAPFM to ensure that accrual accounting standards are respected in the preparation of scheme financial statements.

It is recommended that PIA direct trustees and fund managers to require that scheme financial statements be prepared on the full accrual basis and that they disclose all accrued income receivable including both contributions and investment income. The power to issue such a direction exists under the current legislation and is necessary to ensure that the legislative requirement that schemes operate on safe and sound bases is enforced.

PIA should ensure that it has or will secure sufficient powers to require employers and scheme sponsors to furnish trustees and fund managers with all information needed to facilitate the preparation of scheme financial statements on a full accrual basis included contributions of employees and the employer due and accrued. This requires that PIA’s power to direct extend to all entities, including employers and sponsors, to disclose any and all information relevant to a pension scheme’s operation on safe and sound principles as contemplated by the provisions of the current legislation. Review of the existing legislation suggests that PIA may not now have this authority but this should be verified by way of formal analysis be legal counsel.

At the very least, PIA should immediately take action to ensure members are made aware of the non-disclosure of contributions receivable. This can be accomplished by directing trustees to ensure that the annual benefit statements that are required to be furnished to scheme members include a clear statement that they are prepared on a cash basis and not an accrual basis and may exclude contributions that are due but have not been remitted by the employer or plan sponsor.

It is further recommended that the regulations that are pending clearly require the timely remittance of contributions by employers and scheme sponsors. An example of a regulation in that respect is set out below. It is taken from the regulations passed under the Authority of the Pension Benefit Standards Act of the government of Canada. This is the pension scheme legislation that applies to all persons employed in employment in Canada that is subject to federal jurisdiction (broadly speaking those in inter-provincial transportation, banking, certain crown corporations, nuclear power, special occupational pension schemes for employees of native groups supported by federal funding etc.).

It is subsection (14) of section 9 of the Regulations.

“(14) Payments to a plan shall be made as follows:

(a) the normal cost of the plan and any special payment to be made during the plan year shall be paid in equal instalments or as an equal percentage of the anticipated remuneration to be paid to the members during the plan year and shall be paid not less frequently than quarterly and not later than 30 days after the end of the period in respect of which the instalment is paid;

(b) the contributions of plan members shall be remitted to the administrator not later than 30 days after the end of the period in respect of which such contributions were deducted;

(c) any other payment shall be remitted to the administrator not later than 30 days after the end of the period in respect of which it is made; and
(d) the administrator shall forthwith pay into the fund any amount remitted to the administrator. SOR/94-384, s. 3; SOR/95-171, s. 6(E).

4. **Private Occupational Pension Scheme Environment**

Demographic Overview

The population is some 10.8 M (IMF Estimate) and is distributed as follows (these are aggregate male and female data; the disaggregated data are not available):

- <15 46.5%
- 15-64 51.5%
- >65 2.0%

US Census Bureau

Projected population growth rate: 2% pa

Life expectancy according to UN data:

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Economic

Real GDP growth in the last 5 years has varied between 3.3% and 5.1%. GDP is currently approximately USD 6B or ZK 28.4T.

Recent deficits were running close to 10% of GDP but have subsided dramatically in 2004 to about 2% of GDP.

The inflation rate has declined from 26% pa in 2000 to 19% pa currently.

The Treasury bill yield has declined from 32% pa in 2000 to about 15% currently.

Only 10% of those in employment are in the formal sector, about .5M persons.

Earnings of individuals in the formal sector: these vary considerably by type of employment, e.g. senior government teachers’ wages are about USD 200/mth or ZK .9 M. per year. Note that the tax-exempt pension contribution amounts to ZK 15000 per month or .18M per year. Assuming a 5% employee contribution rate implies that contributions by persons earning up to .18/.05 = ZK 3.6M per year would be exempt from income tax.

Actuarial Assumptions for Pension Schemes

The following is based on a review of a large multi-employer scheme covering workers in the mining industry. Note: these assumptions would not necessarily apply to those used to compute life annuity rates and reserves.
Mortality: the basis for active members was the SA56-62 life table plus a loading for aids. For retired members the British a (55) table was used.

Economic: inflation rate of 11%, interest rate of 15%, salary increase rate of 13% and a pension increase rate of 5%.

Effect of HIV/AIDS Pandemic

Notice has been taken of a view that considers the HIV/AIDS Pandemic to have had the net effect of increasing the financial burden of providing private funded occupational pensions. It would be interesting to ascertain if this is a prevailing view in other afflicted jurisdictions and to analyse the rationale for such a conjecture. It would appear that the increased mortality would indeed increase the present value of death benefits, survivor benefits, and orphans benefits, but would decrease the present value of retirement benefits. In addition, while the incidence of death benefits and survivor benefits might well increase, their present value would likely decrease.

5. INPRS Principles for the Regulation of Private Occupational Pension Plans

The International Network of Pension Regulators and Supervisors (INPRS) Endorses Principles for Private Occupational Pensions has approved a set of principles for the regulation of private occupational pension plans designed to safeguard the interests of beneficiaries and ensure the efficient running of such plans.

They are as listed below together with comments as to the extent to which the current regulatory and supervisory system in Zambia complies with their intent. These comments are amplified in the discussion of the compliance/self-assessment of PIA and the legislation with the 8 Core Principles that follows.

FIFTEEN PRINCIPLES FOR THE REGULATION OF PRIVATE OCCUPATIONAL PENSIONS SCHEMES

Adequate regulatory framework

Principle No1: An adequate regulatory framework for private pensions should be enforced in a comprehensive, dynamic and flexible way (taking into account the complexity of the schemes) in order to ensure the protection of pensions plans beneficiaries, the soundness of pensions funds and the stability of the economy as a whole. This framework should however not provide excessive burden on pension markets, institutions, or employers.

Comment: the regulatory framework is not deemed to be adequate at this time. Although there is legislation in place that is based on reasonable principles and that confers regulatory powers on PIA, it is compliance based and somewhat restrictive in terms of the capacity of the regulator to intervene. There is a great need for upgrading of staff and other resources (a key component of an adequate regulatory framework) to enable PIA to approach compliance with this principle. Scheme members and beneficiaries do not enjoy adequate protection for a variety of reasons, including very significant gaps in the remittance of contributions, negative real net rates of return on funds, tied purchasing of retirement annuities, and inadequate monitoring and enforcement of employer support obligations for scheme funding and administration.
APPENDICES

Appropriate regulation of financial markets

Principle N°2: A productive, diversified investment of retirement savings which spreads risk requires well-functioning capital markets and financial institutions. The development of advance-funded pension systems should go hand-in-hand with a strengthening of the financial market infrastructure and regulatory framework (including the development of new financial instruments and new markets such as inflation-indexed markets and the improved functioning of retirement annuity markets).

Comment: since the assessment of the regulation of financial markets was not a component of the current consultancy it is not possible to comment on this point. However, there was little evidence in discussions with industry officials of developments in this area. Some comments suggested industry dissatisfaction with the depth and liquidity of the equity market, and there were negative comments regarding the over-weighting of portfolios with real estate. The securities markets do not appear to offer substantial opportunities to earn positive net real rates at low levels of risk.

Rights of the beneficiaries

Principle N°3: Non-discriminatory access should be granted to private pensions schemes. Regulation should aim at avoiding exclusions based on age, salary, gender, period of service, terms of employment, part-time employment, and civil status. It should also promote the protection of vested rights and proper entitlement process, as regard to contributions from both employees and employers. Policies for indexation should be encouraged. Portability of pension rights is essential when professional mobility is promoted. Mechanisms for the protection of beneficiaries in case of early departure, especially when membership is not voluntary, should be encouraged.

Comment: the access conditions are subject to the rules of the Zambia Revenue Authority and, possibly other laws. As the investigation of such matters was beyond the scope of the consultancy, it was not possible to evaluate compliance with this principle. However, there is a requirement for portability in the PSRA 1996. There is no apparent encouragement for any policy on indexation, a matter of seemingly great concern in Zambia.

Adequacy of the private schemes

Principle N°4: Proper assessment of adequacy of private schemes (risks, benefits, coverage) should be promoted, especially when these schemes play a public role, through substitution or substantial complementary function to public schemes and when they are mandatory. Adequacy should be evaluated taking into account the various sources of retirement income (tax-and-transfer systems, advance-funded systems, private savings and earnings).

Comment: this component was not specifically addressed as part of the activities of the consultancy. The strategic focus of PIA does not extend to these issues as it is primarily concerned with its responsibilities as a prudential regulator and which are cited in the preamble to the PSRA 1996. However, it is noted that the occupational system in Zambia covers a relatively small proportion of the employments in the formal sector. Since it appears that few schemes provide indexed benefits the question of adequacy is a matter of considerable urgency.

Regulatory system and separation

Principle N°5: An institutional and functional system of adequate legal, accounting, technical, financial, and managerial criteria should apply to pension funds and plans, jointly or separately, but without excessive administrative burden. The pension fund must be legally separated from the sponsor (or at least such separation must be irrevocably guaranteed through appropriate mechanisms).
Comment: There is substantial compliance. However, administrative expenses appear inordinately high relative to contributions and investment income (in part this may be attributable to a lack of economies of scale given the small size of the formal sector in Zambia), there is a significant problem regarding the consistency of schemes’ audited financial statements, and there is a lack of actuarial resources at PIA.

Funding

Principle N°6: Private schemes should be funded. While full-funding exists in principle for defined contribution plans, other types of plans should be subject to minimum funding rules or other mechanisms to ensure adequate funding of pension liabilities. Rules based on winding-up approach (e.g. ABO, PBO) may be promoted as a minimum level to complement the on-going approach. Flexibility can be allowed for temporary limited under-funding under restricted circumstances. Consideration should be given to the development of adequate but flexible requirements for minimum capital/guarantee in pension funds, taking account of the long term nature of their liabilities. Tax and prudential regulations should encourage a prudent level of funding. Private unfunded pay-as-you-go schemes at individual company level (i.e. overheads schemes) should be prohibited.

Comment: The funding of schemes is not subject to any set of regulatory rules. Actuarial reporting is required but no authority exists for the override of unsatisfactory or inadequate actuarial bases. This could be hailed as a triumph of reliance, but as a regulatory strategy it lacks proper safeguards. However, all fund managers and schemes are presently required to appoint and actuary. This should ensure that any capital guarantees are identified and appropriate funding instituted. It is not clear what PIA requires of employers or scheme sponsors in terms of the selection of a funding program from among a menu of options for funding prior service unfunded liabilities or deficits. There is no requirement to provide a solvency opinion in general for defined benefit schemes nor is there a requirement to file a solvency valuation report where the scheme is unfunded.

Calculation Techniques

Principle N°7: Appropriate calculation methods for asset valuation and liabilities funding, including actuarial techniques and amortisation rules must be set up and based on transparent and comparable standards. Increased reliance on modern and effective risk management, industry-wide risk management standards for pension funds and other institutions involved in the provision of retirement income should be promoted. The development of asset liability management techniques should be given proper consideration.

Comment: PIA relies on actuaries to determine the bases for their reports. PIA lacks the resources to monitor the compliance of such bases with proper actuarial practice and there is no evidence that PIA has referred any cases to an institute of actuaries for review and comment. PIA plans to issue regulations following the amendment of PSRA 1996 that may assist in filling these gaps.

Supervisory structures

Principle N°8: Effective supervision of pension funds and plans must be set-up and focus on legal compliance, financial control, actuarial examination and supervision of managers. Appropriate supervisory bodies, properly staffed and funded, should be established in order to conduct when relevant off and on site supervision, at least for some categories of funds and in particular when problems are reported. Supervisory bodies should be endowed with appropriate regulatory and
supervisory powers over individual plans, in order to prevent miss-selling cases arising from irregularities in the distribution and expenses methods.

Comment: There is inadequate compliance with this principle at present. PIA lacks sufficient resources to effectively and efficiently supervise the 200 schemes currently in force. Individual pension plans are not a part of PIA’s mandate under the PSRA 1996. However, it is not clear that any such plans exist in Zambia in any case.

Self-supervision

Principle N° 9: Self-regulation and self-supervision should be encouraged. The role of independent actuaries, custodian services and internal independent supervisory boards should be promoted within an appropriate regulatory framework.

Comment: There is substantial compliance. However the independence of current Boards of Trustees could be argued. PIA has proposed amendments to the PSRA 1996 that will require 50% member representation on the Boards of Trustees.

Fair competition

Principle N°10: Regulation should promote a level playing field between the different operators and take account of the usefulness of a functional approach. The fair competition should benefit to the consumers and allow for the development of adequate private pensions markets.

Comment: The existing regulation prevents employer sponsors from administering their own schemes using whichever service providers they wish to employ for those purposes. Pending amendments to PSRA 1996 will permit the registration of such schemes. Solutions to the problem of accommodating the re-structuring of existing schemes that are affiliated to multi-employer trusts are being considered.

Investment

Principle N°11: Investment by pension funds should be adequately regulated (see selected principles for regulation of investments by insurance companies and pension funds in Annex). This includes the need for an integrated assets/liabilities approach, for both institutional and functional approaches, and the consideration of principles related to diversification, dispersion, and maturity and currency matching. Quantitative regulations, and prudent-person principles should be carefully assessed, having regard to both the security and profitability objectives of pension funds. Self-investment should be limited, unless appropriate safeguards exist. Liberalisation of investment abroad by pension funds should be promoted, subject to prudent management principles.

Comment: Compliance with this principle is incomplete. The PSRA 1996 mandates that all pension trusts and schemes must operate in accordance with an investment policy. However, there are no minimum standards set by PIA for the governance of the establishment, design and monitoring of schemes’ investment policies. PIA needs to carefully implement proposed investment guidelines in order to ensure that they do not inappropriately interfere with or override the pursuit of prudent investment policies and practices. The guidelines should emphasize the need for prudent portfolio management rather than promoting a narrow focus on prescribed maxima and minima for specific asset classes.

Insurance mechanisms
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Principle N°12: The need for insolvency insurance and/or other guarantee schemes has to be properly evaluated. These mechanisms may be recommended in some cases but in an adequate framework. Recourse to insurance mechanisms (group and reinsurance) may be promoted.

Comment: This issue is not currently under evaluation by PIA.

Winding-up

Principle N°13: Proper winding-up mechanisms should be put in place. Arrangements (including, where necessary, priority creditors’ rights for pension funds) should be put in place to ensure that contributions owed to the fund by the employer are paid in the event of his insolvency, in accordance with national laws.

Comment: There is partial compliance. Section 31 of the PSRA 1996 protects contributions in the event of employer insolvency. Section 36 permits the Registrar to establish an asset distribution plan where a de-registered scheme is insolvent. There is no apparent control over the wind-up of solvent schemes including how surplus should be allocated, if any. Proposed amendments to the PSRA 1996 will introduce additional provisions and relevant regulations have been drafted that will amplify regulation of wind-ups.

Disclosure and education

Principle N°14: Appropriate disclosure and education should be promoted as regards respective costs and benefits characteristics of pensions schemes, especially where individual choice is offered. Beneficiaries should be educated on misuse of retirement benefits (in particular in case of lump sum) and adequate preservation of their rights. Disclosure of fees structure, plans performance and benefits modalities should be especially promoted in the case of individual pensions plans.

Comment: Compliance of PIA with this principle appears inadequate. More needs to be done in terms of member education – mere requirements to provide them with plan rules and annual statements may not be useful unless accompanied by informational material that explains the necessary detail. Disclosure of expenses and rates of returns needs to be completely reviewed and uniform disclosure rules designed and enforced.

Corporate governance

Principle N°15: The corporate governance role and capacity of pension funds should be considered. This includes: the role of guidelines (statutory or voluntary) for governance activities; the impact of shareholder activism by pension funds on corporate behaviour; and the governance of pension funds themselves and the role of trustees.

Comment: Compliance is inadequate. However, PIA has proposed amendments to PSRA 1996 that will impose some specific duties on scheme trustees. PIA should document good governance practice and performance criteria for trustees, employers, and other key role players in the private occupational sphere and issue relevant guidelines that it can then monitor.

6. Fees for Supervision of Private Occupational Pension Schemes

The system for recovering costs of supervision of private occupational pension schemes in Canada is prescribed by regulation. The fee calculation for a scheme is made every year and is to be remitted with the scheme’s annual information return. The process is administrative, i.e. does not require ministerial action in order to be effective. The calculation is based on the number of scheme...
members so as to, in part, reduce the volatility of the cost recovery process, an issue that can be problematic should the fees be based on contributions or investment income of the fund.

The following is an excerpt from the Canadian Pension Benefits Standards Regulations that sets out the detail involved in the calculation. Note that the fee is subject to a minimum and maximum per scheme.

FEES

25. (1) In this section,

"number of plan members" means the number of employees who are on the payroll of an employer or the total number on the payroll of all participating employers in a multi-employer pension plan

(a) in respect of a plan that is filed for registration pursuant to section 10 of the Act, at the time the plan is filed for registration, and

(b) in respect of an information return filed pursuant to section 12 of the Act, on the last day of the plan year in respect of which the information return is filed; (nombre d'adhérents)

"office year" means the period beginning on April 1 in one calendar year and ending on March 31 in the next calendar year. (année administrative)

(2) In respect of a pension plan, the plan fee base is the number that is equal to the aggregate of

(a) 20;

(b) the lesser of

(i) the number of plan members in excess of 20, and

(ii) 980; and

(c) the lesser of

(i) 50 per cent of the number of plan members in excess of 1,000; and

(ii) 9,000.

(3) A fee shall be paid for the registration of a pension plan by the Superintendent

(a) at the time the plan is filed for registration pursuant to section 10 of the Act, in an amount that is equal to the plan fee base multiplied by the basic rate that is in effect at that time; and

(b) where the last day of a plan year of that plan occurs after the plan is filed for registration and before the plan is registered, on filing an information return pursuant to section 12 of the Act, in an amount that is equal to the plan fee base multiplied by the basic rate that is in effect six months after the last day of the plan year in respect of which the information return is filed.

(4) [Repealed, SOR/2001-222, s. 4]

(5) The basic rate for an office year beginning on or after April 1, 2002 is the rate determined in accordance with the formula

(A + B)/C
where

A is the estimated total of expenses expected to be incurred during the office year for the registration of plans and their supervision, including inspection, by the Superintendent;

B is 20% of the amount by which the total of expenses incurred for the registration of plans and their supervision, including inspection, by the Superintendent in the second to sixth preceding office years, but not those years ending in or before 2000, exceeds the total of fees and expenses paid under this section and subsection 34(3) of the Act in the second to sixth preceding office years but not those years ending in or before 2000; and

C is the estimated total of the plan fee bases of all plans expected to be filed for registration under section 10 of the Act during the office year, or for which an information return is expected to be filed during the office year under section 12 of the Act.

(6) Each time an information return is filed for a plan under section 12 of the Act, a fee shall be paid for the plan's supervision, including inspection, by the Superintendent.

(6.1) The fee referred to in subsection (6) is the amount determined by multiplying the plan fee base in respect of the plan by the basic rate that is in effect six months after the end of the plan year in respect of which the information return is filed.

(7) The Superintendent shall publish in the Canada Gazette Part I a notice setting out the basic rate that is established pursuant to subsection (5) in respect of each office year beginning on or after April 1, 1992, not later than 180 days before the beginning of that office year. SOR/90-363, s. 5; SOR/91-228, s. 1; SOR/2001-222, s. 4.

7. Specimen Code of Conduct for a Service Provider

For Intermediaries Registered by the AUTHORITY

The following is suggested as an appropriate code of conduct applicable to individuals registered by the AUTHORITY to transact with members/clients/policyholders/subscribers of/to the Occupational Pension System or the Insurance Industry. It is adapted from a code drafted by the Financial Services Commission of Ontario.

A registered/licensed intermediary shall not contravene or fail to comply with the following code of ethics in respect of any transactions or communications with potential members/clients/policyholders/subscribers or members/clients/policyholders/subscribers to the Occupational Pension System or the Insurance Industry

A registered intermediary shall:

Maintain at all times high standards and integrity and fairness in all their dealings and in the conduct of their business.

Maintain at all times high standards of service, exercise due diligence and ensure proper care and exercise independent professional judgment.
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Make a diligent and businesslike effort to learn such information about a member/client/policyholder/subscriber as is necessary to be informed about such person’s retirement, insurance and financial plans or objectives, needs and constraints.

Place the member’s/client’s/policyholder’s/subscriber’s interests ahead of the intermediary’s own direct or indirect interests and act at all times in the best interests of the member/client/policyholder/subscriber.

Provide a quality of service that is reasonably to be expected of a service provider acting in good faith with a client and act in a timely, efficient, respectful and courteous manner.

Use best efforts to obtain information about a member/client/policyholder/subscriber directly from the member/client/policyholder/subscriber and do not obtain such information from another source without the knowledge and consent of the member/client/policyholder/subscriber.

Advise a member/client/policyholder/subscriber subscriber as to the purposes for which personal information is being collected and of any changes in such purposes.

Protect personal information obtained from a member/client/policyholder/subscriber with security safeguards appropriate to the nature and sensitivity of such information.

Not disclose information about a member/client/policyholder/subscriber to another party before informing the member/client/policyholder/subscriber and obtaining his/her the written approval.

Provide to the member/client/policyholder/subscriber, prior to giving any advice, counsel or other information, such information as is prescribed by the AUTHORITY regarding the Intermediary, member/client/policyholder/subscriber rights and obligations, including right to redress, and the roles and responsibilities of Intermediaries and the AUTHORITY.

Provide the member/client/policyholder/subscriber with documentary evidence of the Intermediary’s registered status.

Provide the member/client/policyholder/subscriber with a written statement showing all sources of remuneration or compensation or fees, and the manner of their determination, which the Intermediary will receive as a result of, and in respect of, all amounts paid to the Intermediary by the member/client/policyholder/subscriber in trust or in consideration for the member’s retirement account or insurance contract.

Present accurately, honestly, completely and in clear, plainly and easily understood language, all answers to questions posed by a member/client/policyholder/subscriber and all facts known to the Intermediary to be relevant to the person’s circumstances and needs so as to permit the member/client/policyholder/subscriber to make an informed decision regarding his or her pension scheme membership or insurance contract.

Provide a member/client/policyholder/subscriber with full and fair disclosure of all risks that the member/client/policyholder/subscriber is undertaking and ensure that all communications of such risks and return expectations are in accordance with the prescriptions of the AUTHORITY for such purposes, and that no elaborations, interpretations, extensions or modulations of such risks and return expectations are provided.
Inform a member/client/policyholder/subscriber that all information that the individual provides to the Intermediary must be accurate and complete and that failure to do so could compromise the subscriber’s rights or interests.

A registered Intermediary shall not:

Use any unethical means to sell, market, or induce any member/client/policyholder/subscriber to take any action or refrain from taking any action with respect to the individual’s pension scheme membership or contracting with an insurance company.

Hold out, directly or indirectly, by representation or omission, in a way that is misleading, or likely to mislead, regarding pension scheme benefits or privileges or insurance contract benefits or rights or services.

Misrepresent his or her training, qualifications or skills.

Make any false or misleading statement or representation in the course of communicating or transacting with a subscriber.

Induce or attempt to induce, directly or indirectly, by way of rebate, payment or provision of a benefit of any kind or otherwise to a subscriber or a person related to a subscriber, to subscribe, continue to subscribe, alter or terminate his or her subscription or alter, modify rescind, or refrain from altering, modifying or rescinding, any choice or election with respect to any option open to a subscriber under the NPS.

Use coercion or undue influence in order to control, direct or secure subscriptions to the NPS.

Take advantage of a subscriber if the Intermediary knows or ought to know that the subscriber is unable to understand the character, nature, language or effect of a transaction or a proposed transaction.

Submit information on behalf of a subscriber that the Intermediary knowing that the subscriber has misrepresented or failed to provide any required information.

Fail to deliver in a timely manner any information destined for the subscriber that has been provided to the Intermediary by any other Intermediary, POP, the CRA or the AUTHORITY.

Charge any fee to, or solicit any amount, payment or benefit from, a subscriber

Use any material or advertising related to the NPS, a POP, Intermediary or PF that has not been approved by the AUTHORITY.

Present any comparisons of rates of returns, expenses, options, benefits, rights, obligations, product features, market index data, or financial statements of registered Intermediaries, POPs or PFs that have not been authorized by the AUTHORITY for such purposes.
8. Fees and Costs – Private Pension Schemes

The following material on the subject is quoted from the World Bank Report “Old-Age Income Support in the Twenty-first Century: An International Perspective on Pension Systems and Reform” published in web format on February 18, 2005

The relevant URL is http://www1.worldbank.org/sp/incomesupport.asp

“Fee Structure and Levels

The amount of fees or charges levied on financial retirement products is an area of considerable debate and research. For critics of a funded pillar, these fees are much too high, in particular compared with the best unfunded and public benchmark; they reduce the net rate of return to sometimes unacceptably low levels and thus dominate the potential return advantage of a funded pillar; and the structure of fees is often non-transparent and anti-poor, which prevents a broader pension coverage of lower-income groups. Also, supporters of a funded pillar (including the Bank) recognize the need to bring fee levels down and to rework the structures. But they see the problem as much more manageable, with fee levels in client countries much more in line with those of popular financial services in developed countries and failing after start-up costs have been covered. Still various areas require closer investigation in and across countries and regions (first stock-taking exercises include those by James, Smallhout and Vittas 2001; Whitehouse 2000; World Bank 2002 and Yermo 2002. This submission concentrates on three issues dealing with the measurement of fee levels and the approaches for their reduction or limitation.

Measuring and Comparing Fee Levels

Across countries, charges and fees (administrative charges and management fees) on long-term financial products, such as pensions, are levied in many different ways. Some are one-off fees, usually a fixed sum payable up-front or at maturity. Others are ongoing and can take the form of a fixed fee per period, a percentage of contributions or premiums, or a percentage of assets. One main problem with international comparisons is that products offer different services and pension systems have different structures. For example, some plans have guaranteed minimum returns or guaranteed minimum pensions, while others do not. Obviously, everything else being equal, guaranteed products should have higher fees. Also, some plans provide better services, such as higher rates of return and immediate benefits to plan members, and could justify being more expensive. Finally, funded pillars that rely on the public pillar to collect contributions (for example, Argentina) should have lower administrative costs than those that are independent of government.

A national and international comparison of fee levels requires a comprehensive and life-cycle-type approach in which all types of charges, for, say, a full working life are considered and, for example, the gross amount and the net accumulated amount are compared at retirement (Whitehouse 2000). Time-specific comparison of fees and flows (contributions) and stocks (assets) alone are of little value.

Fee-Level Limitation via Regulation of Structure

Countries have taken different approaches to regulating the fee structure of pension funds. For example, Australia, Hong Kong (China), the United Kingdom, and the United States have few, if any, explicit restrictions on charges and instead regulate charges under the broader “prudence” or “reasonableness” standards. This is partly explained by the fact that private pensions in the United States remain voluntary, while in other countries they are built on pre-existing voluntary systems. Most World Bank client countries limit the structure of charges, and quite a few have restrictive
regimes in that companies are limited to two charges (an asset-based and a contribution-based charge), one of which is subject to a ceiling (asset-based charge) while the other can take any value.

It is still unclear to what extent these limitations on the structure lead to effective lower fee levels or what they imply for the longer supply structure (number of funds) or demand structure (scope of coverage). It appears that these limitations (for a first assessment of four European and Central Asian countries, see World Bank 2003). We suggest that a simple and transparent fee structure with well-thought-through price caps is a useful approach when such new pillar is introduced. But these limitations need to be reviewed regularly and adjusted with other pillar characteristics if deemed necessary; it is quite likely that they will be relaxed as time progresses and individuals become more familiar with the system.

Fee-Level Limitation via Special Organisation of Providers

Several models of pension fund management are aimed at reducing fees by reducing costs. The basic idea is that, in competitive markets, costs are the major determinant of fees and, moreover, we should be concerned with the real cost of producing the services. International experience indicates that close-end funds (those limiting membership to employees of a firm, industry or profession) have lower fees than open-end funds, perhaps because they incur lower marketing costs. Some countries use a centralized competitive-bidding process to outsource fund management (Bolivia, Kosovo, and Latvia but not Sweden). These systems have resulted in lower fees, although it is not clear whether the related reduction in worker choice is sustainable. In this regard, the experience of the Federal Thrift Savings Plan in the United States (covering only Federal government workers) is encouraging. Its gross expense ratio has declined steadily as the fund assets have grown, from an average of .67 percent of funds in 1988 to .07 percent in 1999 (Hustead and Hustead 2001; James, Smallhout and Vittas 2001). It is by far the lowest fee structure in the industry. (Footnote – However, record keeping is subsidized to some extent through the administrative structures of government agencies that separate and forward payroll deductions.) Another important case for reducing fees while providing almost unlimited investment choices to plan members is the Swedish scheme. The majority of Latin American and some Eastern European countries adopted a model of open-end and specialized fund managers, with either centralized or decentralized collection and record-keeping systems. These models have produced relatively high management fees, especially in their early years. Although their fees are not higher, and in some cases are lower, than those of personal and stakeholder plans in the United Kingdom, there is still room for reducing them by addressing the issue of industry concentration.

Deregulation of fees and market contestability (for example, providing options to plan members) promotes competition but require stronger disclosure of information. Fund managers have to provide affiliates with statements of their accounts. In addition, at least once a year they need to provide affiliates with basic information about the pension fund management company (ownership, managers, directors, and audited financial statements, including the auditor’s report) as well as information on the fee structure and rate of return relative to the respective system’s average, taking into account the long-term view. The greater the choice and contestability, the greater the incentive of fund managers to spend money on public relations and marketing – costs that are eventually passed on to worker-affiliates.

Again, it is too early to make strong recommendations, but the experience, so far, suggests three promising approaches. First, limit costs by saving on the administrative costs of contribution collection, account administration, and so forth (that is, by adopting the clearinghouse approach). Second, limit the incentives for marketing expenditures by pension funds through blind accounts or...
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constraints on the ability of individuals to change funds as a result of laws or exit fees. Last, but not least, limit asset management fees by restricting the choice of individuals, including the use of passive investment options, employers’ choice of financial provider, or competitive bidding for a restricted number of service providers.”

Note – the extended titles of the references cited in the above material may be obtained by consulting the report at the web co-ordinates previously mentioned.

Additional data regarding fees and charges may be obtained from the papers submitted to the September 2003 OECD Moscow Conference available at the OECD web site. In particular refer to the document entitled “Costs and Charges of Pension Funds in Transition Economies (Room Document No. 11, Session 9) by Agnieszka Chlon-Dominczak, Ministry of Labour and Social Policy, Poland.


9. Detailed Comment on the 1996 Pension Scheme Registration Act

There is provision for the investment of funds in such investments as may be approved by the Registrar, the issue of guidelines relating to the upper limits for investment categories and for the investment of up to 30% of a fund in ‘offshore’ investments. Guidelines for investments have been proposed but are pending.

These guidelines will not necessarily be appropriate for all schemes whose circumstances will change over time. For example, a scheme that is about to be discontinued should not be required to maintain a minimum proportion of its investments in volatile categories such as equities and real estate. On the other hand, some schemes may wish to offer members the opportunity to follow ‘life-cycle’ principles of investment management of their accounts. The imposition of arbitrary limits will interfere with this option. It is suggested that the guidelines recognize the need for additional flexibility and permit schemes to apply for exemption subject to PIA review and approval.

The Registrar has, in addition to prescribed functions, the duty, jointly shared with the auditor and actuary, to protect members and monitor the viability of pension schemes and ensure they operate on sound financial and actuarial principles. The Registrar shall also ensure that the recommendations made by the scheme actuary are carried out by the manger and trustees within the deadlines fixed by the Registrar in consultation with the actuary, the manager and the trustees.

This is an important feature or the legislation and presents PIA with opportunities to press for improvements in scheme management. For example, PIA could issue directives requiring increased monitoring activity in the case of schemes that are attempting to amortize solvency deficiencies, by, for example, requiring annual actuarial investigations and monthly reporting of contribution remittances for such schemes. Where schemes do not comply with sound management, e.g. where contribution remittance arrears exceed some reasonable threshold, PIA could issue a directive to trustees and fund managers to notify scheme members of the delinquency.

The Registrar has the authority to enforce any conditions imposed under the Act on a pension fund, trust or manager of a fund or trust. The Registrar may also attach such conditions to a certificate as
the Registrar may determine are necessary to ensure that members’ rights under the pension scheme are protected.

The Registrar has the authority to issue directives to the manager of a pension scheme to refrain from adopting or pursuing any unsafe or unsound act or practice whether this is in respect of the manager, the auditor or the actuary.

This authority should be exploited to ensure that unsafe or unsound practices are identified (see comments above) and suppressed. Scheme members should be made aware of these directives and of non-compliance. Where non-compliance persists, PIA should pursue termination and wind-up of the scheme.

The Registrar must perform on-site inspections in the event of specific occurrences but may do so at any time so as to determine the viability of the pension fund and whether it is operation prudently.

PIA should ensure that its inspection program is risk-based and driven by the needs of the members of schemes most at risk given its mandate to protect the rights and benefits of members. That implies appropriate measures to enhance date collection and analysis in respect of plans that are funding solvency deficiencies and increased inspection frequency of such schemes. It should be realized that non-remittance of contributions is tantamount to a growing solvency deficiency in the case of a defined contribution scheme. Where solvency of any scheme is deteriorating it should be subject to termination and wind-up.

The Registrar may de-register a pension scheme in the event of non-compliance by the manager in respect of requirements of the Act, regulations or scheme rules. The Registrar, prior to de-registering a pension scheme, may appoint a curator for purposes of devising a plan of rehabilitation for a pension scheme. Where a scheme rehabilitation plan is not accepted the Registrar may de-register the scheme and in the event the Registrar finds that the scheme is insolvent, the Registrar may take over the distribution of assets and the supervision of the scheme.

Decisions of the Registrar may be appealed to the Minister and those of the Minister may be appealed to the High Court.

The Registrar may, in consultation with actuaries and auditors, prescribe and publish guidelines or other regulatory statements as may be considered desirable or necessary for the administration and execution of the Act.

The Act further provides for the submission of audited statements of pension funds and for the filing of quarterly returns in prescribed form relating to the investments of pension funds. The quarterly returns are available for inspection by the public free of charge.

PIA should seek to obtain the authority to publish more financial information regarding the financial condition of pension schemes. While there may be justification for protecting the identity of schemes in that regard, the public should be informed of the distribution of covered members by solvency ratio, for example. The annual report of PIA should be a source of more information of relevance to the protection of members. The distribution of scheme members by degree of contribution arrears would be another salutary disclosure. The public should know what %’s of schemes and of members are exposed to arrears over 3, 6, 9, 12 months respectively.
Detailed Comment on the Pending Amendments to the PSRA

The amendments are, in large measure, useful extensions of, and remedies of gaps in the legislation. However, PIA will have to conduct a careful study of the implications of their coming into effect for its administration and organization. There is already ample indication of the need for greater activity on the part of PIA in order to effectively discharge its present legislated mandate and the increased expectations of the new provisions will have to be recognized and addressed. Specifically, PIA must inventory these requirements and identify those that will involve increased work that cannot be managed through the application of risk-based principles, i.e. what items will produce increased processing of information and approval, e.g. applications for registration and review of filings, compliance with new requirements related to fit-and-proper criteria, items involving Board or Ministerial approval, and other situations where specific effort is required irrespective of the degree of risk putatively being managed through the existence of the requirement.

The new requirements will have to be supported with well thought-through and documented administrative procedures so as to minimize the bureaucratic measures and engagement of skilled staff needed to address other pressing high-risk situations.

The results of this exercise should be reflected in the design of internal work procedures and staff training.

The following are some specific comments regarding the provisions of the proposed amendments.

New paragraph 5(1)(f) – include reference to fund managers, administrators and custodians.

Confirm that paragraphs 5(1)(p) and 7(4)(l) permit the contracting with outside auditors, actuaries and other experts.

Confirm that the legislation authorizes PIA to control all surplus refunds and contribution holidays. PIA should document its objectives in regard to those spheres in consultation with stakeholders, and analyze the requirements of its counterpart regulators in neighbouring jurisdictions. At least, no refunds or holidays should be made or commenced without the written approval of the PIA Board or Registrar.

Termination and Wind-Up Provisions

It is recommended that the legislation be comprehensively reviewed to ensure that, as amended, it will provide for a logical and consistent approach to the process of terminating and winding-up pension schemes. The normal sequence is for a scheme to voluntarily terminate or to be terminated for cause which may include specific causes such as failure of the sponsor or unwillingness of the sponsor to continue to meet minimum funding requirements. Termination must be notified to all parties including members and beneficiaries allowing time for objections and inquiries and for their disposal. Following that process, winding-up should proceed and the regulations should make provision for those particulars. The last action, once all assets have been distributed and appeals etc. have been exhausted, the scheme should be de-registered. Where it is deemed necessary or desirable to interpose a rehabilitation exercise, such as contemplated by sub-section 33(3) of the PSRA, it should be executed prior to the giving of the termination notice, and should be under the control of the Registrar.
APPENDICES

It should be required that, in the event of termination of the scheme, all benefits vest with full rights to all privileges (e.g. to early retirement without trustee or sponsor consent) immediately irrespective of the terms of the scheme or trust, and that no funds may be paid to the sponsor or other party without the approval of the Registrar. The winding-up mechanics may be delegated to a winding-up agent who has been appointed by the Registrar. Legal opinion should be obtained regarding whether the authority to appoint a winding-up agent should be in the Act or the Regulations and whether it may be discharged by the Board or the Registrar. During the winding-up process the Registrar should remain in control, i.e. should approve all payments to or by the winding-up agent.

The authority of the Registrar or Board to require that members be notified of information that the Registrar or Board wishes to bring to their attention should be available, either in the Act or the Regulations. More importantly, the authority of the Board or Registrar to direct trustees or other parties to convene meetings of members to consider matters that the Board or Registrar wishes them to consider and, possibly, vote on, should be obtained. Procedures for such meetings should be contained in the Regulations and, if possible, should prevail over conditions in the respective trusts should there be any conflict.

It should be possible to suspend the certificate of registration of a pension scheme intermediary, e.g. an administrator or custodian for a time during which some issue is resolved.

There should be some administrative flexibility included in the provision of paragraph 17D(3)(b) as the current requirements may prove to be too restrictive in some specific future instances.

The authority of the Board or Registrar to cause a trustee or trustees to be discharged and replaced should be specifically granted in the Act.

Where an auditor or actuary is to be replaced by the trustees, PIA should be notified and the cause confirmed. The trustees should be required to ensure that the replacing professional receives the cooperation of the professional being replaced. PIA should have the authority to report issues of a specific nature to the governing bodies of professionals who performs services for pension schemes.

The levy system for pension schemes should allow numbers of scheme members and beneficiaries to be used for purposes of determining the quantum of the fee or levy.

Funding and Solvency requirements (proposed in Regulations that have been drafted but not reviewed as part of the on-site consultancy) should be reviewed and following review, exposed for comment to stakeholders. At the very least, insolvent plans should be subject to special reporting with increased frequency and subject to close monitoring. Scheme members should be clearly informed of all pertinent issues and their views solicited and considered by the trustees and PIA.
10. **Assessment of Supervisory System Against IAIS Core Principles**

**ICP 1  Conditions for effective insurance supervision**

Insurance supervision relies upon

- a policy, institutional and legal framework for financial sector supervision
- a well developed and effective financial market infrastructure
- efficient financial markets

**Comments:**

There is no evidence that the Government of Zambia has established and publicly disclosed a public policy statement of the type anticipated by the Core Principle. However the Financial Sector Development Plan provides an indication of the intentions for the financial system. In addition, the Insurance Act, at section 99, lists the duties of the Registrar and the expectations of the GOZ. The Registrar is to protect the rights of policyholders and monitor the solvency of insurers. There is no framework for dealing with system-wide issues.

Legal framework is in place and court delays are not long. There is also an arbitration process.

There is no resident actuarial association and no standards have been prescribed. Actuarial work is carried out by actuaries from Zimbabwe and South Africa and pertains to life insurance only.

Accounting standards are set by the Zambia Institute of Chartered Accountants and all companies must appoint an auditor who is a member of ZICA. However there are no specific standards prescribed for insurance accounts, other than those set by PIA.

New insurance legislation was passed in 1997 and a series of amendments is currently under consideration. However Regulations to give effect to the 1997 Insurance Act were never promulgated.

Money and securities markets are very shallow and insurers are hard-pressed to find suitable investments. Many companies have been forced to be over-invested in real estate.

**Assessment**: Partly Observed

**Recommendations:**

- The amendments to the legislation must be adopted as soon as possible and the full set of supporting Regulations issued.
- PIA must publish comprehensive accounting standards for insurance companies
- Full compliance with this principle will only be possible with the maturity of the local capital markets
ICP 2 Supervisory objectives

The principal objectives of insurance supervision are clearly defined

Comments:

The objectives have not been defined explicitly although the recitation of the duties of the Registrar makes it clear that the protection of the rights of policyholders and the solvency of insurance companies are the principal concerns.

In some papers, officials have also listed the development of the domestic insurance market as an objective. Suggestions include rules for minimum local shareholding in all insurance companies and the establishment of a local reinsurance company supported by mandatory cessions.

There does not seem to be a formal process through which PIA reports on its success in meeting objectives

Assessment: Partly observed

Recommendation:

- When next announcing the introduction of amendments to the Insurance Act, GOZ could take the opportunity to specify clearly its objectives with respect to insurance supervision
- Subsequently, PIA could use its annual report to describe its success in meeting the objectives or, if appropriate, explain reasons for any deviations from the objectives
- The objectives could then be communicated in some formal manner to all staff of PIA and also to all supervised institutions

ICP 3 Supervisory Authority (a)

The supervisory authority:

- has adequate powers, legal protection and financial resources to exercise its functions and powers
- is operationally independent and accountable in the exercise of its functions and powers
- hires, trains and maintains sufficient staff with high professional standards
- treats confidential information appropriately

Legal Framework

Comments:

Legislation makes it clear that PIA is responsible for the supervision of insurance companies. Regulations necessary to give effect to the Act have not been
promulgated and PIA has adopted the practice of using the regulations that existed under the previous legislation to the extent that they do not conflict with the current law. However, Registrar does appear to have the necessary powers.

<table>
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<tr>
<th>Assessment: Largely observed</th>
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<tbody>
<tr>
<td><strong>Recommendation:</strong></td>
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<tr>
<td>• Legislative amendments should be completed as soon as possible</td>
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<tr>
<td>• All regulations, guidelines and directives needed to support the legislation should be promulgated promptly</td>
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</table>

### ICP 3 Supervisory Authority (b)

The supervisory authority:

- has adequate powers, legal protection and financial resources to exercise its functions and powers
- is operationally independent and accountable in the exercise of its functions and powers
- hires, trains and maintains sufficient staff with high professional standards
- treats confidential information appropriately

**Independence and accountability**

**Comments:**

There are no explicit procedures regarding the appointment and dismissal of the Registrar. The appointment is subject to a contract that is believed to be of three years duration. PIA itself has not been given full legal autonomy and exists as a sort of department within the Ministry of Finance. Not clear what relationship exists with the Ministry. At present, PIA is financed through grants from the Ministry.

Changes to legislation are subject to full consultation with affected parties.

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<th>Assessment: Not observed</th>
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<tr>
<td><strong>Recommendation:</strong></td>
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<tr>
<td>• Legislative amendments should be completed as soon as possible to establish PIA as an autonomous body</td>
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<tr>
<td>• The legislation under consideration will provide the authority for PIA to levy assessments on licensed entities and this should provide financial independence</td>
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</table>

### ICP 3 Supervisory Authority (c)

The supervisory authority:

- has adequate powers, legal protection and financial resources to exercise its functions and powers
### APPENDICES

- is operationally independent and accountable in the exercise of its functions and powers
- hires, trains and maintains sufficient staff with high professional standards
- treats confidential information appropriately

#### Powers

**Comments:**

Registrar has the power to suspend or remove a license (section 68). Fines may also be levied. Registrar may issue “cease and desist” orders (section 65). While liquidation normally proceeds under the Bank Act, the Registrar can initiate an action when necessary and can arrange reinsurance or propose a compromise arrangement (section 57) if that is in the best interests of the policyholders.

**Assessment:** Largely observed

**Recommendation:**

- Legislation should be reviewed to ensure the proper coordination between the provisions of the Bank Act Chapter VII and the Insurance Act. It may be preferable to include in the Insurance Act all provisions dealing with troubled insurance companies.

#### ICP 3 Supervisory Authority (d)

The supervisory authority:

- has adequate powers, legal protection and financial resources to exercise its functions and powers
- is operationally independent and accountable in the exercise of its functions and powers
- hires, trains and maintains sufficient staff with high professional standards
- treats confidential information appropriately

#### Financial Resources

**Comments:**

PIA prepares an annual budget and its annual report includes a financial statement showing its income and expenditures during the year. However, it has not had sufficient resources to hire its full “establishment” of staff and this is worrisome since it is believed that additional staff will be needed to discharge all the responsibilities that will devolve upon PIA under new legislation. Funding for essential training has not been provided. Information systems need to be upgraded but PIA lacks the resources.

**Assessment:** Not observed

**Recommendation:**
Legislative amendments should be completed as soon as possible
It is hoped that the introduction of the new system of levies will provide sufficient resources

ICP 3 Supervisory Authority (e)

The supervisory authority:
- has adequate powers, legal protection and financial resources to exercise its functions and powers
- is operationally independent and accountable in the exercise of its functions and powers
- hires, trains and maintains sufficient staff with high professional standards
- treats confidential information appropriately

Human Resources and legal protection

Comments:

Professional staff of PIA do not appear to have legal protection against lawsuits for actions taken in good faith in the performance of their duties. It is not clear that GOZ would assist with the legal expenses of such a defence.

PIA staff may not hold shares in a licensed insurer or broker. However there is not a clear conflict of interests’ policy to which professional staff members must adhere.

PIA does not have its own Code of Conduct. However staff members would be expected to adhere to codes relevant for public servants.

Assessment: Partly observed

Recommendation:
- Once legislative amendments have been completed, PIA should seek legal advice to secure adequate protection for professional staff
- PIA

ICP 3 Supervisory Authority (f)

The supervisory authority:
- has adequate powers, legal protection and financial resources to exercise its functions and powers
- is operationally independent and accountable in the exercise of its functions and powers
- hires, trains and maintains sufficient staff with high professional standards
- treats confidential information appropriately

Confidentiality
APPENDICES

Comments:

Professional staff at PIA treat all information collected from licensed entities as confidential. However there does not appear to be a confidentiality clause in the legislation.

Section 122 of the Insurance Act appears to be a Freedom of Information provision and the Registrar is required to provide to any person who make a formal request any document that is filed with PIA by a licensed entity.

Assessment: Partly observed

Recommendation:

- The legislation should be amended to confirm the confidential nature of information
- It may be necessary for PIA to prepare some rules for the administration of section 122 recognizing the fact that there may be prudential reasons not to release information in some cases.

ICP 4 Supervisory process

The supervisory authority conducts its functions in a transparent and accountable manner.

Comments:

Section 116 provides that most decisions and actions of the Registrar are subject to appeal to the Minister. However, by virtue of section 117 an appeal does not stay the effect of the Registrar’s decision. Need to understand the consequences of the second paragraph of section 117.

PIA is a small agency and the power to act is vested in the Registrar. We can presume that actions can be taken as soon as required without undue forbearance.

Assessment: Largely observed

Recommendation:

- PIA is about to establish documented procedures. It will be important that these procedures be applied consistently and that the decision-making lines are clear and conducive to immediate action.

ICP 5 Supervisory cooperation and information sharing

The supervisory authority cooperates and shares information with other relevant supervisors subject to confidentiality requirements

Comments:
PIA has entered into Memoranda of Understanding with banking supervisors in BOZ and also with securities market supervisors in SEC.

PIA officials are in contact with other insurance supervisors in nearby countries and would exchange information as needed. However no MOUs have been executed for these purposes.

**Assessment:** Partly observed

**Recommendations:**

PIA should ensure that it has entered into MOU with any other supervisory authority before sharing confidential information

### ICP 6 Licensing

An insurer must be licensed before it can operate within a jurisdiction. The requirements for licensing are clear, objective and public.

**Comments:**

Licensing is dealt with in a satisfactory manner by the legislation.

Fit and proper tests are presently applied only to the CEO although the Minister has the authority to prescribe more complete application to Directors and others.

No information is collected at present regarding the risk management systems of an applicant other than with respect to its reinsurance program. No information is collected with respect to internal controls and information systems

**Need to establish** the degree of contact with supervisors in the home jurisdiction of a parent company, such as in the case of NICO.

At present composites are permitted to the extent that separate and distinct accounts, funds and assets are maintained. However this will be removed in new legislation and existing composites will be obliged to split into separate companies

Need to establish what kind of follow-up activities take place in the first years following the granting of a new license

**Assessment:** Largely Observed

**Recommendations:**

- Use of fit and proper tests should be extended to Directors and other senior officers
- Need to develop a system for assessing risk management and internal controls of an applicant
- Once pending legislation is enacted, composites will have a short grace period in which to divide their affairs
### ICP 7  Suitability of Persons

The significant owners, board members, senior management, auditors and actuaries of an insurer are fit and proper to fulfil their roles. This requires that they possess the appropriate integrity, competency, experience and qualifications.

**Comments:**

At present the Insurance Act in Zambia refers only to the CEO (section 26). However, by virtue of section 29, Minister can extend the rules to other officers. Not clear that it can be extended to Directors and owners.

Section 46 requires a life insurer to appoint an actuary but does not indicate the minimum qualifications for an actuary. Registrar must be supplied with reasons for any change in this appointment.

Company must appoint an auditor by virtue of section 63. Amendments proposed will make that appointment subject to the approval of PIA in order to ensure that insurance company auditors have a minimum of experience in the audit of insurance companies.

There are no conflict of interest rules specified for actuaries; auditors; Directors and senior managers. **Verify this.**

**Assessment:** Partly observant

**Recommendations:**

It would be preferable if the legislation were amended at this time to reflect these requirements. However since it is unlikely that the draft amendments being considered by Parliament will be changed at this late date. It will be necessary to invoke the Minister’s power to issue regulations to bring about the enhancement of practices.

### ICP 8  Changes in Control and portfolio transfers (a)

The supervisory authority approves or rejects proposals to acquire significant ownership or any other interest in an insurer that results in that person, directly or indirectly, alone of with an associate, exercising control over the insurer.

The supervisory authority approves the portfolio transfer or merger of insurance business.

**Changes in Control**

**Comments**

There is no evidence that the Registrar has any influence over changes in control. Applicants seeking to acquire control of an insurance company should be obliged to satisfy similar criteria to those applicable to new licenses.
### APPENDICES

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<th>Assessment: Not Observed</th>
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<tr>
<td><strong>Recommendations:</strong></td>
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<tr>
<td>PIA should have legislated authority over any transfer of controlling interests in insurance companies. Such transfers should be rejected if criteria are not satisfied. This must apply even in cases where the ultimate owners are located outside the country</td>
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<table>
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<tr>
<th>ICP 8 Changes in Control and portfolio transfers (b)</th>
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<tbody>
<tr>
<td>The supervisory authority approves or rejects proposals to acquire significant ownership or any other interest in an insurer that results in that person, directly or indirectly, alone of with an associate, exercising control over the insurer.</td>
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<tr>
<td>The supervisory authority approves the portfolio transfer or merger of insurance business.</td>
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<tr>
<td><strong>Comments</strong></td>
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<tr>
<td>Portfolio transfers are governed by sections 50 – 53 of the Insurance Act. Registrar’s prior approval is required; provisions include a review of the terms of the agreement; and Registrar must be satisfied that the policyholders will not be disadvantaged</td>
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<tr>
<td><strong>Recommendations:</strong></td>
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<tr>
<td>PIA should prepare documented procedures for dealing with requests of this nature and make these procedures available to those affected</td>
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<tr>
<th>ICP 9 Corporate Governance</th>
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<tbody>
<tr>
<td>The corporate governance framework recognizes and protects rights of all insured parties. The supervisory authority requires compliance with all applicable corporate governance standards.</td>
</tr>
<tr>
<td><strong>Comments</strong></td>
</tr>
<tr>
<td>Insurance Act is silent on corporate governance, for all practical purposes. There are no references to a company’s Board of Directors. While there are occasional references to Directors, the “fit and proper” provisions do not apply to Directors.</td>
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<tr>
<td>Insurance companies are incorporated in accordance with the Companies Act, which dates from 1985 and hence does not reflect current practices in corporate governance. For example, Boards need have only 2 Directors; there is no requirement under the Companies Act for an Audit Cttee; nor does there seem to be any reference to the need for independent directors.</td>
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</table>
However in the Banking and Financial Services Act there are relevant sections. For example, the majority of the Board must be persons who are neither officers nor employees of the bank. Bank directors are expected to “…act honestly and in good faith…” and “…exercise care, diligence and skill…” Banks are also expected to establish an Audit Ctte of at least three Directors, the majority of whom are neither officers nor employees of the bank.

Companies must establish a formal investment policy (section 44) and file regular annual updates with the Registrar. While it might be reasonable to presume that any such policy would require Board approval, the Insurance Act does not require that such approval be obtained.

There is no requirement for companies to establish an Audit Committee nor to develop internal audit capacity. While companies have staffs of reduced size, this is not serious, although not observant of ICP expectations. For mature companies, this could become a serious shortcoming.

It should be noted that some well-managed companies are practicing good corporate governance on their own initiative. In some cases, the company’s actual Articles of Incorporation will specify requirements that help to promote good governance.

**Assessment** Not Observed

**Recommendations**

A concerted effort must be made to develop corporate governance rules to be applied by PIA to licensed insurance companies. These requirements would go beyond those specified in the Companies Act and would be such as to ensure that policyholders interests are safeguarded as a responsibility of the company’s Board. The work reflected in the Banking and Financial Services Act represents a good guidepost to direct PIA’s efforts at strengthening this area.

**ICP 10 Internal Control**

The supervisory authority requires insurers to have in place internal controls that are adequate for the nature and scale of the business. The oversight and reporting systems allow the board and management to monitor and control the operations.

**Comments**

PIA circulated a questionnaire on internal controls in 2004 and all companies responded. In some cases companies provided copies of their internal control manuals. Findings from the questionnaires are proving useful in the conduct of inspections.

**It is not clear** to what extent the Board is engaged in the internal control process. There is no formal authority through the Insurance Act that compels the Board to monitor a system of internal controls. In Zambia, some of the audit firms are forthright in reviewing and demanding strong internal controls from their insurance company clients, although we understand that this is not always to case.
We are advised that PIA inspectors have made the review of internal controls an essential component of their on site work.

Internal audit functions have been established in larger insurance companies.

In the absence of effective corporate governance requirements, the Boards of Directors of insurance companies in Zambia can not be expected to be discharging the functions that a proper internal control system would expect of them (Essential criteria d,e,f).

Assessment Not Observed

Recommendations The Registrar could issues Guidelines pursuant to section 99 of the Insurance Act (Specifically 99(2)(a)), as he is empowered to do. These guidelines could outline the desired level of internal controls within an insurance company. The guidelines could also establish a minimum standard for corporate governance. According to section 99 these guidelines would be binding on the company and even if only partly implemented in initial phases, would be an excellent preparation for the ultimate solution that will involve amendments to the Insurance Act

ICP 11 Market Analysis

Making use of all available sources, the supervisory authority monitors and analyses all factors that may have an impact on insurers and insurance markets. It draws conclusions and takes actions as appropriate.

Comments

PIA publishes an annual report that provides an overview of the industry together with statistics showing separately the performance on the industry in life insurance and general insurance. While most statistics are on an aggregate basis, the report does give information on the market share of different industry players.

The report also includes comments of the Registrar on the state of the industry and on significant events during the year in review. Also included is the financial report on the operations of PIA for the year in question.

At present PIA lacks the resources, both human and technical, to conduct regular trend analysis of market conditions.

Assessment: Largely observed

Recommendations:

PIA should be provided with the necessary resources to enhance its data-gathering activities. Reports should be filed electronically by supervised institutions. Once this conversion has been completed PIA should develop the necessary skills and acquire the necessary software to perform the desired trend analysis.

ICP 12 Reporting to supervisors and off-site monitoring

The supervisory authority receives necessary information to conduct effective off-site
monitoring and to evaluate the condition of each insurer as well as the insurance market.

Comments

PIA sets reporting requirements for insurance companies including the filing of reports from auditors and actuaries. There are no groups of insurance companies in Zambia. However as noted in ICP 11, PIA lacks the information systems needed to ensure most efficient, effective and consistent use of the data filed.

At the present time, no particular attention has been paid to off-balance sheet liabilities and they are believed to be of little consequence for Zambian companies.

PIA has not yet prescribed rules for the valuation of assets and liabilities, although it has the authority to do so (section 34 and 40).

PIA has established a framework for on-going monitoring of companies, using both the reports filed by companies and the on-site inspection results. However this framework has not yet been properly documented.

Assessment: Partly observed

Recommendations:

As for ICP 11

ICP 13 On-site inspection

The supervisory authority carries out on-site inspections to examine the business of an insurer and its compliance with legislation and supervisory requirements.

Comments

PIA has begun to perform on-site inspections only within the past two years. Some companies have been inspected only once. The inspection process is in a developmental stage.

The legislation does not prescribe any minimum frequency for company inspections, although PIA would prefer to visit each company at least once each year. Inspections can be conducted on either a full-scale or focused basis.

The legislation provides PIA with all the authority that it needs to conduct inspections and gather information. There is little contact between PIA inspectors and external auditors.

The examination process followed at PIA requires the inspector to discuss findings with senior company officials at the conclusion of the inspection. Following the on-site work, the Registrar will write a letter to the CEO of the insurance company to underscore salient findings.

PIA has not yet developed procedures manuals for on-site inspection.
## APPENDICES

<table>
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<tr>
<th>Assessment</th>
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<tr>
<td>Recommendations</td>
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<tr>
<td>PIA should develop documented procedures for on-site work including the process of following-up on inspection findings. Documentation could include the creation of working paper standards. The completion of carefully designed working papers will ensure consistency and completeness in the inspections.</td>
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### ICP 14 Preventive and corrective measures

The supervisory authority takes preventive and corrective measures that are timely, suitable and necessary to achieve the objectives of insurance supervision.

**Comments**

Insurance Act provides the Registrar with broad powers to prompt insurance companies to adopt preventive and corrective action as required.

PIA has not established a “ladder of compliance” through which it might manage its use of the available powers. For example, it is important that the action taken by an insurance supervisor in the face of problems be proportionate with the gravity of the problem encountered and the risks it presents for the insurance company and its policyholders. There is no “progressive escalation of action”.

PIA can issue guidelines or directives to a company or to all companies (section 99) that are binding in their application. These could be used to reduce the risk that small problems become large ones.

While these powers exist in the legislation, they have not been invoked.

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<th>Assessment</th>
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<td>Recommendations</td>
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<tr>
<td>• PIA should develop a ladder of compliance that it will publish. This ladder will indicate to insurance companies the type of regulatory/supervisory intervention that will be invoked in the event an insurer is in breach of statutory requirements; places policyholders at risk; or fails to follow sound business practices</td>
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<tr>
<td>• PIA should issue guidelines and directives in a number of areas, using its powers under section 99</td>
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<td>• PIA could also issue “cease and desist” orders using section 65 in order to ensure prompt remedial action.</td>
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### ICP 15 Enforcement or sanctions

The supervisory authority enforces corrective action and, where needed, imposes sanctions based on clear and objective criteria that are publicly disclosed.
### APPENDICES

#### Comments

Registrar can issue formal directions; can order a company to stop writing new policies; can arrange for the compulsory transfer of policies from a failing insurer.

Rules have not yet been issued regarding the computation of a proper solvency margin. It is unlikely that the Registrar could require a company to increase its capital levels. Registrar cannot apply fit and proper tests to owners directors and managers and could not remove them in problem cases. However it has demonstrated that it can seize a company for purposes of winding up its affairs when serious problems exist.

Registrar lacks the authority to issue a complete range of fines, such a fine for late filing of returns.

**Assessment**  Partly observed

#### Recommendations

Once a complete solvency monitoring system has been instituted, Registrar should be given the authority to order a company to raise its capital when that appears appropriate. Registrar should also be given the power to apply fines for certain levels of non-compliance. Such penalties can be effective and are certainly less severe than a withdrawal of a license for a minor breach of rules.

#### ICP 16 Winding-up and exit from the market

The legal and regulatory framework defines a range of options for the orderly exit of insurers from the marketplace. It defines insolvency and establishes the criteria and procedure for dealing with insolvency. In the event of winding-up proceedings, the legal framework gives priority to the protection of policyholders.

**Comments**

Registrar has power to suspend or revoke an insurance license under a variety of scenarios (sections 65 ff). Such action can be taken before a company is declared to be bankrupt. Registrar can petition for a winding-up even if bankruptcy has not yet occurred (72) if the Registrar is of the view that this would be in the best interests of the policyholders.

When an insurer is deemed to be insolvent, winding-up proceeds in accordance with Chapter VII of the Bank Act. Sections of the Bank Act are made to apply to insurance companies by means of a cross-reference in the Insurance Act (section 71).

Priority of policyholder claimants in a case of liquidation of an insurance company is ensured by section 59. In addition, section 58 provides that the assets of any of the statutory funds can only be used to cover liabilities arising from policies issued through that fund.

**Assessment:** Largely Observed
Recommendations

- Provisions governing the liquidation of insurance companies should appear in the Insurance Act directly and not by reference to another piece of legislation. This would provide for greater clarity in the application of the rules.
- PIA should develop a written set of procedures and instructions for its staff to ensure that any actions that involve winding-up of companies are accomplished as expeditiously and at as little cost as possible.

ICP 17 Group-wide supervision

The supervisory authority supervises its insurers on a solo and a group-wide basis.

Comments

It is not clear whether any conglomerates exist in Zambia. There are no cases where two or more insurance companies have the same owner (insurance groups). However, it does appear that Finance Bank and Professional Insurance are controlled by the same shareholders. Cavmont is another example.

In addition, there are licensed insurance companies that are members of conglomerates, including some that involve insurance companies that operate in other jurisdictions. As noted earlier, Zambia has not made any formal arrangements for sharing of information with insurance supervisors in other countries. While MOU’s have been executed with BOZ and SEC, there is no formal arrangement for cooperation and coordination in the supervision of member companies in a conglomerate.

Solvency tests and all other supervisory tools applied by the Zambian authorities will be applied on a solo basis.

Assessment Not Observed

Recommendations

PIA should establish procedures for dealing with conglomerate situations, including all the communication protocols with other supervisory agencies.

ICP 18 Risk assessment and management

The supervisory authority requires insurers to recognize the range of risks that they face and to assess and manage them effectively.

Comments

PIA has not issued any instructions to insurers with respect to risk assessment and management.

Inspection procedures have not been established in a formal way but it appears
that a review of a company’s risk management policies and risk control systems is not yet a part of the inspection function

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<td>PIA must prepare guidelines for companies to follow as they put in place the kind of comprehensive risk management policies and systems that conform to international best practices. This will be a coaching assignment in the initial stages.</td>
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<tr>
<td>Once PIA addresses the question of documenting inspection procedures, it should be in a position to direct its inspectors in making an assessment of an insurance company’s risk management policies and risk control systems.</td>
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**ICP 19 Insurance activity**

Since insurance is a risk taking activity, the supervisory authority requires insurers to evaluate and manage the risks that they underwrite, in particular through reinsurance, and to have the tools to establish an adequate level of premiums.

**Comments**

PIA has not issued any directions or guidelines concerning underwriting and pricing polices. As noted elsewhere, the regulatory system has not yet been modified to reliance upon controls by the Board of Directors.

Companies follow a file and use with respect to new policy forms and changes in premium pricing. If Registrar does not respond within 30 days of the filing, the company may begin using the new policies/rates. While there is authority to request that life insurance rate submissions be accompanied by a supporting actuarial opinion concerning the adequacy of the rates, this practice is not being followed.

There are no prescribed limits concerning maximum retention per risk and, except for those involving Africa Re and PTA Re, there are no compulsory cessions. However each company is expected to make an annual filing with information on all its reinsurance arrangements.

Reinsurance companies can accept reinsurance ceded by Zambian companies, even where the reinsurer is not licensed in Zambia.

The annual report on reinsurance is reviewed by PIA in order to ensure that all reinsurance is placed with sound companies. There are no written standards for this assessment and no rules have been formulated regarding rating agency reports and deposits by reinsurer. These latter tools are being used in other jurisdictions to verify the credit of the reinsurer.

<table>
<thead>
<tr>
<th>Assessment</th>
<th>Not observed</th>
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<tbody>
<tr>
<td><strong>Recommendations</strong></td>
<td></td>
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PIA should insist that all rate change requests be supported by an accompanying actuarial report.
PIA should prescribe a maximum retention per risk and per accident as the basis for each company’s reinsurance program. That retention will be expressed as a function of the company’s net worth (capital and surplus).

PIA might consider adoption of standards for qualification of a reinsurance company. One approach would be to rely on the rating of the reinsurer by one of the major rating agencies.

<table>
<thead>
<tr>
<th>ICP 20 Liabilities</th>
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<tbody>
<tr>
<td>The supervisory authority requires insurers to comply with standards for establishing adequate technical provisions and other liabilities, and making allowance for reinsurance recoverables. The supervisory authority has both the authority and the ability to assess the adequacy of the technical provisions and to require that these provisions be increased, if necessary.</td>
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<tr>
<th>Comments</th>
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<tr>
<td>Insurance Act (sections 33 and 34) specifies that the liabilities of an insurance company must include a reserve for unearned premiums; for claims incurred but not settled and for claims incurred but not reported. However, while the Minister is given authority to prescribe the method for calculating these provisions, no such prescription has been made.</td>
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<tr>
<td>PIA has not established procedures for the review of claims administration and the establishment of provision for losses by licensed companies. Procedures of this nature should form part of each on-site inspection. Inspectors rely on the auditors to verify that all reported claims are included in the provision for unsettled claims.</td>
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<tr>
<td>There is no monitoring of the adequacy of the claims provision through the use of a run-off table or other such supervisory tool.</td>
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<tbody>
<tr>
<td>There are no standards that cover the reporting of reinsurance transactions. Figures for amounts recoverable from reinsurers are accepted if they have the endorsement of the company auditor.</td>
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<tr>
<td>PIA does not require companies to perform stress tests on the adequacy of the provisions for liabilities.</td>
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</table>

| Assessment | Partly observed |
|------------|
| Recommendations |
| A top priority for PIA is the establishment of standards for establishing technical provisions with respect to reported but unsettled claims. The supervisory process should also include the monitoring of reserve adequacy through the use of multi-year run-off tables. |

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<th>ICP 21 Investments</th>
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</table>
The supervisory authority requires insurers to comply with standards on investment activities. These standards include requirements on investment policy, asset mix, valuation, diversification, asset-liability matching, and risk management.

**Comments**

PIA has not issued any rules regarding mixture of assets by type; diversification; limits on particular types of assets; matching; liquidity. Insurance Act contains no such provisions.

While Insurance Act (section 40) appears to authorize the Registrar to review the valuation of assets, he has not done so. By virtue of section 99 Registrar could introduce all the customary rules regarding investments. Some of these could be transferred into the Insurance Act at a future revision. At present company asset portfolios have excessive amounts tied up in land and buildings (as a proportion of total assets) and in receivables, including especially outstanding premiums.

Companies are required (section 44) to prepare a formal investment policy but Insurance Act does not specify the elements that must be in the policy. IN the absence of good corporate governance practices, it is not clear that the policy would be reviews and approved by the Board of Directors.

In the absence of risk management systems, it is unlikely that companies will deal effectively with market risk, credit risk and liquidity risk.

**Assessment** Not observed

**Recommendations**

PIA must proceed with the issue of guidelines (section 99) to govern the investment activity of insurance companies. These guidelines would set limits on asset concentration. They would also deal with the question of asset/liability management.

PIA staff will likely need extensive training in these areas.

Registrar (or Minister, as the case may be) must establish rules for valuation of assets.

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**ICP 22 Derivatives and similar commitments**

The supervisory authority requires insurers to comply with standards on the use of derivatives and similar commitments. These standards address restrictions in their use and disclosure requirements, as well as internal controls and monitoring of the related positions.

**Comments**

No rules have been established regarding the use of derivatives. However it is also very likely that insurance companies in Zambia will not be making use of derivative products, having regard for the limited amount of investible assets each possesses.

There are no specific disclosure requirements with respect to derivatives. However inspectors will examine the published financial statement of a company where the Notes prepared by the auditors will often indicate the existence of such derivatives.
Before any company begins to make use of derivative products, PIA should insist that companies prepare a policy for their use. This policy should be subject to review by the company’s Board.

| Assessment | Not applicable |
| Recommendations | PIA should take steps to prohibit the use of derivative products by domestic insurance companies. In such a shallow capital market it is hard to imagine that derivatives would be employed by institutional investors in the short term.

Once it is decided to permit companies to utilize derivative products, PIA would be expected to develop comprehensive rules and guidelines regarding their use.

### ICP 23 Capital adequacy and solvency

The supervisory authority requires insurers to comply with the prescribed solvency regime. This regime includes capital adequacy requirements and requires suitable forms of capital that enable the insurer to absorb significant unforeseen losses.

| Comments | In the absence of specific rules regarding valuation of assets and liabilities, the solvency test in the Insurance Act (section 37) has little effect. Solvency test does not consider issues of liquidity, matching of assets and liabilities, and suitable forms of capital.

Capital adequacy requirements are fixed and not sensitive to the size, complexity and riskiness of the company’s operations.

Solvency control levels have not been established. Control levels apply to ensure that the supervisor and company management take corrective action before insolvency occurs.

| Assessment | Not observed |
| Recommendations | In the short term, PIA should issue capital adequacy and solvency guidelines using the authority available to the Registrar pursuant to section 99 of the Insurance Act. Longer term measures would embed these requirements in the legislation.

Guidelines must cover valuation of assets; valuation of liabilities; liquidity requirements.

Rules should impose a series of solvency controls mandating different degrees of supervisory intervention at varying levels of coverage of the solvency margin.

### ICP 24 Intermediaries

The supervisory authority sets requirements, directly or through the supervision of insurers, for the conduct of intermediaries.

| Comments | Requirements for licensing of intermediaries are specified in the Insurance Act. |
APPENDICES

Applicants for such licenses must satisfy specified fit and proper tests.

There do not appear to be requirements for security deposits by intermediaries, even though the majority of insurance policies are placed by brokers. There is no requirement that brokers obtain professional indemnity insurance, a requirement that exists in many countries to safeguard funds the clients place with brokers.

Registrar appears to have the powers necessary to take corrective action against brokers and against any persons who attempt to carry on insurance business without being licensed to do so.

**Assessment**  Largely observed

**Recommendations**

Amendments proposed for the Insurance Act will impact on brokers in three ways:

- Brokers will need to establish separate accounts to hold clients’ money
- Premiums must be remitted to insurance companies within 30 days
- Brokers will be expected to file quarterly reports with insurance companies identifying all those clients for which the brokers are holding money and giving the amounts of such deposits

In the medium term it would be desirable to adopt the “no premium no cover” approach to premium collection. Also brokers should be obliged to procure professional indemnity insurance.

**ICP 25 Consumer protection**

The supervisory authority sets minimum requirements for insurers and intermediaries in dealing with consumers in its jurisdiction, including foreign insurers selling products on a cross-border basis. The requirements include provision of timely, complete and relevant information to consumers both before a contract is entered into through to the point at which all obligations under a contract have been satisfied.

**Comments**

PIA has not issued any guidelines to insurance companies regarding their dealing with consumers. Companies are not required to establish rules of conduct for their employees and representatives to follow in their dealings with the public.

Insurance Act, section 96, allows a purchaser of a life insurance policy to cancel the policy, up to 30 days following issue and to receive a refund of the premium paid, less a charge for any medical examination expenses. This is a version of the “free look” seen in other countries.

PIA carries out an investigation of any complaint brought to its attention by a policyholder. It attempts to clarify the policy terms and conditions for the policyholder in the case of ambiguity and will send an inspector to visit the company if there appears to be cause to do so.

**Assessment:** Partly Observed

**Recommendations**

PIA should prepare guidelines that require all licensed insurance companies and brokers to act with due skill, care and diligence in dealing with their customers.
Insurers and brokers should be obliged to develop written policies for fair treatment of customers and to provide training to ensure these policies are observed. PIA could collaborate with the trade associations in developing code of good conduct standards.

**ICP 26 Information, disclosure & transparency towards the market**

The supervisory authority requires insurers to disclose relevant information on a timely basis in order to give stakeholders a clear view of their business activities and financial position and to facilitate the understanding of the risks to which they are exposed.

**Comments**

Insurance Act requires insurance companies to file annual returns of operations using prescribed forms. Companies must also file with the Registrar copies of any reports filed with shareholders or other authorities. Insurance companies prepare and publish financial statements using accounting principles adopted by the Zambian Institute of Chartered Accountants. These statements must include an opinion from a qualified auditor. The statements will contain considerable disclosure of background to the financial statements in the form of Notes to the financial statements. All financial information filed with PIA by insurance companies pursuant to the provisions of the Act is available on short notice to the general public upon payment of a modest fee.

**Assessment** Largely observed

**Recommendations**

Regulations made under the Insurance Act prescribed the forms to be used by insurance companies in reporting their results. These forms are more detailed than those appearing in the financial statements for shareholders because the supervisor needs more detail in certain areas, such as the analysis of reserves and provisions. Since the regulations were made under the provisions of the 1968 Act, they are less than satisfactory for the current legislation. It is hoped that once the amendments to the Act are passed, new regulations will be prescribed by the Minister and a more complete prescribed form can be introduced that will form the basis of analytical work by PIA.

**ICP 27 Fraud**

The supervisory authority requires that insurers and intermediaries take the necessary measures to prevent, detect and remedy insurance fraud.

**Comments**

PIA has the necessary powers to establish regulations and to communicate with enforcement authorities in combating fraud. It is doubtful that it has all the resources it would need for this purpose. The Insurance Act does not address insurance fraud although we have been assured that fraud of any kind would be subject to punishment as a criminal activity.

While PIA has issued no guidelines that would require insurance companies and
brokers to ensure high standards of integrity, its inspectors will use moral suasion to achieve this purpose.

Most companies have developed their own programs for dealing with fraud, although they will likely be focussed on fraud caused by consumers.

<table>
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<tr>
<th>Assessment</th>
<th>Partly Observed</th>
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**Recommendations**

PIA should develop guidelines that describe its expectations in respect of detecting and finding remedies for fraud in insurance, whether by consumers or by insurance companies and their intermediaries. Helpful information is available from other supervisory groups, including IAIS, and the trade associations will collaborate in the development of the guidelines.

<table>
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<tr>
<th>ICP 28 Anti-money laundering, combating the financing of terrorism (AML/CFT)</th>
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The supervisory authority requires insurers and intermediaries, at a minimum those insurers and intermediaries offering life insurance products or other investment related insurance, to take effective measures to deter, detect and report money laundering and the financing of terrorism consistent with the Recommendations of the Financial Action Task Force on Money Laundering (FATF).

**Comments**

PIA has the authority to monitor and ensure compliance with AML/CFT requirements. However, they would not be in a position to prevent the take-over of an insurance company by known criminals. At present, fit and proper tests apply to CEO of an insurance company but not to the owners, Directors or other managers.

Insurance companies have not previously been asked to comply with AML/CFT requirements.

Zambia has established a special unit within its Drug Enforcement agency which has the responsibility for implementing the AML program.

**Assessment** Partly observed

**Recommendations**

PIA has participated in the drafting of a memorandum that is shortly to be circulated to all insurance companies. A comparable guideline has previously been circulated by BOZ to the institutions it supervises.

Implementation of the guidelines will require PIA to adopt procedures for dealing with reports of suspicious activity that are supplied to it. It will need to appoint an officer responsible for its activities in AML/CFT and for contact with the appropriate law enforcement organizations.
11. PENSIONS & INSURANCE AUTHORITY ORGANISATION CHART

- Chris Mapipo
  Registrar

- Muyoya Chibiya
  Deputy Registrar - Insurance

- Nicholas Mbuya
  Senior Inspector - Insurance

- Titus Nkwale
  Inspector

- Aubrey Masumbu
  Inspector

- Raphael Chanda
  Finance & Administration Manager

- Maureen Tresha
  Legal Counsel

- Martin Libinga
  Deputy Registrar - Pensions

- Mwelwa Mwale
  Senior Inspector - Pensions

- Nkandu Chilombo
  Inspector

- Raphael Foseka
  Accounting Officer

- Alphonsina Mwale
  Executive Assistant

- Ireen Mulauzi
  Personal Secretary

- Delphine Lisselo
  Personal Secretary

- Juliele Phiri
  Driver

- Aaron Chishimba
  Driver

- Magaret Kalaba
  Office Assistant

- Frank Chanda
  Inspector
PENSIONS & INSURANCE AUTHORITY - PROPOSED ORGANISATION STRUCTURE

REGISTRAR
X 1

PERSONAL ASSISTANT
X 1

DIRECTOR - INSPECTIONS
X 1

SENIOR INSPECTOR
X 2

INSPECTOR
X 8

DIRECTOR - LICENSING & ENFORCEMENT
X 1

LEGAL OFFICER
X 1

SECURITY
X 2

DIRECTOR - FINANCE & CORPORATE AFFAIRS
X 1

SECRETARY
X 2

ACCOUNTANT
X 1

ANALYST
X 2

DIRECTOR - POLICY, RESEARCH & MARKET DEV.
X 1

ACCOUNT OFFICER
X 1

DRIVER
X 3

CLEANER
X 2

ACCOUNTS OFFICER
X 1

ICT OFFICER
X 1

ADMINISTRATIVE OFFICER
X 1