

Individual Consultant
To Prepare a Pension Strategy Study for Maldives
Terms of Reference

I. Background and Challenges to Old Age Income and Poverty Protection in the Maldives

Background. The structure of the current system reflects a substantial legislative reform in 2009 under which the mandatory, defined-contribution *Maldives Retirement Pension Scheme (MRPS)* was put in place for public and private sector workers. The *Old Age Basic Pension (OABP)* is a non-contributory scheme financed by the Government that provides financial security for individuals who had no access to employment-based income prior to retirement age. It provides a lifelong pension benefit to all Maldivian Citizens who have reached the age of 65, subject to meeting the eligibility criteria of the scheme. During 2014, the government introduced a top-up allowance to OABP to ensure all retirees at a minimum received MVR5000 from the Government. Subsequently this allowance was stopped following a change to Pension Act to raise the OABP to MVR5000.

Over the past decade, the Maldives Pension Administration Office (MPAO) has invested heavily in establishing a strong data management and delivery system as the platform for the MRPS. The MPAO operates all the individual accounts of its members. Employers, workers and retirees can access their accounts through a user-friendly application and make contributions and receive benefits through the formal banking system. The collection of pension contributions is carried out by the national bank, Bank of Maldives, which has the biggest network of retail branches throughout the archipelago. The MPAO has also established a cloud-based IT infrastructure for efficient management and enabled easily accessible nationwide through the Internet.

Challenges. The MRPS and OABP have faced a number of challenges over the past decade. These include concerns over the adequacy of pension benefits with relatively low contribution densities, continuing challenges to provide coverage for informal workers, a growing fiscal burden for Public Sector including civil servants and for the OABP as the society ages, difficulties in ensuring compliance with contribution requirements, and “double pensions” to Public Sector. Finally, the MPAO has faced challenges in compliance, including a tendency for employers to understate the basic salary (Pensionable wage). Further on a public perception point of view, the MPAO is also facing enormous public demand to introduce greater benefits (e.g housing, disability insurance) for members of MRPS during the accumulation of the retirement scheme which is estimated to be greater than 20 years, since the 85% of fund members are still below 45 years of age.

II. Scope of Work

Proposed scope of work. A seasoned expert on pension systems design and reform is needed to formulate a holistic strategic direction and time-bound action plan, addressing each of the issue areas below.

A. Monitoring and Supervision of Contribution Remittance

The consultant should evaluate the monitoring and supervision of compliance and suggest options for strengthening. This should include an assessment of the on- and off-site compliance supervisory process, including an evaluation of the risk-based supervision system employed by MPAO. It should also include an assessment of links with the Maldivian Inland Revenue Authority, including reconciliation of corporate and personal income tax records on the one hand, and retirement savings contributions on the other. It should review the grievance redress system as well as the process for the validation of work histories. The consultant should review options for linking with corporate and personal bank information to reconcile reported income and wages with that reported to MPAO. From this assessment, the consultant should develop a recommended program of compliance monitoring, supervision and potential rule changes to improve the level of taxable salaries and reduce the level of evasion.

B. Treatment of Non-salary Allowances in Defining Pensionable Wages

The consultant should carefully review the available data on pensionable salaries and non-salary allowances, including the treatment for personal and corporate income taxes. This assessment should include evaluating the distributional effects between workers of the inclusion of different allowances. Some professions that rely on allowances for compensation will require special attention. The assessment should also consider how the inclusion of allowances could impact the underreporting of compensation to both the tax authorities and the MPAO. The consultant will formulate a plan for the gradual inclusion of select allowances into the pensionable wage base, linked to the tax collection and computation system.

Depending on the size and variability of non-wage allowances, it is worthwhile to consider transition arrangements in moving to the broadening of the definition of pensionable wage. Transition arrangements try to smooth the process of levying contributions for non-salary allowances and therefore ease the contribution burden. For example, if a worker had non-wage allowances equal to 30% of their pensionable wage and there was no transition period, the worker would have to immediately finance 7% of the 30% (or 2.1%) of their pensionable wage as a pension contribution. Similarly, employers would have an additional 2.1% labor cost without transition. A more constructive design would be transition over a period of say 3-5 years in the Maldivian case. In addition, the authorities may consider providing additional transition time for those workers that have very high proportions of allowances as a proportion of total compensation over a threshold.

C. Evaluation of the Old Age Basic Pension and Formulation of a Reform Strategy

Background. The OABP is a non-contributory pension established in 2009 as a part of the framework for old-age income protection under the Maldives Pension Act. The fiscal costs of this demogrant is substantial and is anticipated to grow with the old population growing and the increased **life expectancy**. The authorities are therefore interested in reviewing the design features and fine-tuning the parameters of the OABP based on cost projections and an assessment of the coverage and poverty impact of the scheme.

The consultant should conduct a comprehensive evaluation of the Old Age Basic Pension. The scope of this evaluation should include: (i) an actuarial exercise to project the costs of these programs as the number of workers over 65 years increases in the Maldives; (ii) the projected level of individual income replacement provided by these programs across the income spectrum of retirees and the appropriate return target the MRPS should target to achieve acceptable replacement targets; (iii) the actual and

anticipated impact on elderly poverty protection provided by these programs; (iv) the estimated impact on the incentives for work and contributions to the *Retirement Pension Scheme*; and (v) the role of other State transfers to old age poverty protection. The consultant should also holistically look at the pension regime in Maldives which includes the pensions provided under the Maldives Pension Act, and pensions and allowances provided by various state institutions outside of the Pension Act and formulate policy options for harmonising these benefits, suggest appropriate indexation techniques and review key parameters such as eligibility age and/or claw back features to improve incentives and ensure the long-term fiscal affordability of the pension system as a whole.

D. Formulation of a Strategy for Maximizing Retirement Savings and Worker Coverage

The consultant should evaluate the level of worker coverage, including the profile of firms and individuals participating in the pension system, the patterns of worker participation, the length of service observed prior to retirement, and the reported wages. They should also review the delivery systems supporting informal worker participation. This includes the efficiency of registration, contribution remittance, account access, payments and customer communication processes. The review should also include recommendations for strengthening the delivery systems as needed.

The consultant should formulate a program of incentives for worker participation in addition to monitoring and supervision above. This program should include, but need not be limited to:

- (i) An auto-enrollment system for workers in the formal sector and alternative enrolment mechanism for the informal sector.
- (ii) A voluntary auto-payment system for informal workers by which a specified amount could be automatically deducted from a specified bank account and deposited into one's pensions account;
- (iii) An electronic auto-reminder system for making pension contributions and a small Government contribution to individual accounts for individuals that register for either auto-payments or auto-reminders;
- (iv) An option for partial withdrawal of pension balances in cases of life-threatening events. These could include for example, life-threatening medical conditions, life-threatening catastrophic events such as hurricanes and other natural disasters, and life-threatening accidents or other disabilities; and
- (v) Product features that encourage people to participate in and contribute to the pension program.

E. Formulation of a Strategy for the Elimination of "Double Pensions"

The consultant should evaluate the practice of paying both benefits under the pre-2009 pension and retirement benefit scheme and benefits under the post-2009 defined-contribution Maldives Retirement Pension Scheme and the defined benefits given under various laws. This should include an evaluation of precisely which workers have received which entitlements and which workers are anticipated to receive what entitlements in the future. It should include an assessment of the past and anticipated future fiscal costs of these double pensions and the replacement rate for affected workers.

The consultant should formulate a strategy for the elimination of such double pension payments. Such a strategy should include legal amendments and other legal provisions needed to effect such elimination, identification of implementation agencies and their respective roles and, as necessary, a transition mechanism.

F. Payout Phase Assessment

The consultant should prepare a mapping of payout options, including simulations of the effects on workers with different incomes and work histories. Although there has previously been extensive study and consideration of payout phase options, the consultant should provide the authorities with inputs into payout phase options. These options likely include: (i) a phased withdrawal; (ii) a phased withdrawal with insurance for longevity and, possible death; (iii) partial or full annuitization; and (iv) partial or full annuitization with price indexation. All of these options need to be assessed while also considering the interface with the OABP. As such, it is very possible that a program of phased-withdrawal and/or annuitization would apply only up to balances at a given threshold to be determined.¹ In addition, the consultant should provide relevant comparisons of payout options offered in countries with defined-contribution pension arrangements.

A phased withdrawal offers an attractive option for Maldives because retirees also receive the Old Age Basic Pension. In this way, the investment and longevity risks associated with the phased withdrawal can be balanced against the stream of payments from the OABP. These non-contributory programs can assure the basic livelihoods of Maldivians in retirement though they also have risk characteristics including inflation and political risks.

A transition program may be needed for a phased-withdrawal program so that the plans of those retiring soon after the enactment of the program are not adversely affected. Public sector workers approaching retirement may have made arrangements anticipating their lump-sum payouts and therefore would be adversely affected by the abrupt establishment of a phased withdrawal without transition arrangements. One option, for example, would be to phase the program in over 10 years. In this way, a retiree during the first year after enactment would be entitled to 90% of his or her benefit as a lump-sum and the remaining 10 percent as a phased-withdrawal benefit while in the second year the retiree would be entitled to 80% of his or her benefit as a lump-sum and so forth.

Another option to consider for reasonable payouts at older ages when phased-withdrawal balances become too low for reasonable benefits is to invest a portion of the account accumulation in a longevity insurance premium.² This can then ensure a payout throughout retirement regardless of individual longevity. Of course, the premium for such longevity would reduce the individual's benefit.

¹ There are two slightly different variants: (i) the first simply calculates the benefit based on the account balance divided by the individual's life expectancy at his or her age in such year; and (ii) the second calculates the benefit by calculating an annuity based on an assumed interest rate for the individual's life expectancy at his or her age in such year.

² For example, see Solange Berstein, Marco Morales, Alejandro Puente, *The Role of Longevity Insurance in Latin America: Cases of Chile, Colombia, Mexico and Peru*, Multi-pillar Pension Systems: Investing in the Future, FIAP Internacional, 2016.

Currently there is only one insurer in Maldives licensed to provide life insurance products and other insurance providers primarily provide accident insurance. The assessment of the consultant could also include whether it would be feasible for the MPAO to introduce its own licensed annuity products to keep the costs low and provide greater benefits to members of the retirement scheme rather than outsourcing this function to a third party private insurer.

G. Strategic Direction and Options

This section should draw on the analysis undertaken in sections A-F above to take a more holistic view of the design and implementation of the Maldives public pension and elderly assistance schemes. The consultant should:

- (i) Identify any other gaps in the design and implementation of the schemes with respect to their effectiveness and efficiency in achieving worker and elderly coverage; providing a strong framework for adequate smoothing of income from work-life into retirement; and providing for elderly poverty protection on a fiscally sustainable basis.
- (ii) Formulate options for addressing these gaps on a multi-year basis, including providing reasonable transitions.
- (iii) Formulate an integrated strategy for strengthening the design, parameters, and implementation mechanisms for the areas identified, including leaving scope for the refinement of policy options by the authorities.
- (iv) Formulate a time-bound action plan for pension system reforms, in consultation with all relevant stakeholders.
- (v) Provide recommendation for additional benefit programs during the accumulation phase of the retirement scheme and provide a roadmap for the implementation of such programs.

III. Consultant Qualifications

The required consultant will be seasoned in public pension policy and implementation as well as providing more specialized expertise in specific areas. The consultant should have the following qualifications:

- (i) At least 10 years' experience working with the design and implementation of public pension and social security systems;
- (ii) Demonstrated experience assessing and modeling the sustainability, adequacy and welfare impact of pensions and elderly assistance; and
- (iii) Experience working in developing countries with large informal sector populations.

The consultant will also be expected to demonstrate experience advising on the following areas:

- (i) Supervision of pension or social insurance compliance and collection, including linkages with tax authorities;
- (ii) Pension or social insurance contributor coverage, ideally in a developing country context;
- (iii) Public pension governance and investment management; and
- (iv) Options for payouts of the defined contribution scheme, including scheduled withdrawals.

IV. Process and Deliverables

This assignment should begin with a careful review of the wealth of documentation prepared in 2009 when the scheme was established, including the minutes of committees established at the time. This information will be gathered and provided to the consultant by the MPAO. The consultant will use this review to prepare an inception report, laying out the work plan, structure of the report, timeline and any further information needs (20 working days).

The consultant will then need to conduct a scoping visit (or a virtual visit, if travel conditions do not permit a physical mission) to interface with the key counterparts, clarify the expected deliverables and outcomes, and collect the data necessary for the modeling and other projections required in the study. Travel, accommodation and subsistence costs of such trips will be paid by the client provided all such expenses are approved in advance and substantiated with adequate receipts, etc. (10 days).

The consultant should prepare a draft report and PowerPoint presentation of their findings in each of the areas outlined in the Scope of Work above. (20 days).

The PowerPoint should be used as a basis for workshops to be held in Male during a second visit (or virtually if travel is not possible). This visit should serve three functions: (i) present the initial findings to multiple counterparts and stakeholders while soliciting reactions and inputs; and (ii) discuss the draft report with key counterparts while noting reactions, comments and requests for further elaboration or clarification. (10 days).

The consultant should then revise the report as needed and submit to the counterparts for review and approval. (10 days).

V. Payment

The consultant will be reimbursed based in US dollars on the outputs provided by applying a negotiated daily rate to the estimated contract length of 70 working days. Payment of the total sum will be paid in installments, according to the following proportions:

- (i) Inception report (30%)
- (ii) Draft report (30%)
- (iii) Final report (40%)

Extensions or revisions to this arrangement are possible by mutual agreement.