

# Approaches to Evaluation of the Reliability of Private Pension Funds

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**Abstract.** The article examines the issues of assessing the reliability of private pension funds in the Russian Federation. The pension system has an important role in the social, economic and political life of society. The social and economic development of society depends on an effective pension system. Over the past twenty years, Russia has been actively reforming the pension system. Recent changes in the issues of accrual and distribution of pensions have led to the active development of private pension funds in the country. Private pensions funds greater returns on investment for members than state funds. But the downward trend in the number of funds leads to a loss of members confidence, which is confirmed by a decrease in the growth rate of new fund's members. In relation to the importance of the effective work of private pension funds for the country, in Russia the Expert RA Agency has developed a reliability rating for pension funds. The article analyzes the foreign and Russian methodology for assessing the reliability of pension funds and the criteria that are considered in these estimates. Based on the analysis of foreign and Russian experience, the author proposes an improved methodology for evaluating the reliability of Russian private pension funds. The application of this technique will increase the level of confidence of members in private pension funds. And funds will be able to influence the rating, improving their positions according to weaker criteria.

## 1. Introduction

In modern conditions of reforming the pension system in Russia, changes are taking place in the calculation and distribution of pensions, which leads to the need to transfer funds to private pension funds. A private pension funds, within the framework of compulsory pension insurance, implements programs for managing the funded part of the labor pension of the population [1].

Private pension funds in Russia are developing quite dynamically from 2015 to 2018, and despite the reduction in the number of funds from 102 to 52 units. During these years, the number of participants in the voluntary pension system increased from 5,806,697 to 6,131,624 people, assets grew from 2,886,906.2 to 4,056,956.6 million rubles, owned capital grew from 160,348.9 to 384,795.7 million rubles, and the investment portfolio of pension accumulations of private pension funds increased from 1,734,359.0 to 2,595,066.4 million rubles [2, 3].

It is also important to consider that private pension funds, although more flexible in their investment strategies, in contrast to the state fund, also have legislative restrictions on the management and investment of pension savings funds, which significantly reduces the possibility of increasing their profitability and pensions for future pensioners [4].

Despite the active growth of private pension insurance in the country, there is a problem of mistrust in this system, especially after a serious reduction in the number of funds and the withdrawal of licenses from the Central Bank.

In this regard, the emergence of a reliability rating of private pension funds in the country, based on a reliable and comprehensive assessment of various criteria responsible for the long-term and stable functioning of these pension funds in Russia, becomes relevant.

## **2. Literature review**

Please follow these instructions as carefully as possible so all articles within a conference have the same style to the title page. This paragraph follows a section title so it should not be indented. Research on the provision of pensions and the activities of private pension funds often emphasize the importance of the reliable functioning of the funds and their responsibility to members.

Some researchers note that recent trends in the world lead to the need for pension funds to show clients their reliability, while taking into account sustainable development and make trade-offs between social and environmental objectives on the one hand and financial objectives on the other [5].

Foreign studies also note that the older the pension fund, the more financially stable it is. However, some studies suggest that a large fund does not always give a large financial return (profitability), but it is more reliable [6].

Russian researchers note that when choosing a private pension fund, they viewed such qualities as profitability and reliability. At the same time, a significant characteristic of reliability is the size of the fund's own funds, the "age" of the fund and a moderate investment strategy [7].

Terekhova and Suslyakova note that private pension funds have several socially significant functions and to reduce risks for clients when choosing pension fund, it is important to consider not only profitability, but also the reliability of the fund [8].

Loktionova and Illarionova noted several reliability criteria when choosing a private pension fund, among them: the year the fund was established, the founders of the fund, the fund's profitability, position in ratings, the openness of the fund, the reputation of the fund, the site's user-friendliness and services [9].

Analysis of studies reflects that the issues of choosing a reliable private pension fund are relevant, both in Russia and in the world. Researchers have taken different approaches to reliability when choosing a pension fund, but they clearly note its importance, as well as the importance of the rate of return on investments.

## **3. Methodology**

As part of the study, an analysis was made of foreign and Russian experience in calculating the reliability rating of pension funds. The approaches to assessing the reliability of the pension funds of the Russian agency RA Expert were investigated, as well as the approach of the international company Chant West.

## **4. Discussion**

The importance of reliability analysis of private pension funds for their comparison and investment choice led to the emergence of various ratings and criteria for assessing the reliability of pension funds. By the reliability of the pension fund, the author understands the ability of the pension fund to perform its functions of pension provision on the conditions provided for by the agreement with the fund's members.

The international company Chant West has developed its own methodology for assessing pension funds. The purpose of their rating is to give the average person a reliable means of comparing one fund with another [10]. Their rating is expressed in "apples", where 5 "apples" are the highest rating, and 1 "apple" is the lowest rating. 5 Apples is the Highest Quality Fund, 4 Apples is a High Quality Fund, 3 Apples is a Fair Quality Fund, 2 Apples is a Low Quality Fund and 1 Apple is the Lowest Quality Fund [11].

Pension fund ratings are based on both publicly available information and the information that the funds provide to the company Chant West. According to the Chant West methodology, they evaluate pension funds according to four groups of criteria: investment; member services; fees; organization [11].

In the table. 1 presents a classification of the main criteria of this methodology, their weight, as well as Sub-Criteria. Consider each of the criteria. Investments are obviously important and account for 45% of overall rating. This category focuses on criteria such as portfolio management, investment governance, manager research, capital markets research, past performance. The second criterion is the member services, in these services are education (public website and secure website), communication materials (member statements, campaigns and newsletters), and financial advice services. The third criterion is fees, when assessing a fee, not only at the costs that the member pays, but also on how clearly and completely the fund discloses those costs. The fourth criterion is organization, in this criterion it is estimated who owns or controls it, the strength of its management team and its strategy for the future.

**Table 1.** Pension Ratings Methodology Chant West.

| Main Criteria   | Weigh | Sub-Criteria                   | Weightings |
|-----------------|-------|--------------------------------|------------|
| Investment      | 45%   | Portfolio Management           | 35%        |
|                 |       | Investment Governance          | 20%        |
|                 |       | Manager Research               | 15%        |
|                 |       | Capital Markets Research       | 15%        |
|                 |       | Past Performance               | 15%        |
| Member Services | 30%   | Communication Materials        | 50%        |
|                 |       | Education                      | 30%        |
|                 |       | Advice Services                | 20%        |
| Fees            | 20%   | Management Costs               | 80%        |
|                 |       | Disclosure                     | 20%        |
| Organization    | 5%    | Ownership                      | 50%        |
|                 |       | Management & Business Strategy | 50%        |

Complied by the authors according to [11]

In Russia, the RA Expert rating agency conducted a study of the reliability of private pension funds in accordance with its own developed methodology in assistance of the National Association of Pension Funds. This assessment was carried out based on information provided by the funds [12].

The financial reliability rating of a private pension fund is the opinion of the Expert RA rating agency on the possibility of full and timely fulfillment by the fund of its current and future obligations under private pension schemes and compulsory pension insurance [13].

The methodology is mastered on the calculation of indicators for five groups of criteria: company and staff; market positions; investment process; management and control methods; operational stability [14]. Table 2 describes in more detail the criteria and Sub-Criteria of this methodology.

**Table 2.** Methodology for assessing the reliability of private pension funds.

| RA Expert Agency.              |   |
|--------------------------------|---|
| Main Criteria                  | Sub-Criteria  |
| Company and staff              | Market life   |
|                                | The influence of owners on the development of the company   |
|                                | Key staff experience and stability  |
|                                | Basic development strategy  |
|                                | Organizational structure  |
| Market positions               | Scope of activities   |
|                                | Geography of activity   |
|                                | Market share  |
|                                | Customer Base Features  |
|                                | Key performance indicators  |
|                                | Agent network   |
| Investment process             | Competitive advantages  |
|                                | Amount of funds managed by the fund   |
|                                | The dynamics of funds managed by the fund   |
|                                | Quality assessment of risks and infrastructure  |
|                                | Investment strategy   |
|                                | Portfolio Quality   |
| Management and control methods | Return on investment  |
|                                | Risk Management System Assessment   |
|                                | Risk Management Independence  |
|                                | Risk Management Approaches  |
|                                | Corporate Governance  |
|                                | Information Disclosure Level  |
| Operational stability          | Investment Decision Making Procedures   |
|                                | Assessment of a portfolio of financial investments  |
|                                | Assessment of the stability of funding sources  |
|                                | Performance Evaluation  |
|                                | Diversification of revenue and customer base  |
|                                | Assessment of the resource base necessary to maintain stability and quality of the investment process |

Complied by the authors according to [14]

An analysis of the international methodology shows that it is presented more clearly and reveals the weight of the criteria in the overall rating score. The Russian methodology is not fully disclosed in the public domain, clear criteria and their weight in the overall ranking are not presented.

## 5. Results of the study

An assessment of the reliability of private pension funds and a rating compiled by this assessment are necessary for the formation of a more open pension system. However, the analysis of the methodology for assessing the reliability of pension funds revealed the shortcomings of the current methodology of RA Expert due to the low level of openness of the methodology.

In order to improve the methodology for assessing the reliability of private pension funds in Russia, the introduction of the author's methodology is proposed (Table 3). This technique is based on five basic criteria: investment process; fund member support; market positions; company and staff; operational stability.

**Table 3.** Methodology for assessing the reliability of private pension funds.

| Main Criteria         | Weight | Sub-Criteria  | Weightings |
|-----------------------|--------|---|------------|
| Investment process    | 40%    | Investment Portfolio Quality                              | 20%        |
|                       |        | Return on investment                                      | 20%        |
|                       |        | The amount of pension savings managed by the fund         | 15%        |
|                       |        | The dynamics of pension savings managed by the fund       | 15%        |
|                       |        | Risk assessment   | 15%        |
|                       |        | Investment strategy                                       | 15%        |
| Company and staff     | 20%    | Market life   | 20%        |
|                       |        | Business management strategy                              | 20%        |
|                       |        | Key staff experience                                      | 20%        |
|                       |        | Internal control  | 15%        |
|                       |        | Information disclosure                                    | 10%        |
|                       |        | The influence of owners on the development of the company | 15%        |
| Fund Member Support   | 20%    | Advice Services   | 50%        |
|                       |        | Education   | 50%        |
| Market positions      | 10%    | Market share  | 20%        |
|                       |        | Customer base dynamics                                    | 20%        |
|                       |        | Customer base quality                                     | 20%        |
|                       |        | Volume of assets  | 20%        |
|                       |        | Management costs  | 20%        |
| Operational stability | 10%    | Financial stability                                       | 40%        |
|                       |        | Operational efficiency                                    | 30%        |
|                       |        | Availability of resource base                             | 30%        |

Compiled by the author

The main weight is the assessment of the investment process, among which the most important sub-criteria are the quality of the portfolio of financial investments and the level of return on investment.

The second important criterion of the company and staff is based on the analysis of several sub-criteria devoted to the study of the fund's life in the market, its business management strategy, and the experience of key staff. Sub-criteria also include an internal control system, the level of information disclosure and the influence of owners on the development of the company.

The third criterion for supporting members of the foundation is based on sub-criteria education and advice services. For the successful functioning of the fund, it is important to have loyal members willing to knowledge to increase their retirement savings.

The fourth criterion for market positions consists of several sub-criteria, the most important of which are the fund's market share, the dynamics and quality of the client base, the volume of the fund's assets, and the fund's management costs.

The fifth criterion for operational stability includes such important Sub-Criteria as financial stability, operational efficiency and the availability of a resource base.

Implementation of the proposed methodology, considering international experience, will ensure transparency in the methodology for assessing the reliability of non-state pension funds. It should be noted that in order to ensure the transparency of these data, they must be collected and analyzed by the Central Bank.

In Russia, the activities of private pension funds are regulated by the state, represented by the Central Bank. The Central Bank, in accordance with the legislation, exercises supervision and control over the activities of funds, carries out licensing of pension and pension insurance activities, maintains a register of funds, and discloses information on funds [15]. Therefore, it is advisable to transfer the functions of data collection and calculating the reliability rating of private pension funds to the Central Bank of the Russian Federation.

The openness and accessibility of the data included in the reliability assessment of non-state pension funds will increase trust on the part of clients, while funds will allow them to evaluate their weaknesses and solve problems for the growth of rating indicators.

## **5. Conclusion**

The introduction of new criteria and clarification of the significance of already existing criteria in the methodology for assessing the reliability of private pension funds will solve the problems of distrust in private pension funds. The proposed methodology will make it possible to use the results of calculations in popularizing the services of private pension funds and will lead to an increase in participants in the private pension system.

In relation to the importance of private pension funds for the Russian pension system, data collection and research on the reliability of private pension funds in Russia should be carried out by the Central Bank of the Russian Federation.

The proposed approach to assessing the reliability of private pension funds allows us to assess the role of various criteria in the overall assessment and allows private pension funds to improve their performance, influence the position in this rating and forecast it.

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