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Pension Reform Act 2014
The good, the bad and the ugly

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According to the federal government of Nigeria, the value of pension assets in Nigeria is about 4.21 trillion Naira at the end of March 2014. Globally the figure is put at over 70 trillion dollars as at the end of 2013. On one hand, what we have achieved in Nigeria is worthy of celebration given that we were in a deficit position of over 2 trillion Naira before the 2004 pension reform. On the other hand, the revelation that there are only about 2.4 million contributors to the pension scheme leaves a lot to be desired. Based on the information by the Bureau of Statistics, there are about 60 million Nigerians of working age. Effectively, this means less than 5% of Nigerians are covered leaving over 95% exposed to social insecurity in their old age.

On 1 July 2014, President Goodluck Jonathan signed into law the new Pension Reform Act 2014 which repealed the Pension Reform Act of 2004 (repealed Act). The key objectives of the reform are to ensure contributors receive their benefits as and when due and to assist improvident individuals to save in order to cater for their livelihood during old age.

While the new act is generally a step in the right direction, some of the changes introduced appear not to have been well thought through and some of the changes appear to have been made at the last minute thereby creating some gaps, ambiguities and inconsistencies within the law. The salient changes are outlined in this article and categorised broadly under "the Good", "the Bad" and "the Ugly".

The Good

Exemption from tax - The Act clearly states that any interests, profits, dividends, investments and other income accruable to pension funds or asset are not taxable. In addition, withdrawal of voluntary contribution is no longer subject to tax if withdrawn within 5 years. Tax is limited only to the returns on such contributions if withdrawn within 5 years. It should be implied however that where such returns relate to exempt income like interest on government securities, then tax should not apply.

Withdrawal from Retirement Savings Accounts - The new Act creates another condition in which a contributor may be allowed to withdraw from his retirement account. An employee who disengages from employment or is disengaged before the age of 50 and is unable to secure employment within 4 months of disengagement is allowed to make withdrawals from the account not exceeding 25% of the total amount credited to the retirement savings account.

Choice of Pension Fund Administrator - Employees continue to have the right to choose their PFA. This right has been extended to cover employees whose employers operate a closed pension scheme. Such employees now have the right to choose an external PFA. Where an employee fails to open a Retirement Savings Account (RSA) within 6 months after assumption of duty, his employer can now request a PFA to open a nominal RSA for such employee for the remittance of his pension contribution.

Investment of pension funds - The Act expands the scope of investments in which pension funds can be invested and this includes specialist investment funds and other financial instruments the Commission (Pension Commission or PenCom) may approve. While this is a good thing on one hand, care should be taken not to lose sight of the need to protect and preserve contributors' wealth.

Offences and penalties - The Act includes a few novel provisions with respect to offences and penalties. The Act criminalises an attempt to commit an offence and imposes the same penalty as the offence itself. The penalties for misappropriation have also been increased. In addition to a prison term of 10 years and a fine of three times the amount misappropriated, a convicted person would refund the amount misappropriated as well as forfeit to the federal government any property, asset or fund with accrued interest or the proceeds of any unlawful activity under the Act in his/her possession, custody or control. In addition to the above and with particular reference to Pension Fund Custodians (PFCs), the Act imposes a penalty of at least 10 million Naira upon conviction, where the PFC fails to hold the funds to the exclusive preserve of the PFA and PenCom or where it applies the funds to meet its own financial obligations (in the case of a director, 5 million Naira or a term of 5 years imprisonment or both).

Pension protection fund - A pension protection fund has been created under the new Act to include an annual subvention of 1% of the total monthly wage bill payable to employees in the public sector, an annual pension protection levy (the percentage of which is to be determined by PenCom) and income from investments of the Pension Protection Fund. The objective of the Fund is to guarantee a minimum benefit to contributors in the event of any shortfalls in the investment of pension funds and any other use PenCom may determine from time to time.

Dispute resolution - Any employee aggrieved with his employer or PFA is obligated to approach PenCom for a redress before exploring arbitration or commencing an action at the National Industrial Court. Under the repealed Act, the avenues for dispute resolution were limited to Arbitration and the Investment and Securities Tribunal.

The Bad

Scope and coverage - The Scheme applies to employees in both the public and private sectors. Mandatory contribution is applicable to organisations in which there are 15 or more employees (previously 5 employees). This effectively reduces the number of employers and employees that are likely to benefit from the scheme. Given the low level of contributors under the Scheme, this change is counterproductive.

Basis of contribution - Contributions are now to be based on 'monthly emoluments' being the total emolument as defined in the employee's contract of employment provided it is not less than the total of the employee's basic salary, housing and transport allowance. This definition is vague and could be interpreted to mean that all items that are paid on a monthly basis (in addition to basic, housing and transport) would form part of the base on which the pension rates are applied. This potentially larger base could well mean that many employers will see an increase of over 100% in their pension contribution obligations while employees' net pay will reduce unless their employers chose to increase their salaries to accommodate the additional contribution.

Rates of contribution - The rates of contributions to be made under the new Scheme by both the employer and employee are a minimum of 10% and 8% respectively (7.5% of the employee's monthly basic, housing and transport allowances by both parties under the repealed Act). Again, this will increase the cost of employment and may force many employers to take drastic measures such as rationalisation of staff strength.

The Ugly

Commencement date - The Pension Reform Act 2014 (Act) was signed into law by the President on 1 July 2014. The Act does not specify a commencement date. The Interpretation Act provides that where no date of commencement is contained in an Act, the commencement day shall be the day the Act is passed or signed into law. Unless a commencement date is inserted before the Act is gazetted, the commencement date will be 1 July 2014. This does not give room for transition arrangement and proper planning by affected employers.

Gaps in coverage - Only employers with a minimum of 15 employees are required to contribute to the new Scheme. The Act provides that in the case of private organisations with less than 3 employees participation in the Scheme would be governed by guidelines issued by the National Pension Commission (PenCom). However, the Act is silent on the applicability of the Scheme to private organisations with more than 3 but less than 15 employees. Also what happens to employers with 5 to 14 employees regarding their past contributions under the old Act?

Sole contribution by employers - The new Act provides that an employer can take full responsibility of the contribution but in that case, the contribution shall not be less than 20% of the employee's monthly emolument. This does not make sense given that the combined contribution by both parties is 18%. Employers will therefore be discouraged from taking full responsibility.

Conclusions

PenCom should promptly issue regulations and guidelines to address the bad and the ugly sides of the new law. Where an amendment to the law is required, this should be done by the national assembly in proper consultation and engagement with stakeholders. Employees may find some satisfaction in the fact that employers would contribute at least 10% of their monthly emoluments but only for those who are lucky to keep their jobs. Employers must prepare for either an increase in their staff costs or some restructuring of staff compensation to keep the costs at affordable levels.

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