

The background of the cover is a photograph of an elderly woman from behind, wearing a bright green patterned sari and a black crop top. She is standing on a concrete step in front of a blue-painted wall and a wooden door. The wall has a textured, peeling paint effect. The woman is looking down, and her right foot is visible, wearing a simple silver anklet.

SAVING THE NEXT BILLION FROM OLD AGE POVERTY

global lessons for local action

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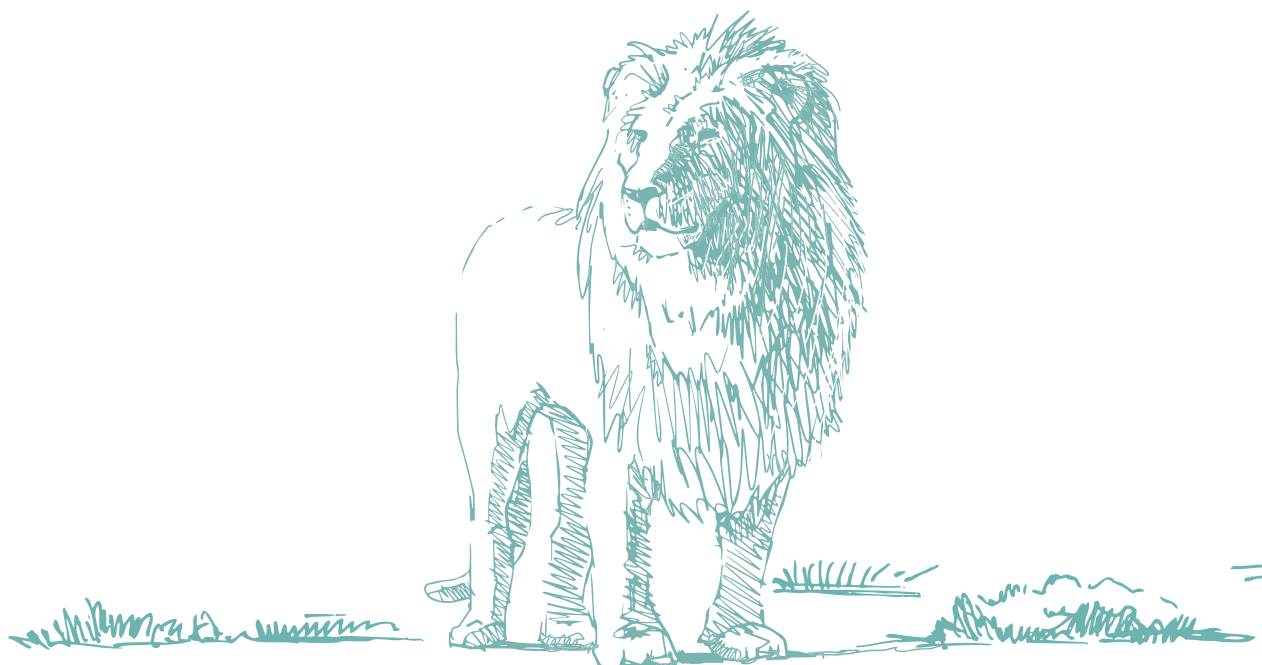
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PENSION REFORM CHALLENGES AND **PROSPECTS IN NIGERIA**

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INTRODUCTION

Pension reform in Nigeria was engendered by the imperative to examine the myriad challenges bedevilling the retirement benefit system in both the public and private sectors. The public sector's hitherto Defined Benefit (DB) scheme had become unsustainable as a result of a paucity of funds and inadequate budgetary provisions for salaries and pensions. There were also several demographic shifts due to rising life expectancies in addition to weak, inefficient, opaque, and cumbersome administrative structures. The private sector schemes, which were akin to the Provident Fund (PF) schemes, had similarly been characterized by low coverage and compliance ratio as a result of ineffective regulation and supervision.

Upon the return to democratic governance in 1999, the Federal Government of Nigeria embarked on a holistic reform of the pension industry. A cardinal objective of this reform was to institutionalize a sustainable retirement pension system with the capacity to achieve the ultimate goal of providing a stable, predictable, and adequate source of retirement income for each worker in Nigeria. The reform also sought to establish a uniform set of rules and regulations for the administration and payment of retirement benefits for both the public and private sectors; stem the growth of outstanding pension liabilities; reduce the fiscal cost of pension to government; stimulate domestic savings; generate a pool of long-term funds for financing developmental projects; and promote private investments into the economy.

COUNTRY PROFILE

The Nigerian Government is a democracy comprising federal, state and local governments. The country's estimated population of about 170 million makes it the eighth most populous country in the world. Nigeria's population can be profiled as follows: 0 – 14 years (41.5%); 15 – 64 years (55.5%); and 65 years and above (3%). Located in Western Africa, bordering the Gulf of Guinea, between Benin and Cameroon, as well as the Niger Republic, Nigeria covers an area of 923,768 square kilometers, which is made up of 910,768 square kilometers of land and 13,000 square kilometers of water. Natural resources include natural gas, petroleum, tin, iron ore, coal, limestone, niobium, lead, zinc, and arable land. Periodic droughts, flooding, and erosion are the most common natural hazards.¹

The total adult population stands at 94 million out of which 48.6% have access to financial services, whilst 36.3% of all adults have direct/indirect access to deposit money in banks in addition to banking products such as ATM cards, credit cards, savings, and current

¹ <https://www.cia.gov/library/publications/the-world-factbook/geos/ni.html>.

accounts, mortgage, loans or non-interest banking products. In addition, 12.3% of all adults have access to other formal institutions and financial products, such as insurance, microfinance, pension, or equities.²

Mortality Tables representing the entire population were published by the National Population Commission (NPC) in October 2015³. However, these projections are only useful when considering the population as a whole, and separate tables are needed for the insurance and pension industries to more accurately price retirement benefits and life assurance products since those benefitting from these products tend to be wealthier and live longer.

A REVIEW OF THE NIGERIAN PENSION SYSTEMS

PUBLIC PENSION SCHEMES

In Nigeria, the first public sector pension scheme was the Pension Ordinance of 1951, with retroactive effect from 1st January 1946. The law provided public servants with both a pension and a gratuity. Pensions Decrees 102 and 103 (for the Military) of 1979 were enacted, with retroactive effect from April 1974. These Decrees remained the operative laws on public service and military pension in Nigeria until June 2004. However, there were several government circulars and regulations issued to alter their provisions and implementations. For example, in 1992, the qualifying period for gratuity and pensions was reduced from 10 years to five years and from 15 years to 10 years (Report of the Vision 2010 Committee, 1997).

In 1997, State Owned Agencies and Enterprises were allowed to have individual pension arrangements for their staff and appoint Boards of Trustees (BOT) to administer their pension plans as specified in a Standard Trust Deed and Rules prepared by the Office of the Head of the Civil Service of the Federation. Each BOT was free to decide on whether to maintain an insured scheme or self-administered arrangement. Robust pursuit of pension reforms came as a result of a privatization programme embarked upon by the Federal Government under the supervision of the Bureau for Public Enterprises. It was noticed during the exercise that most public enterprises had huge pension liabilities, which eventually turned out to be the case with the main stream civil service as well. Virtually all the bidders for these enterprises realized that there was no benefit to acquiring the assets as the pension liabilities would obliterate any gain that could be realized from the assets. Hence, the government was confronted with a huge pension challenge with an actuarially estimated liability of about 2 trillion of Nigeria's local currency at that time (USD 6.6 billion at the prevailing exchange rate of NGN 305/USD).

² <http://www.efina.org.ng/assets/ResearchDocuments/A2F-2014-Docs/Updated/EFInA-Access-to-Financial-Services-in-Nigeria-2014-Survey-Key-FindingswebsiteFINAL.pdf>.

³ Abridged Life Tables of Nigeria 2006 - 2017.

PRIVATE PENSION SCHEMES

The first private sector pension scheme in Nigeria was set up for the employees of the Nigerian Breweries in 1954, which was followed by United African Company (UAC) in 1957. National Provident Fund (NPF) was the first formal social protection scheme in Nigeria, established in 1961 for the non-pensionable private sector employees. It was largely a savings scheme, where both employee and employer would contribute a sum of NGN 4 (~ USD 0.013) each on monthly basis. The scheme provided for only a one-off lump sum benefit. The Nigeria Social Insurance Trust Fund (NSITF) was established by Decree No. 73 of 1993 to provide enhanced social protection for private sector employees. The NSITF took over the assets of the NPF and commenced operations in July 1994. Thus, all registered members of the NPF became automatic members of the NSITF. Similarly, all private sector employers and employees were mandated to register as members as soon as they commenced operations and assumed duty respectively (Report of the Vision 2010 Committee, 1997).

REGULATORY LANDSCAPE

Prior to the enactment of the Pension Reform Act 2004, there were three agencies of the government responsible for policies and rules governing the operations of the institutions providing pension services. The first was the Securities and Exchange Commission (SEC), which regulated asset management companies. The second was the National Insurance Commission (NAICOM), which regulated insurance companies that handled insured schemes. The third was the Joint Tax Board (JTB), which approved and monitored all private pension schemes with enabling powers from Schedule 3 of the Personal Income Tax Decree 104 of 1993 (Odia and Okoye, 2012).

INSTITUTIONAL CHALLENGES

PUBLIC PENSION SCHEMES

Nigeria had operated particularly in the public sector, a DB pension scheme, which was largely unfunded and non-contributory. The system was characterised by annual budgetary provisions by various organs of the government. Given the fact that this was, for the most part, unfunded, the DB system led to massive accumulation of pension liabilities, which by June 2004, was estimated at about USD 6.6 billion⁴. In addition, there were demographic shifts due to rising life expectancy rates, while administration of the scheme was weak, inefficient and cumbersome, inexorably causing a lack of accountability by those managing the system.

PRIVATE PENSION SCHEMES

Although the private sector schemes exhibited a higher level of organization, with some companies establishing structured retirement benefits for their employees, a good number had accountability and transparency issues, which resulted in the arbitrary dispensation of pension rights. Employees on short term contracts and daily wage earners did not have any

⁴ Journal of Professional Administration; vol8, No.1. April 2007 (24-29).

retirement benefits extended to them. Coverage was not obligatory as there was no law mandating private employers of labour to establish pension schemes for their employees.

The schemes were also inundated with the problems of poor record keeping, lax supervision of the pension funds and delays in approving pension scheme applications. There was no mechanism for effectively assessing the technical and professional competence of institutions managing pensions.⁵

NEED FOR A REFORM

There were several attempts to reform the Nigerian Pension System. In this regard, a number of Committees were set up to look into the challenges of pension schemes and proffer solutions towards a sustainable pension system for the country.

During the privatization of public enterprises, the Nasir El-Rufai-led Bureau for Public Enterprises (BPE) realized the inherent difficulties in privatizing such companies due to their huge pension liabilities. The BPE drew the attention of the government to the urgency of tackling this public sector pension's liability estimated at about USD 6.6 billion⁶.

In light of all the previous efforts and the discovery made by the BPE on pension liabilities, President Olusegun Obasanjo set up the Fola Adeola Pension Reform Committee (FAC) to collate all previous efforts made on pension reforms and work towards a workable and sustainable scheme for the country. The FAC recommended in its report, that a Contributory Pension Scheme should be established to cover both public and private sector employees. The Committee also drafted the bill that established both the recommended Scheme and the National Pension Commission.

THE PENSION REFORM ACT OF 2004

The Pension Reform Act of 2004 was, among other things, enacted to attenuate the challenges of Nigeria's hitherto inefficient pension system. Given the status quo in the industry at the time, the federal government essentially had two policy options:

- a. The introduction of parametric short-term measures that may have addressed the symptoms rather than the root cause of the problem.
- b. The institutionalization of reforms that would address the underlying weaknesses of the previous schemes and entrench measures for the sustainability of the new framework.

In deciding to adopt the latter option, the Federal Government introduced the Contributory Pension Scheme (CPS) with fully funded, privately managed individual

⁵ National Pension Commission was the first regulator and supervisor of all pension matters in Nigeria.

⁶ Nasir El-Rufai. Pension Reform: To be or Not to be?

Retirement Savings Accounts (RSAs), to ultimately engender the strategic objective of ensuring that every worker in Nigeria is covered by a retirement benefit arrangement that is easily accessible and pays periodic income at the end of an individual's working career.

The main objectives of the pension reform were to:

- i. Ensure that workers receive their retirement benefits as and when due.
- ii. Assist workers to save in order to cater for their livelihood during old age.
- iii. Establish uniform rules, regulations, and standards for administration of all pension matters in Nigeria.
- iv. Establish a strong regulatory and supervisory framework for the pension industry.
- v. Stem further growth of pension liabilities.
- vi. Impose fiscal discipline in budgetary process as pension obligations would be accurately determined.
- vii. Reduce fiscal cost to government, stimulate domestic savings, generate a pool of long-term funds for financing developmental projects and increase private investments.

LEGAL FRAMEWORK

COVERAGE OF THE CONTRIBUTORY PENSION SCHEME

The Pension Reform Act (PRA) 2004 stipulated that the CPS shall be mandatory for all workers in the Public Service of the Federation, the Federal Capital Territory, and in the private sector where the total number of employees is five or more. However, Judicial Officers whose pension was provided for under Section 291 of the 1999 Constitution of the Federal Republic of Nigeria were exempted from the CPS.

MINIMUM RATE OF PENSION CONTRIBUTION

The minimum contribution rate was set for 15% of the employee's monthly emoluments, where employers and employees contribute 7.5% each. An employer may, however, elect to contribute the entire 15% on behalf of the employee. Furthermore, an employer is obligated to deduct and remit the employee's pension contributions to his RSA through a Pension Fund Custodian (PFC) within seven days of payment of salary, and the PFC shall notify the Pension Fund Administrator (PFA) within 24 hours of the receipt of the contribution.

LIFE INSURANCE POLICY

Every employer was mandated to take a life insurance policy in favour of its employees for a minimum of three times their total annual emolument. Benefits were paid on death in active service.

WITHDRAWAL OF RETIREMENT BENEFITS

A holder of an RSA could only withdraw from his RSA upon retirement or at attaining the age of 50 years, whichever comes later. Payment of retirement benefits shall be either through programmed withdrawal (offered by PFAs) or purchase of life annuity from life insurance companies licensed by NAICOM.

ACCRUED PENSION RIGHTS

As part of the transitional arrangements, the accrued pension rights of federal government employees who worked prior to the commencement of the CPS were recognized.⁷ Accordingly, a fund known as the Retirement Benefit Bond Redemption Fund (RBBRF) was established and was maintained by the Central Bank of Nigeria. The Federal Government was obligated to pay, on a monthly basis, an amount not below 5% of its total monthly wage bill into the fund, to be used to redeem all established accrued rights. Payments into this fund were to cease after all accrued benefits had been redeemed.

SUBSIDIARY LEGISLATIONS

The PRA 2004 empowered the Commission to issue subsidiary legislations for the pension industry. Consequently, in order to ensure the smooth functioning of the pension industry as well as guide the operations of the licensed pension operators, the Commission issued a number of subsidiary legislations in the form of guidelines, regulations, frameworks, circulars, and codes. All the subsidiary legislations issued can be found on the Commission's website: www.pencom.gov.ng.

INSTITUTIONAL FRAMEWORK

The National Pension Commission was established by the PRA 2004 to regulate, supervise and ensure the effective administration of pension matters in Nigeria. As the regulator of pension matters, it is statutorily mandated to approve, license, and supervise all pension fund operators as well as establish standards for the management of pension funds.

INDUSTRY OPERATORS

- a. **Pension Fund Administrators (PFAs):** These are licensed by the Commission to register contributors and open an RSA for eligible workers. In addition, the PFA is responsible for investment and management of the pension funds; maintaining books of accounts on all transactions relating to the pension funds under its management; provision of regular information and other related customer services to the beneficiaries and payment of retirement benefits to contributors upon retirement.
- b. **Pension Fund Custodians (PFCs):** These have the responsibility to receive contributions from employers on behalf of the PFAs, hold pension assets in safe custody, execute transactions and undertake activities relating to pension fund

⁷ Under the old Defined Benefits scheme, the qualifying periods for gratuity and pension were five and 10 years. However, in the calculation of the accrued benefits, the benefits were prorated to allow employees who worked for shorter periods to be apportioned some amounts.

investments on behalf of the PFAs. Indeed, in line with the core of the pension reform law, the function of custody of pension fund assets has been separated from its management. In this arrangement, only PFCs can hold pension assets.

- c. **Closed Pension Fund Administrators (CPFAs):** An employer may apply through a wholly owned subsidiary for a CPFA license to manage its own existing scheme provided that the scheme meets stipulated conditions. On issuance of the license, the Commission supervises and regulates the activities of the CPFA, which registers and manages the pension fund of the employees of the sponsoring organization only. In addition, select private companies were allowed to apply to the Commission for approval to continue with their pension schemes that were in existence prior to the enactment of the PRA 2004. However, the pension fund assets of the Approved Existing Schemes (AES) are managed by PFAs and are in custody of the PFCs.

Pension Transitional Arrangement Directorate (PTAD): The PTAD was established as an extra ministerial department under the Ministry of Finance to coordinate the administration of pensions for retirees and persons not transiting to the CPS. The Commission is empowered to regulate and supervise the PTAD that shall cease to exist after the demise of the last pensioner under the defunct DB scheme.

AMENDMENT TO THE PRA 2004

In April 2011, the PRA 2004 was amended to exempt personnel of the military and security agencies from the CPS. This followed a Private Bill sponsored by a member of the Committee on Pensions of the House of Representatives. These personnel are now exempted from the CPS.

THE REFORMS OF 2014

A national conference was organized in 2009 by the Commission in conjunction with the National Assembly to conduct a comprehensive review of the implementation of the pension reform initiatives and obtain inputs from stakeholders towards enhancing the implementation of the reform. The main objectives of the conference were to:⁸

- i. Determine the suitability and/or adequacy of certain provisions of the PRA 2004;
- ii. Identify ways to fully integrate the informal sector, states, and local governments into the Scheme;
- iii. Examine ways to diversify pension fund investments to support infrastructure development while providing adequate returns and guaranteeing safety of the pension assets; and
- iv. Distil inputs from all stakeholders and professionals with a view to conducting a comprehensive review of the PRA 2004.

⁸ Report of the Review of the Implementation of Pension Reform Act 2004.

CHALLENGES IN THE IMPLEMENTATION OF PRA 2004

The conference provided the Commission with the opportunity to identify the challenges in the implementation of the provisions of the PRA 2004. The key challenges are highlighted below:

- i. The CPS did not adequately cover states and local governments, employers with less than five employees, and the self-employed.
- ii. There was a dearth of investment instruments to facilitate the deployment of pension funds in financing infrastructure projects and intermediate in the real sector of the economy.
- iii. The sanctions defined in the PRA 2004 were no longer sufficient deterrents against infractions by operators and eligible employers.
- iv. There was no provision for protecting the pension assets against any losses or adverse effects.
- v. The 5% of the monthly wage bill set aside by the Federal Government to pay the accrued rights for past service was no longer sufficient.
- vi. Although the PRA 2004 made provisions for the payment of a Minimum Pension Guarantee (MPG) to RSA holders who have contributed for a number of years under the CPS, there was no provision for the funding of the MPG.
- vii. Provision for tax exemptions were at the point of accumulation and payment of retirement benefits only. The Act was silent on taxation of income from investment of pension funds. This could prevent the achievement of real returns on the investment of pension funds with dire consequences on a retiree's retirement benefits.
- viii. Employees who lost their jobs had a waiting period of six months before accessing the balances in their RSAs.

PROMULGATION OF THE PENSION REFORM ACT 2014

Against the backdrop of consultations between the Commission and the executive arm of government, an executive bill for the enactment of PRA 2014 was transmitted to the National Assembly. The bill sought to address the challenges that characterized the implementation of PRA 2004. After a comprehensive review and legislative scrutiny, PRA 2014 was signed into Law on 1st July 2014. Some of the new key provisions of PRA 2014 are enumerated below:

- i. In order to address the challenge of limited coverage, PRA 2014 expanded the eligibility criteria for employers to include those with at least three employees as against five employees in PRA 2004. In addition, the self-employed could also participate in the CPS. Similarly, states and local governments are now covered by the CPS.
- ii. The sphere of permissible investment instruments was expanded to accommodate investments in infrastructure without compromising the safety of pension fund assets.

- iii. New offences were addressed and stiffer penalties were introduced to serve as deterrents against mismanagement or diversion of pension funds and assets under any guise, as well as against other statutory infractions.
- iv. PRA 2014 has provided that the 5% deduction of the monthly Federal Government of Nigeria wage bill should be the minimum amount needed to fund the RBBRF Account and the Commission should determine and advise the Federal Government of Nigeria on appropriate rates, from time to time, that are sufficient to address the projected yearly pension liability of the government.
- v. A Pension Protection Fund (PPF) was established to fund the MPG as well as compensate the pension funds in the unlikely event of adverse losses that may be sustained from their investment activities.
- vi. The waiting period to access a percentage of the balance in the RSA by persons who lost their jobs and are unable to secure another job has been reduced from six to four months.
- vii. The rate of contribution has been increased from 7.5% by both employee and employer to 8% by employee and 10% by employer.
- viii. Tax exemption has been extended to the income from investment of pension funds.
- ix. PRA 2014 provides for an enhanced regulatory authority and efficiency of the Commission to provide greater oversight on the Pension Transition Arrangement Directorate (PTAD). This was to ensure greater efficiency and accountability in the administration of the DB scheme.

PLANNED IMPLEMENTATION

The National Pension Commission found it expedient to make contingency plans for the successful implementation of the provisions of PRA 2014 in order to avoid the pitfalls encountered during the implementation of PRA 2004. In this regard, the Commission developed a corporate strategy, and in collaboration with the pension industry operators, developed an industry strategy, to refocus the industry towards achieving the desired objectives. Both strategies were designed on the following thematic areas that were extrapolated from PRA 2014^{9,10}

- i. Inclusive and expanded coverage
- ii. Excellence in service delivery
- iii. Safer and broader investment portfolio
- iv. Positive real returns and visible impact on the economy

For each initiative identified towards the full achievement of the thematic objectives, a team was set up between the Commission and the umbrella organization of the pension operators, nominating one member each, as a co-champion, to ensure its successful

⁹ National Pension Commission, Corporate Strategy – Recommendations.

¹⁰ Nigerian Pension Industry in 2024: Positioning for the Next Decade

implementation. The idea was to have the full participation of all relevant stakeholders in the design of the implementation road map to ensure their buy-in and willingness to deploy all necessary resources as would be required by each initiative.

To drive inclusive and expanded coverage, the Commission established two functions in its organisational structure to facilitate the adoption of the scheme by states and local governments as well as by the informal sector employees.

In order to support economic development, it is fundamental that the pension fund portfolio is diversified to include investments in critical infrastructure, real estate, and other key aspects of the economy. Hence, both the corporate and pension industry strategies consist of initiatives and activities that would increase investment in infrastructure and other alternative assets from 4% in 2014 to 40% by the end of 2019.

As an initial step to diversification, the maximum allocation to Federal Government securities was reduced from 100% of the Assets under Management (AUM) to 80%. In addition, allocation to corporate debt securities was increased from 30% to 35% while infrastructure bonds and funds were introduced and allocated maximum 15% and 5% of the AUM. Private equity funds were also introduced and allocated a maximum 5% of the AUM. The focus is to allow investments in vehicles that could facilitate infrastructure financing and make a visible positive impact on the economy.

In line with global best practices, especially with a view to stimulating sustainability, the Commission, in collaboration with the University of Edinburgh, Scotland, has commenced work on the development of sustainable pension principles that would mainstream the tenets of sustainability, responsible investment, and Environmental, Social, and Governance (ESG) considerations in all investment decisions being undertaken by the industry. In addition, the Commission has inaugurated an impact investment workgroup to fashion out a road-map for the channelling of pension funds into investments that have both an economic and environmental impact.

THE MICRO PENSION SCHEME

To provide legal backing for achieving the objective of covering this category of workers that constitute the larger percentage of the working population in Nigeria, Section 2(3) of Pension Reform Act 2014 expanded coverage of the CPS to the self-employed and persons working in organizations with less than three employees. In addition, given their widely dispersed nature and generally low and irregular incomes, there was the need to provide a pension plan that would meet their specific characteristics. In this regard, the Micro Pension Plan initiative was conceived within the context of an industry wide strategy to bring pension products and services to this class of workers.

In implementing this initiative, the informal sector has been segmented into two broad categories: the low income and the high income earners. Each of these categories will be targeted with appropriate pension products and sensitization programmes that meet their respective peculiarities.

Similarly, the Commission has developed policy documents that set out the eligibility criteria for participation in the Micro Pension Scheme; specified the minimum documentation requirements and registration process for prospective micro pension participants; defined the account services, covering contribution collection, rendering account statement, resolution of issues and accessing the RSA; defined how the Micro Pension Fund would be managed by PFAs; provided incentives for participants; specified minimum technology requirements; and outlined how participants could switch between the Micro Pension Scheme and the Formal Contributory Pension Scheme.

In order to ensure effective and efficient implementation of the micro pension initiative, sensitization activities have commenced through print and electronic media as well as town hall meetings, conferences, roundtable discussions, and seminars. The Commission has developed working relationships with a significant number of relevant stakeholders particularly trade unions, associations and chambers of commerce. This is targeted at their existing memberships, which could easily give a boost to the efforts being made to extend coverage to 40% of Nigeria's working population. This strategy focuses on anticipated quick access to the 37 million small and medium scale enterprises registered by the Small and Medium Enterprises Development Agency of Nigeria (SMEDAN) out of which 5 million were already registered by the Corporate Affairs Commission. Similarly, obtaining buy-in from trade unions and associations would significantly facilitate registration by their members, who in this case are mainly self-employed.

As a consequence of their characteristics, most informal sector workers are less likely to save or embrace schemes that require suspension of their current consumption rate. To ameliorate this concern, the Commission has proposed some incentives that will encourage their participation in the CPS. In this regard, any contribution made by micro pension participants would be divided into two. One portion will be treated as savings for pension, while the second portion, which shall be the smaller, will be treated as contribution that could be withdrawn not more than once every quarter. However, eligibility criteria have been established for accessing the latter portion of the contribution. In addition, contributions under the Micro Pension Scheme would not be subject to tax when accessed as they are viewed as contributions from the disposable income of the participants, which are presumed to have been earlier taxed.

Following the provision of Section 89(2) of PRA 2014 and subject to guidelines to be issued by the Commission, micro pension participants may apply a percentage of the pension assets in their RSA towards payment of an equity contribution for a residential mortgage.

However, it is evident that a robust technology platform that would support the provision of customer services is necessary to effectively and efficiently register, collect contributions, provide RSA support, pay benefits, and provide financial advisory services to this class of workers.

The mode of registration for micro pension would be done via an electronic platform utilizing mobile devices and registration centers. The process, which includes capturing of basic bio-data and biometrics, would be user friendly. The registration module would have controls to ensure that there are no duplications of registrations. This would include sector codes that would serve as unique identifiers to enable micro pension contributors be assigned with Personal Identification Numbers (PIN). A special fund would be established for the participants of the Micro Pension Scheme. It will make adequate provisions for the itinerant nature of this group and create fair value for the investments whilst ensuring adequate security of their assets.

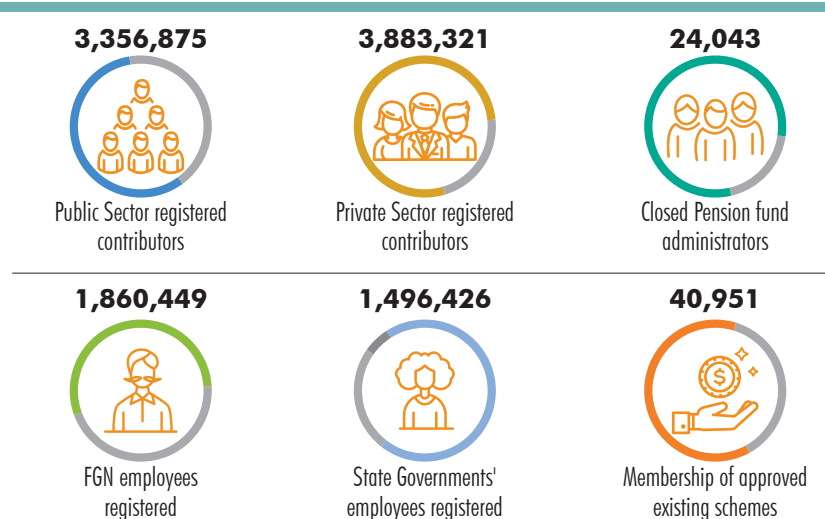
Consequently, the Commission has commenced discussions with service providers and relevant regulators as well as the targeted workers in the informal sector on the intended technology with a view to creating the enabling environment and buy-in. As highlighted in many chapters in this volume, this element will be absolutely vital to create a low cost and efficient platform that can ensure small contributions can be efficiently invested for the benefit of members. Interoperability and account portability will also be critical as will ensuring that the contributions can be invested at scale to ensure the best governance and the lowest implementation costs.

IMPLEMENTATION UPDATES¹¹

- The Commission, as regulator of all pension matters in Nigeria, licensed 27 PFAs, five PFCs and seven CPFAs. However, following mergers and acquisition, there are currently 21 PFAs and four PFCs while the number of CPFAs remains seven.
- The Industry has registered 7.24 million contributors from both the public and private sectors as on 30th September 2016. The public sector made up 46.41% while the private sector constituted 53.59%.

Figure 8.1

Distribution of Memberships of Various Pension Schemes as at Q3:2016



Source: National Pension Commission Statistics

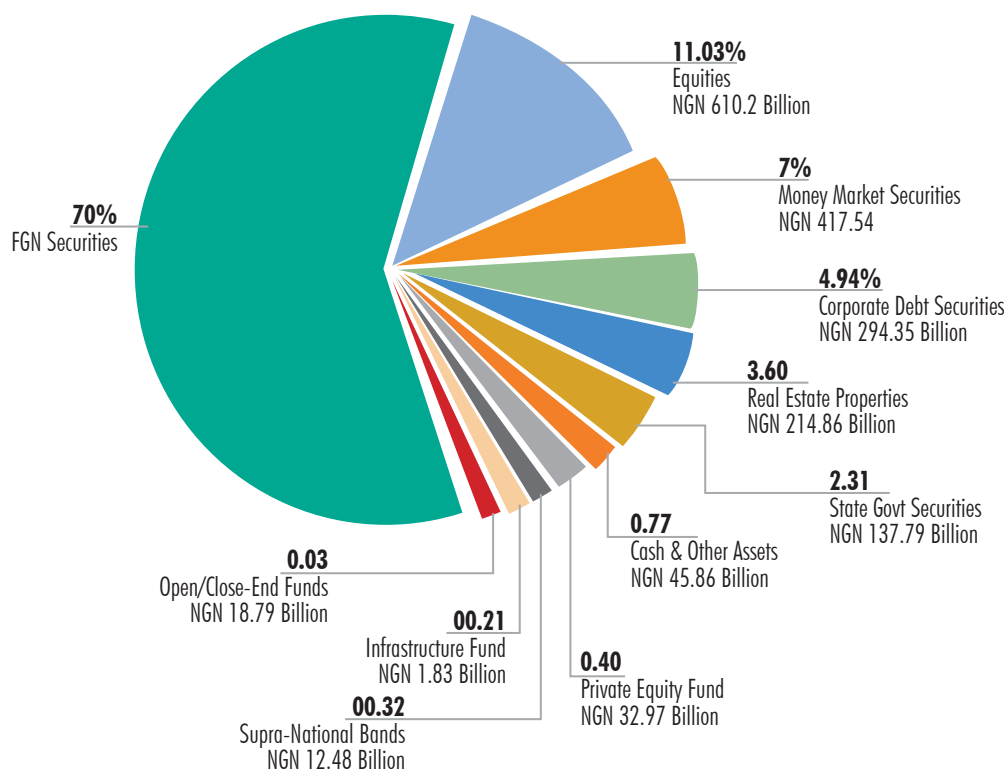
¹¹ All statistics were based on a database generated and maintained by the National Pension Commission

- c. The value of pension fund assets grew from NGN 405.95 billion (USD 1.33 billion) in 2006, which was the year of actual commencement of investment activities, to NGN 5.96 trillion (USD 19.55 billion) as on 30th September 2016. All currency conversions were done at the official rate of NGN 305 per 1 USD.¹²

The portfolio of the pension fund was skewed towards Federal Government Bonds and Treasury Bills due to the high interest rates.

Figure 8.2

Distribution of Members According to Number of Contracts Owned



Source: National Pension Commission Statistics

Traditionally, the PFAs ensure that their portfolios are revalued on a daily basis to ensure that risks are minimised while maintaining fair return on investments. However, investment decisions are taken based on the individual PFA's strategy, which was developed based on the provisions of the regulations on investment of pension fund assets that were issued by the Commission.

The increasing relative importance of the pension sector is reflected by the proportion of the pension assets to Nigeria's GDP, which grew from 1.4% in 2006 to 7% in 2010. It was estimated at 6.26% as on 30th September 2016 of the rebased Nigerian GDP estimated at an annualized value of NGN 97.4 trillion at the end of the third quarter of 2016.

¹² Official exchange rates are issued by the Central bank of Nigeria.

A total of 174,820 contributors from both public and private sectors have already retired as at end of the third quarter of 2016 and are receiving their monthly pension as and when due. So far, a total of NGN 395.18 billion (USD 1.3 billion) has been paid as pension with an average monthly pension of NGN 6.39 billion (USD 21 million).

IMPACT OF THE REFORM

The CPS has stemmed the growth of pension liabilities as well as generated a pool of investible funds in Nigeria, which has deepened the financial sector and the economy in general. The scheme has also promoted the development of the corporate debt market with the collaboration of the World Bank/IFC. Provision was made for the pension funds to invest up to 35% of the total AUM into corporate debt.

The capital market is perhaps the highest beneficiary of the pension reforms among all the sectors in the financial industry. The reform has significantly increased the volume of trading and the size of the market capitalization of both the bond and stock markets. In addition, the pension operators, as large institutional investors, continue to demand high corporate governance standards and practices in investee companies. Indeed, a Pension Index had been created in the local stock exchange, which comprises stocks that qualify for pension fund investments.

The Investment Regulation provides that pension funds can only invest in debt instruments that have a minimum investment-grade rating. This has facilitated the development of the credit/risk rating industry as well as increased the capacity of local rating agencies.

The private equity industry was also under-developed. The Commission obtained the support of the Commonwealth Secretariat in organizing roundtable discussions towards developing the industry in Nigeria. Private Equity was made an allowable asset class for pension funds in 2010. The Commission has continued to organize seminars and workshops for the education of the board and management of the pension fund and there is an increasing appetite for pension fund investments in the asset class.

Provisions have been made in both PRA 2004 and PRA 2014 for Group Life Insurance (GLI) cover for all employees. This has deepened the GLI market in a country where not many people were even aware of GLI products. Similarly, the annuities market was very shallow. Also, given that there are provisions in both PRA 2004 and PRA 2014 for life annuity as one of the two options for accessing retirement benefits, the Commission had to organize a foundation course on life annuity in conjunction with the National Insurance Commission for both the regulators and operators in the pension and insurance industries. Presently, there are many insurance companies offering this product.

Previously, Nigeria did not have locally developed Life Tables. The A (55) Mortality Tables, which were based on the 1946 – 1948 experience collected from the U.K. insurance companies are currently in use, but are inherently non-comprehensive and

non-representative. This led the Commission to start championing a project to develop Life Tables for Nigeria so as to facilitate the accurate computation of pension benefits and insurance related benefits.

Education is the root to successful implementation, and as such, the pension industry is promoting the establishment of a Pension Institute that will drive capacity building for the industry locally. Already, there is a bill before the National Assembly to enable the emergence of the institute. Similarly, the Commission and other financial regulators in the country developed a curriculum to teach financial products and services, including pensions, to senior secondary schools across the country.¹³

The Nigerian Contributory Pension Scheme has been a subject of study by many African countries and the Commission has provided a platform for promoting the scheme across the Continent through the African Pension Awards (APA), an annual event established in 2015.

CHALLENGES

The Commission has encountered some challenges in the implementation of the reforms. The key challenges are highlighted as follows:

Lack of adequate understanding of the pension reforms by the general public, which was occasioned by inadequate resources to fund extensive public awareness campaigns. There is also the lack of a robust database of employers of labour and employment records as well as identifiable contact addresses in the country, which made enforcement activities of the Commission difficult. Similarly, the lack of unique identifiers has made it difficult to maintain a clean database of contributors for the provision of robust pension account services and the ever changing and demanding IT infrastructure tends to make running the scheme relatively expensive. Indeed, getting better unique IDs is critical to delivering the best long-term outcomes in pension provision.

Compliance by the private sector was found to be a challenge largely due to the fact that pension coverage in this sector was just about 1.3% in 2004 when the reform was introduced. Some of the employers viewed the employer contribution as an additional operational cost and were reluctant to comply. To mitigate this, the Commission had to engage recovery agents to follow up on defaulting employers and recover the outstanding contributions with interest penalties. In this regard, the Federal Government issued a policy that made the submission of a Compliance Certificate issued by the Commission a requirement for companies bidding for contracts in any of its agencies. These steps assisted greatly in ensuring compliance by eligible employers.

The maturity of the local financial industry is key to the success of the funded pension scheme. The experience in Nigeria still demands more depth of the financial system in terms of liquidity, availability of quality investment instruments, and adequate understanding of the workings of the financial system. The inflationary environment

¹³ MOUs were also signed with some select universities across the country in order to promote pension related courses in Nigeria through them.

and the dwindling value of the Naira against major currencies impacts the ability of the industry to meet returns on investment. There is also lack of adequate alternative asset classes in Nigeria that would facilitate diversification of investments.

The funded scheme has recognized the pension liability that accrued under the defunct DB scheme as of 30th June 2004. For the public sector, the financing arrangement to defray this liability is not robust, as a result, many retirees are facing delays in the payment of their full benefits as and when due.

FUTURE OUTLOOK

The Pension Reform Act 2014 expanded coverage of the Contributory Pension Scheme to the Organized Private Sector with three or more employees and the informal sector, which accounts for a greater percentage of the Nigerian labour force, as well as to States and Local Governments. Against this backdrop the Commission in conjunction with the Pension Industry operators developed strategic plans to advocate for compliance with the scheme from these sectors. The Industry would actively pursue an inclusive and expanded coverage, whilst also ensuring excellence in service delivery. This is expected to significantly increase RSA registrations from employees of these very important sectors of the Nigerian economy.

The Micro Pension Scheme has been developed and designed with certain incentives targeted at motivating employees in informal sector of the Nigerian economy and the self-employed to have retirement benefits. In this regard, strategic engagement is currently ongoing between the Commission and relevant key stakeholders including Trade Unions as well as other Associations, to enlighten them on how their members can participate in the Scheme. To drive this initiative, there are various incentives conceptualized including using a portion of the RSA balance to make an equity contribution for residential mortgage, accessing a certain percentage of the total contributions for personal use, Group Life and Health Insurance Schemes, etc. These would be pursued to ensure buy-in and sustainability of the scheme.

The guidelines for a Multifund Investment Structure for RSA Funds have been finalized and are awaiting necessary approval, before release and subsequent implementation. When operational, the guidelines would ensure that the pension assets are appropriately invested to align with the risk appetite of members as well as refocus the investment strategy of PFAs into long term impactful investments in infrastructure and housing/ real estate development as well as the normal government bonds and listed equity. Consequently, initiatives have been developed in the Commission's Corporate Strategy to grow the total pension assets under the management of Pension Funds to 10% of GDP as well as increase investments in identifiable infrastructure and other alternative assets to 40% by the end of 2019. These initiatives would continue to be pursued to actualize the anticipated positive impact of pension fund investments on the Nigerian economy.

The Commission is working to engage a service provider to develop and implement the Pension Administration System (PAS), which is expected to provide the platform for maintaining a robust database on pension matters in the country as well as allow the setting up of the necessary technology for provision of robust services to the micro pension participants. Efforts would be intensified to develop a database of employers and working population in Nigeria to enable full monitoring of compliance by all eligible employers. As highlighted in other chapters in this volume this will be absolutely critical to delivering the full potential of digital pension Inclusion in Nigeria.

These will be achieved through excellence in service delivery across all service levels and establishment of an enabling pension industry that is knowledge based and with highly motivated staff.

LESSONS LEARNED

POLITICAL WILL

The importance of political will cannot be overemphasized. Much cannot be achieved without the express buy-in of the presidency. It was clear from the onset that the success of the Nigerian Pension reform and the introduction of the CPS was driven by the robust support from the highest office in the country. Indeed, in the face of prevalent policy somersaults and changes across the globe, the CPS remains the flagship for continuity as four successive governments have lent support to the implementation of the scheme.

EDUCATION AND SENSITISATION

Education and sensitisation of all arms of government, stakeholders, industry operators, and workers themselves is essential to douse controversies often generated by ignorance or misinformation by individuals with less than altruistic motives. Failure to so do will often result in lengthy, often very public, disagreements at best or an outright rejection of the scheme at the worst. The controversies that trailed the passage of the Nigerian Pension Reform Bills into law could have been avoided if adequate sensitisation was done before the transmission to the legislature. It was evident during the processes that led to the passage of both the laws, 2004 and 2014, that there was no avoiding crucial one-on-one engagements with diverse stakeholders to educate them on the workings of the scheme and the importance of seizing ownership of their future.

The Commission remained collaborative and consultative in rule making, facilitating the establishment of excellent working relationships with other regulatory agencies. This entrenched the understanding of the CPS and prevented regulatory arbitrage in the implementations of the reforms.

SAFEGUARDS

A critical safeguard of the pension reform has been the segregation of administration and custody of the pension fund assets. Prior to the reform, a major concern was the weak and inefficient administration of the pension system. To address this issue, the reform designed an institutional framework that professionalized the administration of the scheme. A two tier management system was established that gave full administration to the PFAs while the custody of the pension assets was given to the Pension Fund Custodians. Thus, there is full separation of administration and custody functions under the CPS, which has assisted immensely in addressing conflict of interest issues, promoted transparency and improved oversight over benefit and investment decisions.

The law stipulates that PFCs must provide a guarantee to all the pension assets under their custody. In addition, the custody is done in the name of the pension contributors, whose contributions are being credited into their personalized accounts, for which they receive regular statements. This ensured that the pension fund assets were ring fenced. Indeed, for the entire 12 years of the reform, there has not been any case of fraud in the system.

INDEPENDENT COMMISSION

The independence of the Commission as a regulatory body was firmly established with reporting lines going directly to the President and Commander in Chief of the Nigerian Armed Forces. In addition, appointments of the heads of the Commission are done by the President subject to confirmation by the Senate. The governance structure of the Commission was diversified to improve the quality of decision making and includes representations from the pensioner associations, labour unions, Ministry of Finance, head of the Federal Civil Service, Central Bank of Nigeria, the Securities Exchange Commission, the Nigerian Stock Exchange and the National Insurance Commission.

USE OF TECHNOLOGY

For a successful pension reform, it is pertinent to develop a robust database of all pension matters. This was one of the major pre-occupations of the Commission during the early days of the reform and remains a factor in its successful implementation. Without a robust database, it will not be possible to establish accrued and future benefits accurately and it will be very difficult to enforce compliance by all eligible employers. Technology continues to play a key role in both the operation and supervision of pension fund assets.

The Commission realized the importance of using technology to conduct off-site reviews of the activities of both the PFAs and PFCs, and as such, developed and deployed the risk management and analysis system. This enabled the PFAs and PFCs to send periodic returns on all required reports for review by the Commission. For investment activities, the reporting is done daily except for weekends when there is no trading. The daily reviews enables the Commission to note risky investments and intervene promptly to avoid major losses.

In addition, the process to implement a PAS has reached an advanced stage. The application was designed to, among other things, have an Automatic Fingerprint Identification System (AFIS) and Governance, Risk and Compliance (GRC) Modules, that would provide capabilities for unique identification of registered members and on-line real-time monitoring of all activities of the operators.

CONCLUSIONS

The reforms of the Nigerian pension system were embarked upon to address the challenges faced by the defunct DB scheme. The CPS, which was introduced by the reforms, has been successfully implemented within the last twelve years, during which time strong institutions, systems, and processes were established to ensure effective operations of the new pensions industry and meet the objectives of establishing a sustainable pension scheme for Nigeria.

The pension reform has simplified the process of payment of retirement benefits through the issuance of effective regulations and guidelines for accessing such benefits. It has gained public confidence and acceptability within the short period of its implementation. The private sector, which had just about 1.3% pension coverage before the reforms, had 54% of the total registered members by the end of the third quarter of 2016. Indeed, the pool of pension funds and assets generated by the CPS has aided the deepening of Nigeria's financial sector and provided a platform for attaining strategic programmes of the government in the area of infrastructure, real estate, and the development of the real sector of the economy. The total value of pension industry assets is in excess of NGN 6 trillion as of 30th September 2016. Furthermore, the CPS has increased transparency and accountability in determining budgetary estimates for payments of pensions by the Federal Government and all the state governments that adopted the scheme.

In spite of the efforts, however, many challenges have arisen in the course of implementing the CPS, which need to be addressed in order to consolidate the gains of the scheme. These challenges are not insurmountable, and the Commission has been championing various initiatives by all relevant stakeholders in order to address them. These efforts have been yielding positive results, particularly, the promulgation of Pension Reform Act 2014 to provide the necessary legal basis for addressing the challenges. In addition, both corporate and industry strategies were developed to establish a roadmap for achieving the objectives of the provisions in the Act. With the Micro Pension Scheme as an initiative in the two strategic plans, the pension industry is set for exponential growth, both in terms of membership and asset size, and continues to contribute significantly to Nigeria's economic development.

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