PENSION REFORM ACT 2004: AN ASSESSMENT OF THE ADEQUACY OF THE LEGAL FRAMEWORK

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INTRODUCTION

I am grateful to the management of the National Pension Commission and the organizers of this Conference for the privilege of addressing this gathering on certain aspects of the Pension Reform Act. I commend the management of the Commission for their consistent, devoted, transparent and enlightened implementation of the Act. If we are far from solving the problems associated with pensioners and their pensions the fault is certainly not that of the management of the Commission. It is to the law that we must look. The law itself is only a few years old and it is our duty to examine it in the light of experience to enable us achieve the objectives for which the law was enacted.

If, after that law was passed, we sat back and congratulated ourselves on the assumption that we had finally solved the problems of pensioners and their pensions once and for all, then we were quite mistaken. Experience has exposed the inadequacies of the solutions that have been proffered. A Conference such as this provides a unique opportunity for frank and dispassionate examination of the law with a view to having its inadequacies addressed.

I have been asked to assess the adequacy of the legal framework under the pension reform. In discharging this responsibility, this paper examined some provisions of the Pension Reform Act 2004 (PRA 2004) in the light of the 1999 Constitution and other laws as well as the experience gained from the implementation of the PRA in the last few years.

THE PROVISIONS OF SECTIONS 3 AND 4 OF THE PENSION REFORM ACT 2004

Before examining Sections 3 and 4 of the Pensions Act it is necessary to examine the provisions of Section 11 of the Act which establishes the Retirement Savings Account sought to be regulated under Sections 3 and 4.

Under section 11 of the Act every employee is required to maintain a retirement savings account in his name with any pension fund administrator of his choice. His pension contributions (both the employer and employee portions) are deducted by the employer and remitted directly to the Pension

Fund Custodian (PFC) for the employee's RSA to be managed by the Pension Fund Administrator (PFA).

Section 9(1) of the Act specifies the rate of contribution to the retirement savings account as minimum of 7.5% each for the employer and the employee in the case of the public service of the Federation and the FCT as well as the private sector. However, in the case of the military, the minimum rate of contribution is 12.5% by the employer and 2.5% by the employee.

In practical terms an employee on a minimum wage of N7,500 saves only N13,500 per year. In an economy where the value of the currency is declining all the time this savings is incapable of making any appreciable difference in the life of the pensioner.

Under section 4(1), withdrawals are programmed on a monthly or quarterly basis calculated on the basis of the expected life span of the pensioner. This provision effectively ensures that the pensioner continues to live at subsistence level and cannot use as he pleases funds that are called his own except as provided by the Act.

Section 11(8) of the PRA 2004 provides that government contribution to the pension of employees of the public service of the federation shall be a charge on the consolidated revenue fund of the federation. It seems to me that this provision is unconstitutional having regard to the provisions of section 80(2) of the Constitution to the effect that no moneys shall be withdrawn from the consolidated revenue fund of the federation except to meet expenditure that is charged upon the fund by the constitution or where the issue of those monies has been authorized by an appropriation act, supplementary appropriation act or an act passed in pursuance of section 81 of the constitution.

Let us now examine the provisions of sections 3 and 4 of the Act in relation to the following:

a) **<u>Pensionable Age:</u>**

The Pension Reform Act does not define pensionable age. Pensionable age simply means the number of years an employee has put in service to be entitled to pension. Nevertheless, in the light of the provisions of section

3 of the Act, a person may be said to have become pensionable on the happening of certain events which entitle him to avail himself of his retirement savings. Ordinarily, a person is said to be pensionable once he becomes eligible to retire from his employment either on account of age or on account of the number of years he has put into the service. It may also be said that once an employee starts contributing, he or she becomes potentially pensionable. Pension is defined as ‘a fixed sum paid regularly to a person (or to the person’s beneficiaries) especially by an employer as a retirement benefit.’ A Pensioner is defined as ‘a recipient or beneficiary of a pension plan’. In the light of the above, a person becomes pensionable when he becomes entitled to receive the benefits of a pension plan.

Because the Act provides that an employee cannot withdraw from his retirement savings account until he or she is 50 years of age, it may be said that that is when the employee becomes pensionable. This is subject to the exceptions provided under sections 3(2) and 4. That is, ill health, permanent disability, and as provided by the condition of service under which the employer is employed. Unless these conditions are met an employee cannot avail himself or herself of his or her pension until he or she attains 50 years of age.

On attaining the age of 50, the employer is entitled to withdraw from the funds monthly. The Act specifies that the pensioner should withdraw at least 50% of his or her last pay as monthly programmed withdrawal amount.

b) <u>Voluntary Retirement</u>

This is when an employee on his/her own, resigns from his/her employment. This could be for personal reasons or on medical grounds. When that happens, the employee, who is a contributor under the Pensions Reform Act, is not entitled to withdraw from the scheme except in cases of retirement due to medical condition or permanent disability as stipulated by Section 3(2)(a) & (b) of the Act. This is because of the provisions of section 3(1) of the Act to the effect that no person is entitled to make any withdrawal from his or her retirement savings account before attaining the age of 50 years.

c) Forced Resignation

This happens when an employee is requested, for whatever reason, by his employers to resign or retire. This could be on health grounds, gross misconduct, redundancy or retirement in the public interest – an expression which came into vogue with the promulgation of Decree No 17 of 1984. Whatever is the case, an employee is entitled to his savings. The act proceeds on the assumption that unless the lives of pensioners are managed for them after retirement they may become a burden on the public. The concern seems to be, not so much for the pensioner as for the general public. Employees should be trusted to manage their own affairs after retirement. The law cannot take over and manage the lives of retirees any better than it can take over and manage the lives of infants. The pension scheme as conceived can only guarantee that pensioners live a meagre or impoverished life.

d) Early Resignation

Under the public service rules, an employee's retirement is determined by his natural age which is 60 years (65 years in the case of academic staff of Universities) or when he has put in 35 years of service. Early resignation therefore means disengaging from the service before the attainment of 60 years or 35 years. But the employee can decide to disengage from service before he attains any of the stated age or length of service. When he does that, he is not entitled to start drawing from the pension fund unless certain conditions are met – provisions which ensure that whatever he can get can only barely sustain him if at all. See section 3(1).

It ought not to be so. At a time when it has become obvious that the public service is over-bloated and should be reduced, public servants should be given every encouragement to leave the service and occupy themselves more profitably in the private sector. The pension scheme should be so conceived as to be attractive to pensioners not by encouraging them to live an idle life but by making them more useful members of society. If the scheme as presently conceived has failed to achieve its objective, one solution might be to allow employees to remain in the public service or in their various employments for as long as they are physically and mentally healthy enough to serve.

THE PROVISION OF SECTION 5 OF THE PENSION REFORMS ACT VIS-A-VIS THE LAWS OF TESTATE AND INTESTATE SUCCESSION

Section 5 of the PRA 2004 in effect divests the Administrator General of the powers vested in him by law over the estates of deceased persons. This cannot be since the real and personal estate of a deceased person falls outside the scope of the Pensions Reform Act. The control and administration of the estate of a deceased person is governed by the administration of estates law of the respective states of the federation. Once a man or woman dies his or her property devolves on the executors of his will or the administrator general of the state. It is no longer regulated or governed by the Insurance Act which is a federal legislation. Section 5 of the Pensions Reform Act is unconstitutional in that it is a clear federal legislation outside the exclusive and concurrent legislative lists. It is a matter under the residual list and only the states can legislate on it. In this regard, the applicable law is the Administration of Estates Law which empowers the Administrator General (not the Pensions Fund Administrator) to administer the estate of the deceased.

However, section 9(3) of the Pension Reform Act, provides as follows:

> 9(3)-In addition to the rates specified in sub-section (1) of this section, employers shall maintain life insurance policy in favour of the employee for a minimum of three times the annual total emolument of the employee.

Section 5 of the PRA 2004 then goes on to provide that in the event of death the entitlements of an employee under the life insurance policy shall be paid into his or her retirement savings account. The section provides as follows:

> “(1) Where an employee dies, his entitlements under the life insurance policy maintained under subsection (3) of section 9 of this Act shall be paid to his retirement savings account.
>
> (2) The pension fund administrator shall apply the amount paid under subsection (1) of this section in accordance with section 4 of this Act in favour of the beneficiary under a will or the spouse and children of the deceased or in the absence of a wife and child, to the recorded next-of-kin or any person designated by him during his life time or in the

absence of such designation, to any person appointed by the Probate Registry as the administrator of the estate of the deceased.

It might seem, on the face of it that since the insurance policy was obtained by the employer under the provisions of the Act, the Act should have a say in the disbursement of the proceeds of the policy on the death of the employer. We observed earlier that the Act approaches pensioners and employees as if they were infants and seeks to regulate virtually every aspect of their lives. Here is an attempt to continue to rule them even when they are dead. The Act does not appear to distinguish between those employees who have died intestate and those who have left a will. Furthermore, the manner of distribution of the proceeds of the policy leaves much room for confusion.

Thus, in the event that the spouse and children are not the beneficiaries under the will of the deceased, that is a clear indication that the deceased intended to disinherit them. On the other hand if they are the beneficiaries under a will, then they take under the will and not under the Act. Yet again, if the payment is made to a recorded next of kin or a person designated by the deceased during his lifetime then such a person takes by virtue of such designation and not by virtue of the provisions of the Act. Assuming, however, that the employer has died intestate, succession to his estate ought to be governed by the laws of succession in his place of domicile. These laws include Customary and Sharia laws of succession.

The Act does not reckon with the fact that an employee who has left a will might well have willed that the proceeds of the policy be paid to a person other than the spouse or recorded next of kin.

ADEQUACY OF SANCTIONS REGIME UNDER THE PRA 2004

Concerning the failure of the Pension Administrator or Custodian to obtain licence before operation, Section 48 provides the following sanction:

> Any person who contravenes the provisions of sections 44 and 46 of this Act commits an offence and shall be liable on conviction
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> (a) in the case of an individual, to a fine of not less than N5,000,000 or imprisonment for a term not exceeding 5 years or to both such fine and imprisonment; or

(b) in the case of a corporate body, to a fine of not less than NI0,000, 000 and in addition, the directors or officers shall each be liable for a fine not less than N2,000,000 each or a term of imprisonment not less than 5 years or to both such fine and imprisonment

Section 54 provides that the Commission shall revoke the licence of any pension Administrator or custodian who discloses false information of material particulars, whose affairs do not conform with the provisions of the PRA; who is in danger of being wound up or dissolved; who becomes ineligible to manage the pensions fund; or is in breach of the conditions attached to its licence. Such revocation shall be published in the Federal Gazette.

The Pensions Administrators or Custodians are under obligation to engage external auditors to audit their account and report same to the Commission. Where they fail to do so they shall be sanctioned in accordance with Section 58(3) of the act which provides as follows:

58(3) Any auditor of a pension fund administrator or custodian who acts in contravention of or fails deliberately or negligently to comply 'with any of the provisions of subsection (1) of this section commits an offence and is liable on conviction to a fine of not less than N10,000,000 for the firm or imprisonment of a term not less than 3 years for the responsible partner or principal officer or to both such fine and imprisonment.

For failure to comply with the provisions of sections 61, 62, and 63, dealing with returns on fraud and forgery; notification of dismissal of staff for fraud and prohibition on employment of a staff dismissed for fraud respectively, section 64 prescribes the penalty as follows:

64.-(I) Any pension fund administrator or custodian who fails to comply with any of the provisions of sections 61, 62 and 63 of this Act shall pay a penalty of an amount not less than N1,000,000 to the Commission for every violation.

(2) In addition to the penalty specified in subsection (1) of this section, the Commission may revoke the licence of the pension fund administrator or the custodian, in the case of persistent contravention of any of the sections referred to in subsection (I) of this section.

Section 78 provides for penalty for failure to comply with the provisions of the Act as follows:

> “Any pension fund administrator who fails to comply with any provision of this Act shall be liable to a penalty of an amount to be determined by the Commission but in any case shall not be more than N500,000 for each day that the non-compliance continues and the pension fund administrator shall forfeit the profit from that investment to the beneficiaries of the retirement savings accounts and if the investment has led to a loss, the pension fund administrator shall be made to make up for the loss.

Sections 85 to 90 of the PRA 2004 provide for general sanctions for offences committed under the Act. The sections stipulate various amounts as fine for individual or corporate offenders and/or terms of imprisonment as the case may be where no specific penalty is stipulated elsewhere in the Act.

The fundamental essence of criminal law is that laws are violated at the risk of sanctions or punishment. Such punishment must be sufficient deterrent against the repeat of such crimes by the offender or other members of the public. Therefore the gravity of the punishment must bear a corresponding weight on the danger posed to society by that offence. Pension matters are serious and weighty in that they touch on life-long investments and savings which explain why the Pensions Reform Act distinguishes between those who administer the fund and those who keep custody of it.

However, in society such as ours, ridden with touts and impostors, the tendency is for many unlicensed persons to engage in this business for ulterior motives, seeing that huge sums of money belonging to individuals who are often helpless and unsuspecting will be entrusted to them to misappropriate or steal at will.

There is therefore the need to review the fine and terms of imprisonment in such a way that the punishment would fit the crime. Thus, where there is an element of breach of trust in the offence created by the PRA 2004, the punishment of criminal breach of trust in the Penal Code could be adopted, which is fourteen years imprisonment. It is accordingly suggested that the punishment for an unlicensed pension funds administrator or custodian under section 48 of the Act should not be less than fourteen years imprisonment without option of fine since such offenders are very likely to have stolen not just enough for themselves but in the hope that they can use some of their loot to pay fines and, if possible bribe their prosecutors.

RECOVERY OF DEBTS UNDER THE PRA 2004

One of the safeguards to the Contributory Pension Scheme introduced by the PRA 2004 is the insulation of pension fund assets from loan recovery processes. Section 76(1)(c) of the Act provides inter alia that the Pension Fund Administrator shall not apply pension fund assets by way of loans and credits or as collateral for any loan taken by any persons.

By virtue of this provision, Pension Fund Administrators cannot oblige any request by any employer or financial institution to deduct loan repayments or recover loans taken by a contributor against the balance of his RSA.

While this provision is laudable, it has narrowed the opportunity of contributors from accessing credits and loans from employers and financial institutions which hitherto extend such facilities against the terminal benefits of an employee. In the circumstances, it will be beneficial to the contributor if the window could be reopened in a guided manner such that he could still access credit facilities for which repayment could continue even after retirement.

TAX ISSUES UNDER THE CONTRIBUTORY PENSION SCHEME

There are several issues that have arisen in the implementation of the PRA 2004 with regards to the taxation of pension assets and investment income under the new Contributory Pension Scheme. These issues include the treatment of income and/or withholding taxes on pension assets and investment income as well as the application of Value Added Tax (VAT) on services provided to the pension fund.

Section 7(1) of PRA 2004 exempts any amount payable as retirement benefits from tax. Also, Section 10 of the PRA 2004 provides that the contribution under the scheme shall form part of tax deductible expense in the computation of tax payable by both the employer and employee. The PRA 2004 however, is silent on the tax status of investment income in the process of managing contributions that would later become retirement benefits.

It is hereby submitted that no Income Tax should be charged on the income of all pension fund assets. Furthermore, no Withholding Tax should be charged on interest, rental, dividend and other income of pension funds.

Services provided to pension funds are "services provided for consideration". By virtue of Section 5 of the Value Added Tax (VAT) Act 1993, such services are subject to VAT. Thus, services such as management/administration and custody services for which PFAs and PFCs charge fees as well as audit and other services provided to pension funds by approved external parties are subject to VAT under the present tax structure.

In view of the attachment of such services to pensions however, a case could be made for their exemption from tax. For instance, amongst the services exempted from VAT are medical services and services provided by Community Banks, Peoples Bank and Mortgage institutions (1st Schedule, Part 2 of the VAT Act 1993). The underlying rationale of the law is that these are essential services from which the government wants the citizens to enjoy maximum benefits. The same reasoning can therefore be extended to pension fund management, administration and custody, which aim at promoting the welfare of the workers.