PUBLIC SECTOR PENSION REFORM IN NIGERIA: A HISTORICAL PERSPECTIVE.

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ABSTRACT
The paper examines the public sector pension reform in Nigeria. Dressed in a historical form it traces the origin of pension in Nigeria, which dates back to the Colonial Nigeria. In particular, the paper unveils the roots of the crisis which made reform inevitable. Also an x-ray of the 2004 pension reform features was undertaken with a highlight of their strength and weaknesses and what could be done to remedy obvious fault lines.

Key Words: pension, contributory pension; pay-as-you-go; funded pension; programmed withdrawal; annuity.

Introduction
Systems providing pension for the public sector workers in both advanced and developing countries for sometimes now have been problematic for government and tax payers (Heubeck, 1999; Lindsay, 2009 and Okpugie, 2011). This has, in particular, laid the foundation for a global call for a review of the funding model in the public sector, traditionally, provided on pay-as-you-go basis (Hemming, 1998).

In the recent time, in Nigeria, public sector pension matters showed up in the public domain, through the mass media, with some negative imports: huge pension arrears, discovery of fictitious pensioners and discrepancies between pension appropriations and the actual amounts released (Oloja, 2010). These are indices of a system in crisis.

Government responded to the crisis by changing the funding modality, in keeping with global trend, from the pay-as-you-go to the contributory funded pension through the passage of the Pension Reforms Act of 2004. This article undertakes a study of the public sector pension in Nigeria, from inception till date, with a view to unveiling the root of the pre-reform management crisis. The paper also reflects on the new contributory pension scheme with highlights of its strength and weaknesses.

The historical development of public pension is reviewed in part I. Part II reviews important pension laws and regulations. Part III undertakes itemization of factors that are perceived to have created the crisis in the public pension sector. Part IV examines the new pension system and its prospects for success. Part V concludes the article.

Part I: Historical development of public sector pension schemes
British incursion into West Africa has affected the political, social and economic life of her former colonies (Stride and Ifeka, 1971). Nigeria, being a former colony of Britain, received a pension tradition into her public sector that is entirely modeled after the British Structure (Oluoma,
According to Uzoma (1993) the Nigeria civil service was a brainchild of the colonial administration and the colonial office handed over to Nigeria what may be called a “Model Pension Legislation”. Actually, the commencement of pension scheme for the Native Administration servants/staff (as public servants were then called) dates back to 1946, when the Colonial Government in Nigeria, through the Chief Secretary to the Government (in a circular No 19/1945 of 24th march, 1945) announced a superannuating (pension) scheme for African staff employed by Government (Public Notice No 4, 1946). The appropriate legal enactment that brought the scheme into being was the Pensions Ordinance of 1951 but which took retroactive effect from 1946 (Ogunshola 1984 as quoted in Oluoma, 1986).

The said Pension Ordinance of 1946 contained vital information about the public sector pension scheme ranging from the identification of who a Native Administration Servant is, the nature of benefits (pensions and gratuity) and eligibility conditions; the minimum annual salaries that qualify for either pension and gratuity or gratuity alone; the rules for the condonation of service, to rules on misconduct leading to a reduction in or outright forfeiture of benefits entitlements.

Similarly, staff of government corporations and parastatals were to enjoy pension schemes and other similar benefits as the core public service schemes (Oluoma, 1986), but differed only on funding modalities. The corporations included, Railway Corporation, National Electricity Commission (now Power Holding Company of Nigeria), and the Nigerian Ports Authority. They run non-contributory funded schemes with some rates at 2.5% of the employees’ salary (Uzoma, 1993). It is important to note that the schemes of these corporations must first be approved by the Joint Tax Board as being comparable with the benefit structure of the core civil service scheme. Other appropriate public sector pension legislations, together with relevant circulars have since followed (we look into this issue at a later level) after the Act of 1946.

As will be demonstrated later, the public sector, as an employer of Labour, has grown in size and its pension bill as a percentage of the Gross Domestic Product (GDP) has also risen significantly (Anyafo, 2000). The unchecked/unconstrained growth in the public sector employment and the attendant heavy pension burden is not unconnected with the nation’s lack of clear policy on employment which is often pursued to achieve ethnic balancing. It seems demand for benefit increases have been met without harmonizing adequacy with affordability (Okafor, 2000). Nigerian scheme, in some quarters, was once believed to be the most generous scheme in the world (Ogunsola, 1984). In fact it was speculated that had the Government not reformed the system, pension obligations might exceed salary of current workers in few years (Legal Brief Africa, 2004). Over the years therefore government had accumulated huge debts of pension and gratuity that peaked at N2trillion in 2004 (Legal Brief Africa, 2004). Pension arrears therefore became a blackmail from which government seeks an escape. Until the Pension Reforms Act.2004, government had reacted, rather, uncaringly to the problem. It had employed, even before current public service reform programme, a gradual downsizing of the public sector by way of retrenchment, compulsory retirement and natural old-age disengagement in the public sector (Anyafo, 2000). And these measures were taken without provisions in the budget to contain the economic consequences of such steps.

**Part II Legislative impact on pension debt growth.**

Anyafo (2000) pointed out that 1963, 1979 and 1999 Constitution of the Federal Republic of Nigeria guarantees protection of pension rights in the public services of the Federation and State. In particular, section (159) (1) (2) of 1979 constitution provides that,

> The right of a person in the public service of the Federation to receive pension or gratuity shall be regulated by law; any benefit to which a person is entitled in accordance with or under such law as referred to in subsection (1) of this section shall not be withheld or altered to his disadvantage.
except to such extent as is permissible under any law, including the code of conduct. The same constitutional provisions apply to the state public service staff as may be seen in section 190 (1) (2) of the 1979 constitution.

Two important issues emerge. The first is that pensions for both public and private sector workers are a constitutional right to be defended by organized labour. This is particularly enlightening in an era where politicians are known to display shocking perfidy in handling issues concerning public servants.

Secondly, the constitution provides that laws regulating pension should be enacted. This second point is the focus of attention under this portion of the work with particular emphasis on how these laws and regulations have impacted on the scale and size of pension benefits in the public sector.

Section 3 of the 1951 pension Ordinance provides as follows:-

Native Administration servants who retire, in circumstances, which qualify pensionable government servants for pension, from posts with salaries or maximum salaries of fifty pounds (£50) per annum or over will be eligible for retiring allowances (pension) not exceeding the annual pensions for which they would have been eligible under the laws in force applicable to pensionable government servants.

Section 4 reads:

Native Administration servants who retire in similar qualifying circumstances from posts with salaries or maximum salaries of less than fifty pounds (£50) per annum will be eligible for gratuities on a basis of 1/20th of a month’s pay for each month of continuous service.

Since Independence 1960, several laws that amended the first legislation have been made. In 1979 a new law on pension, which repealed all other legislations, came into being (Uzoma, 1993). This Law called “Pensions Decree 102 of 1979” remained the Law on pension in Nigeria until the Pension Reform Act, 2004.

Prior to the enactment of Decree 102 of 1979, Government had realized the need to shield pension receipts from inflation (Uzoma, 1993). Thus, paragraph 111 of the government’s White Paper on the report of the Udoji Public Service Review Commission of 1974, states that, “Provisions should be made whereby retirement benefits could be automatically adjusted in line with rising cost of living and that the proposed arrangements for periodically reviewing remunerations would apply mutatis, mutandis, to pensions”.

The latest pension law in Nigeria is the Pension Reform Act, 2004. Its birth arose from the urgent need to address the perceived and obvious inadequacies of the former pension regime that depended on the budgetary allocation to cater for pension debts. The new pension scheme represents a paradigm shift. In the old regime, responsibility for providing fund for pension payment rested solely on government or its agencies. In the new regime, government and Labour co-operate in the form of a shared partnership to accumulate pension assets in advance to accommodate emerging pension liabilities (Odo, 2007). Details of the new Pension Act are taken up in part IV.

Part III: Factors responsible for the crisis in the public sector pension system.
A number of factors are believed to be at the root of the pension problems (Odo and Igbeka, 2011). They are briefly looked into below.

(a) The funding modality
Civil servants, prior to Pension Reform Act of 2004, bore no direct responsibility, by way of payroll tax, for the provision of pension; instead pension benefits were paid through budgetary allocations to be kept in the Consolidated Revenue Fund (Okafor, 2000). Budgets are estimates of revenues and expenditures for the fiscal years concerned. It is entirely possible that the amount released may fall short of the actual appropriation for pension payment. For instance, in fiscal year 2001, ₦6.4b was needed for payment of military pensions but only ₦2.1b was released for Defence, leaving a balance of ₦4.3b pension arrears (Onuorah, 2002). This fund’s inadequacy is what is being tackled by the contributory pension scheme.

(b) Political control of the public sector pension
Both Davis (1993) and Diamond (1995) argue that social security pensions provided on the basis of pay-as-you-go are subject to political risks. The risks contemplated take three forms. The first relates to the tendency of politicians, eager to capture the votes of the electorate, to offer fabulous pension increases that they are either not going to pay or which may fall on regimes other than theirs. The second aspect of the risk refers to the fact that the pension account, in not being distanced from political control, falls easy prey to politicians who dip hands into pension funds to cushion up temporary fiscal shocks. The third relates to the socio-political indifference to the plight of pensioners by politicians.

(c) Pension payment default by state governments
Furthermore, it is also claimed that pension debts in the public sector mount, in part, because of the failure of some state governments to provide their counterpart funds necessary to make up the amount provided by the federal government, in situations where the affected pensioners worked for both federal and state governments. As a rule, further release of money by the Federal Government to the State government can only happen on proven evidence that pension for the previous month has been settled. This seems to explain why a state would fail to collect federal government counterpart funds, for months, because the States affected could show no evidence of being up to date in payment of pensions.

(d) Pension record and disbursement flaws
Both the way a record of pensioners in the public sector is kept and the procedure for payment of pension create avoidable problems. In some establishments no accurate record of actual pensioners exists. Corruption breeds more in the absence of facts and figures. This claim was dramatized in bold relief when verification of military pension account led to the discovery of 23,000 fake pensioners on the Army pension roll (Uwujaren, 2004). This account agrees largely with Uzoma (1993) who once disclosed that pension costs in the public sector were inflated through insertion of fictitious names on the list of pensioners.

(e) Tardiness in pension disbursement
Another weakness found in the public sector system concerns the less than dignifying manner with which the senior citizens are treated. One observes how weak and frail-looking elderly citizens are compulsorily required to travel long distances to the point of pension payment. Worse still, they are left, under inclement weather for long hours and sometimes for days, before collecting their stipends. Some pensioners were claimed to have died while standing in a queue waiting to receive pension money (Ovuorie, 1998). This shows poverty of ideas or unwillingness to deploy ideas in the way pension payment should be handled. However, the implementation of the new pension law may yet take care of these flaws.

Part IV: The funded pension system in Nigeria: prospects and pitfalls: a preamble
Funded pension system otherwise called “the defined contribution system” is a method of providing retirement income whereby current pensions are financed by previous savings secured through periodic contributions made by either the worker or the employer (for non contributory schemes) or jointly by worker and employer
(contributory schemes) (Mumy, 1978). This approach anticipates pension debts and makes concrete plan to accumulate assets to defray them when they fall due.

In contributory variant of the schemes, workers are allowed a say in providing their retirement incomes. Chile, in 1981, blazed a trail by terminating the old pay–as–you–go system and switched all its affiliates to a new system funded through periodic contributions (Quisser, 1999).

Under this arrangement each worker elects a fund management administrator with whom he/she maintains an individual account to which contributions are channeled. The pension, for each worker, becomes the sum of the accumulated contributions and the accrued investment incomes. Several other countries after Chile have since followed suit. Nigeria, for instance, through the Pension Reform Act of 2004, patterned her public pension SYSTEM after the Chilean model.

Contributory pension system in Nigeria: features and safeguards.

There are certain features and safeguards that position the scheme with success chances. First we discuss the features.

Features
(a) Individual retirement savings account.
Section 8(1) of the Act provides that every employee shall open and maintain an account in his name with any pension fund administrator of his choice. This account belongs to the employee through life whether he changes job or otherwise. This is the account that receives the monthly contributions from the employee and his employer. This fund is to be invested in such prescribed investment outlets.

For security reasons, pension fund’s administrators are allowed to invest 75% of fund assets in federal government backed securities while the balance of 25% assets may be invested in publicly quoted companies.

(b) Pension fund administrators (PFAs)
The Act provides for the licensing of PFAs whose duty is to open retirement savings account for employees, invest and manage the funds in fixed income securities and other instruments as may be determined by the Regulatory Agency, National Pension Commission (NPC).

(c) Pension assets custodians (PACs)
The law also provides for the licensing of PACs to keep all pension fund Assets. That is, all monthly contributions on behalf of each employee are sent to a Pension Asset Custodian who, upon receipt of such contributions, duly instructs the PFA to credit the account of the employee(s) concerned with the total contributions thus remitted. Evidently, the person who keeps the assets (PAC) is different from the person who carries out the investment (PFA). The custodian will execute transactions and undertake activities relating to the administration of pension fund investments upon instructions by the PFA. (Fed. Min. of Information and National Orientation, 2006)

In view of the large amount of assets to be handled, the licensed Pension Fund Custodian, being a limited liability company, and a licensed financial institution, must have a minimum capital base of N5, 000,000,000.

(d) The National Pension Commission (NPC).
To ensure effective administration of pension matters in Nigeria, the Act established a regulatory agency, (NPC) to regulate and supervise the scheme. The commission is to make certain that payment and remittance of contributions are made and retirees are paid when due. Furthermore, the agency will ensure safety of funds by issuing guidelines for licensing, approving, regulating and keeping a tab on the investment behaviour of PFAs. It is the watch dog of the scheme who must act in the interest of all stake holders.

(e) Transition gap: the retirement benefit bond redemption fund
To switch from the pay–as–you–go to the new scheme creates a financing gap for workers who have earned pension rights under the old scheme. The retirement benefit bonds are to be issued to
workers concerned, the value of which will be equal to the accrued pension benefits up till that commencement of the funded scheme. The bonds are redeemable at the retirement date for each worker as appropriate.

The law provides that a fund known as the Retirement Benefits Bond Redemption fund be established and maintained by the Central Bank of Nigeria (CBN). FGN pays 5% of its total monthly wage bill in the public service of the Federation and Federal Capital Territory into the fund to retire any retirement benefit bond issued. The fund shall cease to exist after all affiliates in the old scheme have had their bonds redeemed.

1.2.3. Scheme safeguards

The new pension scheme enjoys some safeguards likely to improve its viability, all things being equal. We mention them briefly.

(a) Separation of PFA and PAC.
The roles of these entities are clearly described and are never intended to overlap at any point. For instance at no time will the PFA have the custody of contributions of the employee, neither will the Custodian invest the assets in his care except to the order of the PFA.

(b) Pension Assets Custodian Guarantee
In recognition of the huge assets it is expected to handle, a Custodian shall issue a guarantee to the full sum and value of the pension fund and assets held by it or to be held by it.

(c) Government Pension Contribution
Government contribution shall be a first charge on the Consolidated Revenue Fund of the Federation.

(d) Risk Rating Institutions
The National Pension Commission requires that credible risk–rating institutions that have the professional capacity, be involved in assessing the risk profile of the investment channels that PFAs contemplate. Investment of fund’s assets readily brings to focus the important role of SEC and NSE in ensuring security of pension fund’s assets. This requires stricter regulation of companies that access the stock market.

Compliance Office.
The PFA shall employ Compliance Officer who will be held accountable for ensuring compliance with the law in regard to pension matters. He is required to liaise with the NPC and the Board of Directors with respect to the PFA. There are other Safeguards that have not been cited. These five suffice us for now.

1.3 Assessments of the Scheme Implementation: Success and Failure

Sparse data have been accumulated in the life of the new scheme having begun in June 2004.

It has been observed that some employers, including government agencies, have not been faithful in remitting contributions to the Pension Custodians. Public sector records the highest rate of remittance default (Iyatse, 2011). He also revealed that some government departments never remitted deducted amounts. Furthermore, “hanging funds” have become an issue. These refer to contributions sent to various custodians without clear schedule, showing workers’ identification, including PIN. Hanging funds do also arise in situations where employers, for workers who change jobs, fail to notify custodians accordingly.

Eke (2008) observed that already the first set of beneficiaries on the scheme have emerged. These were workers who either were exempted from the new pension on the basis of age to retirement or those who joined the scheme in 2004 but worked for three years and few months before retirement (Takor, 2008:29). According to Eke (2008) an estimated number of 5000 beneficiaries, mainly public servants, were due for payment of their benefits through their various pension fund Administrators. It was revealed further that the federal government, having anticipated this upsurge, had issued over N56 billion to contain the debt obligation under the scheme.

However, five major concerns to the retirees appear to have arisen in the management of the scheme. The first relates to the issue of whether the total balance standing to their credit should be withdrawn or a part of it. The issue involved here
is clearly stipulated in the Act and should be resolved following the provisions of the law (see sec.4 (1) (c)). The second cause of worry relates to what retirees regard as the reticence on the part of fund administrators to disclose benefit options namely, programmed withdrawals and annuity path with their individual merits (Okpugie, 2011). They complained that rather than tell them of annuity option, fund administrators urged them to use only gradual withdrawal option that soon got exhausted, thus leaving them without pension. The third issue focuses on the deficiency of the programmed withdrawal window. It was pointed out that this payment option offers a constant amount throughout without recognition of interest additions on the periodic balances (Iyatse, 2011). This was considered as being unfair. Fifth and finally, the failure of NPC to compel PFAs to disclose their mortality rates and interest rates assumptions in converting RSA account balances at retirement into a monthly or quarterly benefit streams. This has been criticized as lacking in transparency and would lead to an absurd situation where two equal balances result in different withdrawal outcomes ( Odulana, 2007).

As could be seen there exist few imperfections with the new scheme. But these have nothing to do with availability of funds at retirement. This is clearly a departure from the past which was characterized by scarcity of funds.

Part V: Conclusions and recommendations

On a general note, it is observed that for the first time in Nigeria, employers and employees are compelled by law to provide money intended to pay pension entitlement at retirement. This marks a departure from the past where no such provisions were made, rather payment of pension depended on budgetary allocations which were hardly adequate.

Some of the features of the new pension system that inspire confidence include, the separation of custodianship of pension fund assets from their investment, the inclusion of all stakeholders in the composition of the Regulatory Agency, NPC, the immediate establishment of Retirement Benefits Bond Redemption Fund housed within the Central Bank of Nigeria to pay pension debts from the defunct pension regime, the reporting requirement for PFAs (to encourage transparency), the prescription and setting of rules for the investment of fund’s assets and the insertion of minimum pension guarantee, among others. These features, if implemented, provide a foundation for a regime of pension system in public sector that fixes the weakness of the old order. This can only happen if the following grey areas are acknowledged and tackled in time.

(a) On Compliance: The issue involved here takes two forms, namely compliance with regard to Government’s (or its agency) deduction and remittance of same to the Pension Assets Custodian and the issue of compliance with respect to the rules guiding the operation of PFAs. The law expects that the deductions for both worker and employer be effected simultaneously at the time worker’s salary is being paid on monthly basis. However compliance with respect to sanction for defaulters should be implemented.

On the second leg of compliance, section 68(a) (b) (c) (d) provides that every pension fund administrator shall employ a compliance officer who shall ensure compliance with the provisions of the Act and any other rules and regulations made there under and the internal rules and regulations made by the pension fund administrator. He is expected to liaise with NPC in carrying out his functions. It is suggested the NPC should both employ and pay the compliance officer. This encourages transparency in the process. To further strengthen monitoring of compliance at company or ministry level it is suggested that labour should appoint a liaison who forms an important interface between employer, PFA and NPC. He should be able to report issues like hanging funds.

(b) On the integrity status of Quoted companies on the Nigerian stock Exchange Market: It is the statutory function of both the Securities and Exchange Commission (SEC) and the Nigerian Stock Exchange (NSE) to screen and certify companies that access the Nigerian Stock Market.
Failure to regulate as appropriate can diminish the expectations of stakeholders of the new pension scheme. This has happened elsewhere. For instance, in 2001, poor corporate governance led to the collapse of ENRON, an energy company based in U.S.A; following its collapse 5,600 jobs, US$2.1 billion in retirement savings and US$60 billion in market value were all sacrificed (Asein, 2007:20).

It is recommended that stricter regulation of the stock market in Nigeria is therefore a necessity more so because the market is likely to warehouse 25% of the pension fund assets.

Other forms of sharp practices are known to have played themselves out in Nigeria. For instance, the current bearish stance of the Nigeria capital market has been traced to several causal factors including divestment and repatriation of funds by foreign investors (Adegboye, 2009). He, however, argued that the manipulation of prices by capital market operators and lack of adequate supervisory oversight by regulators played a key role. Price manipulation led to unreasonable stock price appreciation that was out of alignment with firm fundamentals. Oluba (2009) pointed out that in some cases manipulation took the form of direct intervention whereby banks lent money to stockbrokers with the sole aim of buying their own shares. This was to sustain an upward pressure on the affected stock prices. This was what was believed to have thrown the banks’ balance sheets into disarray.

However, the persistent slide in price that has adversely affected investment in equity began with the release of the report of JP Morgan (J.P Morgan is a consulting firm that assessed the risk status of Nigerian banks) which claimed that more than 56% of Nigeria banks where over valued (Adigun, 2009). Reaction to the report began with expatriate withdrawal from the market and the subsequent loss of confidence by local investors as could be seen in rapid drop in share prices.

(c) On the impact of inflation and devaluation of pension assets.

The law provides that 75% of the pension fund assets are invested in Federal Government backed fixed income securities and instruments. The fund therefore is likely to bleed severely during inflation since a large chunk of its assets are to be invested in Government backed fixed income securities.

In the old pension regime pensioner’s income were made to appreciate along with raises in workers’ salary. The current system should therefore incorporate safety net that takes care of short falls in investment expectations. The need for this safety net for pensioners has become imperative in the face of the current global credit crunch and the unending bearish posture of the Nigerian stock market (Atedo, 2008).

References


