IMPLICATIONS OF THE NEW PENSION REFORM FOR SOCIAL SECURITY PLANNING IN THE LOCAL GOVERNMENT

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Abstract

Pension systems were introduced into the country by the colonial administrators. The first legislative document on pension in Nigeria was the 1951 Pension Ordinance. Equally, the last legislation on pension matters in the country is the Pension Reform Act 2004, which established a Contributory Pension Scheme and unified the administration and management of pension for both the Public and Private Sectors. It established for the first time, a single Regulator to oversee both public and private pension schemes in the country. The contributory pension scheme addresses the pension liability by stemming its further growth and provides a platform for addressing this liability. The scheme is contributory in the sense that both the employees and the employer contribute towards the retirement benefit of the employee. This paper seeks to examine and analyze the contents of the Pension Reform Act (PRA) 2004. It equally tries to analyze the implications of the Pension Reform Act (PRA) and its contributions towards the retirement social benefits of employees both in the Public and Private sector.

Key words: Pension, Retirement, Contributory Pension, Social security, Reform.

INTRODUCTION

Pension is a form of income that workers or their dependents receive after workers retire, become disabled or die. Pension plans benefit people who have had careers in private industry; in a nation’s armed forces or in national, state and local governments. Many individuals who benefit are self-employed or whose employers do not provide a pension plan establish their own pension plans (World Book Encyclopedia, 1999).

Put differently, pension schemes exist to provide post-retirement benefits to employees. Pension scheme was introduced into Nigeria during the Colonial era to provide old age income and security to British citizens working in the country upon retirement. Nigeria’s first ever legislative instrument on Pension matters was the Pension Ordinance of 1951, which had retrospective effect from 1st January, 1946. The National Provident Fund (NPF) Scheme established in 1961 was the first legislation enacted to address pension matters of Private Organisations. It was followed 18 years later by the Pension Act No. 102 of 1979, as well as the Armed Forces Pension Act No. 103 of the same year. The Police and other Government Agencies’ Pension Scheme were enacted under Pension Act No. 75 of 1987, followed by the Local Government Pension Edict which culminated into the establishment of the Local Government Staff Pension Board of 1987. In 1993 the National Social Insurance Trust Fund (NSITF) Scheme was established by Decree No. 73 of 1993 to replace the defunct NPF Scheme with effect from 1st July, 1994 to cater for employees in the private sector of the economy against loss of the employment income.

As identified earlier by Orewa and Adewumi (1983) Local government system also established pension schemes for their staff, with a separate board known as the Local Government Pension Board. It was established to take care of the local government staff that would have retired from 1st April, 1979.

The new Pension Reform Act 2004 up to year 2004 when the Pension Act was passed by the National Assembly the government operated an unfunded defined Benefits Scheme and the payment of retirement benefits was budgeted annually under the Pay-As-You-Go Benefit Scheme against the backdrop of an estimated N2 trillion deficit, arbitrary increase in salaries and pensions as well as poor administration. The Obasanjo administration initiated a Pension Reform in order to address and eliminate
problems associated with the Pension Scheme (Federal Ministry of Information and Communication, 2004). The problems associated with the unfunded defined benefit pension are as follows:

First, by 2004, the occupational pension industry in Nigeria found herself in desperate financial straits.

Secondly, the coverage ratio of Nigerian workers (workers covered by a formal pension) was a dismal 1.3% which pales in comparison to Cameroon and Mauritius with coverage ratio of 30% and 60% respectively (Legacy, 2005).

Thirdly, the covered federal and state civil service workers were owed by an estimated N2 trillion or 25% of the GDP of Nigeria as indicated by the publications of the Federal Ministry of Information and Communication (2004) and Legacy (2005). The reason that was advanced for this heavy debt was that the Federal Government operated an unfunded Defined Benefit Pension Scheme, on a “Pay-As-You-Go” basis.

The regulation of the various pension schemes was fragmented between separate government agencies. This led to weak and ineffective administration Pension administration in Nigeria. The effect of the above scenarios was to create long line of pensioners waiting to collect their entitlements and bankrupt scheme that did not address the contributor needs.

The essence of the paper is to examine the implications of the new pension reform for social security planning in the local government service. To achieve this objective, the first section of the paper examines conceptual issues. The second section discusses the epochal-historical development of pension scheme in Nigeria. The third section explores the problems and challenges associated with the old pension scheme and the goes on to highlight the essential features of the new pension scheme. The fourth section assesses the implications of the new pension reform for social security planning in the local government. The final paper concludes the paper and offers some useful suggestions.

CLARIFICATION OF CONCEPT

Pensions

Pension has been defined as a periodic income or annuity payment made at or after retirement to employee who has become eligible for benefits through age, earnings and service. Oxford Advanced Learner’s Dictionary defined pension as a sum of money paid regularly by a Government to people above a certain age and to widowed (Widow) or disabled people or by former employer or financial institution to retriwed people Micro Word Encarta Dictionary has two definitions of pension:

1. Retirement pay: a fixed amount of money paid regularly to somebody during retirement by the government, a former employer or insurance company.
2. Regular sum of money paid regularly as compensation for an injury sustained on a job, or as a reward for service. For example, to an ex-worker. (Amujiri, 2009:139-140).

According to Ozor (2006), pension consists of lump sum payment paid to an employee upon his disengagement from active service. According to him payment are usually in monthly installments. He further stated that pension plans may be contributory or non contributory; fixed or variable benefits; group or individual; insured or trustee; private or public, and single or multi-employer. In many advanced countries of the world, income from pension to an individual may be supplemented by social security benefits, which apply to all citizens of a citizen in such country whether or not they belong to the working class. However, since most citizens in such countries might have at one time or another, been workers, it would appear that social security benefits are co-terminus with the working class. It is different from gratuity. According to Ugwu (2006), there are four main classifications of pensions in Nigeria. These are:

1. **Retiring Pension**: This type of pension is usually granted to a worker who is permitted to retire after completing a fixed period of qualifying service usually practiced in Nigeria between 30-35 years.
2. **Compensatory pension**: This type of pension is granted to a worker whose permanent post is abolished and government is unable to provide him with suitable alternative employment.
3. **Superannuating Pension**: This type is given to worker who retires at the prescribed age limit of 60-65 respectively.
4. **Compassionate Allowance**: This occurs when pension is not admissible or allowed on account of a public servant's removal from service for misconduct, insolvency or incompetence or inefficiency (Amujiri, 2009:140).

Gratuity is a once and for all lump of money paid to an employee on retirement, upon death or retirement or on total incapacitation while at work. According to Nwajiagu (2007), in some cases, workers are only entitled to gratuity upon withdrawal of service, in others; they may be entitled to both gratuity and pension. But in all cases, a worker who qualified to receive pension is usually also entitled to the payment of gratuity. Even if he is indebted to the organization at the time of retirement, he is still qualified unless he was specifically dismissed without benefits based on misconduct.

Pension and gratuity plan for public servants in Nigeria states that public officer on completion of 35 years of unbroken service or 60/65 years of age for public servants and professors respectively which ever comes first, shall receive the maximum pension and gratuity for their respective grades and ranks. The calculation of these terminal benefits is guided at any point in time by a legal framework or law.

**METHODOLOGY**

The necessary information required to address the issues under discussion were sourced from secondary sources. Secondary data refers to information that is already amassed or collected by other people for different purposes and which the researchers find useful to their study. The relevance of secondary data is that they often exhibit degree of validity since they were not initially collected for the purpose of the research and not by the researcher himself/herself.

Secondary data include the census, the federal office of statistics, the World Bank, Seminar papers, internet materials, conference papers, newspapers, and magazines, academic journals, books and statistics or reports concerning specialized areas of social life. The main problem with the secondary data is that the way it was collected may not be exactly how the researcher would have preferred it. Thus, often there is the problem of making it amenable to a particular research purpose.

The technique of content analysis will be used to analyze and interpret the data generated for this study. The central goal of content analysis is to convert recorded raw information into data which can be treated in a scientific manner so that a body of knowledge may be built upon. The justification behind the use of this technique is that it allows researcher on areas where the researcher cannot have physical access to the respondents and thus, cannot by any other method.

**EVOLUTION OF RETIREMENT/PENSION LEGISLATIONS IN NIGERIA**

In the old Nigerian Pension System, only public sector employees were covered, by way of statutory compulsion. In the private sector, not all employers had pension schemes in place as there was no statutory demand on them to do so more often than not, those who had pension schemes in place related to lump sum payments at the verge of retirement, known as pay-off.

The first Public Sector Pension Scheme in Nigeria was the Pension Ordinance of 1951, with retroactive effect from January 1, 1946. The law allowed the Governor-General to grant pensions and gratuities in accordance with the regulations, which were reviewed from time to time with the approval of the Secretary of State for Colonial Affairs in the UK government. Vesting period was fixed at 10 years of service. Though pensions and gratuities were provided for in the legislation, they were not a right as they could be reduced or withheld altogether if it was established to the satisfaction of the Governor-General that, the officer was found guilty of negligence, irregularity or misconduct.

The pension scheme in the public sector has undergone various developmental stages after the first Pension Ordinance. For example, the civil service pension scheme was established by the Basic Pension Decree 102 of 1979, the Local Government Pension Scheme was established by Military Fiat in 1977 and the Armed Forces Pension Scheme created through Decree 103 of 1979 with retroactive effect from April 1974. There was also the Pensions Rights of Judges Decree NO.5 of 1985 as mended by

Governmental Parastatals and agencies directly funded by the Treasury had a unified pension scheme that was virtually managed by insurance companies and many were unable to honour their pension obligations. However, the pension schemes of the self funded agencies were better managed.

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 pension 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 Four Naira (N4) each on monthly basis. The scheme provided for only one-off lump sum benefits. The Nigeria Social Insurance Trust Fund (NSITF) was established by Decree No. 73 of 1993 to take over the NPF Scheme and provide enhanced pension scheme to private sector employees.

The first Pension Reform Act No 102 of 1979 was introduced before the Nigerian Second Republic by the Federal Government with effective date of 1st April 1974. The Act consolidated all enactment on pensions and gratuity scales devised for public officers by Udoji Public Service Review Commission 1974. The Pension Act 102 of 1979 was the basic pension laws from which other pension laws in public service of Nigeria have developed as follows: Nwanegbo (2007):

a) The Armed Forced Pension Act 103 of 1979
b) The Pension Right of Judges Act No. 5 of 1985

The pensions Act 103 of 1979 like its counterpart 102 of the same 1979 consolidated all enactment dealing with pension, disability benefits and gratuity scales devised for the armed forces, public service organizations established by decree in the Federal and edict in the state operated pension schemes similar to what obtains in the civil service. Local government system also established pension schemes for their staff, with a separate board known as the local government Pension Board. It was established to take care of the local government staff that has retired from 1st April 1979 (Orewa and Adewumi, 1983).

The New Pension Reform Act 2004 up to year 2004 when the Pension Act was passed by the National Assembly the government operated an unfunded defined Benefits Scheme and the payment of retirement benefits was budgeted annually under the Pay As You Go Benefits Scheme against the backdrop of an estimated N2 trillion deficit, arbitrary increase in salaries and pensions as well as poor administration. The Obasanjo administration initiated a Pension Reform in order to address and eliminate problems associated with the Pension Scheme (Federal Ministry of Information and Communication, 2004). The problems associated with the unfunded defined benefit pension are as follows:

First, by 2004, the occupational pension industry in Nigeria found herself in desperate financial straits.

Secondly, the coverage ratio of Nigerian workers (workers covered by a formal pension) was a dismal 1.3% which pales in comparison to Cameroon and Mauritius with coverage ratio of 30% and 6% respectively Legacy PFA, (2006).

Thirdly, the covered federal and state civil service workers were owed by an estimated N2 trillion or 25% of the GDP of Nigeria as indicated by the publications and Federal Ministry of Information and Communication (2004) and Legacy PFA (2005). The reason that was advanced for this heavy debt was that the Federal Government operated an unfunded Defined Benefit Pension Scheme, on a “Pay-As-You-Go” basis.

The regulation of the various pension schemes was fragmented between separate government agencies. This led to weak and ineffective administration Pension Administration in Nigeria. The effect of the above scenarios was to create long line of pensioners waiting to collect their entitlements and bankrupt scheme that did not address the contributor needs. The government clearly recognized the problem and met it head-on. A committee was established to restructure the entire pension sector in Nigeria. The committee after extensive study of pension schemes in operations worldwide selected the Chilean model of private contributory retirement accounts as the base model for the new proposed Defined contributory scheme.

After very extensive dialogue with the civil service, and the organized public sector and open sessions by members of the public the former president chief Olusegun Obasanjo signed the Pension
Reform Act into law after public president chief being passed by both houses of the parliament on June 25th 2004.

The principal aim of the Act was to empower the individual contributor whilst establishing uniform rules the govern pension management in Nigeria through an effective regulator.

CHALLENGES OF THE OLD PENSION SCHEMES

The need for pension reform was necessitated by the myriad of problems that plagued both the Defined Benefit arrangement - Pay-As-You-Go- (PAYG) in the public sector and other forms of pension systems like occupational schemes, mixture of funded and DB schemes that operated in the private sector.

One of the challenges of the public sector DB scheme lied in its dependence on budgetary provisions from various tiers of governments for funding.

The scheme became largely unsustainable due to lack of adequate and timely budgetary provisions. This was the reason for the soaring gap between pension fund obligations and revenues, which threatened not only economic stability but also crowded out necessary investments in education, health and infrastructure. This was exacerbated by various increases in salaries, which ultimately led to increase pensions and hence undue pressure on government fiscal responsibilities.

Pension Administration had been largely weak, inefficient and cumbersome due to poor staffing and equipping. This had more often than not led to poor record keeping at all pension offices throughout the country as a result of which many pensioners had to spend years before their retirement benefits were paid.

The exit phase was quite challenging where payment procedure was often very tedious, sometimes the pensioners had to wait for days and years, to collect their entitlements. Similarly, the reimbursement process for the split of pension and gratuity payments between Federal and State services and other agencies was very clumsy, untidy and sometimes fraught with bribery and corruption. There were undocumented cases where the reimbursing agency holds the recipient to ransom.

The private sector schemes were characterized by very low compliance ratio due to lack of effective regulation and supervision of the system. Most of these schemes were akin to Provident Fund Schemes, which did not provide for periodic benefits. Even at this, many private sector employees were not covered by any form of pension scheme.

FEATURES OF THE 2004 PENSION REFORM ACT
1. The act will cover all Federal, and civil service workers in Nigeria, al private sector employees employing more than 5 people are also mandated to register their employees under the scheme.
2. Individual Retirement Savings Account: This established private Retirement Saving Account (“RSA”) in the names of individual contributor not the employer, these are principle’s accounts where pension contribution will be made
3. Contributory: The act provide for contribution by the employee and a matching contribution by his/her employer to ensure a minimum contribution of 15% into the Retirement Saving Account (RSA)
4. Fully Funded: The act mandates that the employer must take good his portions of the employees’ contributions every month into the RSA. Hence pension contribution cannot be carried forward but must be settled in the month they all due. The funding element increases their security of the Pension on behalf of the contributors.
5. **Privately Managed**: The act stipulates that only professional fund managers, licensed and approved by the National Pension Commission ("PENCOM") are allowed to manage pension funds as Pension Fund Administration ("PFA"). The Act stipulate strict conditions and guidelines to be complied with to become PFAs.

6. **Separation of Custody of Assets**: The Act separates the functions of physical custody of pension assets from that of management of the RSA. The assets of the Pension Scheme are held in custody, in trust, for the benefit of the individual contributors by Pension Fund Custodians ("PEC"). The Act stipulates strict conditions and guidelines to be complied with to become PFCs.

7. **Strictly Supervised and Regulated**: The Act stipulate uniform rules guidelines for the supervision and regulation of the pension sector in Nigeria through one single regulator, backed up by an Act. Hence all previous laws in Nigeria have been rescinded. Where there are conflicts in the interpretation of pension laws in Nigeria the pension Reform Act 2004 will take precedence.

This whole scheme is being regulated and supervised by the National Pension Commission (PENCOM). The Commission will ensure that the payment and remittance of contributions are made and beneficiaries of retirement savings are paid when due.

Heneman and others (1980-150) defined pension as “providing income form retirement until death, based on the employee's years of work and direct pay” in other words, it is based on the year of service and last pay Beach (1975:20) in this own definition saw pension as “the basic retirement income benefits to those who have worked in employment for the required number of years”. To him, the old age pension programme is but a part of the comprehensive old age, survivors, disability and health insurance system. Pensions under a define benefit are usually tied to years of service earning. According to Armstrong (1977:36), “pension schemes are designed to provide employee’s security by currently building on right that will give a guaranteed income to the employee or his dependents on retirement or death. Pension is benefit enjoyed by a servant who retired from service after serving for not after serving for not less than ten years for the old scheme and five years for the new. For gratuity, he must have attained the age of forty-five (45) years and fifty (50) years for pension, in the old and new schemes. It could also, be deferred payment of the income earned by the employee in the public service.

In Nigeria, the first public sector pension scheme was the pension ordinance of 1951, with retroactive effect from January 1, 1946. The law provided public servants with both pension and 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 were reduced from 10 years to 5 years and from 15 years to 10 years respectively.

In 1979, parastatals 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 Service of the Federation. Each BOT was free to decide on whether to maintain an insured scheme or self-administered arrangement.

On the other hand, the first private sector pension scheme in Nigeria was set up for the employees of the Nigerian Breweries in 1954; this was followed by the 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 saving scheme, where both employee and employer would contribute a sum of four naira (#4) each on monthly basis. The scheme provided for only one-off lump sum benefits. The Nigerian Social Insurance Trust Fund (NSITF) was established by Decree No. 73 of 1993 to provide enhanced social protection to 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 commence operations and assumed duty respectively. There were three regulators in the pension industry prior to the enactment of the Pension Reform Act 2004; namely Security and Exchange Commission (SEC), National Insurance Commission (NAICOM) and joint the Joint Tax Board (JTB). SEC licensed pension fund managers while NAICOM is still the agency responsible for licensing and regulating insurance companies in the country. The JTB approved and monitored all private pension schemes with enabling powers from schedule 3 of the Personal Income Tax Decree 104 of 1993.
The Pension Reform Act 2004 is the most recent legislation of the Federal Government at reforming the pension system in the country. It established a uniform pension system for both the public and private sectors. Similarly, for the first time in the history of the country, a single authority has been established to regulate all pension matters in the country.

**IMPLICATIONS OF THE NEW PENSION REFORM FOR SOCIAL SECURITY PLANNING IN THE LOCAL GOVERNMENT**

Social security is a government programme that helps workers and retired workers and their families achieve a degree of economic security. Social security also called social insurance provides cash payments to help replace income lost as a result of retirement, unemployment, disability, or deaths. The programme also helps pay the cost of medical care for people age 65 or older and for disabled workers. For example, about one sixth of the people in the United States received social security benefits.

Social security differs from public assistance. Social security pays benefits to individuals and their families largely on the basis of work histories. Public assistance or welfare, aids the needy regardless of their work records.

All industrialized countries as well as many developing nations have a social security system, Nigerian government has bought the idea and encouraged workers at all levels to subscribe to the newly adopted reform pension programme as a hedge against loss of income as a result of retirement, unemployment, disability or death. To this end, this nascent programme has achieved a total registration of about 2.6 million Nigerians who have opened (Retirement Savings Account; RSA) as at September 17, 2007 (Ahmad, 2007). The breakdown is as follows:

- 68% are from the public sector, of which
  - 48% are FGN employees
  - 20% state and Local Government employees
- 32% are from the private sector.

For those participating in this programme and the more reason why states and local government employees must participate in the new Pension Reform Act (PRA) is to avoid a repeat of the long line of pensioners waiting to collect their entitlements and the bankrupt scheme that did not address the contributors' needs. Assets are also available at exit for payment of pension benefits as and when due, thus no accumulation of pension arrears. Before the year 2004 when the Pension Act was passed by the National Assembly, the government operated an unfunded Defined Benefits Scheme and the payment of retirement benefits was budgeted annually under the Pay-AS-You-Go Benefit Scheme. The covered Federal and State Civil workers were owed an estimated N2 trillion or 25% of the GDP of Nigeria. It is hoped that the new Pension Reform Act will reverse this trend. Furthermore, the importance of the new scheme lies on the fact that demographic shifts and ageing make defined benefits schemes unsustainable.

When the new Pension Reform Act is adopted by local governments, greater benefits can further be realized in the following areas as:

- Stems further growth of pension liabilities and provides a platform for addressing them.
- Facilitates mobility of labour amongst the three tiers of government.

Above all, the advantages of the Pension Reform Act translates to being a social security insurance which is a government programme that helps workers, retired workers and their families achieve a degree of economic security and provides cash payments to help replace income lost as a result of retirement, unemployment, disability or death.
CONCLUSION

Nigeria had Pension Scheme in 1951, which was established by the colonial administration and had limited application.

There were other Pension Reform Acts, but Pension Act No 102 of 1979 consolidated all enactment on Pension and gratuity scales devised for public officers by Udoji Public Service Review commission 1974. Up to year 2004 when the New Pension Act was passed by the National Assembly the government operated an unfunded Defined Benefits Scheme and the payment of retirement of retirement benefits was budgeted annually under the Pay-As-You-Go Benefit Scheme. Under that arrangement, the Federal and State civil service workers were owed by an estimated N2 trillion.

The new Pension Reform Act (PRA) has a defined contribution, contributory and fully funded. It is mandatory for all employees and employers, has uniform application, personalized and very portable.

Above all, these advantages translate into improved social security planning for the retired workers dead or alive and for their families to achieve a degree of economic security and provision of cash payments to help replace income lost as a result of retirement or death.

REFERENCES


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