PENSION REFORM ACT 2004 AND ITS IMPACT ON THE NIGERIAN BUSINESS ENVIRONMENT

Unuigbokhai, O.A. and Ali-Momoh Betty  
Department of Accountancy,  
Auchi Polytechnic,  
Auchi.

Abstract  
This study examines Pension Reform Act 2004 and its impact on the Nigerian business environment. The paper also reviews the funding and management of pension schemes in Nigeria before the Act and decides that if the Nigerian worker wants to ensure his retirement benefits payment on retirement, the Contributory Pension Scheme (now the new Pension Reform Act) has no alternative at the moment. This is to say that under the unfunded non-contributory scheme, pension was removed as a first charge to the consolidated revenue thereby causing a shortfall in the budgetary allocation which has led to pension liabilities accruing over the years. The new pension scheme is therefore, a new innovation, reliable and workable. The act is capable of encouraging a sustainable and durable pension system in Nigeria.

Introduction  
The privilege of receiving grant and pension appears the greatest manifestation of the victory of labour in its fight with the employer over its exploitation. For stability of the employment contract, labour had to work forward to the employment of a favourable welfare package when he leaves employment due to old age or disability. With the institutionalization of pensionable employment, the attractiveness of any employment contract is being judged in terms of whether it is pensionable or not. Pensionable jobs pay less salaries/wages while non-pensionable job pay more. If the salary premium of unpensionable over pensionable ones is high enough, individual worker can save, invest and make provision for old age and accidental disability. With successful investments of their savings, workers on non-pensionable employment would, on retirement, be as well off as those on pensionable jobs. Economic theory would thus predict as high a premium of non-pensionable over pensionable jobs in a market economy to permit individuals to undertake the level of savings and investments that would make both kinds of job equally attractive in the long run.

For a variety of reasons, governments all over the world get involved in pension matters in the form of laying down the legal framework, pension
fund management and regulation of pension scheme. The Federal Government of Nigeria (FGN) recently overhauled the legal framework for pension administration in Nigeria for pension administration in Nigeria by promulgating the Pension Reform Act 2004 (PRA’04). The PRA’04 was passed into law on June 23, 2004 by the National Assembly and assented to by President Obasanjo on June 25, 2004. The PRA’04 embodies the policies of the FGN to solve the pension problem in Nigeria, both in the short and long run. The objective of this paper is to carry out an evaluation of the Pension Reform Act, 2004 and access its potential impact on the Nigeria business environment. It also intends to find out how pension schemes were being managed in Nigeria before the enactment of the Pension Reform Act, 2004.

**Historical Background of Pension**

The first pension law in Nigeria was enacted in 1951 referred to then as the Pension Ordinance. Although, the ordinance was promulgated in 1951, it had a retrospective effect from 1st January, 1946. The colonial pension law was mainly designed for United Kingdom Officers, who moved from post to post in the vast British Empire. The reason was to ensure that they continue in service in respective of whoever they were sent to serve.

Under the ordinance, pension was not an automatic right of Nigerians.

Twenty-eight years later, the ordinance and other pension laws were further consolidated under the Pension Act, No.102 of 1979, as well as the Armed Forces Pension Act No. 103 of 1979 to take care of civil servant and Armed Forces after their retirement. This Pension Act was promulgated in 1979, it had a retrospective effect from 1st April 1974. Under this law, the Government incurred 100% liability for the payment of retirement benefit. In effect, No employee in the public service was required to contribute towards the payment of his retirement benefit. An employee was paid benefit under what was called the pay-as-you-go system. It meant that government had to make budgetary provision every fiscal year in order to sustain the system.

Taking after the Armed Forces’ experience, the Nigeria police force (NPF) and other Government Agencies Schemes were enacted under the Pension Act No.75 of 1987. The Local Government Pension Edict culminated in the Establishment of the Local Government Staff Pension Board in 1987. In 1993, the Nigeria Social Insurance Trust Fund (NSITF) was established by Decree No.73 of 1993 to replace the NPF Scheme with effect from 1st July, 1994. Its primary aim was to cater for workers in the private sector of the economy by protecting them against loss of employment income in old age, disability or for their descendants at the death of the retiree. Pension Scheme in Nigeria, before the 2004 Pension Act can be classified as follows:

- Public Sector Pension Scheme
- Private Sector Pension Scheme
- Armed Forces Pension Scheme
Pensions for Academic Staff of Federal Universities.

Pension Defined
Pension can be said to be a part payment made by an employer to his retired employee until his/her death in consideration of passed service rendered by the former employee. It is a payment made to pension who is no longer working and which will enable the former employee leave and enjoy some or all of the essential and non-essential he was able to avoid during his working life.

Olifade (2003) as cited in Sanni (2005) describes pension as a sum of money paid regularly to a person who no longer works because of a disablement or to his widow, dependent children by the state or by his former employer or from fund of which he and his employer have both contributed.

Ezekiel (2003) states reason for the pension payment as follows: (i) to guarantee a comfortable retirement life after years of active work, (ii) to enable pensioners not to depend on relatives, friends, or the community, (iii) to reward long service and loyalty to an employer, and thus a deferred remuneration, (iv) to provide financial support to the dependents of a deceased employee, and thus protect them against poverty and distress, (v) to ensure that a pensioner reasonably maintains the standard of living which he or she enjoyed during active protection years.

Since pension is a deferred payment by an employer to an employee when he retires from the service, this deferred payment can either be shouldered 100% by the employer or both the employer and employee. A Contributory Pension Scheme is therefore a scheme which both the employer and the employee make contribution by way of jointly setting aside funds into the scheme in order to guarantee payment of retirement benefit to employees on retirement. The establishment of a Contributory Pension Scheme in Nigeria was therefore to achieve certain objectives hence, the passage into law of the Pension Reform Act, 2004.

Reasons for the New Pension Act
The pension crisis, which plagued Nigeria prior to the recent reforms was a part of a global pension problem, characterized by unfunded Public Sector Pay-As-You-Go Schemes with huge implicit pension debts, as well as poorly managed private sector funds (example, Enron, Panam, Maxwell Brothers) with huge deficits. In Nigeria we experienced inability of agencies to pay benefits (retirees dying on queues etc.) due to crisis in administration and management of retirement benefits (Gratuity and Pensions) in both the public and private sectors, with the non-contributory and unfunded nature of public sector schemes aggravating the crisis in those sectors. Unfortunately, the NSITF scheme for the private sector did not live up to expectation as there was apparent distrust and lack of confidence in the fund arising out of the glaring absence of transparency and accountability.

Consumption by employees of every disengagement benefits collected
(from provident schemes) at point of changing jobs in the private sector further aggravated the problem and foretells suffering at old age with no passive income to fall back on after retirement. There was also no standard guideline on retirement benefits (gratuity and pension) and social security administration in the country. All the above led to the pension crises characterize by the following: (i) unfunded arrears of above N3trillion, (ii) pensioners not being paid entitlement regularly, (iii) existence of ghost pensioners in the public service, (iv) pensioners dying of verification queues, (v) unstructured and unfounded private sector schemes; and (vi) diversion and mismanagement of existing pension funds by the Board of Trustees and managers of the fund.

It was in realization of the above pension crisis and the need to proffer solutions that the former President Olusegun’s government set up a committee of core professionals, headed by Mr. Fola Adeola to study the problem and come up with appropriate recommendations. The report of this committee formed the basis of the Pension Reform Bill passed into law by the National Assembly in June 2004 as the Pension Reform Act 2004 and signed into law by former President Obasanjo on June 25, 2004. This indeed marked the beginning of a new era of pension management and administration in Nigeria.

The Pension Reforms Act 2004
The law repeals the Pension Act 1990 and establishes a Uniform Contributory Pension Schemes for both the public and the private sectors in Nigeria. Section 2 of the Act provides the objectives of the new pension scheme to include: (i) to ensure that every person who worked in either the public services or the private sector receive his or her retirement benefits as and when due, (ii) assist improvident individuals by ensuring that they save in order to cater for their livelihood during old age, and (iii) establish uniform set of rules, regulations and standards for the administration and payment of retirement benefits service of the Federation, FCT and Private Sector. The Pension Reform Act 2004 has the following key features: (i) Rate of Contribution to Scheme, (ii) Retirement saving account, (iii) Withdrawal from retirement savings account, (iv) Retirement benefit, (v) Life assurance cover, (vi) Death of an employee, (vii) Missing employees, (viii) Retirement as a result of ill-health, (ix) Retirement benefit to be exempted from tax, (x) Exemption from the scheme, (xi) Contribution to form part of tax deductible expenses (xii) Transfer of entitlement from defined benefit scheme, (xiii) Transfer from one employer to another (xiv) National pension commission (xv) Closed pension fund administration, (xvi) Pension fund administration (PFA’s), (xvii) Pension assets or fund custodian.

Impact of the Act on Nigeria Business Environment
The new Pension Reform Act 2004 will alter the tie paths to all major macro flows and stock-term and long-term. It is one of the most complexes of structural reforms to undertake because it upsets existing political economy equilibrium,
affects public finances, and intervenes severely in the functioning of labour and capital markets and changes on economy’s saving investment and growth patterns from short-term to the very long-term (Anijah, 2005). Under the new system, the employee’s contributions, employer’s contributions and the final benefits will be tax-exempt. This is an advantage to the private sector employees whose retirement benefits were not previously tax-exempt. The funds build up will be available for long-term investments and provide more funds (25% lumpy sum) to the employees in establishing small scale business that will further impact positively on the growth of the Nigerian economy.

Government, corporate organizations and even small and medium scale enterprises will in the long run be able access funds at a cheaper rate from the accumulated pension funds to finance their operations. This will in turn expand their production capacities and provide more job opportunities for Nigerians with its attendant positive multiplier effect on all sectors of the Nigerian economy. The new pension reform and the promotion of funded schemes would definitely cause a large shift in favour of long-term financial savings. The availability of substantial amounts of this long-term financial resources has considerable potential benefits for the development and modernization of capital markets, stimulating innovations and improving information disclosure.

Pension and social reform may also have important and beneficial implications for the functioning of labour markets if incentive for strategic manipulations are removed and any restriction on labour mobility are substantially weakened. The new pension Act will also eliminate or at least substantially reduce the occurrence of perverse and capricious redistribution. Another potential impact of the New Pension Act is likely increase in the rate of savings that may accompany a move from an unfunded to a largely funded system, thereby leading to a higher saving rate. The 2004 pension Act has created a basis for capital for today’s employee to become an entrepreneur in future.

The Pension Reform Act 2004 also opens new business opportunities for Life Assurance Companies by way of sales of Compulsory Group Life Assurance to all organizations with five (5) or more staff and purchase of a Life Annuity by retired employees as an option to the programmed monthly or quarterly withdrawals. By implication, the New Pension Act will bring about the popularity of group life assurance and annuity products, which will in turn, improves the profitability of the Life Assurance Companies in Nigeria. Also, the new Act will bring about more investment in real estate businesses. The implications is that the services of builders, civil, structural and electrical engineers, architects, estate valuers and surveyors, building materials merchants’ etc. would be required. This will in turn affect other facets of the Nigerian economy positively.

**Criticism of the Act**

The 5% of the monthly federal wage bill to be paid into the Redemption...
Bond under the Transitional provisions (part v. section 29 (1,2) appears arbitrary. Proper actuarial analysis that would assist the Federal Government to arrive at a realistic funding formula under the Act is required rather than the use of the arbitrary rate of 5%. The New Pension Act does not make provision for the payment of gratuity. An officer on voluntary retirement will have to wait until the age of 50 years to take a lump sum from the retirement saving account. The lump sum cannot be taken as gratuity because gratuity is an award (gratis). This lump sum to be paid under the new scheme would be taken from the retiring officer’s retirement savings account.

The workers rate of contributing of 7.5% of the monthly total emolument under the new scheme is excessively and counter-productive. Given a plethora of existing monthly deductions such as Personnel Income Tax, National Health Insurance Scheme and others, the public service worker will be divested of more than one-third of his/her disposal income. The benefit to be payable from the new system will be small compared to those payable under the old system especially for the government employees. Under the new scheme, an officer is expected to enjoy programmed monthly or quarterly payments for a period calculated on the basis of an expected life span or buy annuity for life from a life Assurance Company. The Act failed to provide an answer to the natural question that may likely be asked, supposing a retire out live his/her expected life span, what happens?

Under the pension Act 102 of 1979, an officer whose appointment is terminated after qualifying services would be paid gratuity and placed on pension immediately not withstanding the fact that he may have attained the pension drawing age of 45 years. This New Pension Act is silent on termination of appointment of benefit. The pension Act 102 of 1979 provides that an officer who is dismissed from service forfeits his benefits. This is so, because under this system, government bears retirement benefit liabilities of 100%. The Pension Reform Act 2004 is silent on dismissed officers. A very fundamental question is can an officer be denied his contribution under the contributory scheme even if he is dismissed? In my own opinion, he should not be denied his contribution since it is his money, which he has set aside. He may however, be denied the employee’s contribution.

**Recommendation**

For an effective impact of the pension act on the Nigerian business environment, the following recommendations are made.

1. **Notice of retirement.** This should be a joint responsibility of both the employers and the intending retirees. In this case, the blame should be on the intending retirees who will eventually suffer of there is a failure.

2. **Falsification and mutilation of personal records.** In order to avoid or reduce the incident the Government apart from gazette which is recently being played down should programme the computer on the first day the
The Pension Reform Act 2004 has brought about a fundamental shift from the defined benefit scheme that was in existence (most especially in the public sector) to a defined contribution scheme that, if the Nigerian workers want to guarantee their retirement, the contributory pension scheme has no alternative at the moment. Also, as the success of the pension reforms is hinged on the availability of funds to contributors after they retire the safety of the pension fund assets should be given a lot of attention. Therefore, the National Pension Commission should ensure strict monitoring and supervision of the Pension Fund Administrators and Pension Assets Custodians in order to guarantee total and absolute safety of the Pension Fund Assets.

Conclusively, it is believed that the provisions of the Act will enhance transparency in pension management, hopefully clear the huge pension backlogs, ensure employees have fully funded schemes and curb mismanagement of pensions.

References


Ezekiel O. C. (2003). *The nature and administration of pension schemes in*


