EVALUATION OF PENSION REFORMS IN NIGERIA: A COMPARISON BETWEEN THE OLD AND NEW SCHEMES

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ABSTRACT
Contributory pension system (CPS) was introduced in Nigeria in July, 2004 to replace the old defined Benefit (Pay-as-you-go) system. The motive behind the introduction of the new pension system is to reduce the poverty of Nigerian workers in Public & Private sectors and improve their standard of living. The Pensions Reform Act of 2004 brought a new dawn in Nigerian Pension industry which formally was a defined benefit but now defined contributory. Although the new scheme is being adjusted to be better than the old scheme in that it is expected to remedy all the abnormalities, ranging from diversion/looting of Pensions funds to poor records, it is advocated that PENCOMM should be alive to their responsibilities in monitoring, supervisory, coordinating and over-regulating the pension industry in Nigeria to get these objectives of the government over the Pension reform achieved.

Keywords: Pension Scheme, Deferred Benefit Scheme (DBS), Contributory Pension Scheme (CPS), Retirement Benefit, Pension Fund Administrators

INTRODUCTION
A pension is a retirement account that an employer maintains to give the employee a fixed payout when he/she retires. It is a kind of defined benefit plan. Thus, pension is the amount paid by government or company to an employee after working for some specific period of time, considered too old or ill to work or have reached the statutory age of retirement (Adams, 2005). Iwu (2007) asserts that as a scheme, pension is the periodic payment granted to an employee for services rendered, based on contractual legal enforceable agreement, paid by an employer at the agree time of termination of employment. It can also be seen as the monthly sum paid to a retired officer until death because the officer has worked with the organization paying the sum. Prior to the enactment of the Pension reform Act 2004 that gave birth to Contributory plan, Pensions Scheme in Nigeria had been bedevilled by many problems. The public services operated an unfunded defined benefit scheme and the payment of retirement benefit were budgeted annually. The annual budgetary allocation for pension was often one of the most vulnerable items in budget implementation in the light of resource constraints. In many cases, even where budgetary provisions were made, inadequate and untimely release of funds resulted in delays and accumulation of arrears of payment of pension rights. It was clearly evident,
therefore that the defined benefit scheme could not be sustained. The private sector on the other hand did not have many employees covered by the Pension schemes put in place by their employer, and many of these schemes were not funded as well. Where the schemes were funded, the management of the pension funds was full of malpractices between the Fund Manager and the Trustees of the pension funds.

The objectives of a pension system are firstly to reduce poverty among the elderly, secondly to smoothen consumption between the working years and the retirement years and that an individual does not suffer a huge drop in living standards when in old age or disability reduces his earning ability. Recently, the non-contributory unfunded pension system was replaced by a fully funded contributory pension scheme (Schwarz, 2006). In most traditional societies, it is customary for families or communities to care for persons who have reached old age, become disabled or families that suffer the death of a bread winner. However, there are still individuals who do not have children to care for them or whose families or communities are too poor to shoulder the responsibilities of adequately caring for them. Nigeria, especially in the public sector, had in the past operated a deferred pension scheme, which was non-contributory and largely unfunded. The pension scheme was also characterized by a pay-as-you-go scheme (PAYG) as retirees were to be supported not by any previous contribution, but by annual budgetary provisions. Okafor (2001) observed that there is something particularly inhuman and degrading about the plight of most men and women who after spending the most active years of their lives, serving the nation, are left to face the vagaries and vicissitudes of life without security that comes with retirement. The situation is relatively better in the private sector as some companies manage to operate pension schemes which were functional from the perspective that they were able to make some payments. This scenario necessitated a re-think of pension administration in Nigeria by the administration of President Olusegun Obasanjo. The pension reform Act 2004 was promulgated and signed into law by the President on June 25, 2004. The pension fund administrators are expected to open retirement savings account for employees, invest and manage the pension funds and maintain books of accounts while the National Pension Commission was saddled with the responsibility of regulating, supervising and ensuring effective administration of pension matters in Nigeria. The commission will equally be responsible for licensing, approving, regulating and monitoring the investment activities of pension administrators and custodians. The new pension scheme is contributory,
fully funded and based on individual accounts that are privately managed by pension fund administrators with the pension assets held by pension fund custodians (Barrow, 2008). Despite this new pension reform, there has been a hiccups in the planning and administration of the pension scheme ranging from diversion/looting of pension funds by public office holders, enormous pension arrears, difficulties experienced by the retirees or pensioners in accessing their earnings on pension funds, poor records and weak database of retirees, frauds and corruption in the scheme. It is against this backdrop that this study is anchored to examine pension reform in Nigeria as a comparative study between the old and new scheme and the extent of performance they have on the pension operation.

LITERATURE REVIEW

The Chilean Model – Copied by Nigeria

Pension provision in Chile dates to the 1920s when social insurance funds (Cajas de prevision) were established for specific categories of workers providing old age and retirement pensions (Arellano, 1980). These were funded from payroll contribution from employees & employers with benefits determined by final earnings and contributory model. After the 1950’s, there was rapid growth in the number of covering of social insurance funds. By 1976 there were over 35 social insurance funds covering three quarters of the labour force against a wide range of contingencies including disability, dependants, health costs and unemployment. This expansion was financed by raising contribution levels and by fiscal transfers. The military government which took power in 1973, imposed fundamental reform of social insurance in 1980 (Barrientos, 1998). Individual retirement saving plans managed by private pension fund managers were introduced for new entrants to the labour force while existing workers were offered substantial inducements to switch their pension entitlements to the new pension plans.

In 1981, Chile’s pension system was restructured to comprise three pillars: a Poverty prevention/solidarity pillar; a mandatory contribution pillar; and a voluntary saving pillar. The combination of these pillars seeks to guarantee that individuals maintain a similar standard of living during retirement as they enjoy during their working lives and to eliminate poverty among the elderly and disabled. The major objective of the solidarity pillar is to prevent poverty among the elderly and disabled. Dostal and Cassey (2007) argued that the Nigerian authorities embraced the pension reforms of the Chilean government (i.e. emulated and copied it). But they failed to learn the lessons of Chile. By the time Nigeria was busy copying Chilean pensions plan, Chile was preparing for an alternative social pension scheme. Again, while the Nigerian
government was beginning to give serious attention to pension reform (using the Chilean model) in early 2005 the Chilean model was being criticized by supporters of the scheme and the World Bank had come to conclude that the Chilean reform model has not delivered the benefits that it was set out for from the beginning because of the too many assumptions that to realize the claims, other reforms were also required to complement or precede pension reforms (Gill, et al 2005; World Bank, 2005). In 2006, the Chilean government announced a wide-range of change in their pension scheme, placing greater emphasis on solidarity and the financing and higher control on the operation of the individual accounts to which employees are subscribed (Gobierno de Chile, 2017). Again the World Bank has claimed that it advised against the establishment of a “multi-pillar system” in Nigeria on the grounds that the financial sector was insufficiently developed (World bank, 2005) however, the reforms undertaken in Nigeria were radical involving the setting of a new basis for determining pensions and the establishment of new structures.

Pension scheme is broadly divided into the defined contribution plan and the defined benefits plan. In defined contribution plan, a contribution rate is fixed (Odia and Okoye, 2012). For instance, in Nigeria, an employee contributes 7.5% of his monthly emolument while the employer also contributes the same amount or more depending on the category of employee. The retirement benefit is variable depending on the performance of the investment selected. In defined benefit plan, the retirement benefit is stipulated usually as a percentage of average salary, but the contribution will vary according to percentage of the average compensation a participant receives during his or her three earning years under the plan (Owojori, 2008). Basically, the two pension plans create very different investment problem for the plan sponsors. While the defined benefit plan create a liability pattern that must be anticipated and funded, the defined contribution plan creates a liability only as long as there is investment at any point in time. Investment is often left to the people who benefit from the decision or suffers from the consequences (Santamero and Babble, 1997). The inherent problem of the pension fund administration was the non-payment or the delays associated with the payment the funds when available. It was estimated that as at December 2005, the pension back-log or arrears were put at about N2.56 trillion. In fact, pension fund administration became a thorny issue with millions of retired Nigerian workers living in abject poverty and they were often neglected and not properly catered for after retirement (Orifowomo, 2006). It was a distress to witness the tough times the retirees in Nigeria passed through coupled with the rigorous process before the
pension and gratuity are paid as well as other retirement benefit (Abade, 2004). Other problems were gross abuse of pensioners and pension fund benefit which were politically motivated in some cases, extended family and other traditional ways already broken down due to urbanization and increased labour and human mobility. Moreover, considering Statement of Accounting Standard (SAS) No. 8 “on accounting for employees retirement benefits”, the problems of the old pension scheme which led to the pension reforms of 2004 include wrong investment decision, wrong assessment of pension liabilities, arbitrary increase in pension without corresponding funding arrangement, non-preservation of benefits; some were mere saving scheme and not pension schemes and serious structural problems of non-payment and non-coverage. There inadequate safeguarding of the funds to guarantee prompt pension and other benefits payment to retirees.

The New Pension Reform Scheme

The Nigeria contributory pension plan came through the Pension Reform Act of 2004. The scheme is called contributory because it was fully funded on individual accounts that are private managed by Pension Fund Administrator (PFAs) with the pension fund assets held by pension fund custodians. Under the system, the employee contributes a minimum of 7.5% of their basic salary, housing & transport allowance while employers shall contribute 7.5% too. An employer may elect to contribute on behalf of the employees such that the total contribution shall not be less than 15% of the Basic Salary, Housing & Transport allowance of the employees. PFAs are private organization that has been duly licensed to open retirement savings accounts for employees, invest and manage the pensions fund in fixed income securities listed and other instruments as the commission may from time to time prescribe, maintain books of accounts on all transaction relating to the pension funds managed by it, provide regular information or investment strategy to the employees or beneficiaries and pay benefit to employees in accordance with the provision of the Act.

The objectives of the scheme according section 2 part 1 of the PRA of 2004 include to

- Ensure that every person who worked in either the public service of the federation, federal capital territory or private sector receives his retirement benefits as and where due.
- Assist improvident individuals by ensuring that they save in order to carter for their livelihood during the old age.
• Establish a uniform set of rules, regulations and standards for the administration and payment of retirement benefits for the public services of the federation, federal capital territory and private sector.
• To stem the growth of outstanding liabilities
• Secure compliance and promote wider coverage

It is believed that all these reforms put in place, which clearly spelt out in the objectives of the new PRA of 2004, would be able to remedy the situation by adequately tackling the difficulties in the old scheme by being adequate, affordable, sustainable and robust (Balogun, 2006). It must as well eliminate old age poverty and be able to improve standard of living for majority of people. It will also be able to withstand major shocks including economic, demographic and political volatility. Ahmad (2008) remarked that as part of the implementation efforts increased registration of contribution in public & private sector, membership of Contributory Pension Fund Administrator (CPFAs) and custodians (CPFCs), total pension fund assets grew to about $6.08 billion in December, 2007.

Risk Management & Investments of Fund & Committee

The main concern of the new pension scheme is safety of the fund & the maintenance of fair returns on the amount invested. The need for safety is emphasized in determining the quality of the instrument to invest in and a PFA is expected to adopt a risk management profile in making investment decisions with due regard to the Credit rating of companies registered under the investment of securities acts of 1999. It is expected that every pension fund administrator shall establish the following standing committees to assist in carrying out its function & ensuring compliance with the provision of this act.

  a. Risk management committee and
  b. Investment strategy committee

Risk management committee should take care of the following:

• To determine the risk profile of the investment portfolios of the pension fund administrator
• To draw up programmes of adjustments in the case deviation
• To determine the level of reserves to cover the risks of the investment portfolios
• To advice the PFA in maintaining adequate internal control measure & procedures and
To carry out such other function relating to risk management as the board of the PFA may from time to time determined.

Problems Associated with the New Pension Scheme

Olurankise and Adetula (2006) analyzed all available pension reform schemes in Nigeria and argued that the public sector organization at the Federal, State and local government levels have failed woefully to meet up with payment of pension liabilities thereby making retirees to groan under heavy survival burden and hunger before their monthly rights were given to them. They assert that many pensioners gave up the ghost before they could get access to a reasonable percentage of their pension benefits.

According to Ahmed (2008) the problems associated with the new pension scheme include:

a) Lack of knowledge and general misconceptions.

b) Widening the coverage in the informed and private sector, many of the SMEs, private have not yet bought the idea.

c) Securing systems wide buy-in and initial reluctance from employees to register with PFAs

d) Capacity building in the new pension industry

e) Quantifying and transferring legacy funds & asset managed by employees, insurance companies and pension managers.

Table 1: Comparison between the Old and New scheme

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>Old Scheme</th>
<th>New Scheme</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Type</td>
<td>Largely defined benefits</td>
<td>Defined contribution</td>
</tr>
<tr>
<td>2. Funding</td>
<td>Mostly unfunded and pay as you go(PAYG)</td>
<td>Contributory and fully funded</td>
</tr>
<tr>
<td>3. Membership</td>
<td>Voluntary in private sector</td>
<td>Mandatory for all employees in public and private sector, except pensioners and those with three years to retire</td>
</tr>
<tr>
<td>4. Pension Portability</td>
<td>Not portable</td>
<td>Personalized and very profitable</td>
</tr>
<tr>
<td>5. Management</td>
<td>Large state and management union</td>
<td>Private sector and individual choice</td>
</tr>
<tr>
<td>6. Retirement Benefits</td>
<td>Discriminatory</td>
<td>Uniform application</td>
</tr>
<tr>
<td>7. Supervision</td>
<td>Fragmented and unregulated (SEC, NAICOM &amp; JTB)</td>
<td>Strictly regulated by PENCOM</td>
</tr>
<tr>
<td>8. Pension liability</td>
<td>Implicit and not transparent</td>
<td>Explicit through retirement bond and capped</td>
</tr>
<tr>
<td>9. Tax Exemption</td>
<td>Limited</td>
<td>Contribution and retirement benefits</td>
</tr>
</tbody>
</table>
10. Insurance Policy  | Voluntary and mostly in private sectors  | i. Mandatory for all employers ii. Three times the employees emolument
11. Dismissal from service  | No pension benefits  | Full pension benefits
12. Collateral for loans  | Benefits could be used as collateral  | Benefits cannot be used as collaterals
13. Deductions from benefits  | Benefits can be subjected to deductions especially employers in any financial obligation in the employee  | Contents of RSA can be used for payments of retirement benefits only
14. Claiming retirement benefits  | Cumbersome  | Straight forward
15. Minimum service years  | Generally 5 years for gratuity and 10 years for pension  | Month of employment for all benefits subject to minimum wage
16. Gratuity  | Provided to those qualified  | Provided for lump sum withdrawal
17. Risk management  | No provision  | Adequate provision

**Source:** Ahmad, M. K. (2008)

A comparison of the old and new pension show some remarkable differences between them as shown in the table 1. For instance, starting from the type of scheme, funding, membership to risk management of the pension fund, the new scheme seems to be broader, inclusive and more adequately provided for. While the old pension scheme was largely defined benefits and unfunded, the new scheme is to find contribution and fully funded. The new scheme is very portable and enjoys uniform application unlike the old which was not. In fact, employees who leave one employment for another or even dismissed from service have no fear of losing entirely from their pensions or other retirement benefits under the new pension scheme. The regulation and supervision of the new scheme is by PENCOM whereas the SEC, NAICOM and JTB were jointly responsible for the old scheme. Akeni (2009) made a comparison of nine items in the old and new scheme by conducting a survey of the pension fund administrators, pension fund custodians and the beneficiaries in the public and other sector. He found that the new scheme was better than the old in terms of accountability, accessibility, ease of payment of pension and gratuity, funding, management of pension fund, transparency, stakeholders' confidence in the scheme, auditor's control and corporate governance. Although, there was agreement that the new scheme was applauded as far better than the old, he discovered that the new scheme may not address the difficulties currently encountered in the pension industry in Nigeria nor impact positively on the standard of living of the retirees and pensioners unless there was proper co-ordination and supervision by the Nigerian Pension Commission of the pension fund administration and custodian. Therefore PENCOM must undertake periodic
reviews of the investment guidelines of pension fund and create conducive environment for smooth operations by the pension fund administrators and custodians. It must ensure that the administrators and custodians abide by the rules of the pension game in order to ensure their efficient and effective performance. The public must be regularly enlightened and adequately kept abreast of developments in the pension industry by the commission and administrators.

DATA ANALYSIS AND INTERPRETATION

Test of Hypotheses

Test of hypothesis 1: Effect of the new pension scheme on pension performance in Nigeria

Model Summary

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.790a</td>
<td>.683</td>
<td>.036</td>
<td>781.961</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), new pension schemes
b. Dependent Variable: performance

Coefficientsa

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>New PENSION SCHEME</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>94667.455</td>
<td>1582.151</td>
<td>.921</td>
<td></td>
</tr>
<tr>
<td></td>
<td>7.742</td>
<td>2.009</td>
<td>3.852</td>
<td>.033</td>
</tr>
</tbody>
</table>

a. Dependent Variable: performance

ANOVAa

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>Df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Regression</td>
<td>1</td>
<td>13.025</td>
<td>10.273</td>
<td>.002b</td>
</tr>
<tr>
<td></td>
<td>Residual</td>
<td>7</td>
<td>1.268</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>8</td>
<td>116.988</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Dependent Variable: performance
b. Predictors: (Constant), new pension scheme

The results above show how much the variance in the dependent variable (pension performance) is explained by the model. The table provided useful information about the regression analysis, the value is 0.783 which when expressed in percentage terms shows that 78.3% variation in the dependent (pension performance) is explained by the independent
variable (pension scheme) while the remaining 21.7% variation in the dependent variable is affected by other factors not captured in this study. The value of R (0.880) is an indicator of a strong positive difference between the independent variable and the dependent variable (pension performance). The ANOVA table in table 1 shows a significant variation between pension scheme and performance with P value 0.002, which is less than 0.05.

**Test of hypothesis 2: Effect of the old pension scheme on the performance of pension in Nigeria.**

**Model Summary**

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.872*</td>
<td>.792</td>
<td>.036</td>
<td>817.214</td>
</tr>
</tbody>
</table>

Predictors: (Constant), old pension scheme
Dependent Variable: pension performance

**Coefficients**

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>T</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>(Constant) -84539.455</td>
<td>13876.151</td>
<td>-.432</td>
<td>.543</td>
</tr>
<tr>
<td></td>
<td>Old pension scheme 2.345</td>
<td>2.764</td>
<td>.749</td>
<td>2.851</td>
</tr>
</tbody>
</table>

a. Dependent Variable: pension performance

**ANOVA**

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>Df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Regression 18.849</td>
<td>1</td>
<td>18.849</td>
<td>15.749</td>
<td>.000b</td>
</tr>
<tr>
<td></td>
<td>Residual 98.139</td>
<td>7</td>
<td>1.197</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Total 116.988</td>
<td>8</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Dependent Variable: old pension scheme
b. Predictors: (Constant), pension performance
The result of the regression analysis shows how much the variance in the dependent variable (liquidity) is explained by the model. The table provided useful information about the regression analysis, the value is 0.792 which when expressed in percentage terms shows that 79.2% variation in the dependent (liquidity) is explained by the independent variable (old pension scheme while the remaining 16.8% variation in the dependent variable is affected by other factors not captured in this study. The value of R (0.872) is an indication of a strong positive variation between the independent variable and the dependent variable.

CONCLUSION AND RECOMMENDATIONS

The role of pension as a deferred compensation scheme has continued to attract varying interest in major economies of the world. Accountability in the pension scheme today is a vital ingredient in enhancing pension performance in Nigeria. This will directly affect employees’ welfare and boost their morale as observed in the findings above. The results show positive variations between the two pension schemes in the two models developed thereby proving the new to be better. It is therefore recommended that bottlenecks capable of drawing the nation back such as weak records and management be addressed for a better pension scheme.

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