



# **IPSAS & PFM Conference**

## **The Transition to a Contributory Pension Scheme**

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# Session Objectives



- ☐ Rationale for change
- ☐ Explore key benefits under Contributory scheme
- ☐ Main transition provisions
- ☐ Opportunities and challenges
- ☐ IPSAS 39 Implications

# Policy makers Nightmare

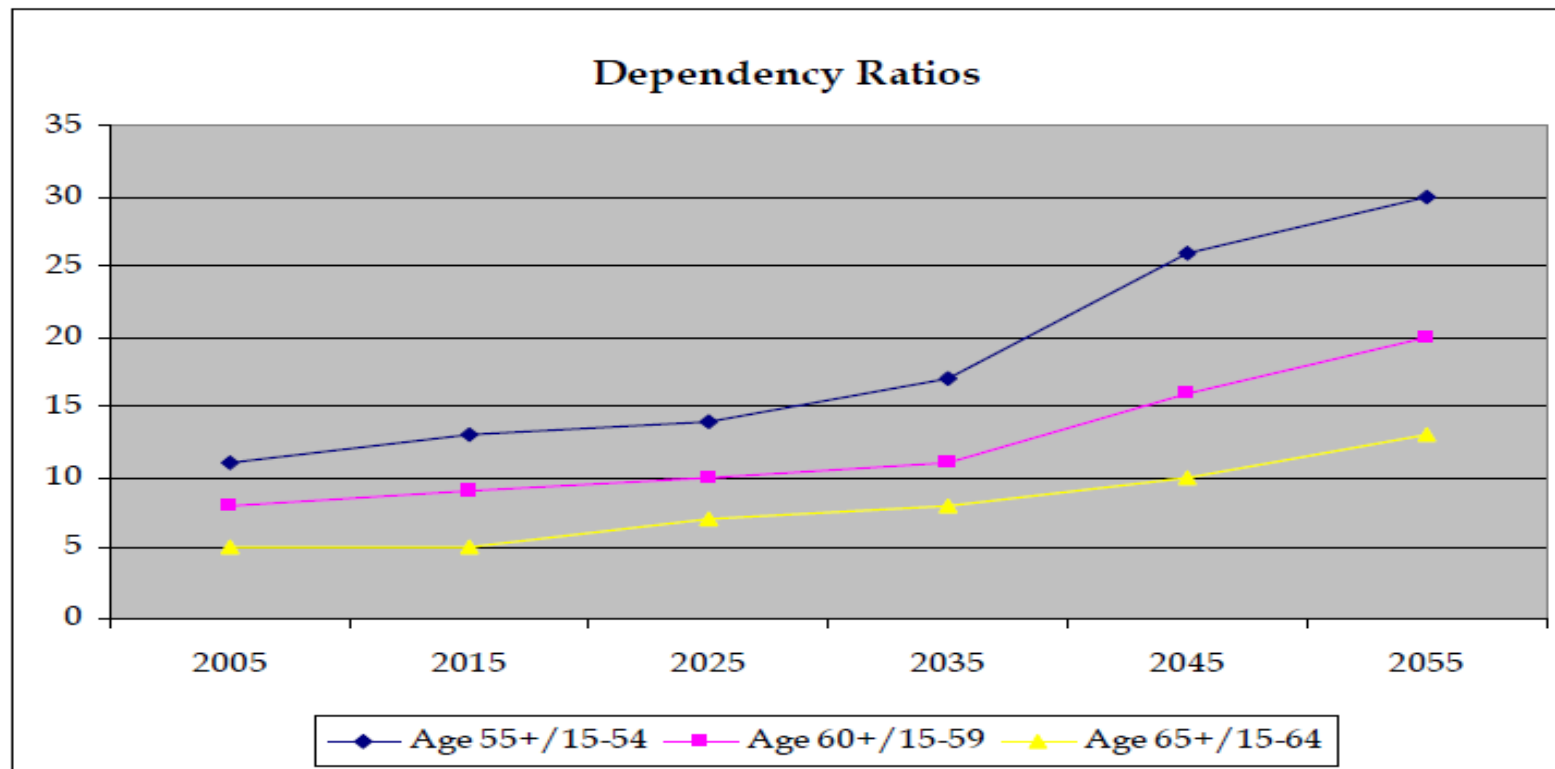


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# Rationale: Evidence



## ❑ Problem of high dependence –inability to save

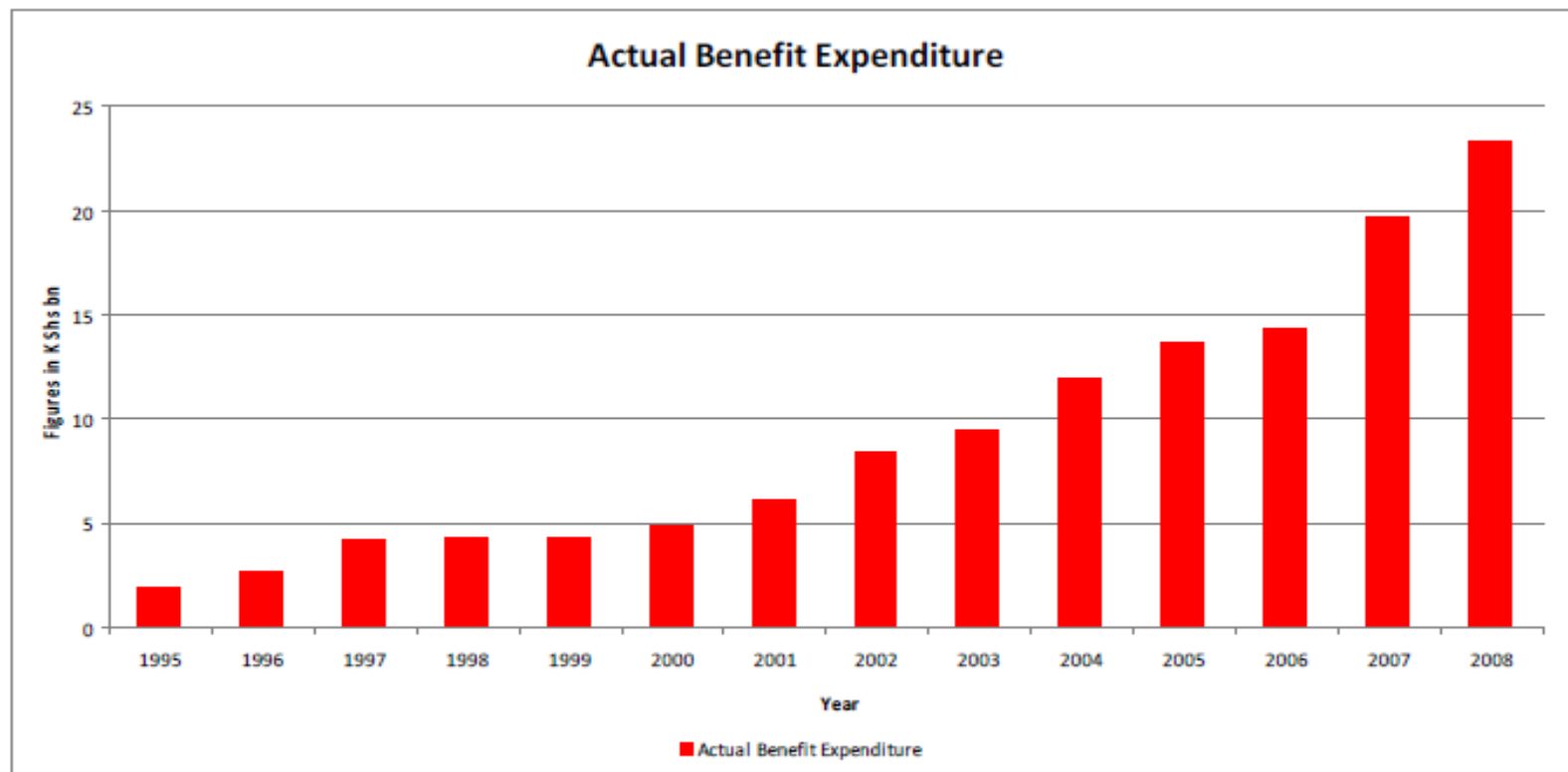


*Source: Can we afford age old pensions by Charles Machira*

# Unsustainable Pension bill



❑ Current financing model 'a pay as you go basis' unsustainable (Source: Review of Pension system in Kenya, Raichura, Sept. 2008)



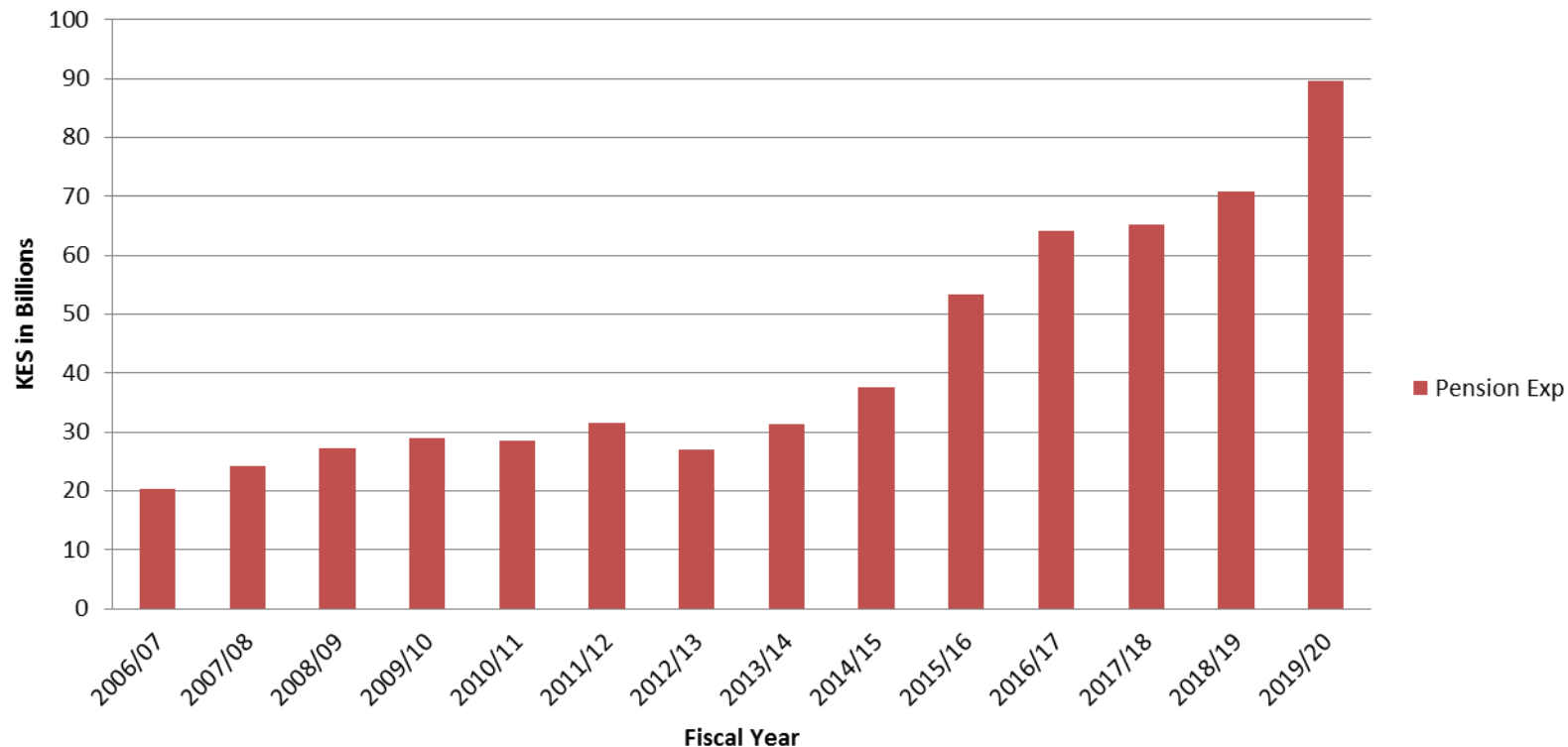
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# Unsustainable bill



❑ More Recent evidence: Own plot fro BROP data

**Pension Expenditure distribution 2006/7 -2019/20**



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# Background



- ❑ Retirement Benefits under Social and Economic pillar of Vision 2030
  
- ❑ Retirement Benefits has 3 Key Pillars:
  1. **Zero pillar** – mainly cash transfers to elderly citizens
  2. **First pillar** – mandatory NSSF
  3. **Second pillar** – Civil Service Pension Schemes, Occupational, Individual and Umbrella Retirement Benefits Schemes

# Purpose of Retirement Benefit Schemes



- ☐ Pay benefits to members on attainment of retirement age
- ☐ Avail benefits to members on leaving service
- ☐ Stabilize financial wellbeing of retirees
- ☐ Provide financial protection to members' dependants on death in service
- ☐ Provide disability benefits
- ☐ Alleviate old age poverty



# Historical Context



- ❑ Government has operated a non-contributory Pension Scheme since independence fully financed through the Exchequer
- ❑ New scheme proposed as part of reforms in the Public Service Pensions' Sector
- ❑ Scheme established by the Public Service Superannuation Scheme Act, 2012
- ❑ The contributory scheme is a follow up to Treasury Circular No. 18 of 2010
- ❑ Directive to convert Defined Benefit (DB) to Defined Contributory Scheme (DC) was to align our pension with scheme with best practice

# Elements of Current Scheme



- ❑ Benefits calculated based on length of service, final annual basic pay and a pension accrual factor of  $1/480$
- ❑ A lump sum equivalent to  $\frac{1}{4}$  (commutation factor of 20) can be accessed on retirement
- ❑ Death gratuity – higher of resultant lump sum or employee's 2 year basic salary
- ❑ Dependants pension – paid to widow or children for 5 years only (Officer must have served for 10 years to qualify & Equivalent to the pension officer would have earned

# Elements Cont...



❑ **Marriage gratuity** – paid to a female officer who resigns after serving for 5 years with a view of marriage or issues surrounding her marriage

❑ **Killed on duty** – for officers killed on circumstances around their duty. Widow's benefit is 10/60<sup>th</sup> pensionable emoluments at time of death; children's portion is 1/8<sup>th</sup> of the widow's pension subject to a max of 6 children

❑ **Injury pension** – additional pension granted to an officer who's permanently injured in the course of his duties (paid at an annual rate in proportion of 5/60 to 20/60 on pensionable emoluments at time of injury. Paid on retirement & is not transferable

# Issues with current scheme



- ☐ Scheme disadvantages officers who may wish to leave service before age of 50 yrs –don't qualify for pension or any other benefit
- ☐ Benefits not portable
- ☐ Defined benefit scheme –doesn't allow for improvements e.g. investment income or voluntary contributions
- ☐ Expensive and unsustainable in long term
- ☐ Discriminatory to male officers on marriage gratuity & Widower benefits

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# Issues cont...



- ❑ Accrued benefits cannot be accessed while in service – denies beneficiaries of personal development
- ❑ Discriminatory against female officers – require additional conditions to be able to contribute to WCPS

# Scope & Membership – New Scheme



- ☐ Civil servants, Teachers under TSC & Disciplined services (NPS, PS & NYS)
- ☐ PnP employees under 45 years on 1<sup>st</sup> January 2021
- ☐ New employees who join service after 1<sup>st</sup> January on PnP terms
- ☐ Employees above 45 yrs on 1<sup>st</sup> January 2021 who opt to join on voluntary basis
- ☐ Employees whose services were transferred to County Government but still under PSPS

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# Key Features



- ❑ Defined contribution at 7.5% employee (graduated at 2% 1<sup>st</sup> yr, 5% 2<sup>nd</sup> yr & 7.5% 3<sup>rd</sup> yr); 15% employer; option for additional voluntary
- ❑ Portable –employee free to transfer benefits to any other scheme (public or private)
- ❑ Benefits can be accessed before prescribed age on account of resignation, dismissal, ill health, immigration, mortgage finance, advance to purchase residential home, death or any other circumstance allowable

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# Key Features



- ❑ Tax benefit to a maximum of the lesser of KES 20,000 or 30% of pensionable emoluments
- ❑ Life insurance and disability cover –minimum 5 times of member's annual pensionable emoluments
- ❑ Commutation of up to 1/3 of accumulated savings on retirement & 100% additional voluntary contributions
- ❑ Allows access of up to 40%, subject to max KES 7 million to purchase residential house

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# Key Features



☐ In case of death while in service –benefits payable to beneficiaries are:

- Members scheme credit;
- The insured benefit up to 5 times annual pensionable emoluments

☐ Members free to choose preferred beneficiaries

# Transition provisions



- ❑ Employees under 45 years automatically joins & above 45 yrs can choose (1<sup>st</sup> January 2021)
- ❑ Above 45 yrs who opt not to join will remain under PSPS, Pension Act Cap 189
- ❑ Employees serving under Temporary Terms of Service and contributing to NSSF will automatically be converted to PnP & shall cease contribution to NSSF
- ❑ Members shall complete beneficiary nomination form

# Transition provisions



- ☐ Contributions to WCPS shall automatically cease on joining new scheme –contributions to be refunded on exit from service
- ☐ Employees joining scheme shall be issued with a letter recognizing their period of service under current scheme
- ☐ WCPS and NSSF contributions shall cease immediately on joining scheme

# Transition provisions



- ❑ Employees on secondment, below 45 yrs automatically joins based on salary of seconding institution; those above 45 yrs opting to join, the 31% pension contribution cease automatically
- ❑ Employees transferred to counties owing to devolution automatically joins

# Current Enrollments



❑ As of April 2021, a total of 340,318 civil servants were enrolled into the new scheme

❑ Contribution to pension scheme 2021/22 – KES 20.8 billion

# Opportunities & challenges



- ❑ Huge opportunity to fund managers and providers of custodial services
- ❑ Brings predictability and stability on government expenditure on pensions & retirement benefits
- ❑ Huge injection into the KES 1.3 trillion (Dec. 2019) pension sector –boost mobilization of savings for investment into other sectors of the economy
- ❑ **Risk of mismanagement – meaning low investment returns for scheme members**

# Recognition –IPSAS 39



- ❑ The transition shall make it easy to account for post-employment benefits. Entity's obligation for each period is determined by the amounts to be contributed for that period – simply recognize amounts payable
- ❑ Removes ambiguity of actuarial assumptions in computing benefits under Defined Benefit schemes –with possibility of actuarial gain or loss
- ❑ Assumed risk for the government due actuarial losses will be eliminate once all civil servant are fully transitioned into the Contributory scheme

# Finally.....



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