

AFRICA CENTRE FOR RETIREMENT RESEARCH (ACRR)



POLICY RESEARCH BRIEF

ACT 766 RETIREES LUMP SUMS SHORTFALLS, POSSIBLE
ELIGIBILITY CRITERIA FOR 'TOP-UP' PAYMENT AND POLICY
IMPLICATIONS TO GOVERNMENT

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1.0 EXECUTIVE SUMMARY

Recent events and media publications on the labor front have been dominated by the Trade Union Congress (TUC) and other affiliates, who advance the argument that Lump Sums received under the new 3-tier pension law, the National Pension Act, 2008 (Act 766 as amended) have fallen short of the corresponding 25% Lump Sum (25%LS) retirees would have received under the old law (PNDCL 247).

Government has agreed to make up for shortfalls in Lump Sum for public sector workers who retired in 2020 under the new pension law, taking the 25%LS under the old law as a benchmark. Questions are, how long will these shortfalls persist and how ready will government be in absorbing this gap? What are the policy implications to government, and impact on social and economic well-being of elderly citizens? What could be the eligibility criteria for receipt of 'Top-up' payment from government?

The new pension law, by design, had the fundamental objective of delivering better value to the Ghanaian retiring workforce. Consequently, this work has compared both Monthly Pension and Lump Sum benefits under the old pension law (PNDCL 247) and under the new pension Act (Act 766), that is, ten years after its implementation. The study used a random sample of 964 pensioners who retired in 2020 under Act 766 and contributed for a minimum of 240 months.

The results of the study project that **81%** of 2020 retirees experienced shortfalls in Lump Sum when compared to the 25%LS they would otherwise have received under the old law. There were 841 Shortfalls as opposed to 123 Gains. Further statistical test (Wilcoxon signed-rank test) confirmed that there was a significant difference between the Lump Sums received under Act 766 and the corresponding computed 25%LS. The 25%LS was significantly higher than the total Lump Sum received by most retirees - Shortfalls among the Act 766 retirees were widespread and significant.

Out of those who had Shortfalls, public sector workers were the most affected - **90%** of them recorded Shortfalls as compared to **64%** of private sector workers. The reduction in benefit amount was estimated to be at **23%** for all affected pensioners in the sample.

In the case of Monthly Pension, the Monthly Pension under Act 766 exceeded the Residual Monthly Pension under PNDCL 247 by **8.65%** on average for the sample examined. Test of Hypothesis using the Wilcoxon signed-rank test proved that there was significant difference between Monthly Pension under Act 766 and PNDCL 247 – the Act 766 monthly pension was found to be higher.

Considering the Past Credit, Workers Second tier contribution, and Second Tier interest income from Fund Managers as components making up the total Lump Sums received by retirees under Act 766, the Past Credit component (paid by SSNIT under the improved interest rate) proved to be the dominant source of the total Lump Sum received by pensioners.

The research found some grievous procedural lapses in the administration of the Second Tier schemes that could deny retirees deserved Lump Sum amounts at the point of retirement or even benefit losses if they are not addressed.

We found for instance that, for the same level of second tier contributions, accrued interest income declared on individual members' Second Tier Statement of Accounts varied significantly among different Corporate Trustees (despite the existence of investment policy guidelines). In some cases, benefits were paid without members' transferred contributions from the temporary pension fund accounts (TPFA).

In addition, some Corporate Trustees paid retirees 90% of the Lump Sum due them while promising to pay the rest at unspecified times.

There are inherent root causes to the shortfalls in Lump Sums under the 3-tier pension system that if not addressed comprehensively will lead to continuous 'Top-up' payments by government long beyond 2020, widening social and economic inequalities, continuous agitations on the labor front, increased pensioner mortality (due to heart related shocks) etc.

The 3-tier pension system is fairly new and supervision in order to control investment risk and operational failures becomes more critical as these systems develop and mature. Policymakers and in particular National Pensions Regulatory Authority (NPRA) should begin to ask how their supervisory approach needs to change as response measures to the revealed Lump Sum Shortfalls under the new pension system.

Examination of the provisions under both Act 766 and PNDCL 247, as well as detailed analysis of the results have proven that retirees who contributed for at least 240 months at the point of retirement and had shortfalls may be the eligible retirees for 'top-up' benefits from government.

We recommend that the 'Top-up' payment by government should be sustained as long as Shortfalls persist and should be extended to cover Private Sector retirees as well for equity reasons.

2.0 INTRODUCTION

Following the implementation of the final phase of the National Pension Act, 2008 (Act 766 as amended) in January 2020, which saw the first full cohort of retirees in 2020 receiving benefits under the provisions of the new pension law, recent events and media publications have witnessed an outcry from unionized bodies regarding pensions and retirement benefits of workers and particularly for those retiring in 2020.

Notably, the Trade Union Congress (TUC) petitioned government to take liability for the shortage in the payment of Lump Sums to pensioners who started retiring from the year 2020 under the new pension law, **(Top up pensions of 2020 retirees – TUC, September 23, 2020, Daily Graphic, pp.1, 3)**. Daily Graphic investigation also reported that, those who received their benefits under the Act 766 got an average of three times lower than their counterparts who retired under the PNDCL 247 **(2020 Retirees worse off – they earn less under pension reforms, October 5, 2020, Daily Graphic, pp.1, 3, 20)**.

The Director General of SSNIT however attributed the observed shortfalls to transitional challenges whilst insisting that the new pension law was the best bet to deliver better value to pensioners in the long term. **(Pension reform best for workers - SSNIT, October 6, 2020, Daily Graphic, p.16)**.

Consequently, government has assured the public sector retirees of payment of shortfalls resulting from differences between 25% Lump Sum under PNDC Law 247 and total Lump Sum received under Act 766. **(Government to pay retirees Lump sum differences, October 14, 2020, Daily Graphic, pp. 1,3)**

The publication of this policy brief is informed by our assessment of the likely impact on the health, social and economic well-being of the vulnerable elderly retiring class. It is regarded as a key social protection issue and must be addressed comprehensively.

To identify the underlying factors that informed the Shortfalls, researchers evaluated and compared, based on empirical data, the retirement benefits levels under the Old Legislation (PNDCL 247) to retirement benefits levels under the new legislation (Act 766).

This work has shown that there is little room for optimism about adequate financial security for current and future retirees when important implementation and supervisory gaps are not identified and addressed.

The brief shares findings from the research with an aim to inform policy responses by decision-makers who are working on social and economic empowerment of the aged in Ghana, given that poverty protection for the elderly should be the minimum requirement for any government's pension system.

Based on the findings of the research as well as the provisions under both PNDCL 247 and Act 766, we propose to government basis of possible award of 'top-up' benefits to retirees in 2020 (and most likely 2021 and beyond) who may be significantly affected by the switch in pension regime.

3.0 RESEARCH APPROACH

3.1 Sample Size Justification

A total of 964 randomly selected data of individual retirees who contributed for at least 20 years and retired in 2020 under Act 766 were considered in the study. The study allowed for 3% margin of error with an estimated population size of 24,000 Act 766 retirees which translates into a sample size of 964 retirees.

3.2 Statistical Hypothesis Test

To compare the actual total Lump Sums received by pensioners to the corresponding 25%LS, we adopted sample related Wilcoxon signed-rank test. This is because the observed differences between the total Lump Sums received and the computed 25%LS were not normally distributed.

3.3 Computation

(a) The following were computed for each individual in the sample;

- The Monthly Pension under Act 766 and the residual Monthly Pension under PNDCL 247
- The 25% Lump Sum (25%LS) (assuming worker retired under PNDCL 247)
- The Past Credit (PC) (using quarterly interest compounding rate of full prevailing 91-day Government of Ghana T-bill rates from January 2010 to date of payment of benefit).
- The Total Second Tier contributions from January 2010 to date of last contribution prior to retirement (C).
- Gains/Interest income (I) declared by Corporate Trustees at point of payment.

(b) The difference (D), between the computed 25%LS and the sum of Past Credit paid by SSNIT (PC), Second Tier Contributions (SC) and the interest income accrued by Second Tier (I) for each pensioner was obtained for analysis.

$$\mathbf{D = 25\%LS - (PC+ SC+I)}$$

4.0 RESULTS

4.1 Comparison of Monthly Pension (Act 766 against PNDCL 247)

- Monthly Pension under Act 766 exceeded Residual Monthly Pension under PNDCL 247 by an average of **8.65%** for the sample examined.
- **8%** of the sample contributed for more than 40 years (480 months) and in such cases Monthly Pension under Act 766 is equal to Residual Monthly Pension under PNDCL 247.

4.2 Lump Sum Shortfall Status

Note that this analysis considered the computed 25%LS under the old law as a benchmark, thus all payments are compared to the 25%LS.

- **Overall, 81%** of the sampled 2020 retirees experienced Lump Sum Shortfall, whilst **19%** were better-off under Act 766. They had an estimated reduction in their Lump Sum benefit by **23%**. Further statistical test of hypothesis (using Wilcoxon signed-rank test) revealed that the Shortfalls were widespread and significant.
- **90%** of public sector workers had Lump Sum Shortfalls, whilst **10%** gained under Act 766.
- **64%** of private sector workers had Lump Sum Shortfalls, whilst **36%** gained under Act 766.

Fig 1 and 2 below illustrate the percentage of retirees who experienced shortfalls;

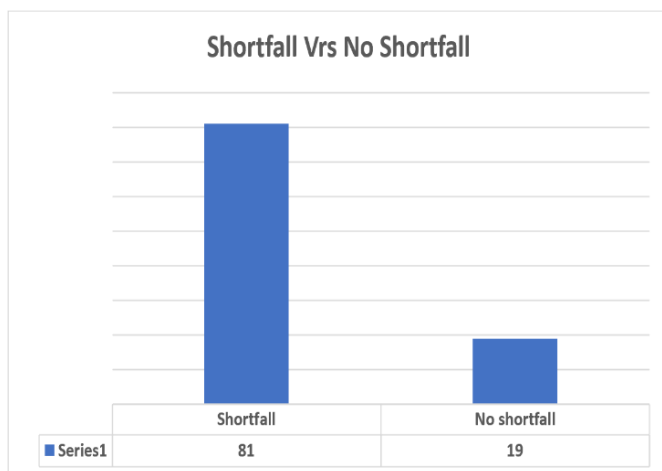


Fig 1: % of Retirees who had Shortfalls/No Shortfall

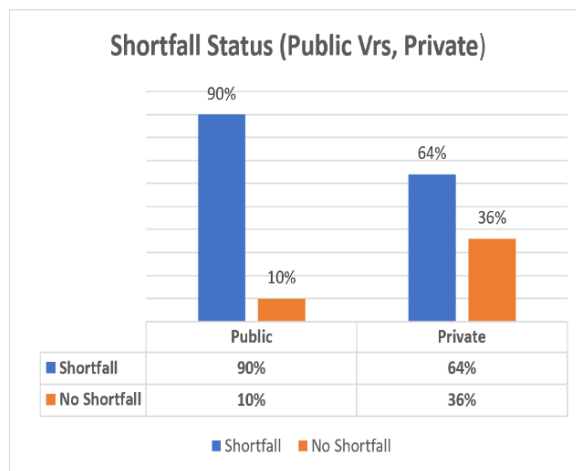


Fig 2: % of Retirees who had Shortfalls/No Shortfall by Sector

4.3 Percentage Distribution to the Total Lump Sum Received by Retirees

For the sake of clarity, the research split the total Lump Sum benefit retirees received into three main components i.e. Past Credit (PC), individuals' Second Tier contribution (SC), and Second Tier interest from Fund Managers (I).

$$\text{Total Lump Sum Received} = \text{PC} + \text{SC} + \text{I}$$

The Past Credit component (paid by SSNIT under the improved interest rate) proved to be the dominant source of the total Lump Sum received by pensioners. Evidently, **8%** of the sample had SSNIT Past Credit alone exceeding the computed 25%LS member would have received under PNDCL 247.

For retirees who experienced shortfalls in their Lump Sum benefits;

- On average, The SSNIT Past Credit contributed **41%** to the total Lump Sum retirees received.
- Members' 5% Second Tier Contributions contributed **32%** to the total Lump Sum retirees received.
- Accrued interest income by Second Tier Corporate Trustees contributed **27%** to the total Lump Sum retirees received.

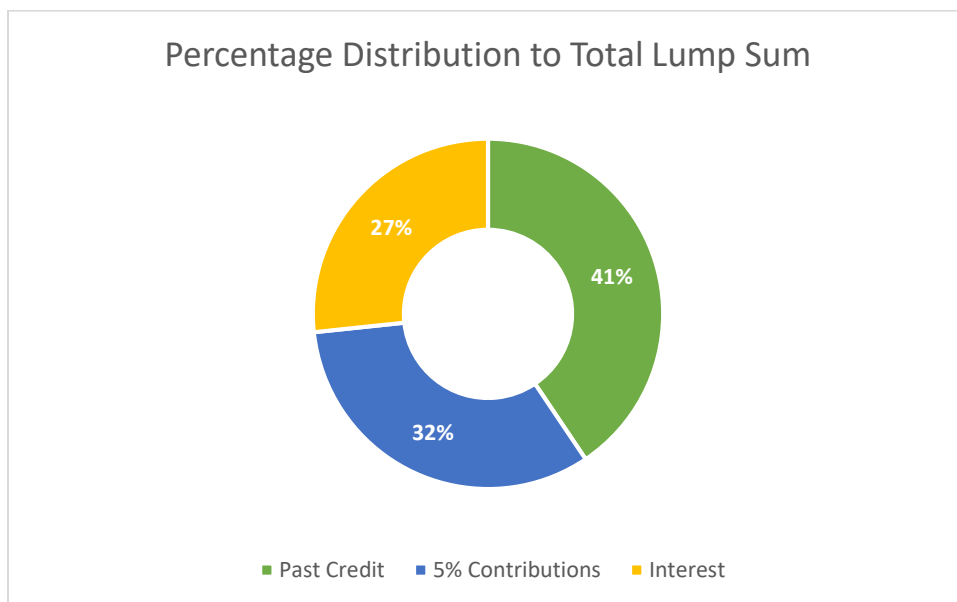


Fig 3: % Distribution to Retirees Total Lump Sum

- For those who had Shortfalls, the PC added to the Tier2 Contributions accounts for **55%** of the computed 25%LS.

5.0 RESULTS DISCUSSION

The Monthly Pension under Act 766 was always greater than the Monthly Pension under PNDCL 247 except for cases where the member contributed for more than 480 months (40 years). In such cases, the two are equal.

Shortfall in Lump Sum (D), in this case refers to positive difference between computed 25%LS and Sum of (SSNIT Past Credit and Second Tier payment)

$$D = 25\%LS - (PC + \text{Second Tier Payment})$$

8% of the sample had their SSNIT PC alone exceeding the computed 25%LS. The study revealed them to be those who worked in well-paying financial institutions and mining companies during periods prior to the year 2010. Again, the Past Credit formed the largest chunk of the Lump Sum received by individuals.

81% of the retirees in the sample received Lump Sums which were less than the computed 25%LS. This confirms that the Shortfall was widespread. The public sector workers were the most affected - **90%** of them recorded Shortfalls as compared to **64%** of private sector workers. The reduction in benefit was estimated to be at **23%** for all affected pensioners in the sample.

Additionally, for those who fell short of the 25%LS, their PC plus Tier2 Contributions accounts for **55%** of the 25%LS. This leaves a funding gap of **45%** to be absorbed by investment returns from the Corporate Trustees. The sample examined however shows that Corporate Trustees investment returns contributed on average **22%** of the 25%LS (hence the Shortfalls)

Moreover, it is worthy to note that, PC strictly speaking should not be considered as part of the Lump Sum under the provisions of Act 766. For instance, members who joined the scheme in 2010 at age 45 would be retiring in 2025 without any PC (they have no PC).

6.0 Possible Eligibility Criteria for 'Top-up' Payment

The benchmark to the Lump Sum benefit shortfall is the computed 25%LS.

The minimum number of months required to qualify for 25%LS is 240 months. Consequently, 2020 retirees who contributed for at least 240 months or more at the point of retirement and have recorded shortfalls as defined in this brief could be the worthy recipients of the Lump Sum 'Top-up'.

Conversely, members who contributed less than 240 months at the point of retirement may not be eligible for the 'Top-up' payment. The justification is that they would not have qualified for Pension and 25%LS under the old law. Instead, they would have qualified for return of contributions plus interest income as benefit (Old-age Lump Sum).

Under the Act 766, workers who contributed less than 240 months qualify for Pension and their pensions are guaranteed for 15 years. The Present Value of the 15-year guaranteed pension (under Act 766) is far greater than the net Old-age Lump Sum they would otherwise have received under the old law in all cases.

7.0 CONCLUSION

By the design of the 3-tier pension system, the Lump Sum paid to retirees at retirement is intended to be a major source of retirement income. Strictly speaking, it is made up of members' contributions plus investment returns, hence the rate of return is critical to the ultimate Lump Sum amount. NPRA Annual reports for 2018 and 2019 suggest that private pension assets for benefits continue to grow. The growth in pension assets, according to the reports, was attributed to impressive performance of private pension funds.

This study however found that investment interest income contributed the least (**27%**) to the total Lump Sum received. In addition, investment interest income was expected to account for **45%** of the computed 25%LS in order to achieve equilibrium between the old and the new pension regimes. In actual terms, it contributed **22%**, hence the Shortfall. This therefore questions the correlation that must exist between market performance and interest income declared on contributors Statement of Accounts. NPRA supervisory approach should focus on the processes that translates investment performance of Corporate Trustees to declared interest income as output. The approach should as well check for insider-trading, given that most Corporate Trustees are commercial financial institutions - conflicts of interest can therefore exist between the fiduciary duty to act in the best interest of contributors and making profits for shareholders. The regulator could also minimize investment risk faced by the contributor by instituting minimum investment performance guarantees for Fund Managers (during pension reforms) – quantitative investment limits measures are not enough!

A review of the NPRA Annual Reports for 2018 and 2019 shows that the supervisory regime is doing its bit in protecting the interest of contributors by controlling operational risk (evidenced in flagging down some Corporate Trustees) and investment risk by the release of investment policy guidelines.

There are however, obvious procedural and supervisory gaps that need to be attended to, considering that a significant **49%** of the sample indicated that they did not understand how the second tier payment was determined, **32%** indicated that they simply completed forms and later received payment without any receipt or knowledge of content of their Statement of Accounts, some retirees received part payment of their Lump Sum benefit, others received Lump Sum benefits without transfers from the TPFA Accounts, accrued interest income declared on members' Second Tier Statement of Accounts varied significantly among different Corporate Trustees (for the same level of contributions). Under Defined Contribution arrangement, the risk is borne by contributors (investment and operational risks) and the research has assessed this to be high and therefore requires the supervisory authority to update his oversight supervisory approach.

The research predicts that Lump Sum benefit Shortfalls may persist longer than expected and many retirees would be denied deserved retirement benefits if the supervisory authority does not consider reviewing its monitoring mechanism. Generally, in Defined Contribution schemes, outcomes (investment interest income) are determined by the efficiency of the processes used to measure and manage investment and operational risks facing contributors. More directly, such processes should ensure optimum market performance as well as accurate crediting of members' contributions and interest income.

The study particularly found that lack of transparency and member education with appropriate disclosure requirements by Corporate Trustees (as required by OECD guidelines 2003) leads to inaccurate Lump Sum Payments and potentially benefit losses.

1.0 POLICY RECOMMENDATIONS

- (1) Not all retirees in 2020 should receive “top-up” but only those with Shortfalls.
- (2) The “Top-up” should not be limited to only Public Service retirees but also retirees in the Private sector (for equity reasons).
- (3) At most, 3% of the established shortfall should be added to the actual difference for each retiree in order to cater for time value of money, and to reinforce the objective of the 3-tier pension system.
- (4) The “Top-up” should continue after 2020 up till the anomaly has corrected itself (that will surely happen after some years).
- (5) Government should consider amending the law to include minimum investment performance guarantees for Fund Managers in order to minimize investment risk contributors have to bear.

UP NEXT:

- **Covid-19 among the Pensioner Population: Assessing the impact on Individuals' Expenditure on Medical Care, Policy Responses.**