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REFORMING KENYA'S LEGAL REGIME ON STATE PENSIONS FOR THE JUA-KALI SECTOR

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DECEMBER 2018

DECLARATION

STUDENT'S DECLARATION

I, hereby declare that this thesis is my original work and has not been previously published or presented for award of any degree in any other university or any other examination body. No part of this thesis should be reproduced without my consent or that of University of Nairobi.

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The thesis has been submitted for review with my approval as university supervisor.

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I acknowledge my supervisor Dr. Njaramba Gichuki for his invaluable insight in this thesis.

DEDICATION

I dedicate this thesis to my lovely family - I thank you for your support and constant encouragement to pursue higher education.

ABSTRACT

Prior to enactment of the NSSF Act 2013 - which is the law that sets up the Kenyan state pension scheme (the National Social Security Fund "the NSSF") - the antecedent law was the NSSF Act 1965. The NSSF Act 1965 mainly focused on the formal sector, leaving out the informal jua-kali sector persons in structured pension arrangements. This was a major problem given that this group is characterized by low income, with vulnerability to economic volatility and change. This was the genesis of low uptake of state pensions among persons in the jua-kali sector. However, the enactment of the NSSF Act 2013 shows the Kenyan Government's intent to improve pension coverage among persons in the jua-kali sector. Despite this noble initiative, there exists legal issues in the legal regime governing the NSSF, which hinder participation by persons in the jua-kali sector.

For instance, the NSSF Act 2013 lacks incentives that target the jua-kali sector such as flexibility in contributions and withdrawals. The NSSF also suffers from excessive government control and interference in its activities, as a result of its governance structure. This leads to mal-practices and lack of adherence to the provisions of the Retirement Benefits Act 1997. A case in point is the NSSF's lack of observance of statutory administrative fees, resulting in high administrative expenses and low investment returns to a pensioner. Therefore, the excessive government control and interference in NSSF affairs, makes it difficult for Retirement Benefits Authority to perform its regulatory and supervisory duties. Conversely, the government has demonstrated less enthusiasm for the annuities insurance market as compared to the NSSF, leading to unattractive annuity product prices to the detriment of pensioners. Notwithstanding challenges in the

annuities market, the government still requires income tax on investment in annuities, also to the detriment of the pensioners.

This study therefore draws its recommendations from South Africa, India and the Code of Corporate Governance for State Corporations in Kenya – Mwongozo 2015.

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The Retirement Benefits Regulations2000.

Universal Declaration of Human Rights.

CHAPTER ONE

INTRODUCTION

1.0 Background of the Study

There are a number of Statue laws that have evolved to govern state pension in Kenya. These are, the National Social Security Fund Act 2013,[1] the Retirement Benefits Act 1997,[2] the Insurance Act[3] and the Income Tax Act.[4] These laws currently contain provisions that hinder participation by the jua-kali sector, as elucidated in chapter three.

First, the National Social Security Fund Act 1965 ("the NSSF 1965), which is antecedent to the NSSF Act 2013, was the first legal regime to govern state pension in Kenya. Its evolutionary process is discussed in detail in chapter two. Secondly, the RBA 1997 is the law that regulates all public and private pension schemes in Kenya, with the exception of the civil service pension scheme. The RBA 1997 was enacted with a view to bring sanity to the pension industry, which was largely unregulated.[5] Among the problems that the pension industry faced includes: mismanagement of schemes' funds; the schemes were not adequately funded; the arbitrary investment of funds without independent professional advice and records and books were not well kept.[6]

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[1] The National Social Security Fund Act, Number 45 of 2013 ("the NSSF Act 2013).
[2] The Retirement Benefits Act (No.3 of 1997), Chapter 197 of the Laws of Kenya ("the RBA 1997").
[3] The Insurance Act, Chapter 487 of the Laws of Kenya (the Insurance Act).
[4] The Income Tax Act, Chapter 480 of the Laws of Kenya, s 3(2)(c)(i).
[5] Pension Industry in Kenya: Recent Changes in the Regulatory Framework <http://www.natcomreport.com/kenya7/livre/pensions.html> accessed 30 June 2016.
[6] Ibid.

In the absence of a regulatory framework, the pension industry was characterized by lack of protection of the interests of members (employees) and dominance of sponsors (employers) in pension scheme affairs. In addition, many schemes were run through insurance companies that tended to operate in a non-transparent manner. As a result, investment decisions were in many cases made in the best interest of vested parties and not in the interest of pension scheme members or of the Kenyan economy as a whole.[7] The RBA 1997 was therefore enacted to provide a regulatory framework for the pension industry. This regulatory framework was necessary to streamline the pension industry and gain the required confidence from stakeholders and employees. Moreover, the regulatory framework was necessary to enable employees save more for retirement and contribute towards the national effort of raising the domestic savings rate.[8] The RBA 1997 created the Retirement Benefits Authority to oversee the pension industry's management and development, in a prudent and appropriate manner. The said Authority's operations are vested in an independent board of directors with a majority private sector representation and the autonomy to run the pension industry without undue state interference.[9] The RBA 1997 also has detailed regulations for effective management of schemes.[10]

Thirdly, the Insurance Act is the law regulating the insurance industry. The said Act intertwines with the law on pensions due to the element of annuity.[11] In Kenya, annuity first featured in

[7] Ibid.
[8] Ibid.
[9] Ibid.
[10] These regulations are the Retirement Benefits (Individual Retirement Benefit Schemes) Regulations, 2000; the Retirement Benefits (Occupational Retirement Benefits Schemes) Regulations, 2000 (the Occupational Regulations 2000); the Retirement Benefits (Managers and Custodians) Regulations, 2000; the Retirement Benefits (Administrators) Regulations, 2000 (the Administrators Regulations 2000); the Retirement Benefits (Minimum Funding Level and Winding-up of Schemes) Regulations, 2000; the Retirement Benefits (Tribunal) Rules, 2000; the Retirement Benefits (Transitional) Regulations, 2000; the Retirement Benefits (Forms & Fees) Regulations, 2000; and the Retirement Benefits (Mortgage Loans) Regulations, 2009.
[11] Annuities are retirement products offered by insurance companies in Kenya, in the form of contracts which are sold to individuals by life insurance companies to provide a guaranteed income from the date of purchase (or coming into effect for deferred annuities) until death.

pensions due to an amendment to the RBA 1997 in 2005.[12] The amendment sort to compel retiring members of occupational schemes operated as pension schemes, to invest two thirds of their accumulated retirement savings in annuities (exceptions being available for those permanently migrating away from Kenya, those with terminal illness and those whose pension earnings are considered trivial).[13]

Annuities are now more important than ever before, in light of the NSSF Act 2013. The NSSF Act 2013 requires a beneficiary of the jua-kali sector member, upon his death to purchase annuity on survivors' pension.[14] A survivors' pension is an amount to be paid if a jua-kali

member dies before pensionable age and was contributing to the NSSF Provident Fund, at the time of his death.[15] The NSSF Act 2013 further requires its deceased member to have made not less than thirty six (36) monthly contributions.[16]

Lastly, the Income Tax Act came into operation on 1 January 1974 and has undergone a number of amendments since then. This is the law that makes provision for among other things, the charge, assessment and collection of income tax in Kenya. Currently, the Income Tax Act requires tax to be paid on investment income derived from annuities.[17]

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[12] Keizi Lazarus, *Annuities Markets in Kenya*: 'Problems and Possible Solutions,' (Policy Working Paper, Retirement Benefits Authority June 2007) 3.
[13] Amos G. Njuguna, *Competition in the Financial Services Sector: 'A Case of Kenyan Annuities Market'* (2014) 10, 04 International Journal of Business and Social Research 83.
[14] The NSSF Act 2013 (n1) s 43.
[15] Ibid, s 37.
[16] Ibid.
[17] The Income Tax Act (n4), s 3(2)(c)(i).

1.1 Statement of the Problem

The low uptake of state pension by the jua-kali sector in Kenya has its genesis in the NSSF Act 1965, which focused on the formal sector. However, despite the introduction of the NSSF Act 2013, there still exists legal challenges, which perpetuate the low uptake of state pension among the jua-kali sector. Equally, other statue laws governing the NSSF such as the RBA 1997, the Insurance Act and the Income Tax Act, contain provisions which continue to be responsible for low uptake of state pension by the jua-kali sector. For instance, the NSSF Act 2013 lacks incentives such as flexibility in contributions and withdrawals, notwithstanding that the jua-kali sector comprises a number of categories. The NSSF also suffers from excessive government control and interference in its activities, as a result of its governance structure, leading to mal-practices and lack of adherence to the provisions of the RBA 1997. A case in point is the NSSF's lack of observance of the statutory administrative fees leading to high administrative expenses and low investment returns to a pensioner. Therefore, the excessive government control and interference, makes it difficult for Retirement Benefits Authority to perform its regulatory and supervisory roles. Conversely, the Kenyan Government has demonstrated less enthusiasm for the annuities insurance market as compared to the NSSF. This leads to unattractive annuity product prices to the detriment of pensioners. Moreover, the government, through the Income Tax Act, still requires income tax to be paid on investment in annuities to the detriment of pensioners.

1.2 Significance of the Study

The findings of this study hope to be of benefit to the Kenyan Parliament to aid in legislative reform on the laws concerning the retirement sector for the benefit of the jua-kali sector. The findings may also be used as a source of reference for other researchers. In addition, academic researchers may need the study findings to arouse further research in this area and as such form a good background for further researches.

1.3 Objective of the Study

The specific objectives of the study are:

1.3.1 To investigate the low uptake of the state pension among jua-kali sector persons in Kenya.

1.3.2 To investigate the legal issues in the legal regime governing state pension, that hinder participation by jua-kali sector persons in Kenya.

1.3.3 To investigate the social security systems of jurisdictions with similar social security systems to Kenya.

1.3.4 To give proposals to the Kenyan parliament to review and amend the laws governing state pension in Kenya, in a bid to promote participation among the jua-kali sector.

1.4 Research Questions

1.4.1 Whether or not there is low uptake of state pension among the jua-kali sector in Kenya.

1.4.2 Whether or not there are legal issues in the legal regime governing state pension that hinder participation by jua-kali sector persons in Kenya.

1.4.3 Whether or not Kenya can learn from the social security systems of similar jurisdictions and the soft law for state corporations in Kenya.

1.4.4 Whether or not the Kenyan Parliament can review and amend the statue laws that have evolved to govern state pension in Kenya based on recommendation presented in this study.

1.5 Research Hypothesis

1.5.1 There is low uptake of state pension among the jua-kali sector persons in Kenya.

1.5.2 There are legal issues in the legal regime governing state pension that hinder participation by jua-kali sector persons in Kenya.

1.5.3 Kenya can learn from other jurisdictions with social security systems similar to itself in addition to the soft law for state corporations in Kenya.

1.5.4 The Kenyan parliament will find this study useful to review and amend laws governing state pension in Kenya, in a bid to promote participation among jua-kali sector persons in the NSSF.

1.6 Research Methodology

1.6.1 Research Design

This study utilizes the descriptive survey design technique, particularly the use of secondary information, gathered from different works by scholars and professionals, desktop research and case studies.

1.6.2 Research Instruments

The main research instrument for this study will encompass secondary data which will be obtained from books, journals, dissertations and the internet.

1.6.3 Data Collection Procedures

The method of data collection is library research and desktop research.

1.7 Scope of the Study

The expected limitation of the study is lack of accessibility of up-to-date information from the NSSF, in addition to reserved information from the Retirement Benefits Authority as regards the NSSF.

1.8 Theoretical Framework

This study cuts across two (2) theories; the theory of justice by John Rawls and the theory of economic regulation as propounded by George Stigler.

Rawls belongs to the social contract tradition similar to Hobbes, Locke, Rousseau and Kant. However, Rawls' social contract takes a different view from that of previous thinkers. Specifically, Rawls develops what he claims are principles of justice through the use of an artificial device he calls the original position in which everyone decides principles of justice from behind a veil of ignorance. This "veil" is one that essentially blinds people to all facts about themselves so they cannot tailor principles to their own advantage.[18]

The first principle of justice is that each person is to have an equal right to the most extensive basic liberty compatible with a similar liberty for others. These basic liberties as he states are the political liberty to vote and run for office, freedom of speech and assembly, liberty of conscience, freedom of personal property and freedom from arbitrary arrest. On the other hand, the second principle of justice indicates that social and economic inequalities are to be arranged so that: they are to be of the greatest benefit to the least-advantaged members of society (the

[18] John Rawls, *A Theory of justice:* 'The Original Position (Belknap Press: An Imprint of Harvard University Press, 2nd Edition, 1999) 1.

difference principle); and secondly, offices and positions must be open to everyone under conditions of fair equality of opportunity.[19]

Rawls' theory of justice is relevant, as this study is of the view that the jua-kali sector, being a sector that is characterized by low and irregular income, require incentives to enable them effectively participate in an opportunity for old-age income. Among the incentives are flexible withdrawal and contribution terms among others to be detailed in this study. The government intervention will in turn increase the NSSF membership coverage, which translates to reduction in old-age poverty of a group, which would ordinarily be unable to access old-age income, due to socio-economic inequalities in Kenya.[20]

A major challenge to social theory (like Rawls theory) is to explain the pattern of government intervention in the market ("economic regulation.").[21] This is answered by the theory of economic regulation as propounded by George Stigler.[22] The theory is based on two simple but important insights. The first is that since the coercive power of government can be used to give valuable benefits to particular individuals or groups, economic regulation -the expression of that power in the economic sphere- can be viewed as a product whose allocation is governed by laws of supply and demand. The second insight is that the theory of cartels may help us locate the demand and supply curves. The theory of cartels illuminates both the benefit and the cost side.[23]

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[19] Ibid.
[20] Ibid.
[21] Richard Posner, *Theories of Economic Regulation*, (2007) 5(2) The Bell Journal of Economics and Management Science 335.
[22] George J. Stigler, *The Theory of Economic Regulation, (1971) 2(1)* The Bell Journal of Economics and Management Science 1.
[23] Ibid.

Therefore, the afore-mentioned theories, in my view, are relevant to this study as they explain the need for government intervention in the legal regime governing state pension. The need for government intervention is to increase its state pension coverage, for the benefit of persons in the jua-kali sector, who due to their socio-economic status do not prioritize pension. This is regardless of the benefit of an old-age income during retirement. This government intervention will in turn lead to economic development of the country.[24] This is because pension fund assets are invested in government securities which assist the government achieve the country's economic goals.

1.9 Literature Review

1.9.1 State Pension Schemes

The International Labour Organization (ILO) in examining pension schemes in developing countries observed in general that pension schemes in Africa are very weak and badly managed. The report identifies five main causes for failure of pension schemes in developing and reforming countries to provide wide coverage. For example, in many developing countries, the majority of people work in the informal sector or in rural regions that provide few or no benefits or worker protection of any kind. Further, employees in small companies (with ten or less employees) are often excluded from participation in social security pension schemes. Moreover, many pension schemes in existence are badly managed, with the consequence that they have overly high administrative costs and do not deliver benefits when they should. Also, many schemes are unable to collect contributions from all the people that should pay into them, which leads them into financial deficit. Lastly, many schemes are based on weak and unregulated financial systems and may be open to corruption. The writers broadly conclude by noting that

[24] Ibid 334.

there have been improvements in provision of old age pensions in terms of extension of coverage and in the improvement of benefits. The writers further reiterate that the task is only half complete as an overwhelming majority of the world's population is still without some form of income security in old age or disability.[25]

In Ghana, Kumado and Gockel studied the Ghanaian state pension scheme and noted that the current state scheme in Ghana unlike the antecedent one is more encompassing in terms of coverage. The current law on state pension provides that the scheme is open to all classes of employees, both in the formal and informal sector of the economy, inclusive of the jua-kali sector who may opt to join the state pension scheme.[26] The writers go ahead to state the problems facing the state scheme as poor investments, negative rates of returns on overall investment portfolio, excessively high administrative costs, low coverage with marginalization of the informal sector, excessive government control and interference in the activities of the scheme.[27]

The writers are however categorical that despite problems faced by the Ghanian state pension scheme, privatization is not the way forward. He gives examples of the United Kingdom[28] and the United States of America,[29] of private dishonesty in pension management. In overall

[25] Ninety per cent of World Excluded from Old Age Pension Schemes (ILO) < http://www.ilo.org/asia/info/public/pr/WCMS_BK_PR_19_EN/lang--en/index.htm > accessed 24 June 2016 <http://www.ilo.org/public/english/standards/relm/ilc/ilc89/pdf/rep-vi.pdf> accessed on 24th June, 2016.
[26] Kofi Kumado & Augustine Fritz Gockel, *A Study on Social Security in Ghana* (Faculty of Law, University of Ghana Legon, 2003) 11 < http://library.fes.de/pdf-files/bueros/ghana/50022.pdf> accessed 24 June 2016.
[27] Ibid 27.
[28] Robert Maxwell siphoned at least 400 million pounds from various employee funds in the United Kingdom.
[29] Various scams have affected private pensions to the extent that Government was forced to use between $ 200-500 billion of taxpayers' money, to bail out these private companies and to ensure that depositors receive their pensions.

conclusion, the writers state that Ghana can draw from Swiss Chilanpore (Switzerland, Chile and Singapore) experiences, in improving the pension system in Ghana.[30]

Equally, Bhattacharya in examining pension among the informal sector in India, noted that people from the organized sector (comprising 6.5% of the working population) enjoy proper social security measures as opposed to people from the unorganized sector.[31]

1.9.2 Role of State Pension in Poverty Reduction

Ousmane Faye, explores the feasibility of introducing in sub-saharan countries like Kenya, a minimum income for old age, independent of the workers history of earning. The writer draws evidence from the Senegalese household income-expenditure data survey. The writer indicates that Senegal like in most African countries has a very small coverage rate of the social protection system; the rest of the population relying on social network support.[32] The writer concludes by indicating that, basic pension benefits have sizeable impact on poverty reduction amongst households with elderly members, which he says translates into large decreases in aggregate poverty measures. The paper goes on to indicate that the key challenge is to appropriately identify the poor households with elderly persons and deliver benefits effectively and in due time. The writer further indicates that these pensions can play an important role in encouraging economic activities and human capital accumulation. For example, available evidence from

[30] Kumado & Gockrel (n26) 26.
[31] Prakash Bhattacharya, *Micro pension Plan*: 'Indian Perspective' (Presented at the living to 100 and beyond Symposium, Society of Actuaries 2008) 6.
[32] Ousmane Faye, *Basic Pensions and Poverty Reduction in Sub-Saharan Africa*,' (HEC Management School, University of Liege, CREPP Working Papers 2007) 4.

South Africa shows that pensions have improved children's outcomes and have also favored a rise of female labor force participation.[33]

A study by Subbarao and Kakwani examined the role of social pensions for the elderly while focusing on fifteen low income Sub Saharan countries, with Kenya featuring on the list. The study found that a universal social pension for all of the elderly above sixty five (65) years of age would cost about two per cent of gross domestic product, a level comparable to, or higher than, the current levels of spending on health care. The writers indicate that increasing the age cut-off to 70+ or 75+ might lower costs, but few would be eligible for the pension, and it would have little impact on poverty reduction at the national level. The study found however, that there is a case for a non-contributory social pension to some of the elderly in all the fifteen focused countries.[34]

Barbone and Sanchez examined social security in Africa - with the exception of Mauritus, Botswana and to a certain extent South Africa, countries which provide universal pension coverage for all its population.[35] The writers observe that formal social security systems in Africa are at present a prerequisite of the middle class. The writers go further to indicate that there is need to improve governance of business for existing formal social security institutions, which have all too often failed to deliver on promises to their members due to mismanagement (and sometimes outright pillage) of assets.[36] The main tasks involve increasing transparency,

[33] Ibid 18.
[34] Kalanidhi Subbarao and Nanak Kakwani, *Ageing & Poverty in Africa & the Role of Social Pensions*,' (Social Protection Discussion Paper Series Number 0521, 2005) 35.
[35] Luca Barbone and Luis-Alvaro Sanchez, *Pension & Social Security in Sub-Saharan Africa Issues and Options*, (A Paper presented at the XIII International Social Security Association African Regional Conference, Accra, Ghana 6-9 July 1999) 1.
[36] Ibid 1.

curtailing opportunities for corruption, and most importantly protecting beneficiary rights. The writers go further to indicate that an important component of improving governance is the creation of protective barriers around the social security organizations, to prevent undue interference from outside interests, facilitate precise allocation of responsibilities and their oversight and enforcement; the creation or strengthening of regulatory institutions being an important step in this direction.[37]

The writers further observe that formal social security institutions need increased membership to thrive. They indicate that this will not be possible if an adequate set of incentives is not in place. In conclusion, the writers emphasize on the need for pension systems to be fully funded because of reduced fiscal risk and improved savings.[38]

1.9.3 Should the Jua-kali Sector be Compelled to Contribute to a State Pension Scheme?

Hu and Stewart examined whether state pension by the jua-kali sector should be mandatory or voluntary. The writers observed that in developing countries - particularly those with the lowest income levels - there is always a group of population whose main challenge is to meet basic needs, for example food, clothing and housing. For instance, in South Africa, one survey study shows that for poorer households with savings in South Africa, emergency needs, food, and funeral costs are the three most important reasons for saving, while retirement is only considered the eighth most important.[39] They further observed that it would be very difficult (if not impossible) for governments to undertake any meaningful actions to bring these individuals into

[37] Ibid 35.
[38] Ibid 2.
[39] Yu-Wei Hu and Fiona Stewart, *Pension Coverage and the Informal Sector Workers: International Experiences*, (OECD Working Paper on Insurance and Private Pensions No. 31, OECD Publishing January 2009) 8.

formal pension systems. The conclusion is that such developing countries should provide social assistance to all of the poorest elderly, on a non contributory basis.[40]

Laiglesia, also in looking at developing countries noted that statutory contributory schemes in developing countries mostly cover employees and sometimes their dependants. The jua-kali sector workers sometimes have access to social security systems on a voluntary basis resulting in low coverage rates.[41] The writer goes further to note that incorporating informal workers into the social protection system is a necessity, a challenge and an opportunity. Despite their being non-poor, many workers in these "middle sectors" are vulnerable and can fall into poverty in times of crisis.

The writer goes ahead to suggest three different general strategies to help cover the missing middle.[42] The first consists of generalizing unbundled contributory instruments with limited risk pooling. By limiting the amount of risk pooling, entitlements are brought in line with contributions, which helps limit adverse incentives for informality.[43] A second strategy consists of drawing workers into contributory systems by subsidizing their contributions.[44] A case in point being West Bengal in India which has a provident fund designed to cover workers in the informal ("unorganized") sector and is means-tested. Although not as yet integrated into India's New Pension Scheme, the defined-contribution character of the scheme makes portability and integration easier.[45] The third strategy is seen in Thailand's introduction of a universal coverage

[40] Ibid 3.
[41] Juan R.de Laiglesia, *Coverage gaps in Social Protection: What Role for Institutional Innovations?* (OECD Development Centre January 2011) 4.
[42] Ibid 19.
[43] Ibid 19.
[44] Ibid 21.
[45] Ibid 22.

scheme in 2001, to extend coverage to all uncovered citizens – workers in the public sector and in private enterprises with more than 20 employees were already covered by occupational schemes. This compulsory universal coverage scheme helped Thailand reach coverage rates of 98 percent by 2007 (ILO, 2010).[46]

1.9.4 Informal Work Force and Social Security

Chen reviewed available national data for the Middle East, North Africa, Latin America, Asia, and sub-saharan Africa regarding informal employment and social protection. She pointed out that the informal workforce is unregulated by the respective regions, untaxed, and also unprotected. In other words, the self-employed and informal wage workers do not have the legal or social protection that their counterparts in the formal sector have. She continued that the self-employed in the informal sector are independent and as a result, are ineligible for employer-based pension schemes. Chen also stated that workers in the informal sector could not afford to save for pension funds as most of them do not have disposable income to commit to a contributory pension scheme. She concluded that the respective states could extend contributory pension schemes to informal sector workers, who could afford to make contributions and simultaneously, through means-tested schemes, determine those who could not afford and subsidize their contributions accordingly.[47]

[46] Ibid 22.

[47] Afenyadu Akpene, *Official Retirement Can Wait:* 'A Study of Petty Traders in Ghana to Identify Barriers to Participation in ISF Pension Scheme,' (A thesis presented to the University of Guelph, Ontario, Canada, May 2014) 10.

1.9.5 Uniqueness of Pension Systems

Dostal and Cassey examined the need for a country to undertake pension reforms according to its circumstances, with Nigeria as a case study. They argued that the Nigerian Authority saw the Chilean reforms to be emulated and copied but she failed to learn the lessons of Chile.[48] In fact, at the time Nigeria was copying, 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 made. Therefore, it was advocated that to realize the claims, other reforms were also required to complement or precede pension reforms.[49] In conclusion, the writers recommend that before a country adopts a pension system from another, there are two issues for consideration. These are: whether the infrastructure exits that permits the operation of such a system and, yet more fundamentally, whether such a system is appropriate for the needs of a country.[50]

1.9.6 Law on Annuities

Stewart addresses why the annuity markets remains underdeveloped in many OECD countries (of which Kenya is part). Among the issues identified are that insurance companies are increasingly unwilling to offer annuity products at attractive prices due to the risks (liquidity risk, investment risk, longevity risk ecetera), In addition, few re-insurance companies are prepared to take on their risks, due to difficulties in forecasting mortality. They also face the

[48] Dostal, Jorg Michael and Casey, Bernard .H, *Pension Reforms in Nigeria:* 'How not to learn from others,' (57th Political Studies Association, Annual Conference 11-13 April, 2007, Bath).
[49] Ibid 3.
[50] Ibid 22.

challenge of having trouble finding assets to match the liabilities represented by the annuity product they sell.[51] Further, these annuity providers face solvency issues, which have the capacity to affect annuity supply. Also, complexity of the product was seen to affect the uptake of annuity products stemming from surveys across countries. In addition, individuals complained about the lack of flexibility in annuity products - from a lack of ability to vary income levels and the timing when they must be purchased, to the inability to bequest assets to survivors.[52] Yet another challenge is the lack of understanding of the different annuity products. Lastly, annuity products face tax disadvantages as a result of regulation.[53]

In conclusion, the writer gives policy options which exist for encouraging annuity markets to develop. These include, improving the mortality tables and forecasting, asset liability matching, risk pooling, solvency regulations which should not be too strict as to limit supply, regulation to encourage competition among annuity providers, financial education and awareness of annuity products and their benefits, regulation to ensure that taxation of annuities is at least as favourable as other options in the pension pay-out phase. The writer importantly notes that mandatory annuitization may be more appropriate where a well-developed annuities industry exists[54]

In Kenya, Amos Gitau, on examining annuities market, looked into a number of challenges facing the annuities market. For example, notwithstanding the number of companies dealing with life insurance products, the market is highly concentrated with four companies controlling over

[51] Fiona Stewart, *Policy Issues for Developing Annuities Markets*, (OECD Working Papers on Insurance and Private Pensions, No. 2, OECD Publishing 2007) 4.
[52] Ibid 5.
[53] Ibid 6.
[54] Ibid 6-9.

90% of the market share.[55] The writer went on to indicate that the main contributors to acquisition and protraction of market power are: the enabling retirement regulation, the long-term irreversible nature of the annuity contracts, absence of close substitutes in provision of retirement income, collusion between the pension fund administrators and the firms providing annuities and lack of differentiation of the products.[56] As a result, high concentration market leaders conduct themselves in such a way that they protect their market shares, while market followers adopt aggressive strategies to capture the elusive market share. The strategies include, creation of mergers and strategic partnerships, offering low returns to annuitants, information asymmetry, low bargaining power of the consumers, diseconomies of scale and lack of innovation.[57]

The writer indicates that other problems facing annuity providers relate to adverse selection and mortality risk associated with mortality improvements, interest rates, reinvestment and inflation risk. Other challenges include the use of outdated tables that fail to reflect the modern market conditions, governance issues in the management of the insurance companies and mispricing. These risks threaten the solvency of the companies forcing them to adopt protective policies that could be eventually harmful to the overall industry.[58] The writer concludes by calling for regulation in the annuity market, to protect the consumers in the presence of market inefficiencies, so as to ensure fair pricing and healthy competition.[59]

[55] Amos Njuguna (n13) 87.
[56] Ibid.
[57] Ibid 87-88.
[58] Ibid 87.
[59] Ibid 88.

Rocha examined annuities in Chile, where he noted that the successful development of an active annuity market was not only supported by the new pension system, but other factors as well. For instance, the restrictions that have been applied to lump-sum withdrawals, the offer of inflation-protected annuities, in addition to the robust prudential regulation of providers. The writer notes that as a result of the increased demand for annuities, government came in to provide regulation as evidenced in the 2008 Chilean pension re-reforms: the government provided a guarantee in the case of insurance company failure.[60] The writer goes on to indicate that, in an effort to reduce the influence of brokers in the selection of annuities, the government came up with a new quotation system, known as *Sistema de Consultas y Ofertas de Montos de Pension* (SCOMP). The aim is to enhance the quality of information available to consumers as well as to enable direct access to a full range of annuity quotations.[61]

The new quotation system became effective in August 2004. Early experience showed an increase in the average number of quotations, an increase in price competition as the final selection of provider has been closely associated with the ranking of quotes and a reduction in commissions to 2.2 percent. The writer concludes by indicating that the Chilean annuitants have generally received a better deal than annuitants in other countries, especially considering that Chilean annuities are indexed to inflation. This result is explained, at least in part, by the larger supply of inflation-indexed instruments in Chile, including not only indexed government bonds, but also other higher-yield fixed-interest instruments that allow providers to hedge inflation risk, while obtaining more attractive returns.[62]

[60] Roberto Rocha and Craig Thorburn,, *A Summary and Update of Developing Annuities Markets: 'The Experience of Chile'* (Non-Bank Financial Institutions Group June 2010) 10.
[61] Ibid.
[62] Ibid 21.

James and Sane, in their analysis of the annuities market in India, pointed out several key weaknesses in the annuities market. For example, low rates of participation by the public, absence of a well developed mortality table, a small number of providers, and limited product innovation.[63] In conclusion, the writers recommend that better data are needed on expected mortality rates of different sub-groups within the diverse Indian population, and on probable improvements in these rates over time. Also, long term financial instruments, including long term government bonds (possibly price-indexed) must be further developed, to enable insurance companies to match the long term liabilities implied by annuities. In addition, investment regulations and regulatory authority should be modernized. Furthermore, new products, including variable (participating, for-profit) annuities with and without floors, need to be constructed to attract consumers with diverse preferences for risk. This, in turn implies more complex standards and regulations and mechanisms should be developed for dispersing information about products and payouts offered by various insurance companies, as they enter the market.[64]

A paper presented to facilitate discussion in South Africa, noted two forms of annuities in South Africa that is, conventional annuities and living annuities. Conventional annuities provide an income for life, guaranteed by an insurance company or a pension fund, regardless of how long the purchaser lives. Living annuities on the other hand, are similar to a bank account: purchasers bear the risks of the underlying assets and the risk that they will outlive their assets. The paper indicates that by 2011, fewer individuals were choosing to buy conventional annuities - the only

[63] Estelle James and Renuka Sane, *The Annuity Market in India: 'Do Consumers get their Money's Worth? What are the Key Public Policy Issues* in Rethinking Pension Provision in India, S.A. Dave, Robert Palacios and Gautam Bhardwaj G & 2 others (eds) (New Delhi 2003) 5.
[64] Ibid 29.

products offering longevity protection and instead opting for the latter. The paper further noted that demand for conventional annuities is probably reduced by the protection afforded by public old-age pensions.[65]

The paper further noted that the means test could also discourage people from purchasing conventional annuities with provident fund money. The paper states that the fore-going might encourage low-income workers to choose living annuities and withdraw their assets quickly in order to qualify for the grant at a later date.[66] Other reasons why individuals may not purchase life annuities in South Africa is: If low-income workers expect to die soon after stopping work, they could perceive – correctly – that annuities represent poor value. Another reason is that individuals can pool mortality risk privately, with their spouse and families, and other informal support networks. Further, retirement money from one family member could be used to invest in the education or health of younger members. Once they are earning, they would in return support the retiree.[67]

The paper indicates the minimum requirements for a functioning market in conventional life annuities as: A supply of high-quality long-term bonds that insurers can use to back their annuity liabilities without exposing them to high levels of interest rate or reinvestment risk; mortality data of sufficient quality to allow insurance companies to price their annuities reasonably accurately; a competitive insurance market or sufficiently low barriers to entry, to ensure that

[65] *Enabling a Better Income in Retirement*, (Technical Discussion Paper B for Public Comment, National Treasury 21September 2012) 28.
[66] Ibid 29.
[67] Ibid.

annuities are fairly priced; and a regulatory environment that ensures an appropriate level of insurer solvency.[68]

The paper further notes the above requirements as existent in South Africa, with two important exceptions. First, there may be an insufficient number of high-quality bond issues at the long end of the yield curve, particularly in the inflation-linked segment. Second, mortality data at a sufficiently disaggregated level to permit accurate rating for all segments of the population may not be available. The absence of suitable mortality data of sufficient quality may have hindered the introduction of more accurate rating policies.[69] In conclusion the paper states that the conditions for a functioning market in life annuities exist in South Africa. However, sufficient mortality data, disaggregated by market segment, may not yet be available.[70]

1.9.7 Profile Analysis

Chapter two of this paper seeks to examine social security practice in Kenya. Specifically, the chapter will trace the origin of the concept of social security globally and its eventual introduction into the Kenyan pension system. In particular, this paper will look into the history of the NSSF Act 2013, in a bid to appreciate the different social security systems in Kenya. These social security systems are: the NSSF, the public service pension, the occupational schemes, the individual retirement schemes and old age pension guarantee. This chapter seeks to trace the origin of the concept of social security globally and its eventual introduction into the Kenyan pension system. In particular, this paper looks into the history of the NSSF Act 2013, in order to appreciate the different social security systems in Kenya. The chapter further reveals that the low

[68] Ibid.
[69] Ibid 31-32.
[70] Ibid 32.

uptake of state pension among persons in the jua-kali sector in Kenya, is traceable to the introduction of the NSSF Act 1965. Indeed, literature in this chapter shows that the fore-going problem is not a preserve of Kenya alone, but a challenge in Africa. The chapter concludes that state pension in Kenya, can only serve as an effective tool for old age income for persons in the jua-kali sector, if the Kenyan parliament, addresses the legal issues existent in the legal regime governing state pension. This is in addition to strengthening the other pillars of social security in Kenya.

On the other hand, chapter three explores the legal challenges surrounding the legal regime of state pension in Kenya that hinder participation by persons in the jua-kali sector. In particular, this chapter embarks on a comparison between the NSSF Act 1965 and the NSSF Act 2013. The purpose of the fore-going is to determine, whether or not the NSSF Act 2013, addresses legal issues that hampered participation of the jua-kali sector, in the previous NSSF Act. In addition, this section examines whether or not the NSSF has changed tact to comply with the provisions of the RBA 1997, since the enactment of the NSSF Act 2013. Furthermore, the chapter looks at the existent legal challenges in the insurance annuity market and Income Tax law that make purchase of annuity undesirable, therefore hindering participation of the jua-kali sector in Kenya's state pension. Furthermore, the chapter looks at the existent legal challenges in the insurance annuity market law and Income Tax law that will in future make purchase of annuity undesirable to persons in the jua-kali sector.

Chapter three arrives at the conclusion that there is a fundamental difference between the old and the new NSSF Act. Notwithstanding the difference, the NSSF Act 2013 has failed to accommodate the uniqueness of the jua-kali sector. The jua-kali informal sector is a sector characterized by high volatility in income. In addition, the government has difficulty tracing this particular group for accountability purposes. It is therefore imperative for the Kenyan parliament to come up with unique strategies in a bid to attract this group. This study also concludes that though the NSSF has endeavored to comply with some provisions of the RBA 1997, specifically that on investment guidelines; there still remains much to be desired. In the meantime, the Retirement Benefits Authority is cast as a toothless bull-dog in regulation and supervision of NSSF affairs. Further, this study observes that the Kenyan Government has failed to provide a condusive legal environment to persons in the jua-kali sector, who may opt to purchase an annuity on their own initiative as opposed to accessing their retirement benefits as a lump-sum.

Moreover, chapter four undertakes to evaluate the social security system in South Africa and India, in light of resemblance in their social security systems with Kenya. While acknowledging that no system is perfect, this chapter has proceeded to critique the pension system in the two countries, with the view to determining areas of improvement. The chapter concludes by illustrating what Kenya can learn from the strengths and weaknesses of the South African and Indian pension experience.

Chapter five concludes this study by presenting the findings to the research objectives and hypothesis. In a bid to come up with legal reforms, this paper has presented its recommendations, drawn regionally and globally, by looking at the South African and Indian pension experience. Likewise, this paper draws its recommendations from Kenya’s Code of Corporate Governance for State Corporations in Kenya (Mwongozo 2015).

CHAPTER TWO

SOCIAL SECURITY PRACTICE IN KENYA

2.0 Introduction

This chapter seeks to trace the origin of the concept of social security globally and its eventual introduction into the Kenyan pension system. In particular, this paper looks into the history of the NSSF Act 2013, in order to appreciate the different social security systems in Kenya. These social security systems are: state pension (the NSSF), the Public Service Pension, the occupational schemes, individual retirement schemes and old age pension guarantee. This chapter reveals that the low uptake of state pension among persons in the jua-kali sector is traceable to the introduction of the NSSF Act 1965. Indeed, literature in this chapter shows that the fore-going problem is not a preserve of Kenya alone, but a challenge in Africa.

2.1 Origin of the Concept of Social Security

The background of the term social security reveals that the right to social security is globally recognized. This right is upheld in the ILO, the Universal Declaration of Human Rights ("the UDHRs") and the International Covenant on Economic, Social and Cultural Rights 1966 ('the ICESCRs 1966').[71] Social security protection is defined in ILO conventions as a basic human right – albeit one that a small proportion of people on our planet actually enjoy.[72] According to the ILO, social security is defined as: "... the protection which society provides for its members, through a series of public measures, against the economic and social distress that otherwise would be caused by the stoppage or substantial reduction of earnings resulting from sickness,

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[71] 'Facts on Social Security,' International Labour Organization <http://www.ilo.org/wcmsp5/groups/public/---dgreports/---dcomm/documents/publication/wcms_067588.pdf> accessed 29 November 2016.
[72] Ibid.

maternity, employment injury, unemployment, invalidity, old age and death; the provision of medical care: and the provision of subsidies for families with children."[73]

According to the UDHRs, the concept of social security states that, "Everyone, as a member of society, has the right to social security and is entitled to realization, through national effort and international co-operation and in accordance with the organization and resources of each State, of the economic, social and cultural rights indispensable for his dignity and the free development of his personality.[74] This study will adopt the definition of social security according to the UDHRs, as the definition is broader than that offered by the ILO.

Therefore, Kenya being a signatory to the UDHRs has encompassed the right to social security in its Constitution. The Constitution recognizes that every person has inherent dignity and the right to have that dignity respected and protected.[75] The Constitution 2010 goes further to state that every person has the right: to the highest attainable standard of health; to accessible and adequate housing and reasonable standards of sanitation; to be free from hunger and to have adequate food of acceptable quality; to clean and safe drinking water in adequate quantities; to social security and; to education.[76]

2.2 Origin of Social Security in Kenya

In the pre-colonial period, social security was provided in kind by the extended family system and the community of neighbours. The introduction of a cash economy and the alienation of land

[73] <http://ilo.org/global/standards/subjects-covered-by-international-labour-standards/social-security/lang--en/index.html> accessed 29 November 2016.
[74] Universal Declaration of Human Rights (UDHRs), art 22.
[75] Constitution of Kenya 2010 (Constitution 2010), s 28.
[76] Ibid, s 43.

during the colonial period weakened the mutual social support system by introducing artificial social relationships and individualism especially in the urban centers.[77]

Around 1956, the then colonial government felt that there was a need to introduce some form of social protection for the African workers. However, it was not until 1961 that a recommendation was made for the establishment of a provident fund, as a basis upon which a pension scheme would be built later. It was thought that the introduction of a pension scheme would have required substantial resources in finance and manpower and a large subsidy from the National Treasury.[78]

On attaining independence, the Kenyan Government declared its aim of providing some social protection for its population. Nevertheless, the Kenyan Government noted that its capacity to attain the desired ends, was limited by financial and manpower resources as well as the high rate of population growth. For these reasons, the government chose to initiate a National Provident Fund and National Health Insurance Scheme. The NSSF was to be a compulsory savings scheme for the workers and was intended to serve as the first pillar of social security, for Kenyan workers.[79] According to the World Bank and ILO, a pillar of this nature is referred to as the first pillar of social security.

The World Bank and ILO advocate for a multi-pillar approach to retirement saving that provide supplementary windows for old age saving for the entire strata of the population.[80] The World

[77] P.M. Mullei, *Social Security in Kenya*, (1988) 41(4) International Social Security Review 433.
[78] Ibid.
[79] Ibid.
[80] The Retirement Benefits Authority, *Individual Retirement Benefits Schemes in Kenya*, (June 2007) 1.

Bank advocates for a five pillar model which consists of: A non-contributory "zero pillar" which extends some level of old-age income security to all of the elderly, where social conditions warrant and economic circumstances can sustain such a system.[81] This has been experimented in Kenya and Uganda. Second is an appropriately sized mandatory "first pillar" which is a contributory system that is linked to earnings to replace part of income.[82] Another is a funded mandatory defined contribution "second pillar" which provides privately managed individual savings accounts.[83] Fourth, is a funded voluntary "third pillar" taking many forms, for example voluntary, flexible and discretionary, defined benefit or defined contribution, employer-sponsored or individual.[84] In addition, there is a non-financial "fourth pillar" which includes informal financial and non-financial support, including housing and health care.[85]

On the other hand, the ILO suggests a three-tier pension system, involving workers and employers, both as contributors.[86] The first tier is a minimum anti-poverty pension, universally available but means tested, possibly financed directly from general revenues and indexed.[87]Another is a mandatory public Pay-As-You-Go (PAYGO) social insurance pension, which would be fully indexed against inflation and it would be subject to a ceiling.[88] Lastly, is a fully funded defined contribution scheme, perhaps privately managed, which would supplement the public scheme. This would include occupational as well as individual schemes. However, their operation would need to be closely monitored and regulated.[89]

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[81] Robert Holzmann, Richard Paul Hinz and Mark Dorfman, *Pension Systems and Reform Conceptual Framework,* (Social Protection Discussion Paper Number 0824, the World Bank 2008) iv.
[82] Ibid.
[83] Ibid.
[84] Ibid.
[85] Ibid.
[86] The Retirement Benefits Authority, *Individual Retirement Benefits Schemes in Kenya*, (June 2007) 2
[87] Ibid.
[88] Ibid.
[89] Ibid.

The NSSF was established by an Act of parliament in November 1965, but contributions began in July 1966. The NSSF Act 1965 provided that the administration of the NSSF would be under the control and management of the Ministry of Labour. Consequently, the NSSF Act 1965 was amended to provide for management of the NSSF by a board of trustees.[90]

Critical to note is that Kenya's retirement benefits sector is divided into two that is, public and private pension schemes. The public schemes are established by Acts of Parliament and include: the NSSF which is currently governed by the NSSF Act 2013 and the Civil Servants Pension Scheme governed by the Pensions Act.[91] The former scheme is supervised and regulated by the Retirement Benefits Authority, while the latter is not. The Pensions Act is the main Act which makes provisions for the grant and regulation of the payment of pensions, gratuities and other allowances in respect of the public service, for officers under the Government of Kenya. The Pensions Act came into operation in its present form with effect from 1 January 1946.[92] It has however been amended from time to time in order to up-date and make it easier to administer.

On the other hand, private pension schemes are divided into two that is, occupational schemes and individual pension schemes. Occupational schemes are run by employers, for their employees and are privately managed.[93] These schemes form the second and third pillars of pension respectively, according to the World Bank, where membership is either voluntary or mandatory. Contrary to the public schemes which are set up through Acts of Parliament; occupational schemes are set up through a trust deed, which is considered the constitutive

[90] P.M. Mullei (n77), 433.
[91] Pensions Act, Chapter 189 of the Laws of Kenya (Pensions Act).
[92] Ibid, short title.
[93] <www.rba.go.ke> accessed 30 June 2016.

document of the scheme. Currently, there are one thousand two hundred and thirty two (1,232) occupational schemes as at 6 May 2014,[94] which are supervised and regulated by the Retirement Benefits Authority. On the other hand, individual pension schemes are private schemes designed for the employed and self-employed. These are voluntary schemes which form the third pillar of pension, where membership is voluntary. Like occupational schemes, these schemes are set up through a trust deed, which govern the affairs of the individual pension schemes. Presently, there are thirty two (32) individual pension schemes in Kenya as at 30 June 2016, which are also supervised and regulated by the Retirement Benefits Authority.[95]

Later on in 2013, the NSSF Act 1965 and its regulations were repealed by introduction of the NSSF Act 2013. This move was provoked by Kenya's vision 2013, which highlights the need for the NSSF to expand its mandate, to meet the needs of the jua-kali sector, who were previously overlooked by the NSSF Act 1965. Indeed the membership of the NSSF Act 2013, is drawn from not only the formal sector (which makes mandatory contributions)[96] but the jua-kali sector as well, whose contribution is voluntary in nature.[97] The jua-kali sector is the Kiswahili term for Kenya's informal sector, which means "hot sun." "The hot sun" refers to the typical outdoors situation of such entrepreneurs. It is characterized by many small businesses and artisanship which ply their trade on sidewalks or in alleys without the benefit of offices, factories, or showrooms.[98] Such work results in small scale, irregular sources of income that often make it difficult to plan for the future, specifically retirement.[99] The activities associated with the jua-kali sector include selling of fruits and vegetables; food operation, sale and processing; selling

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[94] Ibid.
[95] Ibid.
[96] NSSF Act 2013 (n1), ss 19(1) and 20.
[97] Ibid, s 19(3).
[98] Amos Gitau Njuguna, *Mbao Pension Plan*: 'A Retirement Scheme for the Informal Sector,' (Biashara Leo, 24 July 2014) 37.
[99] <http://ls.berkeley.edu/stories/archive/2011-judith-lee-stronach-baccalaureate-prize> accessed 24 June 2016.

clothes and shoes (both second-hand and new); kiosks selling various items; water kiosks; small retailers or hawkers who sell cereals, home suppliers, fuels and other goods and small manufacturing, production, construction and repair of goods. The latter is a recent categorization by the World Bank in 2006.[100]

The Kenya National Federation of Jua Kali Associations, upon realization that the informal sector did not have any retirement schemes and had not been served properly by the existing provident funds and pension schemes: the association approached the Retirement Benefits Authority with an aim of getting a pension scheme which catered for the informal sector. After a number of consultative meetings with the Retirement Benefits Authority and the Treasury, the Mbao Pension Plan was registered in October 2009. The scheme is a voluntary retirement savings plan, whose members contribute twenty shillings Kshs. 20/= (mbao) per day.[101] The aim of the scheme is to create affordable, flexible and convenient individual retirement saving plans for the informal sector workers who do not have retirement pensions.[102]

The vision of the Mbao Pension Plan is to create a cost effective, flexible and efficient pension fund for the informal sector in Kenya; the target population being the 12 million informal sector workers.[103] As of 22 June 2014, the scheme membership was 55,000.[104] The challenges faced by this scheme include low awareness of pensions and lack of prioritization of pensions. These challenges are however not a preserve of the jua-kali sector in Kenya, but are a shared global

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[100] Ibid.
[101] Amos Njuguna (n98) 37.
[102] <http://ls.berkeley.edu/stories/archive/2011-judith-lee-stronach-baccalaureate-prize>, accessed on 24 June 2016.
[103] Patricia Odera, *Building Resilience and Opportunity:* 'The Role of Labour and Social Assistance Strategies – Case Study of the Mbao Pension Plan,' (the Retirement Benefits Authority) 8.
[104] Business Daily, Sunday 22 June 2014, Isaiah Opiyo, *Workers in the Informal Sector can plan for a rewarding Retirement*, <www.businessdailyafrica.com>.

problem.[105] In Africa, one of the main social protection problems is coverage. However, a convincing case can be made for the judicious extension of coverage in order to improve the financial base. Still, the governance and management of public social security institutions are the main hurdles.[106]

2.3 Conclusion

This chapter concludes that state pension in Kenya can serve as an effective tool for old age income for the jua-kali sector. This is only possible if the government addresses the legal issues that stifle compliance by persons in the jua-kali sector, in light of their large numbers. This is in addition to strengthening the other pillars of social security in Kenya.

[105] Hu and Stewart (n39) 3.
[106] Arne Tostensen, *Social Security in Africa:* 'Feasible Social Security Systems in Africa,' (Institute of Social Studies, Vol 10, No. 2 November 2008) 5.

CHAPTER THREE

LEGAL CHALLENGES IN KENYA'S STATE PENSION AGAINST THE JUA-KALI SECTOR

3.0 Introduction

This chapter explores the legal challenges surrounding the legal regime of state pension in Kenya that hinder participation by persons in the jua-kali sector. In particular, this chapter embarks on a comparison between the NSSF Act 1965 and the NSSF Act 2013, with a view to determine, whether or not the NSSF Act 2013, addresses legal issues that hampered participation by persons in the jua-kali sector in the NSSF Act 1965. In addition, this section examines whether or not the NSSF has changed tact to comply with the provisions of the RBA 1997, since enactment of the NSSF Act 2013. Furthermore, this chapter looks at the existent legal challenges in the insurance annuity market and Income Tax law that make purchase of annuity undesirable to persons in the jua-kali sector.

3.1 Lack of Flexibility in Terms of Amount and Contribution Requirement

One of the main reasons why the informal sector workers do not want to participate in voluntary pension systems (and in some cases even comply with mandatory schemes) is that they find the strict criteria involved too onerous.[107]

One of the problems faced under the NSSF Act 1965 was modesty in contributions,[108] in the formal and informal sectors. For instance, the NSSF Act 1965 made provision for special

[107] Hu & Stewart (n 39) 4.

contributions in respect of casual workers at five per cent (5%) of an employer's total wage bill.[109] The said NSSF Act also made provision for voluntary contributions payable in respect of self employed persons. Nonetheless, the NSSF Act 1965 did not permit voluntary registration of any employee who was not employed by a contributing employer[110] The voluntary contributions ranged from a minimum of Kenya Shillings One Hundred (Kshs 100/=) to a maximum of Kenya Shillings One Thousand (Kshs 1000/=), as per section 12 of the NSSF Act 1965.

In a bid to reduce old age poverty, the NSSF Act 2013 increased jua-kali sector contributions, despite their volatility in income. The NSSF Act 2013, makes it mandatory for those who choose to register as voluntary members, to contribute a minimum of Kenya Shillings Two Hundred (Kshs 200/=) and a minimum aggregate of Kenya Shillings Four Thousand Eight Hundred (Kshs 4,800/=) in a year.[111]

It is my opinion that even as the need for increased contributions is necessary: an increase in contribution to the jua-kali sector only continues to foster their non-participation in the NSSF. This is because the NSSF Act 2013 has failed to appreciate the different categories of the jua-kali sector workers, who have unique challenges. For instance, some jua-kali sector members would find it burdensome to contribute Kenya Shillings Two Hundred (Kshs 200/=) daily, if he chooses to be enrolled as a voluntary contributor, while another in the same sector would be comfortable to contribute a lesser amount daily. Case in point is a person selling secondhand clothes or shoes

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[108] Under the NSSF Act 1965, each employer and employee was required to contribute Kshs. 200/= a month, amounting to Kshs 400/= a month. If a person works for thirty years, this will amount to Kshs. 72,000/=, as retirement income. However, modesty in contributions still remains a challenge under the NSSF Act 2013 as the new contribution rates of 6% of the employees pensionable earnings, as indicated at section 20 of the NSSF Act 2013, is subject of a court dispute.

[109] NSSF Act 1965, s 13.

[110] Ibid, s 6(b).

[111] Ibid, s 23.

at Adams arcade stalls and a casual labourer. The former may be able to afford a contribution of Kenya Shillings Two Hundred (Kshs 200/=) daily, while the latter may find it burdensome to contribute the same amount, due to the more unpredictable nature of the latter's work.

Unlike the NSSF Act 2013, the Mbao Pension Plan[112] has addressed the fore-going issue by requiring their jua-kali sector members, to contribute a small amount which is within their daily reach, at Kshs 20/= per day. Notwithstanding the amount of Kshs 20/= per day (which translates to Kshs 600/= per month), being more than that prescribed in the NSSF Act 2013, the jua-kali sector would find it affordable, as such a sum is already saved daily by members of merry-go-round groups in Nairobi slums and rural communities. The membership and activation fee for the Mbao Pension Plan is Kenya Shillings One Hundred (Kshs 100/=). No other fees are charged for individuals who remain a member for one year before withdrawing from the scheme.[113] From the fore-going, it is apparent that the proposed amount as per the NSSF Act 2013, is burdensome and not sustainable to persons in the jua-kali sector.

3.2 Lack of Flexibility in Withdrawals

The NSSF Act 2013 is rigid in its accessibility of funds, by persons in the jua-kali sector. For instance, section 45 of the NSSF Act 2013 provides that a member of a provident fund (the fund which is intended for the jua-kali sector), will only be entitled to a lump-sum withdrawal benefit, equal to his provident fund credit, if at the time of claiming the benefit, he is no longer in self-employment.[114] Other benefits available to persons in the jua-kali sector are age benefit, which a

[112] The Mbao Pension Plan is an individual retirement scheme created by the Retirement Benefits Authority. This pension plan is open to the general public but targets the jua-kali sector. The aim of the Mbao Pension Plan is to create affordable, flexible and convenient individual retirement saving plans for workers who do not have retirement pensions.
[113] Lauren Herman, *Expanding the Realm of Consumer Protection Through Education*, Tuesday 15 November 2011, <consumerprotectionkenya.blogspot.co.ke/2011/11/why-are-millions-of-kenyans-not-saving.html>.
[114] This section does not take into account the high volatility in income that most jua-kali sector persons encounter.

jua-kali sector member will only be entitled to, if the member has attained fifty (50) years.[115] Another is survivors' benefit, which dependent relatives of a member will be entitled to upon the member's death.[116]

As regards invalidity benefit, a jua-kali sector member would only be entitled in two instances. That is, if the jua-kali member is subject to such physical or mental disability as to be suffering from permanent total incapacity as certified by a medical doctor.[117] Second is if a member is subject to such physical or mental disability as to be suffering from partial incapacity of a permanent nature and is unable by reason of such disability to earn a reasonable livelihood as certified by a medical board.[118] On emigration benefit, a jua-kali member would only be entitled if he emigrates from Kenya, to a country other than a country with which a reciprocal agreement is made pursuant to section 64 of the NSSF Act 2013, without any present intention of returning to reside in Kenya.[119] Similar to the NSSF Act 2013, the NSSF 1965 did not provide for flexibility in withdrawal by a jua-kali member.[120]

These fore-mentioned provisions are rigid, as they fail to recognize the uniqueness of the jua-kali sector. For instance, this group faces a myriad of problems such as disturbance by the City Counties, demonstrations and strikes which most often than not disrupt their businesses. Also, due to the group's low and irregular income, there is difficulty in accessing life's essentials such as medical services, shelter, and access to education for their children. Nonetheless, flexibility in

[115] NSSF Act 2013 (n1), s 42(1).
[116] Ibid, s 43.
[117] Ibid, s 44(a).
[118] Ibid, s 44(b).
[119] Ibid, s 46.
[120] Ibid, ss 20-24.

withdrawals needs to be balanced with the risk of leakage from the pension system, with large withdrawals leading to insufficient balances upon retirement (as has been the problem with the provident fund in Singapore and pension funds in South Africa,).[121]

3.3 Bad Governance of the NSSF

Similar to the NSSF Act 1965, the NSSF is governed by the NSSF board of trustees, whose current composition does not adhere to the RBA 1997. The RBA requires that in the instance of an odd number in representation in the board of trustees, the same should be construed in favour of the employee. On the other hand, if the board members are equal, then parties should have equal representation.[122]

Currently, the governance at the NSSF is overseen by a nine member board of trustees (in addition to a managing trustee, who is an ex-officio member of the board and is appointed by the board), which is contrary to the RBA 1997, are all appointed by the Cabinet secretary for matters relating to social security. The representation at the NSSF board of trustees is composed of the two Principal Secretaries responsible for matters relating to finance and social security. In addition, two representatives are each to be nominated by Federation of Kenya Employers (FKE) and Central Organization of Trade Union (COTU), who are to be appointed by the Cabinet secretary. The Cabinet secretary also appoints three independent board members, who are persons with knowledge and experience in matters relating to administration of scheme funds,

[121] Hu & Stewart (n 39) 5.
[122] The Occupational Regulations 2000 (n10), s 8(c) (ii).

actuarial science, insurance, accounting and auditing or law. It is from these seven persons that the Cabinet secretary will appoint a Chairperson,[123]

The government in its defense in violating the RBA 1997 on board appointments indicates that the government is keen to only hire people who can work against set targets. The government goes ahead to blame various interest groups – FKE and COTU - for stalling the reform agenda. An example is the standoff that hit National Hospital Insurance Fund (NHIF) board in the year 2015, as the then Medical Services Minister, board Chairman and CEO took conflicting positions in the implementation of the medical scheme for civil servants.[124] Mwongozo 2015 also happens to support the current NSSF board composition, as it recommends that board members of state corporations be appointed by the Cabinet Secretary of the parent ministry.[125] Mwongozo 2015 nevertheless requires a board member to exercise independent judgment in discharging his duties.[126] It is my opinion that the NSSF board as currently constituted does not promote accountability and is contrary to the principles of good corporate governance. The principles of good corporate governance recommends for separation of the position of Chairman and CEO, to ensure a balance of power and authority and provide for checks and balances.[127]

Yet another issue which has dogged the NSSF board, one month following the coming into effect of the NSSF Act 2013, on 10 February, 2014, was the five billion Tassia II housing project. This matter involved irregular approval by six former NSSF trustees, inclusive of the chair, Aden

[123] NSSF Act 2013 (n 1), s 6.
[124] George Omondi, 'Employers fault State on NSSF Board,' Business Daily (2013) <http://www.businessdailyafrica.com>.
[125] Mwongozo 2015, s 1.1(8) (2).
[126] Ibid, s 1.16.
[127] The Capital Markets Act, Chapter 485A of the Laws of Kenya, clause 3.2(i).

Mohammed and the managing trustee, Richard Langat of Kshs. 5 billion, for the regularization of Tassia Two housing project and award of the lucrative tender to China Jiangxi International Kenya Limited. The report by the Ethic and Anti-corruption Commission (EACC), to the Director of Public Prosecution (DPP) failed to recommend prosecution of six (6) NSSF board of trustees members.[128]

As an alternative, the EACC recommended that administrative action be taken against the then NSSF Managing trustee and Chief Executive Officer, Richard Langat, for exposing the NSSF to contractual obligations, when all the funds to finance the project had not been collected from the tenants.[129] On this strength, the COTU Boss, Francis Atwoli sought leave of the court to privately prosecute the NSSF officials; the application of which was dismissed on the basis that it lacked merit. According to Chief Magistrate Daniel Ogembo, the court was not convinced of the necessity of the proceedings and absolved the office of the DPP and the EACC, saying that the two agencies were correct in closing the file against the six.[130]

The fore-going issues raise concern over the NSSF's ability to make wise decisions, independent of influence from the Kenyan Government. Indeed, good corporate governance dictates separation of the role of Chairman and Chief Executive Officer (CEO). The purpose is to provide checks and balances, such that no one individual has unfettered powers of decision making.[131]

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[128] Cyrus Ombati, 'EACC recommends administrative action on NSSF Boss over Shs. 5 billion Tassia II Project,' The Standard (2015). <http://www.standardmedia.co.ke/article/2000172595/eacc-recommends-administrative-action-on-nssf-boss-over-sh5-billion-tassia-ii-project> accessed on 24 June 2016.

[129] Ibid.

[130] Bernice Mbugua, 'Court Dismisses Tassia suit by Atwoli' Mediamax Network (2016). <http://www.mediamaxnetwork.co.ke/news/265608/court-dismisses-tassia-suit-application-atwoli/> accessed 11 January 2016.

[131] Cyrus Ombati (n 128).

Nevertheless, section 10(1) of the NSSF Act 2013, gives the Board unfettered discretion in the performance of its responsibilities.

3.4 Determination of Remuneration by the NSSF Board

Similar to the NSSF Act 1965, the NSSF Act 2013, permits the Board to determine the remuneration, fees or allowances of the Board or committee of the Board, subject to the approval of the Cabinet Secretary.[132] Therefore, the NSSF Act 2013 has the risk of increasing the NSSF's administrative costs above the 2% of total fund assets recommended by both the NSSF Act 2013 and the Retirement Benefits Authority.[133]According to the NSSF's 2013/2014 audited accounts, the administrative costs exceeded the afore-mentioned statutory prescribed of 2%. Similarly, the 2014/2015 audited accounts, reiterates the same position, with administrative costs amounting to 3.73% of the NSSF's total assets. Equally, the NSSF Act 2013 is contrary to the Salaries and Remuneration Commission Act,[134] which requires its commission to set and regularly review the remuneration and benefits of all state officers and advise the national and county government.[135]

3.5 Lack of Transparency by the NSSF

Similar to the NSSF Act 1965, the NSSF Act 2013 requires accountability and auditing of the NSSF.[136] Specifically, the NSSF Act 2013 requires the board of trustees, within a period of six months after the end of each financial year, to prepare, sign and transmit to the auditor-general, its accounts.[137] However, akin to the NSSF Act 1965, the NSSF board under the NSSF Act 2013,

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[132] NSSF Act 2013 (n 1), s 13.
[133] NSSF Act 2013 (n1), s 50(1) as read together with s 50(2).
[134] Salaries and Remuneration Commission Act, Chapter 5F of the Laws of Kenya ("SRC Act").
[135] SRC Act (n134), long title.
[136] NSSF Act, 2013 (n1), s 51.
[137] NSSF Act, 2013 (n1), s 51(2).

has persisted in delay in transmission of NSSF's accounts,[138] contrary to Mwongozo 2015,[139] which requires financial statements to be submitted in a timeous manner, in a bid to instill public confidence. Indeed, the NSSF's lack of transparency is problematic considering that the NSSF has in the past been rocked by multi-million shilling scandals, which have led to questions over its ability to manage more funds.[140]

3.6 Low Return on Investment

Prior to the enactment of the NSSF Act 2013, the NSSF was characterized by award of low interest rates to its members. This was due to poor investment decisions on the part of the NSSF, low contribution rates, corruption and high administrative fees.[141] Since the enactment of the NSSF Act 2013, NSSF has recorded erratic investment rates. For instance, in 2015, the NSSF interest return to members was indicated as 12.5%.[142] However, in 2016 interest declined to a mere 3% due to NSSF's inefficiencies. The fund's expenses stood at Kshs. 6.1 billion in the year, against collections amounting to Kshs 11.7 billion in the period under review. This means that NSSF was left with only Kshs 95 to invest out of each member's monthly contribution of Sh200.[143] The NSSF's inefficiencies include malpractices such as corruption as evident in the

[138] As at 31 August 2016 NSSF had not uploaded its 2014/2015 Audited accounts in its website. This is contrary to the NSSF Act 2013 which requires audited accounts to be submitted within 6 months from the end of the financial year, in this case 30 June 2016. This in turn means that the said audited accounts were yet to be submitted to its regulator.
[139] Mwongozo 2015, clause 3.1.
[140] Cyrus Ombati (n 128).
[141] Retirement Benefits Industry Performance Report of the years 2015 and 2014.
[142] Ibid.
[143] David Herbling, NSSF Spends Half of Employees Contributions on Administration,' Business Daily (2016) http://www.businessdailyafrica.com/NSSF-spends-half-of-employees-contributions-on-administartion/539552-3437832-item-0-xlqdb4z/index.html accessed 11 January 2016.

Tassia II housing project scandal mentioned in this study as discussed.[144] Moreover, high administration fees remain a challenge.[145]

3.7 Non-adherence to Statutory Administrative Fees

The RBA 1997 requires that administration expenses of all retirement schemes should not exceed two per cent (2%) of the total fund value of the scheme.[146] According to the NSSF's 2014/2015 audited accounts, the administrative costs exceeded the Retirement Benefits guidelines.[147]

3.8 Delay in Submission of Audited Accounts

The Retirement Benefits Regulations requires trustees of NSSF to submit audited annual accounts, including the trustees and investment report to the Retirement Benefits Authority, on an annual basis.[148] However, information from the authority reveals that the NSSF is yet to submit its audited accounts for the year 2014/2015 as at July 2016. This delay in transparency makes it difficult for the Retirement Benefits Authority to assess its performance. For instance, the last time the NSSF made the Retirement Benefits Authority aware of its membership was in 2008. This makes it difficult for RBA to know with certainty, the NSSF's coverage of the labour force.

144 Cyrus Ombati (n 128) I
145 David Herbling (n 143).
146 The Administrators Regulations 2000 (n10), s 13.
147 David Herbling (n143).
148 The Occupational Regulations (n10) s. 30.

3.9 Premiums of Life Insurers Determined by a Third Party

The Insurance Act requires life insurance premium rates to be fixed by an actuary.[149] The said premiums are often high due to factors such as adverse selection by service providers; lack of competition among providers due to dominance of a few companies and longevity risks; and use of outdated mortality tables that fail to reflect the modern market conditions leading to mispricing of annuity products.[150]

As regards the lack of competition by service providers of annuity products, the Insurance Act details a number of strict conditions for approval of registration of long term insurance business such as annuity. In addition, the minimum capital requirement for a long term insurance business is quite high.[151] The second schedule to the Insurance Act caps the minimum capital requirement at the higher of four hundred million (Kshs 400,000,000/=), or a risk based capital determined by the Insurance Regulatory Authority or five percent of the liabilities of the life business for the financial year.

In light of the fore-going, Kenya as at 30 June 2016, has eight (8) life insurers that is, ICEA Lion, Jubilee Insurance, Pan Africa Life Insurance, Madison Insurance, Apollo Insurance UAP Insurance, Kenindia Assurance and Britam. However, ninety eight per cent (98%) of annuity business is controlled by the first three (major) companies.[152]

[149] The Insurance Act (n3), s 74.
[150] Amos Njuguna (n 13).
[151] Insurance Act (n3), ss 115 and 116.
[152] Amos Gitau Njuguna & 2 Others, *Strategies to Enhance the Payout Phase of the Retirement Benefits*, United States International University (USIU) 5.

Some of the challenges faced by life insurers due to the longevity risks include: illiquidity, inflation risks, investment risks, company specific risks and the nature of the product.[153]

3.10 Information Asymmetry

Despite the requirement by the NSSF Act 2013, that upon retirement a jua-kali member be entitled to a lump sum benefit, information on annuity is important to enable a pensioner make an informed choice on purchase of an annuity or otherwise. A study by USIU in partnership with the Retirement Benefits Authority discloses low awareness levels on annuities yet information on annuity is of importance during the accumulation stage, to enable a jua-kali member make additional contributions if possible. A study by USIU in partnership with the Retirement Benefits Authority discloses low awareness levels on annuities.[154]

3.11 Taxation of Income from Annuities

The Income Tax Act requires income from annuities to be taxed. This translates to reduced income to a pensioner, whereby the net effect is to discourage purchase of annuities where the same is not made compulsory.[155]

3.12 Inadequate Funds for Investment

The issue of inadequacy of funds is directly linked to the Kenya Parliament's lack in addressing the legal challenges evident in the legal regime governing state pension, that hinder participation by persons in the jua-kali sector. As is, the proposed annual contributory amount of Kshs. 4,800/=, is inadequate to cater to a retiree after 30 years in employment, which amounts to Kshs.

[153] Ibid 5-6.
[154] Amos Njuguna (n 152) 20.
[155] Income Tax Act (n4), s 3

1,440,000/=.[156] The fore-going figure would still require a retired jua-kali sector member, to continue to work during old-age. Worse still, a pensioner's retirement income is accessed as a lump-sum,[157] leaving room for the retiree to outlive his pensions. What's more, if a jua-kali member is to purchase an annuity with the said sum of Kshs 1,440,000/=, a member would be entitled to a mere monthly pension of Kshs 1,440/=.

3.13 Conclusion

Chapter three arrives at the conclusion that there is a fundamental difference between the NSSF Act 1965 and the NSSF Act 2013. Notwithstanding their differences, the NSSF Act 2013 has failed to accommodate the uniqueness of the jua-kali sector. The jua-kali informal sector is a sector characterized by high volatility in income. In addition, the government has difficulty tracing this particular group for accountability purposes. It is therefore imperative for the Kenyan parliament to come up with unique strategies to attract this group. This chapter also concludes that, though the NSSF has endeavored to comply with some provisions of the RBA 1997, specifically on investment guidelines, there is still much to be desired. In the meantime, the Retirement Benefits Authority is cast as a toothless bull-dog in regulation and supervision of NSSF affairs. Further, this chapter observes that the Kenyan Government has failed to provide a condusive legal environment to persons in the jua-kali sector, who may opt to purchase an annuity on their own initiative as opposed to accessing their retirement benefits as a lump-sum. This is because the Income Tax Act requires tax from investment income from annuity. Moreover, this study observes that the Kenya's Parliament, has failed to address the legal challenges in the legal regime governing state pension, hence hindering the jua-kali sector from making additional contributions.

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[156] According to Insurance annuity practice, a monthly pension is calculated at 1% of the purchase price. Therefore, 1% of Kshs 1,440,000/= (Kshs 4,800 x 30) bequeaths a month's pension of Kshs 1,440/= per month.

[157] NSSF Act 2013 (n1), s 41(1).

CHAPTER FOUR

COMPARATIVE STUDY: SOUTH AFRICA AND INDIA

.

4.0 Introduction

Chapter four undertakes to investigate the social security system in South Africa and India, in light of resemblance with Kenya's pension system. To begin with, the state pension scheme for both Kenya and South Africa is the main source of income for a majority of the elderly population in retirement. Second, the state pension scheme for both countries is pension in nature. This means that a pensioner receives a monthly amount as retirement income until demise of the pensioner. Further, the state pension scheme for both Kenya and South Africa are dogged by low and no rates of contributions respectively. For example, in Kenya, both an employer and employee make a monthly contribution of Kshs 200/= each, despite the enactment of the NSSF Act 2013. On the other hand, the state pension system in South Africa is funded from government revenues which are inadequate and which targets men and women of sixty years, and which is means tested in nature.

In both countries, the occupational system can be thought of as quasi mandatory for employees in the formal sector, as some employers require a new employee to join the occupational fund offered by the employer as a condition of service. Also, in both countries, employees in the public sector are covered by separate pension schemes. Furthermore, both countries have a high rate of unemployment and a substantial part of the working-age population is informally employed that is, they are involved in non-standard forms of work.

Further, both national governments of Kenya and South Africa have realized the importance of extending pension system to the informal sector and a range of different policy initiatives have been undertaken, aiming to tackle this problem given the country specific conditions and environments.[158] For instance in South Africa, in order to increase pension coverage, the South African government is considering the introduction of a mandatory pension system for all formally employed workers. The main objective of this proposal is to ensure a basic level of retirement income for all South Africans. Meanwhile, specifically for employees in the informal sector, the government is currently thinking of establishing a national savings fund. This fund will be designed in a way to accommodate needs of the informal sector workers, like flexible contributions and less strict terms for withdrawal. On the other hand, through the enactment of the NSSF Act 2013 in Kenya, the NSSF seeks to broaden its membership by including persons in the jua-kali sector.[159]

At the same time, both countries have a poor retirement savings culture; they do not save or leave it too late in their careers to save enough for retirement. For instance, some employees cash in their savings when they lose their jobs or draw from their savings to meet medical costs. In both countries, majority of workers are in the informal sectors, who contribute less to their retirement.

The Kenyan and Indian pension systems also have similarities. To begin with, the pension system in both countries is complex, with a variety of schemes. To this end, both countries have civil servants pension schemes, occupational schemes and voluntary schemes. However, the

[158] Hu & Stewart (n39) 2.
[159] NSSF Act 2013 (n1), s 4(e).

Indian pension system is more fragmented and complex than that of Kenya. Similarly, the Indian national government just like Kenya, has realized the importance of extending pension system to the informal sector and a range of different policy initiatives have been undertaken, aiming to tackle this problem given the country specific conditions and environments.[160] On the other hand, NSSF Act 2013 has sought to bring within its ambit, self employed persons, to access social security for themselves and their dependants.[161] The Indian government in 2004, in a bid to encourage participation of the informal sector workers, introduced a new system, called the National Pension Scheme (NPS). The NPS is mandatory for those employees in the central government, who start their employment after 1 January 2004, while it is voluntary for state employees and all the other Indian citizens. One of the main features of the NPS is its low cost, which consequently intends to encourage voluntary participation of those people who do not have any form of private pension among other reforms.[162]

What's more, the coverage of the mandatory social security schemes for both Kenya and India, favour the formal sector while informal employment is on the rise. In Kenya, the NSSF covers approximately 20% of the labour force.[163] In India, major retirement savings schemes like the mandatory pension programs, run by the Employees' Provident Fund Organization ("the EPFO"), target formal employment, constituting only about 12 percent of the aggregate workforce.[164]

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[160] Hu & Stewart (n39) 2-3.
[161] NSSF Act 2013 (n1) s. 4(e).
[162] Hu & Stewart (n 39) 19.
[163]<http://www.ilo.org/dyn/ilossi/ssimain.viewScheme?p_lang=en&p_scheme_id=3117&p_geoaid=404 accessed 17 January 2017.
[164] Hu & Stewart (n 39) 19.

Moreover, both countries have an equivalent rate of contribution. For instance, in Kenya the NSSF Act 2013 prescribes an employee and employer contribution rate of 6% each.[165] In India, anyone working for a prolonged period of time will have to pay social security contributions of 12% of their income if they are employed by a company covered by the EPFO, which will in turn match the 12% contributed by the employee.[166]

In both the Kenyan and Indian state pension scheme, the administrative bodies (that is, the NSSF and the EPFO respectively), face governance and transparency challenges. For instance, in Kenya, the NSSF board of trustees is appointed by the Kenyan Government,[167] and the Cabinet Secretary for the time being responsible for matters relating to social security. This is contrary to the principles of good corporate governance which require both stakeholders and shareholders to appoint their representatives, to ensure efficient management. Such a board gives room for dishonest conduct that has been evident in the NSSF Board over the years.[168] In India, the EPFO, has the dual role of being the enforcement agency to oversee the implementation of the Employees' Provident Fund and Miscellaneous Provisions Act, 1952 ("EPF & MP Act 1952"), and is a service provider for the covered beneficiaries throughout India. What's more, the Board of Trustees is bloated and constitutes a majority of government officials. The Board consists of a Chairman, a Vice Chairman, 5 Central Government Representatives, 15 State Government Representatives, 10 Employees' Representatives, 10 Employers' Representatives and the Member Secretary to the Board.[169] This duality has brought about corruption. For example, the Central

[165] NSSF Act 2013 (n 1), s 20 (1)(a) (b).
[166] < https://www.internations.org/india-expats/guide/working-in-india-15315/insurance-and-social-security-in-india-2> accessed 26 December 2016.
[167] NSSF Act 2013 (n 1), s 6(b) & (c).
[168] Cyrus Ombati (n 128).
[169] EPF & MP Act 1952, s 5A

Bureau of Investigation (CBI) in 2016 arrested S. Durga Prasad. According to sources in the agency, the CBI's Anti-Corruption Branch received a specific input that Mr. Prasad had demanded Rs.25 lakh as bribe, relating to subterfuge of wages paid to employees for the purpose of Provident Fund remittance.[170]

Furthermore, both countries also have a low retirement savings culture.[171]

To add on, both countries have a pension arrangement for the aged. In an effort to widen the reach of the social safety net for the aged poor, the Indian central government, in 1995, introduced a more comprehensive old age poverty alleviation program called the National Old Age Pension (NOAP). The scheme aims to provide monthly pension to thirty percent of the poorest elderly.[172] The equivalent of NOAP in Kenya is the Old Age Pension Guarantee. Also, both countries have schemes specifically targeted at the unorganized sector. In Kenya, we have the Mbao Pension Plan, while India has numerous such schemes such as the NPS.

Notwithstanding the comparative study undertaken, this paper acknowledges that no system is perfect. In the circumstance, this chapter also critiques the pension system in South Africa and India, with a view to determine areas of improvement.

4.1 Social Security in South Africa

The South African pension system is composed of three pillars namely: a non-contributory, means-tested public benefit program (Social Old Age Grant), another is voluntary occupational

[170] 'CBI arrests top PF Official on Corruption Charges,'< http://www.thehindu.com/news/cities/chennai/CBI-arrests-top-PF-officials-on-corruption-charges/article14005409.ece accessed 17 January 2016>.
[171] Hu & Stewart (n 39) 19.
[172] Ibid 7.

funds (either pension or provident fund) and voluntary savings arrangements as the third pillar.[173] The voluntary occupational funds can be thought of as quasi mandatory for employees in the formal sector, as many employers require a new employee to join the occupational fund offered by the employer as a condition of service. Employees in the public sector are covered by separate pension schemes.[174]

4.1.1 Public Pensions in South Africa

The Public Pension System in South Africa is known as the old age grant. The qualifying condition for eligibility of old age grant, is a pension age which was equalized at age 60 for men and women in 2010. This form of pension is provided by the South African government under pillar 1 and is the main source of income for over 75% of individuals over the retirement age.[175] South Africa has no compulsory or national pension fund scheme, unlike many other countries. The Government, through its tax payers, funds a social security old age grant to senior citizens, but this is only R1260 per month.[176] The pension is a non-contributory, means-tested Old Age Grant, with individuals having an income of under ZAR 31 296 for singles and ZAR 62 592 for couples and no more than ZAR 518 400 in assets for a single person and ZAR 1 036 800 for a couple. The benefit amount is up to ZAR 1 080 per month for singles and ZAR 2 160 for couples. The average wage used for 2012 was ZAR 135 600.[177]

[173] Ibid 21.
[174] Ibid.
[175] Fiona Stewart and Juan Yermo, *Pensions in Africa,* (OECD Working Papers on Insurance and Private Pensions No. 30, OECD Publishing January 2009) 26.
[176] Mike Brown, *The Retirement Fund Industry in South Africa* (June 2013) 1 <http://www.etfsara.co.za/news/latest/retirement_fund_industry_sa.pdf> accessed on 21 December 2016.
[177] Organization for Economic Co-operation Development (OECD), *Pensions at a Glance 2013*: Country Profiles – South Africa – South Africa, (2013) 336. Organization for Economic Co-operation Development (OECD), *Pensions at a Glance 2013*: Country Profiles – South Africa – South Africa, (2013) 336 <www.oecd.org/els/public-pensions/PAG2013-profile-South-Africa.pdf> accessed on 21 December 2016.

4.1.2 Private Pensions in South Africa

The private and funded pension system consists of an occupational and personal tier. Much of the middle to upper income workers belong to an occupational fund as well as make supplementary retirement contributions through the use of individual pension plans. Occupational pension provision is provided through pension funds (which must pay out at least two thirds in annuities, with employee contributions tax exempt), or provident funds (which are permitted to pay 100% of the member's benefit in the form of a lump-sum).[178] Moreover, occupational plans in South Africa are high by international comparison, estimated to be in the region of sixty per cent. This is comparatively high, even relative to countries with compulsory participation, and it reflects the extent to which membership of an occupational fund is accepted as an obligatory condition for employment.[179]

Individual pension plans are another tax-incentivized savings for retirement, mainly in the form of Retirement Annuity (RA) fund policies, primarily offered by the insurance sector. In the case of RAs, benefits become available from age 55 onwards. They are subject to the same regulations as pension funds in that a maximum of one third may be taken as a cash lump sum and the rest used to purchase an annuity.[180]

4.2 Strengths of the South African Pension System

Firstly, the old social age grant reaches approximately 75% of the South African population, which is funded from government revenues. In addition, the occupational pension plans in South

[178] Stewart & Yermo (n 175) 26.

[179] South Africa National Treasury, *Social Security & Retirement Reform*, (A Second Discussion Paper, February 2007) 5.

[180] <http://euracs.eu/summaries/south-africa-pension-summary> accessed 5 August 2016.

Africa also have large coverage by international comparison. The coverage rate for formal-sector employees is estimated to be in the region of 60%. This is comparatively high, even relative to countries with compulsory participation, and it reflects the extent to which membership of an occupational plan is accepted as an obligatory condition of employment.[181]

4.3 Weaknesses of South African Pension System

South Africa does not have a National Social Security Fund, ensuring participation (whether mandatory or voluntary) of the formal sector and informal sector. Also, the Means Tested Public Benefit System provided by the government, creates disincentives, especially for low-income earners to save for retirement and contributes to a widespread preference for second pillar provident funds that pay a lump sum rather than annuity benefits. Further, there is lack of provision of adequate benefits by the private retirement funds.

Moreover, there are more than 13,500 private pension funds, including occupational pension funds, provident funds and personal plan funds. Approximately 80 per cent of funds have less than 100 members, which raises challenges relating to administration costs.[182]

Further, the high administration expenses in private pension schemes are increasingly eroding the accumulated assets of occupational funds. Moreover, occupational funds are provident in nature; hence there is a risk of the pensioner outliving his retirement. Additionally, the government requires income received from annuities to be taxed. Also, the large withdrawals in

[181] South Africa National Treasury Paper (n 179) 5.
[182] Ibid.

occupational funds lead to insufficient balances upon retirement in the Pension Fund.[183] Last but not least, the vast majority of pension scheme members start contributing too late in their careers to accumulate sufficient assets. Moreover, they cash in their savings when they change jobs.

To add on, studies have indicated that the cost of retirement fund arrangements in South Africa is high, relative to international benchmarks. While occupational funds appear slightly expensive overall, retirement annuity products offered by the 22 long term insurance industry appear to be very expensive when assessed both against local alternatives and international benchmarks.[184]

4.4 Areas of Improvement

South Africa can establish a contributory compulsory National Social Security Fund, for those in the formal sector, up to an agreed earnings threshold. International practice suggests that a rate of between 13 and 18 percent of an after-tax wage (equivalent to between 11.5 and 15 percent of a before-tax wage) would be required to finance basic retirement savings, disability and death (survivor) benefits, unemployment insurance and administrative costs.[185] However, participation by those in the informal sector should be voluntary with incentives targeted at the informal sector, to enhance participation. Such a scheme should provide benefits such as basic retirement, unemployment, death and disability benefits. This will aim to close the wide gap that exists between social assistance grants and current private sector provision.[186]

[183] Hu & Stewart (n 39) 5.
[184] South Africa National Treasury Paper (n 179) 21-22.
[185] Ibid 15.
[186] Ibid 4.

In addition to a mandatory participation in a National Social Security Fund, the formal sector workers should be compelled to participate in private occupational or individual retirement funds.[187] At the same time, South Africa should do away with provident funds and instead embrace provision of annuity benefit.[188]

South Africa can also improve its pension system by removing or significantly increasing the means test threshold, of its social assistance grants that is funded from general government revenue. This will assist in providing a safety net against poverty in old age, and providing basic support to the disabled, children and care-givers.[189]

It is my opinion that, South Africa can benefit by prescribing a minimum number of employees in an occupational fund, in a bid to reduce administrative costs. Therefore, if an employer has a below minimum number of employees in its occupational fund, then the occupational fund should register under an Umbrella Fund, where administrative costs will be lower and there is risk-pooling. Further, the South African regulatory body should curb administrative costs by schemes, as is the case in Kenya.

Moreover, there should be restriction on early withdrawals among the formal sector employees, both in occupational and individual funds (whichever one chooses).[190]

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[187] Ibid.
[188] http://euracs.eu/summaries/south-africa-pension-summary/ accessed on 5 August 2016.
[189] Ibid.
[190] Ibid.

Also, there should be effective competition in the annuities market to curb excessive costs of annuities. One way in which effective competition among retirement product providers can be increased, with a view to lowering the costs of retirement savings products, particularly annuities, is to permit a broader array of providers, including collective investment scheme managers and banks to enter the market.[191]

What's more, income from annuities for private occupational and individual funds should be tax exempt. At the same time, there should be preservation of retirement benefits (currently full withdrawal benefit from retirement funds may be taken in cash on leaving an employer).[192]

It is further my opinion that there should be a National Scheme targeted at the informal sector, similar to that of the Mbao Pension Plan and the National Pension Scheme in India.

4.5 Social Security in India

The Indian old age security system can be classified as: Civil Service Schemes; the EPFO; Voluntary Occupational Pension Schemes; Public Provident Fund; National Old Age Pension (NOAP) Scheme; National Pension Scheme (NPS) and Micro-pensions and other alternatives.[193]

Under the Civil Service Pension Schemes, it is the central and state government employees that receive pension under these schemes. The pension payments under these schemes were defined benefits and were related to final salary. They were paid out of current revenues of respective central and state governments. Recently, these schemes are changing from defined benefits

[191] Ibid 22.
[192] http://euracs.eu/summaries/south-africa-pension-summary/ accessed 5 August 2016.
[193] Ayanendu Sanyal, *Universal Pension Scheme in India*, (Working Policy No: 420, Indian Institute of Management Bangalore August 2013) 7.

schemes to a defined contribution schemes for the new entrants (New Pension System); whereas the old scheme still provides pensions for employees who joined the Civil Service prior to 2004 and the armed forces.[194]

The EPFO Schemes are mandatory pension programs run by the EPFO, which is the equivalent of the NSSF in Kenya. The mandatory pension programs are established under the EPF & MP Act 1952. These mandatory pension programs established by the said Act, consists of three schemes: the Employees' Provident Fund Scheme 1952; the Employees' Pension Scheme 1995; and the Employees' Deposit Linked Insurance Scheme 1976.[195]

The EPF & MP Act 1952 together with the EPFO schemes are framed and managed by a tri-partite board known as the Central Board of Trustees, Employees' Provident Fund, consisting of representatives of Government (both Central and State), employers and employees. The Board (which is assisted by the EPFO) manages a contributory provident fund, pension scheme and an insurance scheme for the workforce engaged in the organized sector in India. It is one of the world's largest organizations in terms of clients and the volume of financial transactions undertaken by it.[196] The EPFO compulsorily covers formal sector workers with monthly earnings of Rs.6,500 or less at firms with 20 or more members in defined industries.[197] The third classification of schemes is the voluntary occupational schemes, also known as superannuation funds, which target the organized sector employees and provide additional pension benefits, mainly in the form of defined contribution plans. The main reason to set up voluntary funds was

[194] Ibid.
[195] Ibid 8.
[196] Ibid.
[197] Ibid.

the low income limit in the Employees' Provident Fund, which means that group pension plans often only cover senior executives. Superannuation funds can either be run internally as a trust fund, or externally in co-operation with life insurance companies.[198]

Another category is the Public Provident Fund (PPF) initiated in 1968. It stands as a voluntary tax-advantaged defined contribution saving option using personalized accounts. This scheme has been open to all citizens (except non-resident Indians), but since it uses income tax rebates as incentives for customers, it has mainly attracted formal sector workers, who pay income taxes. The minimum contribution is Rs 500/- per annum and the maximum contribution is Rs.1, 00,000/- per annum. Withdrawals are allowed from the sixth year and a subscriber is entitled to withdraw the entire fund after the expiry of a period of fifteen years. Also, loan facilities are available from the third financial year up to fifth financial year.[199]

As regards the NOAP, this was introduced by the Indian Central Government in 1995, in an effort to widen the reach of the social safety net for the aged poor. This is a more comprehensive old age poverty alleviation program under the aegis of the National Social Assistance Programme (NSAP).[200] In 2011, the eligibility age was reduced from 65 years to 60 years and the Old Age Social and Income Security project (GOIs) contribution was increased to Rs. 500 per month for persons above 80 years.[201]

The NPS is yet another scheme which has evolved over the years, after 2003. The NPS was made operational from 22 December 2003, for all new recruits of Central Government

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[198] Ibid.
[199] Ibid 9.
[200] Goswami R, *Indian Pension System: Problems & Prognosis*, (Fellow, Indian Institute of Management Bangalore) 7.
[201] Ayanendu Sanyal (n 193) 9.

employees (except for the armed forces) joining service on or after 1 January 2004. The NPS originated based on the Old Age Social and Income Security project (GOI, 2000), Report of the Working Group (GOI, 2001) and Report of the High Level Expert Group (GOI, 2002) commissioned by the Central Government. These reports led to the setting up of a Pension Fund Regulatory and Development Authority (PFRDA) in October 2003 and introduction of a PFRDA bill in Parliament in 2005. An extension of the NPS occurred on 1 May 2009, when this scheme was extended to all citizens of India. On 1 December 2010, the voluntary pillar was introduced. In order to widen the coverage, another scheme called NPS-Lite was introduced. Of importance to note is that both the NPS and the NPS-Lite are contributory schemes with Individual Retirement accounts and do not provide a guarantee of pension. As of 7 May 2013, only 4,90,988 individuals have subscribed to the scheme, of which more than fifty percent are civil servants for which the scheme is mandatory. To encourage people from the unorganized sector to open a pension account, the Indian government has started a new initiative, *swavalamban,* under which government contributes Rs. 1000 per annum for each NPS account in 2010-11 to 2012-13.[202]

As regards the Micro-pensions and other alternatives, Micro-pensions are provided by microfinance institutions. Micro-pensions have gained considerable relevance in India in recent years with the development of Microfinance Institutions and Non-governmental Organizations (NGOs). Micro-pensions adhere to the needs of very specific individual groups or local communities in exchange of low contributions and low premium. In terms of coverage, one of the most successful examples is the Self-Employed Women's Association (SEWA). In 2009, 50,000 self-employed women were enrolled in SEWA's micro-pension scheme. Nevertheless,

[202] Ibid 9-10.

micro-pensions are targeted to specific groups and can certainly be regarded as a measure to reach certain economically disadvantaged groups but not the masses. Other alternatives are long-term saving options offered by banks, and pension schemes offered by insurance companies that provide the investor with a choice of funds.[203]

Therefore, the formal old age income security system in India can thus be classified into three categories. The upper tier consists of statutory pension schemes and provident funds for the organized sector employees; the middle tier is comprised voluntary retirement saving schemes for the self-employed and unorganized sector workers, while the lower tier consists of targeted Social Assistance Schemes and Welfare Funds for the poor.[204]

4.6 Strengths of the Indian Pension System

The NPS, which encourages voluntary participation of those people who do not have any form of private pension, has two accounts that is: tier-I and tier-II. Tier-I does not allow premature withdrawals before retirement, while Tier-II is withdrawable and does not have tax incentives. In addition, upon retirement, members are mandated to invest 40% of the accumulated assets to buy annuities. The remaining assets can be withdrawn in the form of lump sum. The fore-going does away with the risk of a member outliving his pensions.[205] Besides, the NPS requires its unorganized sector to access its retirement benefits through partial purchase of an annuity, which ensures that members do not outlive their pension. What's more, the amount and periodicity of

[203] Ibid 10.
[204] Goswami R (n 200) 7.
[205] Stewart and Yermo (n 175) 19.

contributions are subject to the discretion of employees and employers, with no mandatory requirements.[206]

The NPS also has low administrative costs, which consequently intends to encourage voluntary participation of those people who do not have any form of private pension.[207] Besides, 30% of the poorest elderly, regardless of whether they have contributed over their career life, are covered by the NOAP scheme, which pays a monthly pension of Rs 75. Currently, there are around 7.3 million people covered.[208] In addition, in order to encourage people from the unorganized sector to voluntarily save for their retirement, the Central Government launched a co-contributory pension scheme, 'Swavalamban' in 2010. Under the said scheme, the government contributes a sum of Rs.1,000 to each eligible NPS subscriber who contributes a minimum of Rs.1,000 and a maximum of Rs.12,000 per annum.[209] Additionally, India has numerous schemes that target the uniqueness of its unorganized sector.

4.7 Weaknesses of the Indian Pensions System

Despite the numerous schemes set up in India, that are targeted at the informal sector, like the NPS, the Public Provident fund among others, coverage among the informal sector remain low due to lack of financial education targeted at the informal sector. For example, around 80% of the informal sector employees in India surveyed by the Asian Development Bank (ADB 2006) did not know what a pension was. Likewise, even though they meet the criteria, very few

[206] Hu & Stewart (n 39) 20.
[207] Ibid.
[208] Hu & Stewart (n 39) 19.
[209] https://india.gov.in/spotlight/national-pension-system-retirement-plan-all, accessed on 29 July 2016.

informal sector workers join the Public Provident Fund in India.[210] Also, the EPFO which administers mandatory plans to which the unorganized sector are voluntary contributors, has the dual role of being the enforcement agency to oversee the implementation of the EPF & MP Act and as a service provider for the covered beneficiaries throughout the country.

It is my opinion that these dual roles, presents conflict of interest, and negate the corporate governance principle of existence of checks and balances, in a bid to ensure accountability. In addition, the EPFO has a bloated board of trustees. Such a board is costly, which contributes to high administrative costs and low returns. On the same breath, such a board encourages non-participation of board members. Further, liberal withdrawals under the Employee Pension Fund and consequent poor returns, exposes workers to highly inadequate terminal accumulations and potential destitution in old age.[211] Lastly, the Indian pension system is extremely complicated and fractured.[212]

4.8 Areas of Improvement

There should be financial education targeted at the informal sector in India, in a bid to take advantage of the various schemes that have been set up for this particular group of people. Further, in 2006 Asian Development Bank (ADB 2006) produced a report with a focus on how to encourage people in the unorganized sector to join the NPS. The recommendation was that the system should be designed to target those who are capable of saving (given that there will always be a certain proportion of population in the informal sector who are too poor to save, or put aside

[210] Stewart and Yermo (n 175) 7.
[211] Vaidyanathan. R, *Mandatory Retirement Schemes: Challenges Ahead*, (Special Issue, 2004, the ICFAI University Press) 23.
[212] Hu & Stewart (n39) 2-3.

extra money for the distant future, so that tax incentive, low entry cost, etc might not be sufficient to encourage their voluntary participation). For those who are capable for saving for their retirement, the ADB recommended actions be taken to facilitate their participation, like innovative marketing strategies and public awareness campaigns for private pensions.[213] Furthermore, the Indian pension system should be simplified and less fragmented and efforts made to merge or dissolve existing pension schemes. To add on, the EPFO board of trustees should be reduced to not more than ten, as per global corporate governance principles. Moreover, the EPFO should reduce its administrative costs in order to encourage participation by the unorganized sector. The EPFO should also limit withdrawals from the EPS, to ensure adequacy of terminal benefits. Lastly, there is need for a separate body to regulate and supervise the affairs of the EPFO, to ensure accountability.

4.9 Conclusion

In summary, a critique of the South African and the Indian pension system are informative to Kenya's social security reforms among the jua-kali sector. For instance, the South African old age social grant which non-contributory and means-tested in nature and which covers 75% of the population, informs Kenya that, if a similar scheme is set up in Kenya, then there may be no incentive for the informal sector to save for retirement. Similarly, from the South African quasi-mandatory occupational schemes which are mostly provident funds in nature, we learn that upon retirement, the informal sector in Kenya, who save with the NSSF, are likely to outlive their retirement benefits, which are provident in nature.

Conversely, from the diverse Indian social security systems which encourage participation of the unorganized sector, by offering a range of incentives, the Kenyan legislators can learn to provide

[213] Stewart and Yermo (n 175) 20.

a range of incentives targeted at the informal sector, in a bid to enhance informal sector participation in the NSSF. At the same time, the complex and fragmented Indian pension system is illustrative that diverse schemes targeted at the informal sector is not necessarily the answer. Also, the NPS in Indian, which targets the informal sector and which requires members to access a sizeable portion of their retirement benefits through purchase of annuity, is illustration that if legislators provide for incentives targeted at the informal sector, then the informal sector can save more and make an informative choice to access part of their pension through purchase of annuity. At the same time the Indian experience teaches Kenya the importance of conducting public awareness on pensions to enhance participation of the informal sector in the NSSF Act 2013.

CHAPTER FIVE

CONCLUSION & RECOMMENDATIONS

5.0 Introduction

This chapter concludes by presenting the findings to this study's research objectives and hypothesis. Also, in a bid to come up with legal reforms, this paper has presented its recommendations, drawn regionally and globally, by looking at the South African and Indian pension experience. Likewise, recommendations are drawn from Mwongozo 2015, which is the code of governance for state corporations in Kenya.

5.1 Conclusion

This study observes that appropriate Pension schemes for persons in the jua-kali sector remain a challenge for many developing countries, including Kenya. Pension income may not provide the life that one lived when in active employment, but it provides an avenue to reduce poverty. In the same vein, paying out lump sum benefits is counterproductive. The ILO (1997) argues that provident funds have serious limitations in alleviating old age poverty, because it does not provide protection against the whole length of the contingency. That is to say that there is a high risk that a pension beneficiary will outlive a lump sum payout. Also, the experience of Provident Fund Schemes in India suggests some practical limitations of a pure provident fund arrangement, like the inability to ensure that lump sum payments are used to provide old age protection. This is because majority of the workers being low wage earners have little additional savings and much of the lump sum amount is spent in meeting essential needs after retirement.[214] However, if

[214] Goswami R (n 200) 11.

the Kenyan Parliament adopts the recommendations in this study, there is hope for increased coverage for this critical mass.

5.1 Recommendations

This study calls for an amendment to section 23(1) (a) and (b) of the NSSF Act 2013, to accommodate the jua-kali sector in terms of the amount and manner of contribution**.** In light of the jua-kali sector's high volatility in income, it makes sense to allow for flexible contributions, which correspond to the income pattern of this particular group, as is the case in India. Similarly, in order to encourage more people in the jua-kali sector to join the NSSF, it is advisable to target those who are capable of extra saving, by conducting research, as was the case in India. Such research makes it possible to design new policies that are as attractive and flexible as possible, and adapted to the specific needs of the targeted group.

Also, financial education campaigns should be utilized to promote participation in the NSSF as explained in chapter four. Tax incentives should also be carefully designed, with mechanisms such as tax credits and matching contributions considered, to ensure that incentives successfully reach the jua-kali sector.[215]

Further, the Cabinet Secretary for matters related to social security in Kenya should in consultation with the NSSF Board, come up with regulations to provide for instances of withdrawals. For example, the NPS tier II account in India, permits withdrawals prior to retirement under exceptional circumstances, usually related to provision of health care.[216]

[215] Hu & Stewart (n 39) 12.
[216] Goswami R (n 200) 11.

This study further suggests that a person in the jua-kali sector, who enrolls to be a member of the NSSF, access his benefits partially as a lump-sum (one third), while the reminder utilized as annuity. This will however require a higher rate of contribution. This study suggests that a higher rate of contribution can be achieved by conducting financial education campaigns and by targeting -through research-, those capable of extra saving. The Kenyan Government may in addition match the contributions made by persons in the jua-kali sector, to encourage participation in state pension, as is the case in the Swavalamban co-contributory pension scheme in India.

This study also encourages the NSSF board to adhere to Mwongozo 2015.[217] According to Mwongozo 2015, each Board member has obligations as enumerated at section 1.3. In the circumstances, this paper recommends an amendment to section 7 of the NSSF Act 2013, by adding an additional ground for disqualification of a board member. The additional ground for disqualification being, "failure, neglect and or refusal of a trustee to perform his obligation. This means that in the event a board evaluation is conducted on the board as a whole and on its board members, and the results are below standard, then the fore-going will be a ground for disqualification, to pave way for more competent individuals. Indeed, section 1.5(2) of Mwongozo 2015, states that renewal of a board member's tenure for a second term, be subject to a favourable board evaluation.

[217] Mwongozo is the code of governance for state corporations that are aligned to the Constitution 2010. Mwongozo, 2015 was issued through an executive order by the President of the Republic of Kenya, on 25th March, 2015, to provide directions for the effective governance and oversight of state corporations. Through the executive order, all boards of state corporations were directed to implement the provisions of Mwongozo, except as otherwise provided by an written law.

Also, on board issues, section 1.22 of Mwongozo 2015 recommends separation of the office of the CEO (Managing Trustee of NSSF) and that of Corporation Secretary. This study therefore recommends amendment to section 15(3) of the NSSF Act 2013, to enable separation of the two offices, which is currently held by the Managing Trustee.

Mwongozo 2015 further requires the NSSF Board to ensure effective, accurate, timely and transparent disclosure of pertinent information on NSSF operations and performance. This is supported by the Constitution 2010,[218] and is important as it creates and sustains stakeholder and public confidence. This study recommends the NSSF board recommitment to section 51 of the NSSF Act 2013.

Furthermore, this study is of the view that both the role of the NSSF board and shareholder involvement (NSSF members) is equally important. According to section 5.2(a) of Mwongozo 2015, shareholders are required to monitor the performance of the NSSF board. Being that there is power in numbers, this study proposes that shareholders take pro-active steps to form a shareholder association, to be able to efficiently handle its obligations, similar to that taken by minority shareholders of listed companies. This study therefore suggests an addition of a clause dealing with shareholder obligations, to enable increased shareholder involvement. This study proposes that members of the NSSF have the power to appoint an auditor at the AGM and power to call for an extra-ordinary general meeting.

This study further suggests that the remuneration of board members should be determined by the SRC; this will ensure fairness and responsibility in the use of public resources. On the strength of

[218] Constitution 2010 (n76), s 232(1) (f).

the fore-going, this study suggests an amendment to section 13(1) of the NSSF Act 2013, to enable determination of remuneration of board or committee members by the SRC.

To add on, the Constitution 2010 requires the NSSF board to be guided by the principles of public service.[219] Specifically, the Constitution 2010 requires the board to be efficient, effective and economic in the use of resources.[220] This study therefore suggests a recommitment to section 50 of the NSSF Act 2013, so as to ensure that administrative costs do not exceed two percent (2%) of NSSF's total assets. This will require the NSSF to down-size its staff, with a view to reduce expenses and increase returns.

In view of the challenge of low awareness of the NSSF Act 2013 and pensions in general, the Kenyan Parliament should consider raising public knowledge and awareness on pensions. For instance, the Retirement Benefits Authority, through the Mbao Pension Plan, has undertaken training and financial education projects.

This study also calls for implementation of the existing penalty clauses by the Retirement Benefits Authority, as against the NSSF, in lieu of amendment to the relevant penalty provisions. The RBA 1997 makes it an offence for any scheme to fail to submit a copy of its audited accounts to the Retirement Benefits Authority, within six months after the end of each financial year.[221] The said Act further prescribes a penalty of a fine not exceeding Kshs 500,000/= or imprisonment for a term not exceeding two years or both.[222] The Act further states that where

[219] Ibid, Chpt Thirteen.
[220] Ibid, art. 232.
[221] RBA 1997 (n2), s 34(4)(A).
[222] Ibid.

there is a continuing offence under section 34(4A) of the said Act, then the scheme in default will be liable to a further fine not exceeding Kshs 500,000/=, for each day which the offence continues.[223]

Correspondingly, this paper recommends amendments to the said penalty provisions in the RBA 1997, specifically sections 34(4A) and 34(4A), with a view to implement stiffer penalties. For instance, the Pensions Reform Act 2014 of South Africa provides for stiffer penalties in the case of mismanagement or diversion of pension funds. The operators who mismanage pension funds are liable upon conviction, to not less than 10 years imprisonment or to a fine of an amount equal to three times the amount misappropriated or diverted, or both imprisonment and a fine. In addition, a convicted person would be required to refund the amount misappropriated and forfeit to the federal government any property, asset or fund which accrued interest or the proceeds of any unlawful activity.

Additionally, this research prescribes for review of the mortality tables that currently negatively affect pricing of annuities to the detriment of a pensioner, more so a person in the jua-kali sector.

This study also calls for incentives to attract and retain annuity providers in the market. For instance, on the issue of lack of assets to match the liabilities: The Kenyan Government can introduce policy initiatives to enable the life insurance companies' transfer or share exposure to longevity and other risks.

Lastly, exemption from tax for income emanating from Annuity products is suggested.

[223] Ibid, s 34(4)(B).

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