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UGANDA PENSION LIBERALIZATION:

Implications For Workers

Participants attending the 51st Session of the State of the Nation Platform at Protea Hotel in Kampala

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Abstract

Liberalization of the pension sector is critical for the growth and competitiveness of the economy; however, a comprehensive legal and regulatory system that covers both public and private sectors is necessary. The general aim of liberalization of the pension sector is to protect workers' savings and ensure that their savings are well invested to give a good return while minimizing potential risk, and allowing those who save to receive their benefits in the form of pension, lump sum payments or other forms of benefits. The proposed liberalization of the sector is based on the assumption that NSSF is poorly governed, as evidenced by a record of corruption scandals. Currently, concerns about liberalization of the sector include the creation of additional costs associated with trustees, fund managers and administrators, all of which reduce the value of workers' savings. Questions also exist about the necessity of the Uganda Retirements Benefits Sector Liberalisation Bill, given existing provisions in the NSSF Act that can be amended to include other qualified players.

Advocates Coalition for Development and Environment (ACODE) organized the 51st State of the Nation Platform under the theme "Uganda Pension Liberalization: Implications for Workers". The key speakers for the session were drawn from NSSF, Ministry of Finance, Uganda Retirement Benefits Authority, and academicians. Their presentations dealt with understanding how the proposed Uganda Retirement Benefits Sector Liberalization Bill will address the social protection of workers, the role of Uganda Retirement Benefits Authority, and analysis of the investment environment for an effective NSSF. The

presentations were followed by discussions from which key policy recommendations emerged. It was agreed that there is need for strong regulatory systems and monitoring to ensure that the contributions of workers are secure.

A. Introduction

The 51st STON platform allowed key stakeholders to understand the emerging role that finance and the free market is likely to play with the liberalisation of pensions. The presentations provided an opportunity for the experts to share their knowledge, clarify questions and define terminology. The STON platform intends to facilitate a deeper understanding of the emerging financial markets in Uganda to inform future debates and decisions regarding NSSF contributions, liberalisation, financial regulation and the roles of the government and private sector.

The presenters for the session included Morrison Rwakakamba, Executive Director Agency for Transformation (AFT), who presented AFT's position and future ambitions connected to social security pension savings. Keith Muhakanizi, Ministry of Finance, gave a brief overview of political theory and suggested that civil servants pay their own pensions, whilst Moses Bekabye, Executive Director of the Uganda Retirement Benefits Authority, clarified the meaning of terminology and the roles of regulators and investment managers. J. B.Kakooza, Lawyer & Private Consultant, addressed confusion surrounding responsibilities of money management and the true owners of NSSF money, whilst Ms. Geraldine Ssali, Acting MD, NSSF, gave an overview of the work being done by NSSF and discussed recommendations including the building of local capacity to manage pension funds and the necessity to issue government infrastructure bonds to address limited investment opportunities. Kabumba Busingye, Law don Makerere University, talked at a theoretical level about the advantages of the state adopting responsibility for national concerns, and also suggested that Ugandans who can afford to pay extra tax do so in order to increase the level of social security of the more economically marginalized.

B. Brief Background

Uganda has a working population of approximately 14 million people, most of whom work in the informal and agriculture sectors respectively. The current pension system comprised of the NSSF, the Public Service Pension Scheme, and occupational voluntary savings cover less than 5% of Uganda's workforce. The reforms therefore will expand coverage not only to those in the formal sector, but also to those who are self employed and in the informal sector. The latter comprise majority of workers in Uganda.

In 2011, the Uganda Retirement Benefits Regulatory Authority Act was passed to transform the pension system in the country. The main objective of this Act is to ensure that all pension scheme and service providers are licensed prior to undertaking any business. At the time of writing, the Retirement Benefits Sector Liberalization Bill was before Parliament. The reforms in the pension system are intended for employees in the formal and informal sector, all of whom will be required to make contributions to the existing NSSF and other licensed pension schemes. Workers will be obliged to make contributions to NSSF for a period of 5 years after the law is passed and the savers will be at liberty to transfer their savings to other pension schemes. According to Uganda Retirement Benefits Authority, the planned liberalization is intended to spur growth in employee contributions every year and eliminate a monopoly of NSSF over workers' savings thereby encouraging competition.Liberalization is aimed at opening up the sector to more players, improve governance of the sector as a whole and build trust and confidence to encourage savings.

C. Presentations

1. An Overview of the Investment Environment for an Effective NSSF

Presenter: Ms. Geraldine Ssali – Acting MD, NSSF

Acknowledging the recent silence from NSSF employees on the liberalisation debate, Ms. Ssali highlighted the need to contribute to the debate and requested support from the government who, she says, must resist criticising a statutory organisation [NSSF] that they set up. Promoting national employment and capacity building is vital to being able to run pension funds without using international fund managers. Integral to this is the promotion of healthy and meaningful competition, given the prevalence of bright Ugandan minds.

Currently, fixed income to banks and government is 82% with yield at about 13%. The NSSF is running on income made from investment earned from 17% interest rates, which are currently being reduced. Monthly earnings are at an all-time high of 58 million UGX despite Government investments always being under scrutiny. Infrastructure bonds paid out by the NSSF include 432 billion UGX in Kenya infrastructure bonds, 75 billion UGX in Rwanda government bonds and none to Uganda as bonds still remain to be administered. Ms. Ssali recommended the production of government bonds as safe monies to drive the economy.

External aid support is becoming unnecessary because Uganda can finance itself if the Bank of Uganda and the Ministry of Finance support the issuance of bonds. Ms. Ssali highlighted the absurdity of financing regional governments since the opportunity to buy government bonds do not exist in Uganda. She noted that even if bonds are expensive, all money spent returns to Uganda.

The ambitions of the NSSF include a move into private equity, as the NSSF exists as a large investment player in Uganda. NSSF contributions arrive at a rate of UGX 58 billion a month. This is currently higher than the rate of investment due to limited investment opportunities, causing an imbalance and concentration of risk in the Fund's portfolio. Indeed, hedge fund managers currently cannot absorb all the money being directed to them. Moreover, Ms. Ssali questioned hiring a hedge fund manager to make investments that she is capable of doing for free, highlighting the counterproductive measures that require the authorisation of every transaction. Ms. Ssali noted that the bill is silent on laws that hinder fair competition like PPDA [Public Procurement and Disposal of Public Assets Act], and requested that government not claim the NSSF a failure when laws have been created that directly undermine NSSF activities.

Cautious investment in line with the interests of savers is required to remain focussed on the main objective of the reform. Ms. Ssali suggested that NSSF investors not compete on markets using the 10% NSSF contribution fee, but instead keep the 5% for competition and the savings for 10%. This advice was based on the example of the UK pension scheme which failed, suggesting an aversion to investing heavily in risky hedge funds and managers.

Discussant: Morrison Rwakakamba – Executive Director, Agency for Transformation (AFT)

Clarifying the AFT position that social security pension savings shouldn't be subject to the market for purposes of profit, Morrison highlighted additional options for increasing wealth, including the stock or property market. The pension liberalisation bill, as it stands, pursues an unfavourable liberalisation of workers' money that is vulnerable to hedge fund managers and investment bankers. Given that higher returns require tactical and increasingly risky investment options, such as derivatives, the likelihood of financial loss is high. Losing pension money from risky investments would render any potential profits irrelevant as political crisis would likely ensue.

The current NSSF bill must increase the financial security of pension holdings even whilst additional investment options are explored. Mandatory NSSF contributions must remain NSSF responsibility, although families could make additional contributions beyond the NSSF requirements without repealing NSSF as it currently stands. A NSSF monopoly would see savers less likely to get a return on their savings.

Additionally, the NSSF could embrace social healthcare coverage, insurance and credit for savers by guaranteeing a certain percentage of existing savings. With only 400,000 savers amongst a workforce of 10,000,000, the NSSF must reform, strategize and incentivize workers in the informal sector to join the NSSF, because increasing the number of NSSF members provides the opportunity for government to borrow internally and invest nationally with increased revenues.

Borrowing and lending internally and in local currency (Ugandan Shillings) is beneficial as it reflects local market value and trends as opposed to global exchange rates where the UGX performs comparatively weakly. Borrowing and lending internally would reduce capital flight and see money go back to Ugandans, ensuring value for money on investments.

A degree of financial nationalisation would support the people of Uganda. By contrast, current government borrowing trends (using commercial banks) see commercial banks making a profit on high interest rates with little attention to lending fairly to citizens.

2. Retirement Benefits Sector Liberalisation Bill: How will the proposed law address social protection for workers?

Presenter: Keith Muhakanizi – Secretary to Treasury, Ministry of Finance.

Mr Muhakanizi commented on differences in liberalisation and privatisation, drawing from political theory. Questioning the recent politicisation of pension issues, Mr Muhakanizi highlighted that Norbert Mao was trying to capture votes for 2016 and encouraged participants to be critically aware of additional agendas beyond policy reform.

Liberalising pension funds intends to increase efficiency and coverage, and within the NSSF would lead to irreversible progress. Liberalisation, Mr Muhakanizi suggested, would also regulate the NSSF Mr Muhakanizi opposed the closure of the NSSF noting that funds should not be regulated by the Ministry of Finance if they are corrupt. He suggested that if the Parliament of Uganda invests funds, the NSSF requires technical experts [not ministers] to invest appropriately in line with investors' expectations of a high rate of return. He also proposed that civil servants fund their own pensions.

3. Role of Uganda Retirement Benefits Regulatory Authority in Social Protection for Workers in Uganda"

Presenter: Moses Bekabye – Executive Director, Uganda Retirement Benefits Authority

Mr Bekabye noted that social security extends beyond pension benefits to include policies on the economy, employment, health, education, agriculture, and peace and security. Retirement benefits accrue as a result of employment and additional benefits available depending on the scheme. Social security should be paid for through taxation, not employment participation, and age should be the only eligibility for inclusion. This allows participants to receive uniform and basic benefits for health and social needs.

Increased competition amongst players to manage mandatory NSSF contributions require the government to provide a choice. The NSSF has failed; despite recently improving, running for thirty years with current coverage at 30% is unacceptable. Removing the threshold of five employees before contributions are mandatory remains discriminatory as those in government are not included, nor are those who employ less than five employees – often purposely to avoid contributions. Removing the five employee threshold would see the levels of NSSF inclusion increase to 265,000 businesses, excluding agricultural and household based firms. Whether the NSSF is equipped to handle this is unclear.

Mr. Bekabye also stressed that asset management is a specialised business requiring full commitment to mitigate risk and balance wealth. Locking up funds or investing in fixed income does not safeguard funds. Instead, a diverse investment portfolio is necessary with a regulator to provide security. The Ministry of Finance does not make executive investment decisions and fund managers do not hold funds or assets; rather, they advise a board of trustees as to where to invest. The NSSF could potentially finance the government budget if government or any private organisation wished to borrow from it, but only through transparent means with the issuance of a bond.

Discussant 1: JB Kakooza – Lawyer & Private Consultant

Mr. Kakooza noted that the entire debate was impeded by confusion about the differences between pensions, the NSSF and the various regulations and responsibilities surrounding them. With regards to NSSF contributions, organisations with less than five people can choose to contribute and are not banned from doing so. On pensions, intergenerational support means that current workers support those who are already retired – those paying taxes do not fund the pensions of their peers. The fully funded civil service pension scheme proposed by Mr. Muhakanizi would require financing an obligation that is yet to arise. A self-funded civil service pension scheme requires an additional 10% of the wage bill to pay for the pensions of those who have not yet retired. The fiscal burden would triple for the next three and a half years to solve a problem that is 40 years away.

Regarding the ownership of NSSF savings, the 10% majority contribution from government sees two thirds of NSSF money as government money. Employees are statutorily required to contribute to the NSSF whilst contributions from employers are later taken off in taxes as the government provides tax relief for contributing to the NSSF. Issues with the NSSF include an aging population who require much longer term support than originally anticipated, and unregulated private pension schemes. The NSSF fund ensures that money is available on retirement; thus, retirement money must never be invested in high risk opportunities. Finally, recognising the differences between investing for growth and investing for income is vital.

Discussant 2: Kabumba Busingye – Law don, Makerere University

Dr. Kabumba discussed 'the vulnerable subject and the responsive state,' where citizens are inherently vulnerable and require a response from the state. Pointing out the coercive ways that the Ugandan state has intervened in the market, he argued that no state can truly adopt a pure free market without intervention. The question then, Dr. Kabumba suggested, is not whether the state should respond but how the state should respond.

Using the NSSF as a means to protect vulnerability, including domestic workers as contributors to the NSSF, is a plausible idea as it is unsustainable to ensure pensions for only a few specific Ugandans. With the existing savings in the NSSF and fair competition, any recent increase in the levels of efficiency by the NSSF is not the result of best practice by the institution but is in direct response to increased competition from other establishments. Guidance must also be provided to savers who support high risk/high return investors to alert them to likely losses associated with high risk investments and ensure that they do not later rely entirely on the NSSF for financial support and returns.

Economic competition is attractive for those with existing savings. Dr. Kabumba suggested that a more ambitious approach to ensuring that the needs of all Ugandans are met is to have Ugandans who can afford to, pay extra tax to look after those who can't. This is as an act of self-preservation to avoid a dying population which is not safe or sustainable. He added that this would also require the state to explore the possibility of a national health insurance scheme.

D. Policy Recommendations

1. **Focus on Stakeholders' Interests:** The financial interests of stakeholders, particularly those with investments in the NSSF, must be acknowledged and incorporated into future NSSF developments.
2. **Improve Civic Education on Current Economic Terminology:** Clarity and education for citizens on the NSSF, pension schemes, hedge funds, financial regulators, economic terminology, the roles of the private sector, the pension reform privatisation and liberalisation approaches must be widely shared for civic understanding on current economic affairs. This will increase the quality of debates, allow for the inclusion of civic opinion and strengthen future reforms.
3. **Ensure Capacity Building for Financial Sector Employment:** National employment and capacity building must be facilitated to reduce current reliance on international hedge fund managers and allow Ugandan nationals to engage with the upcoming changes in the national economic architecture. This requires Ugandan nationals to be trained for employment in the financial sector.

4. **Address and Reduce Institutional Corruption before Market Liberalisation:** Currently, vested interests in policy reforms connected to use of foreign funds are both personal and business related. A shift needs to occur to ground these reforms solely in national and business interests. This will require that accountability and punishment for the misuse of funds be constitutionalised coherently. Participants also identified a non-corrupt institutional framework as a prerequisite to liberalisation noting that current management institutions are poorly equipped to successfully manage liberalisation which, following a reduction in corruption, must be pursued gradually and deliberately.
5. **Increase Membership and Inclusion of NSSF:** NSSF should increase the number of active memberships and contemplate managing social healthcare coverage, insurance, and credit options for savers. This would increase the financial base of the NSSF, provide a multitude of options for savers, and increase confidence in government institutions.
6. **Issue Ugandan Bonds:** Following the recommendations of Ms. Geraldine Ssali and other participants, it was advised that borrowing and lending internally with the issuance of Ugandan government bonds must be pursued. Of particular importance is the creation of infrastructure bonds which may reduce reliance on external aid support. The creation of bonds would also address the problem of limited investment opportunities for NSSF investors and the public.