
NIGERIAN BAR JOURNAL

Volume 3 No. 1 January 2005
ISSN 0795/5464

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Errata

**The correct citation of
this volume is Volume 3
No.1 January 2005.**

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The Nigerian Bar Journal is published quarterly by the Nigerian Bar Association.

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NIGERIAN BAR JOURNAL

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THE FEATURES AND CRITICAL APPRAISAL OF PENSION REFORM ACT, 2004.

BIOLA ADIMULA *

INTRODUCTION

The Federal Government of Nigeria sponsored and saw to the Bill that led to what is now known as Pension Reform Act, 2004 which repeal the Pension Act, Cap. 346, Law of Federation, 1990 as from 25th June, 2004 when it was finally signed into Law by the President, Chief Olusegun Obasanjo (GCFR). It is important to note that the persistent problem of under funded pension gaps on public enterprises happened out for privatization led to the inauguration of the steering Committee led by Chief Fola Adeola on Pension reforms¹.

The Committee after careful study of its terms of reference, which among others, include the examination of problems of Pay-As-you-Go (PAYG) Pension system currently being implemented. The major criticism of private sector scheme, as identified by Adeola led Committee, is that there are some organizations that are supposed to operate retirement benefit schemes, but who do not have one in place.

Chief Fola Adeola and his Committee based their work on the need to achieve some objectives, which include:

- (a) Providing hope in the future by eliminating the disorder that marked the previous one.
- (b) Sustainability, safety and security of benefit, transparency, accountability, equity, flexibility, conformity and practicability.
- (c) The need to provide adequate, decent income per retirees and finding short and long term finding solutions to past deficits and outstanding deficits.

* LL.M; Associate Member, Certified Pension Institute of Nigeria, Membership No. 0135.

1. By the NCP on September 17, 2001.

It is the report of Adeola led Committee that gave birth to Pension Reform Act 2004, which established a contributory Pension Scheme for employees in the Public Service of the Federation, Federal Capital Territory and Private Sectors in the Federal Republic of Nigeria. The scheme is contributory, fully funded, privately managed and based on individual accounts. The Act covers private organization with 5 or more employees, together with the Federal and Federal Capital Territory employees² it excludes State Civil/Public services employees. However employee under an existing pension scheme which has three (3) or less years to retire and Judges of the Supreme Courts and Courts of Appeal in accordance with section 291 of the Nigerian Constitution are not affected by the Act³.

The prime objective of the Act is in three folds⁴ viz:

- a. To ensure every Federal, Public and Private Sector employee receive their retirement benefits as and at when due.
- b. To ensure employees save towards their retirement.
- c. To establish a uniform set of rules, regulations and standard for the administration and payment of retirement benefits.

Other perceived motives of the Act includes to create a pool of investable funds that will assist government achieve some of its medium to long term micro economic objectives of reducing interest rate and inflation, encouraging investment in the real sectors as well as develop basic infrastructure⁵.

The Act requires a periodic contribution from employer and employees, a minimum of 7.5% each of the total emolument of the employee to be paid into a retirement savings account held by a custodian on behalf of Pension Fund Administrator (PFA) in trust for the employee.

2. Section 1 (2), Pension Reform Act, 2004.

3. See Section 8 of the Act.

4. Section 2, Pension Reform Act, 2004.

5. Elizabeth Ngozi Ebi article on Essential Features of the Pension Reform Act, 2004, in the official journal of the Certified Pension Institute of Nigeria, January/April, 2005 at page 8.

ESSENTIAL FEATURES OF THE PENSION REFORM ACT, (PRA), 2004

1. Contribution/Benefit
2. Employee
3. Employers
4. Pension Fund Administrator (PFAs)
5. Pension Fund Custodian (PFC)
6. Pension Commission (Pencom)

Brief analysis of the features of the Act:

Contribution/Benefit:

The Pension Reform Act 2004 is a fully funded scheme which means that contribution are actually paid into the employees retirement account. Section (1) stipulate the rate of contribution for the employees and employers in the public and private sectors and the military. The employee and the employer in the public and private sectors shall each contribute 7.5% of the monthly emolument of the employee. For the military, the employer shall contribute 12.5% while the employee shall contribute 2.5% of the monthly emolument. The total contribution shall be a minimum of 15% of the employee's monthly emolument⁶.

However, employer may bear the full burden of the scheme or negotiate its contribution mix i.e an employer can decide to pay 11% while the employee pays 4%⁷. By the provision, corporate entities that are currently having a superior contributory scheme are encouraged to at least maintain the status quo.

Employees are allowed to make voluntary contribution⁸ above the mandatory 7.5% minimum. All contributions are tax-deductible expenses⁹ in the computation of the tax payable by the employee. However, voluntary contributors are taxable if drawn within 5 years from the date of the contribution.

6. See Section 9 (1) of the Act.

7. Provided that in such a case the employer's contribution shall not be less than 15% of the monthly emoluments of the employee. See s.9 (2) PRA.

8. See S. 9 (5) PRA

9. See S. 10 PRA

Employee, upon retirement or attaining the age of 50 years, whichever, is later, has the option of utilizing the accumulated amounts to purchase annuity for life from a licensed life insurance company, programme streams of monthly or quarterly withdrawal for an expected life span or obtain a lump sum from the balance standing to the credit of his retirement account, provided that the amount left after the lump sum withdrawal shall be sufficient to programme withdrawal of an amount not less than 50% of his annual emolument.

In addition to the mandatory contribution, employers are required to purchase a life insurance for the employee up to 3 times his annual emolument¹⁰.

Employee

The Pension Reform Act 2004 is primarily about the employee. The employee is defined by the Act, refers to those under employment in the public sector, Federal Capital Territory and private sector. Specifically, it refers to those having at least 3 years to retirement. With respect to the private sector, it refers to those in employment in organization with at least 5 employees.

The employee has his rights and obligation to the scheme. His prime obligation is to make his minimum statutory contribution. Some of his rights include:

- a. Right to choose and change his Pension Fund Administrator (PFA)¹¹.
- b. Right to reports on the status of his accumulated saving/investment portfolio
- c. Right to obtain benefit at retirement
- d. Right to withdraw additional contribution made above the stipulated minimum even before retirement
- e. Right to report to National Pension Commission where employer fail to remit contribution to the custodian or engage in the activities that contravenes the Act.
- f. Right to life insurance policy up to 3 times his total annual emolument.

10. See S.9(3) PRA.

11. Section 11(1) PRA

Employers

As already defined, the employer, as in the public sector and Federal Capital Territory is the Government (Federal) and in the private sectors, Corporate entities having at least 5 people in employment. The rights and obligation of the employer are enumerated below.

Rights/Obligations

- i. Deduct and source the contribution of the employees in his employment¹².
- ii. Remit the total contribution to the custodian appointed by the Pension Fund Administrator (PFA)¹³
- iii. Maintain a retirement account for all employees in a PFA of their choice.
- iv. Maintain a life insurance policy for the employee for sum up to 3 times his total annual emolument.

Pension Fund Administrator (PFA)¹⁴

The PFA is one of the main services providers introduced by the Act. A PFA must be a limited liability company registered by National Pension Commission. They will have a minimum paid up capital of N150 million as stipulated in section 50 (b) of the Act. The main responsibility of the PFA shall be:

- a. Open a retirement saving account for all employees with a PIN number attached.
- b. Invest and manage pension fund and assets in accordance with the provision of the Act.
- c. Maintain books of account in all transaction relating to pension fund managed by it;
- d. Provide regular information on investment strategy, market returns and other performance indicators to the Commission and employees or beneficiaries of the retirement savings account;
- e. Provide customer service support to employees; including access to employees account balances and statements and statements on demand;
- f. cause to be paid retirement benefits to employees in

12. Section 11 (5) (a) PRA

13. Section 11 (5) (b) PRA

14. See Section 44 of PRA

- accordance with provisions of the Act.
- b. be responsible for all calculations in relation to retirement benefits.
- c. other functions as directed by the Commission.

Licensing requirements for a Pension Fund Administrator (PFA) is Limited Liability Company whose object is to manage pension fund.

- i. Minimum paid up share capital of N150 million.
- ii. Professionally competent to manage pension funds and administer retirement benefits.
- iii. Applicant Company, if the subscribers, directors or officers are not linked to distressed or mismanaged fund.
- iv. Shall not engage in any other business other than management of pension funds.
- v. Satisfies any other requirements set by National Pension Commission.

Prior to the enactment of PRA 2004, the provisions of the Trustee Investment Act of 1962 regulated the investment policy of all pension schemes. The investment portfolios were then dominated by financial securities that have extremely low yield. Under the new scheme, investment restriction was relaxed and the funds investment horizon widened. Additional investment outlets are provided for in the PRA ACT including other instruments as the National pension commission (NPC) may from time to time describe.

It also implies that the PFA will not hold the Funds managed by it. The PFA is not allowed to engage in other activities except for managing pension fund.

Organization that wish to manage its own pension fund can register as a closed PFA provided they meet the minimum requirement for registration as stipulated in section 50 of the Act.

The benefit that will accrue to PFA was not covered by the Act. However, the Commission is expected to release a guideline that will shed more light on matters such as fees and commission to be charged by the PFA.

Pension Asset Custodian (PAC)¹⁵

This is the second service provider, introduced by the Act. The PAC is expected to be a licensed financial institution registered under the Companies Act and National Pension Commission respectively. To be qualified for registration by the commission, they will have a minimum net worth of N5 billion with a balance sheet size of N125 billion or wholly owned by a financial institution with a balance sheet worth of at least N125 billion. This requirement is to guarantee that the PAC has the capacity to hold the huge funds that will be trusted to it thus ensuring the safety of the Pension Fund.

The Function of the PAC shall be¹⁶:

- a. Receive the total contribution remitted by the employer on behalf of the PFA within 24 hours of the receipt of contributions from any employer;
- b. Notify the PFA within 24 hours of the receipt of contributions from any employer;
- c. Hold Pension Fund and assets in safe custody on trust for the employee and beneficiaries of the retirements savings account;
- d. Settles transactions on behalf of the PFA
- e. Provide information to the Commission and the PFA in relation to the assets held in its custody from time to time;
- f. Execute in favour of the PFA relevant proxy for the purpose of voting in relation to the investment.

The employer is mandated to remit all contributions to the PAC within 7 days of the due date.

National Pension Commission¹⁷

This is the regulatory body of the Pension Reform Scheme. It is known as the "National Pension Commission" in the Act. The principal objective of the commission is to regulate, supervise and ensure the effective administration of Pension matters in Nigeria¹⁸.

15. See Section 52 of PRA.

16. See Section 47 of PRA

17. Section 14 PRA

18. Section 15 PRA

The Commission consists of a part-time Chairman, a Director General, four full time Commissioners and part-time members of the commission with professional experience in finance and investments¹⁹.

The Commission operates in four main departments:

- i. Technical
- ii. Administrative
- iii. Inspectorate
- iv. Finance and Investment

Each of these departments is to be headed by the 4 full time Commissioners.

The Commission has the power to formulate, direct and oversee the overall policy on pension matters in Nigeria. This includes powers to charge and collect fees, levy or penalties as may be specified by it. They also retain the power to do other things though not explicitly stated in the Act but in its opinion deemed necessary to the efficient performance of the functions of the Commission.

The Commission also has the mandate to hold workshops and symposia in a deliberate aim of creating awareness and public enlightenment on matters relating to pension in Nigeria.

The Commission shall be sustained by the initial take-off grant from the Federal Government, Annual subvention from the Federal Government; Fees, Fines and commission charged by the Commission, income from any investments of the Commission and all sums of money or income accruing to the Commission by way of testamentary disposition and endowments.

National Social Insurance Trust Fund (NSITF).

This write up will be incomplete without discussing the fate of the employees fund in the possessions of NSITF as well as their role in the new dispensation.

The NSITF is allowed to register as a PFA and jostle for jobs like other PFAs. All pension funds and assets held and managed by

19. Section 16 PRA

NSITF shall be transferred to a custodian from the date of commencement of the Act. Any contributor or beneficiary under NSITF Act can after 5 years of the commencement of the Act transfer their accrued balance to a PFA of their choice. Those under the NSITF Scheme that are already in the retirement will receive their payment in accordance with the new Act as stipulated in section 4 of the Act.

The NSITF will however, retain its social security status, Non-pension contributors to NSITF shall be paid into the respective contributors retirement savings account to be opened by NSITF in accordance with the NSITF Act 1993.

CRITICAL APPRAISAL:

As noble as the Pension Reform Act is, the Act has made its coverage issues too limited, this we believe will pose a challenge to the Commission in discharging its functions and exercising its powers, some of which are highlighted below:

Poor Awareness: The level of awareness among Nigerians in respect of Pension matters and Pension Reforms is still very low, due to high rate of illiteracy, lack of confidence in government policies, poor record keeping/members accounts, of contributions and benefits, poor service delivery, and the fact that 60% of the workers in Nigeria²⁰, who constitute the self employed and small industries with less than 5 workers are excluded from the PRA. The performance of the National provident fund 1962 - 1994, the Nigeria Social Insurance Trust Fund (NSITF) 1994 - 2004, the National Housing Fund (NHF) etc. which are Government Agencies over the years has not been impressive. The PRA and the NPC are government initiatives, though the Administration of Pension PFA's & PFC's will be private sector, driven, the NPC as set up by the Act is formed and funded by the government i.e it is a government parastatal. The NPC must not therefore, see itself as a government mouthpiece, but as impartial

20. C.Y Shikong article on Challenges facing the National Pension Commission, in the official journal of the Certified Pension Institute of Nigeria, January/April, 2005 at page 21.

umpire that will see to the full enforcement of the PRA if its objectives are to be achieved by creating awareness right from the grass root level, for Nigerians to understand the Pension Reforms and Pension issues in the country.

(i) Implementation & Enforcement: The twin problem of implementation and enforcement is another area that will pose serious challenges to the commission. The NPC should evolve a strategy that will enable it implement and enforce the Reforms. To ensure at least 50 - 70% coverage in the next few years, the NPC should device ways and means of detecting non-compliance by employers of labour, necessary protection and safety should also be provided for employees who may dare to expose their employers for non-compliance. The NPC, may find the story of Nigeria Social Insurance Trust Fund useful, in its 43 years of existence 1962 - 2005 the NSITF is said to have collected N37.52 billion as revenue, with a registered membership of about 1.4 million workers.

Though, this is a commendable achievement, a close examination, will reveal otherwise, for an organization that enjoy absolute monopoly of contributions from the entire private sector employers/employees, this result shows NSITF only operated at about 37%^{20a} capacity, leaving out a greater proportion of the private sector employers and employees, this may have been responsible for the unpopularity and lack of confidence an average Nigerian worker has in the NSITF scheme despite its numerous benefits and advantages to the worker. The NPC, therefore, must take bold steps towards achieving 80 - 90% compliance of the PRA within the next 5 years through relevant implementation and enforcement strategy.

(ii) Low Saving Culture: The PRA provides for a retirement savings account, from the monthly income, with the high level of poverty, low wages, inflation and low per capital income. To the average Nigerian worker, surviving today, is better than saving for tomorrow. The

20a. As in 20 above.

(11) The Virginia Board of Education is not to be held responsible for any loss of income or other financial loss which may be incurred by any person. The Board of Education is not to be held responsible for any loss of income or other financial loss which may be incurred by any person. The Board of Education is not to be held responsible for any loss of income or other financial loss which may be incurred by any person.

For example, under the defunct National Provisional Fund (NPF), 1982 - 1984 where a minimum of 5 employees were required for compliance under NPF. A dishonest employer can claim that for instance, of the say, 20 worker in his employment 5 are corporates, 2 are 1/2 students while 2 are his domestic servants who don't earn salary from company and therefore these 2 will ask to be exempted, this is fraudulent. The PRA provides for 5 employees and above for compliance. This is a big challenge to the commission. The Nigeria factor will also likely see employee/employers in agreement understanding their total emolument or gross pay, and leaving out the names of some employees in order to stay out of the PRA by preparing more than one pay roll to beat NPC field inspectors.

Recapitalization Fever and the Nigeria Economy: There is tendency that the Pension Fund Administrators & Pension Fund Custodian will be under pressure as a result of the Recapitalization fever currently blowing in the Nigeria economy, the need for recapitalization will be determined by the how far we can successfully implement, this noble objectives of PRA. The Nigeria political and economic environment, is not investment friendly yet, and this may affect the successful implementation of the PRA by the NPC, issues such as high labour turnover, closing shop, high

rate of unemployment, inconsistent policies on part of government, and the fact that the informal sector which constitute about 60% of the Nigeria economy is excluded, the PRA, is itself a major blow to the reforms. Despite these, NPC has a mandate, which all Nigerians must support it to succeed, for the interest of workers and the country.

Despite the enumerated envisaged challenges of the Act, it is the writer's submission that should the Act be fully implemented, it will improve on the level of saving, reduce interest rates, provide the much needed fund to the real sectors of the economy which will impact on GDP positively, improve employment opportunities and strengthen the Naira in the international market. Most importantly, it will ensure that the pains employees undergo to get their benefit after retirement is reduced to the barest minimum if not completely eliminated.

The scheme should be able to add value to all its stakeholders. The fees charged and commission earned should be high enough to sustain the system. Returns from investment should be higher than the inflation levels in order to forestall apathy and the ends to justify the means.

There should be free flow of information within and without the system with an object of transparency so as to win confidence of the stakeholders.

CONCLUSION:

Against the backdrop of the efficiency and irregularities that characterized the previous Pension Schemes, the new Pension Reform Act and the Role given to the National Pension Commission is a welcome policy to Nigerians. The National Pension Commission must safeguard the PRA by making sure that operators adhere strictly to its rules and regulations and there should not be any sacred cow in the quarterly withdrawals calculated on the basis of an expected life span.

Also, that where an employee dies, his entitlement under the life assurance policy maintained under subsection 3 (a) of the Act shall be paid to his retirement savings account for his administrator to pay to his beneficiary under a will.

It is also the writer's suggestion that the machinery for effective take off and the transition period from the old to new system should be examined for them to be in term with modern reality. The transitional provisions are thus briefly enumerated²¹:

According to Section 12 (1) (a): Any employee who is already under any pension scheme existing before the commencement of this Act and has over 3 years to retire, the federal government retirement Bonds shall be issued in favour of the employees concerned and the amount so redeemed shall be added to the retirement savings account of the employee and applied in accordance with the provisions of section 4 of the Act.

Section 29 states that the Central Bank of Nigeria shall establish the Retirement Benefit Bond Redemption Funds into which 5% of total wage bill shall be paid on a monthly basis till the bond is finally redeemed.

In Section 30: The Act establishes for the Federal Civil Service pension Department as Transitional arrangement Department. This Department comprises of existing Pension Boards or pension offices in the public service and FTC.

- i. The department shall operate under rules and operate under rules and regulations of the National Pension Commission.
- ii. They are responsible for, amongst others, collation of data on pensioners and pensionable staff.
- iii. Make budgetary estimates for existing pensioners and the officers excepted from this scheme under section 8.
- iv. Pay gratuity and pension to existing pensioners and others among others exempted from PRA on the pay as you go basis.

PRIVATE SECTOR:

According to Section 39

- (1) Pension schemes existing in the private sector before the commencement of the Act (PRA) have option of continuing provided that:

21. S.A Bolarinwa on *Managing Debt and Transitional issues in Nigeria Pension Reform*, in the official journal of the Certified Pension Institute of Nigeria, January April, 2005 at page 25.

- (a) The scheme is fully funded
 - (b) The pension funds and assets shall be fully segregated from the funds and assets of the company
 - (c) Funds and assets shall be held by a custodian
- (3B)
- (d) Every employee who opts to come under the new scheme as established by PFA will have his entitlement credited to his account i.e. his contributions and distributable income earned at the date the employee exercises such an option.
 - (e) Any amount computed under paragraph (d) shall be transferred to the retirement savings account of the employee maintained by a pension fund administration of his choice.
 - (g) All investment in assets other than specified as permissible investment for pension fund and Assets may be maintained and from the commencement of this Act, all investments shall be subject to the regulation, rules and standard established by the commission.
 - (h) The employer shall send undertaking to the commission that the pension fund shall be fully funded at all times and any shortfall to be made up between 90 days.
 - (i) The employer demonstrates that it possesses managerial capacity for the management of pension funds and assets for a period not less than 5 years before the commencement of this Act.
- (2) Any employer operating any defined benefits scheme shall undertake actuarial valuation at the end of the every financial year of this pension fund assets.
 - (3) All pension schemes existing before the commencement of the Act shall submit to the Commission a statement of affairs which shall include assets, liabilities, list of members, current statement of affairs which shall include assets, in

case of contributory scheme and pensionable salaries in the case of benefits scheme.

Section 40

- (1) All employer who wants to continue managing its pension fund shall apply to the commission to be licensed as close pension Fund Administrator to be managed either directly or through a wholly owned subsidiary dedicated exclusively for such purpose.
- (2) For such application to be granted, it must.
 - i. Hold a minimum pension funds and assets of N500,000,000
 - ii. Satisfies all requirement of section 50 of the Act.
 - iii. Pension funds and assets less than N500 million shall have such pension scheme administered by a pension fund administration licensed under section 44 and 50.

In whole, it is expected that the take off, implementation and enforcement of the Act will be made simple, as the whole idea reported by Chief Fola Adeola Committee is to be executed under the same head of the Committee, now Chairman of the Commission²². Despite the shortcomings that can be noticed in the PRA, its advantages and benefits are far reaching for the country and its people and therefore, it is the responsibility of all stakeholders to ensure the success for the Pension Reform Act, to benefit Nigerian workers and if the purpose of its enactment is to be achieved, the National Pension Commission which is the sole regulatory body charged with the responsibility of implementing, enforcing and providing the necessary regulatory guidelines from time to time must ensure that the laudable objectives of PRA are achieved.

22. The Senate recently named Chief Fola Adeola as Chairman of the Commission, with six others from the six geo political regions as the members of the Commission. They are: M.K Ahmad, Director General, C.P.NAkubueze, E.T Henshaw, Dr Musa Ibrahim and M.T Mamman.