Pensions & Retirement Plans

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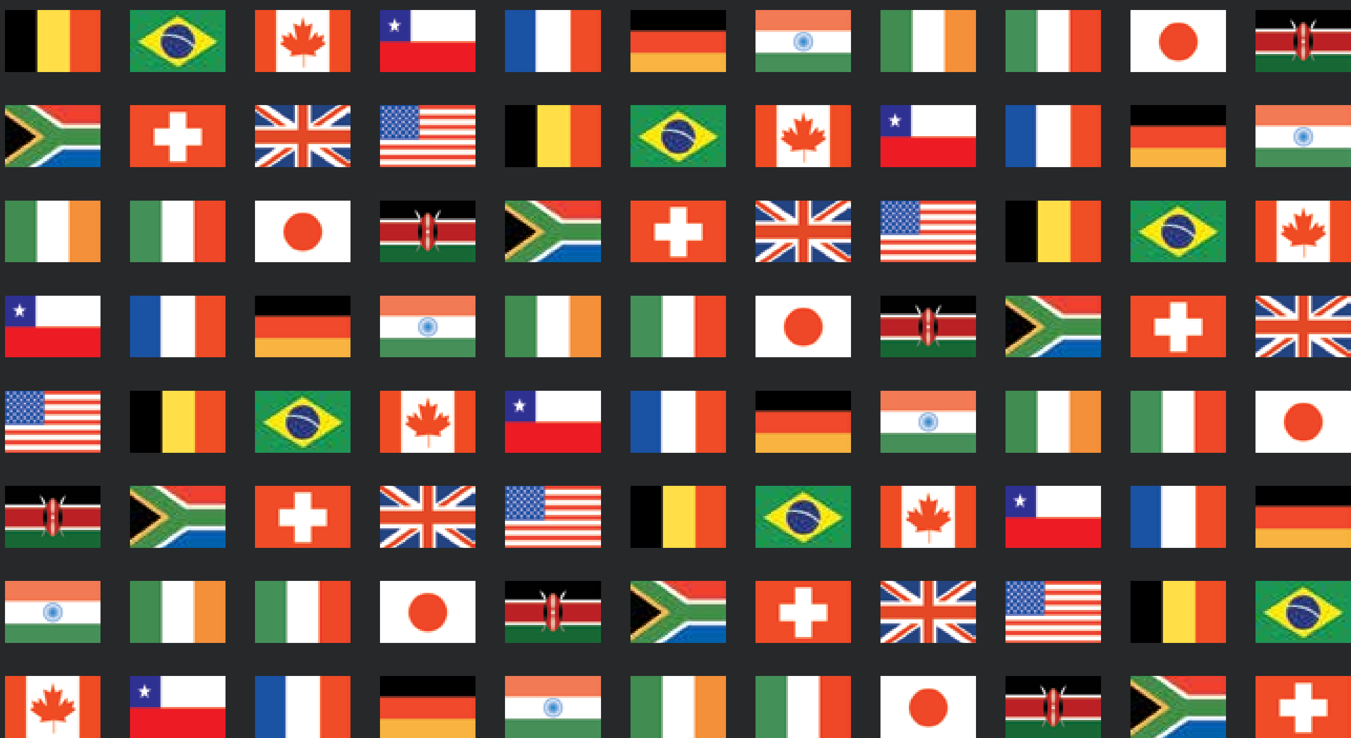

2018

GETTING THE DEAL THROUGH

GETTING THE DEAL THROUGH

Pensions & Retirement Plans 2018

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Pensions & Retirement Plans 2018

Sixth edition

Getting the Deal Through is delighted to publish the sixth edition of *Pensions & Retirement Plans*, which is available in print, as an e-book, and online at www.gettingthedealthrough.com.

Getting the Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique **Getting the Deal Through** format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapters on India and South Africa.

Getting the Deal Through titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at www.gettingthedealthrough.com.

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Getting the Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editor, Jan Van Gysegem, of Claeys & Engels, for his continued assistance with this volume.

GETTING THE
DEAL THROUGH

London
April 2018

Kenya

Carole Ayugi, Elvis Wanjau and Allison Amondi
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Statutory and regulatory framework

1 What are the main statutes and regulations relating to pensions and retirement plans?

The following are the main statutes:

- Pensions Act (Cap. 189);
- Pensions (Increase) Act (Cap. 190);
- Retirement Benefits Act (No. 3 of 1997);
- Income Tax Act (Cap. 470);
- National Social Security Fund Act (Cap 258);
- National Social Security Fund Act (No. 45 of 2013);
- National Health Insurance Fund Act (No. 9 of 1998);
- Provident Fund Act (Cap. 191);
- Public Service Superannuation Scheme Act (No. 8 of 2012);
- Parliamentary Pensions Act (Cap. 196);
- Presidential Retirement Benefits Act (No. 11 of 2003);
- Retirement Benefits (Deputy President and Designated State Officers) Act (No. 8 of 2015);
- Asian Officers' Family Pensions Act (Cap. 194); and
- Asian Widows' And Orphans' Pensions Act (Cap. 193).

The following are the main regulations:

- Retirement Benefits (Individual Retirement Benefits Schemes) Regulations 2000;
- Retirement Benefits (Occupational Retirement Benefits Schemes) Regulations 2000;
- Retirement Benefits (Minimum Funding Level and Winding up of Schemes) Regulations 2000;
- Retirement Benefits (Forms and Fees) Regulations 2000;
- Retirement Benefits (Managers and Custodians) Regulations 2000;
- Retirement Benefits (Mortgage Loans) Regulations 2009;
- Retirement Benefits (Administrators) Regulations 2007;
- Retirement Benefits (Umbrella Retirement Benefits Schemes) Regulations 2017;
- The Income Tax (Retirement Benefit) Rules 1994;
- Income Tax (National Social Security Fund) (Exemption) Rules 2002; and
- Provident Fund Regulations.

The following are guidelines:

- Practices notes and guidelines issued by the Retirement Benefits Authority.
- Treasury Circular 18 of 2010 (for all public service retirement benefit schemes).

2 What are the primary regulatory authorities and how do they enforce the governing laws?

The primary regulatory authorities in Kenya are the Retirement Benefits Authority (the Authority) and the Kenya Revenue Authority.

The objects and functions of the Authority are:

- regulating and supervising the establishment and management of retirement benefits schemes;
- protecting the interests of members and sponsors of the retirement benefits sector;
- promoting the development of the retirement benefits sector;
- advising the minister responsible for finance on the national policy to be followed regarding retirement benefits schemes and implementing all government policies relating thereto; and
- approving trustees' remuneration by members during annual general meetings, after every three years.

The Commissioner of Income Tax also determines what income under the schemes shall be considered tax-exempt and the registration of pension schemes.

3 What is the framework for taxation of pensions?

The taxation of pensions in Kenya is guided by section 8(5) of the Income Tax Act.

The following sums are not subject to tax:

- the first 600,000 Kenyan shillings of lump sums commuted from a registered pension or individual retirement fund;
- contributions that are less than 20,000 shillings per month or 30 per cent of the pensionable salary, whichever is less;
- income earned from investments; and
- pension payments after attaining the age of 65.

The benefits received by members are taxed, but they can opt to receive a tax-free lump-sum payment of 60,000 shillings on retirement for every year of membership, up to a maximum of 600,000 shillings.

State pension provisions

4 What is the state pension system?

The National Social Security Fund Act No. 45 of 2013 (the New NSSF Act) commenced on 10 January 2014. The provisions of this Act have been challenged in court and an order was issued requiring employers, employees and the government to continue making contributions in accordance with the National Social Security Fund Act Cap. 258 (the Old NSSF Act). In effect, therefore, the New NSSF Act is yet to take effect.

Meanwhile, the state pension system that is in place is the National Social Security Fund (NSSF) set out in the Old NSSF Act.

The NSSF is a national scheme, the main objective of which is to provide basic financial security benefits to Kenyans upon retirement. It was set up as a provident fund to provide benefits in the form of lump-sum payments. It works on a contributory basis. This fund, however, only covers formal sector employees, thus limits its coverage by excluding informal sector employees (workers who do not declare their income nor pay income tax).

The NSSF's statutory contributions are set at 10 per cent of the employee's pay, half of which is paid by the employer.

There is also the Public Service Pension Scheme (PSPS) that provides benefits for public service employees (civil servants). This scheme is governed by the Pensions Act and the Public Service Superannuation Scheme Act (No. 8 of 2012). It operates on a non-contributory basis.

With the coming into force of the Public Service Superannuation Scheme Act, specifically section 6, the concept of mandatory contributions to a scheme has been introduced to the public service. Every member shall contribute to the PSPS at the rate of 7.5 per cent, which is deducted from his or her monthly pensionable salary, while the government makes a contribution for each member at the rate of at least 15 per cent of the member's monthly pensionable salary. The government is also mandated to take out and maintain a life insurance policy that has disability benefits in favour of every member of the scheme. These policies must be worth a minimum five times the member's annual pensionable emoluments.

A member may also make additional voluntary contributions to the scheme, as provided for under section 7 of the Public Service Superannuation Scheme Act (No. 8 of 2012).

5 How is the state pension calculated and what factors may cause the pension to be enhanced or reduced?

Currently in accordance with the Old NSSF Act, statutory contributions to the NSSF are set at 10 per cent of an employee's pay. A monetary ceiling on the maximum combined contribution is set at 400 shillings per month.

The New NSSF Act sets the statutory contributions at 12 per cent of the employee's pay, 6 per cent of which is contributed by the employee.

The New NSSF's contributions are divided into two tiers. Tier 1 contributions are based on pensionable earnings up to the lower earnings limit and tier 2 contributions are based on pensionable earnings above the lower earnings limit. The lower earnings limit is set by the cabinet secretary (see below).

The New NSSF Act received assent from President Uhuru Kenyatta on 24 December 2013 and was to be implemented on 31 May 2014. However, implementation has been delayed because of numerous legal issues. This Act sets the transitional period for contributions at five years. Therefore, the lower earnings limit was to increase each year from 6,000 shillings for the first year, to 7,000 shillings for the second year, until the fifth year where it would settle at the amount set by the cabinet secretary at the end of each financial year as the average minimum monthly basic wage (currently 12,600 shillings). This would be published monthly.

It should be noted that the New NSSF allows tier 2 contributions to be contracted out to other private retirement benefit schemes. The proposed contracted-out scheme must be registered with the Retirement Benefits Authority, have a valid exemption from the Kenya Revenue Authority, and comply with investment guidelines in the Retirement Benefits Act and any requirements prescribed by the Retirement Benefits Act and the New NSSF Act.

The New NSSF Act also allows persons not in formal employment to make voluntary contributions towards the fund in order to secure benefits.

6 Is the state pension designed to provide a certain level of replacement income to workers who have worked continuously until retirement age?

Under the Old NSSF Act, a member of a scheme is entitled to an age benefit on attaining the age of 55 years and having retired from regular employment.

Under the New NSSF Act, retirement benefits are payable from the normal retirement age of 60 years, with earlier retirement being possible at age 50. Upon retirement, each individual's tier 1 account balance can be paid out as a partial lump sum, with the remainder used to purchase an annuity from a registered insurer.

An employee will also have the option of taking up to one-third of his or her tier 2 balance as a lump sum, with the remainder taken as scheduled withdrawals. Payment of the tier 2 benefit can be deferred to coincide with the normal retirement date of any occupational plans into which the tier 2 contributions are paid.

However, the lump-sum benefit may be considered inadequate as, given the low monetary contributions, it may not be enough to sustain a member after retirement.

7 Is the state pension system under pressure to reduce benefits or otherwise change its current structure in any way on account of current fiscal realities?

The NSSF has undergone changes to its current structure, so as to increase its level of assessment under the following criteria: adequacy, affordability, sustainability and robustness.

The New NSSF Act introduces changes transforming the NSSF from a provident fund to a pension and provident fund. The pension fund will cover individuals of 18 years old or above in the formal sector and the provident fund will be for self-employed persons who voluntarily register to be members of the fund. Therefore, every Kenyan with an income shall have an opportunity to contribute a percentage of his or her gross earnings and be guaranteed basic compensation in case of permanent disability, assistance to dependants in case of death and a monthly life pension upon retirement.

With regard to pension schemes for persons employed in the public service, the Public Service Superannuation Scheme came into being and introduced mandatory contributions rates by both the employers and members of retirement schemes, thus converting the non-contributory civil service pension schemes to contributory public service superannuation schemes.

This addressed the issue of benefits accruing for civil servants being inadequate because of low levels of salaries, since both the member and employer have mandatory contribution rates. It also enables members to transfer their savings to a new employer.

Plan features and operation

8 What are the main types of private pensions and retirement plans that are provided to a broad base of employees?

There are four types of pension plans in Kenya:

- public service pension funds;
- occupational pension schemes;
- individual pension plans; and
- umbrella schemes (see 'Update and trends').

These plans' structures take two forms:

- Defined contribution plan: Under this plan, members' and employers' contributions are fixed either as a percentage of pensionable earnings or as a shilling amount. The amount a member shall receive upon retirement depends on the total amount of money contributed and the performance of the fund's investments over time.
- Defined benefits plan: Under this plan, the amount a member shall receive upon retirement is determined in advance using a set formula. Members of the scheme contribute a fixed amount and a sponsor meets the balance of the promised benefit. Defined benefit plans are treated as liabilities an employer must pay when an employee retires. Most employers therefore lean towards the defined contribution plan. Benefits are often related to the final salary and/or years of service of the employee.

9 What restrictions or prohibitions limit an employer's ability to exclude certain employees from participation in broad-based retirement plans?

Under Regulation 7(e) of the Retirement Benefits (Occupational Retirement Benefits Schemes) Regulations, a scheme's rules should provide the requirements for admission to membership and the circumstances under which membership ceases.

Regulation 18(1) deals with eligibility of membership of schemes. In particular, it prohibits discrimination or restriction of membership on the basis of gender, race or religion or the exercise of discretionary powers in relation to membership by employers, thus preventing exclusion of membership, unless provided otherwise under the Authority.

In addition, section 5 of the Employment Act (No. 11 of 2007) prohibits discrimination of employees by employers in respect of any employment matter.

The constitution of Kenya goes further, providing, under Article 27, that a person must not discriminate (directly or indirectly) on the basis of any ground including race, sex, pregnancy, marital status, health status, ethic or social origin, colour, disability, age, religion, conscience, belief, culture, dress, language or birth. Direct discrimination occurs when a policy, law or rule treats a person less favourably than others because of that person's protected ground or characteristic. Indirect discrimination occurs when a person, policy, measure, or criterion, though neutral, places a person at a disadvantage compared to others because of that characteristic or protected ground.

However, it is imperative to note that unless it is a defined contribution scheme, no scheme rules will allow an employee to join if they have less than five years remaining before retirement age; provided that the scheme may reduce the qualifying period or vary an age limit in an special case provided in the scheme rules. This has been provided for under regulation 18(1)(c) of the Retirement Benefits (Occupational Retirement Benefits Schemes) Regulations.

10 Can plans require employees to work for a specified period to participate in the plan or become vested in benefits they have accrued?

An employer may, under a scheme's rules, provide for a qualifying period for membership of the scheme. This period should not be more than one year. Regulation 18(d) of the Retirement Benefits (Occupational Retirement Benefit Schemes) Regulations provide for this.

All benefits deriving from contributions should, however, vest in the member immediately.

The employer is therefore not to set a specific period for which one must work in order for the benefits accrued to vest. The same rule applies to sponsor contributions: they vest immediately.

11 What are the considerations regarding employees working permanently and temporarily overseas? Are they eligible to join or remain in a plan regulated in your jurisdiction?

Regulation 19(5) of the Occupational Retirement Benefits Regulations provides that the permanent emigration of a member to another country qualifies as a situation under which retirement benefits may be granted, and he or she may choose to receive the accrued benefits as a lump sum before acquiring retirement age. This will need the approval of the trustees and the Authority.

If a member of a scheme is temporarily absent from service under the employer, the practice is that during the member's absence he or she will retain membership of the scheme and still make contributions, and the sponsor will do the same in this regard. Where the member absent is not in receipt of a pensionable salary then the trustees, with the employee's consent, can opt to suspend the contributions from the member and those made on his or her behalf by the employer until he or she returns.

12 Do employer and employees share in the financing of the benefits and are the benefits funded in a trust or other secure vehicle?

The financing of benefits depends on whether the plan is contributory or non-contributory. Contributory plans are funded through contributions from the members and employers; non-contributory plans are completely funded by an employer.

Under defined benefit plans, which are non-contributory, the employers finance the benefits. The employers meet the promised benefit due when the member completes his or her pensionable service under the employer and attains retirement age.

With a defined contribution plan, which is contributory, both the employee and employer contribute a given percentage towards the fund.

Section 26 of the Retirement Benefits Act provides that pension schemes must be established as trusts and trustees will hold the assets for the benefit of the members of the scheme.

13 What rules apply to the level at which benefits are funded and what is the process for an employer to determine how much to fund a defined benefit pension plan annually?

Benefits are funded by contributions. Under a defined contribution scheme, the level at which benefits are funded is determined in a number of ways:

- the employer compares and analyses the level of contributions that other schemes have set within the pension industry so as to provide competition;
- the employer considers the future benefits that it intends on making available to its employees; or
- the employer considers factors relating to the employees' profiles, such as age and the type of employees. This then will guide it on how much to contribute towards each employee.

The employer can be advised by an actuary, which can make a conclusion based on statistical data about the employees and arrive at a calculated figure.

Defined benefit schemes' funding aims to provide the members with the promised benefit at the end of their service. The determination of the funding level can be left to the discretion of the employer or sponsor. However, in practice, it can be calculated by the multiple of length of one's service and the final pensionable salary. The figure normally arrived at is that where the employer intends to replace 0.2 per cent of the employee's final pensionable salary for every year of employment.

These schemes can also conduct actuarial valuations to determine the future benefits that will, in turn, determine the future contributions. In contrast to defined contribution schemes, the funding level of which is based on contributions that will result in benefits, for defined benefit plans the focus is on the benefits, which will then determine the contributions to be made.

14 What are customary levels of benefits provided to employees participating in private plans?

Under private plans the levels of benefits provided are as follows:

- retirement benefits that vest on the following and are provided to the member until his or her death and thereafter to his or her surviving spouse:
  - attaining normal retirement age;
  - early retirement age with consent of the employer;
  - the ground of ill health; and
  - permanent emigration of the member;
- death-in-service benefits that are payable to his or her surviving spouse and any other dependants when a member dies in service; and
- benefits on a member leaving an employee's service of his or her own free will, dismissal by the employer or on redundancy or retrenchment.

15 Are there statutory provisions for the increase of pensions in payment and the revaluation of deferred pensions?

The Pensions (Increase) Act provides for the rates and dates of increase of pensions. This rate should not exceed 3 per cent per annum, but is subject to the scheme's funding level.

An increase of pensions in payment can also be determined by the scheme or employer, or both.

Under the New NSSF Act, the transitional period with regard to contributions has been set at five years (see question 5). This increase in contributions eventually results in increased pensions.

16 What pre-retirement death benefits are customarily provided to employees' beneficiaries and are there any mandatory rules with respect to death benefits?

Regulation 26 of the Retirement Benefits (Occupational Retirement Benefit Schemes) Regulations 2000 provides that where a member dies before attaining retirement age, a scheme's rules may provide that benefits are payable to the nominated beneficiary.

Customarily, schemes provide benefits to beneficiaries, such as survivor's benefit, orphans' pensions and widows' pensions.

On death, the benefits payable from the scheme shall be paid to the nominated beneficiary. If the deceased member had not named a beneficiary then the trustees shall exercise their discretion in the distribution of the benefits to the dependants of the deceased member.

If a spouse dies while in service, the benefit payable to the surviving spouse and any other dependant shall only become due and payable when the registered insurer, under which the deceased is insured, admits the claim for the benefit.

With respect to public service retirement benefit schemes, the death-in-service benefit will be provided through an insurance policy purchased from a reputable insurance company and it shall not exceed three times the employee's pensionable salary. Where the current provision is in excess of this level, the benefit shall be amended to three times the pensionable salary at the next policy renewal date, but in any case not later than 1 July 2011. This is as provided for under Treasury Circular 18 of 2010.

Death benefits do not form part of the assets in the estate of a deceased member, as provided for under Section 36A of the Retirement Benefits Act.

17 When can employees retire and receive their full plan benefits? How does early retirement affect benefit calculations?

In accordance with the Income Tax (Retirement Benefit) Rules 1994, payment of a pension shall not commence until the member reaches 50 years of age. This is the early retirement age.

The Public Service Superannuation Scheme Act section 27(1) sets the normal retirement age at 60 years and on attaining that age, such a benefit shall be payable. Members may opt to receive lump-sum payments that are calculated depending on whether the member makes or does not make contributions.

A member will receive full benefits when he or she retires before the normal retirement age, if it is on the grounds of ill health, or if the member permanently emigrates from Kenya to another country.

Where a member of a defined benefit scheme leaves employment before attaining retirement age, he or she will receive no more than 50 per cent of the accrued benefits. The remaining 50 per cent will be retained in the scheme and will be paid to the member in accordance with the trust deed and rules upon attaining the normal retirement age.

A member of a defined contribution schemes shall receive his or her contributions and 50 per cent of the employer's contributions, if he or she retires before attaining retirement age. The remaining 50 per cent of the employer's benefit will be retained in the scheme and will be paid to the member in accordance with the trust deed and rules upon attaining the normal retirement age.

18 Are plans permitted to allow distributions or loans of all or some of the plan benefits to members that are still employed?

No scheme funds shall, however, be used to issue a direct or indirect loan to any person. This is in accordance with section 38(1) of the Retirement Benefits Act. Notwithstanding the above provisions, a prescribed portion may be assigned and used by a member to secure a mortgage loan from such institutions and on such terms as may be prescribed in regulations by the minister responsible for finance. This is in accordance with section 38(1A) of the Retirement Benefits Act.

Regulation 8(1) of the Retirement Benefits (Mortgage Loans) Regulations further provides that a member may, if the rules of the scheme permit, assign a portion (not exceeding 60 per cent) of his or her benefits to a scheme for the purposes of furnishing a guarantee in favour of an institution or in respect of a loan granted or to be granted by the institution to a member.

19 Is the sufficiency of retirement benefits affected greatly if employees change employer while they are accruing benefits?

It is not greatly affected. The benefits accrued can be fully transferred to a new scheme and will only be subject to transfer values which are reviewed and certified by an actuary.

20 In what circumstances may members transfer their benefits to another pension scheme?

Transferring benefits is provided for under regulation 40 of the Occupational Retirement Benefit Schemes Regulations. When an employee moves from his of her previous employer to join a new employer, he or she is allowed to transfer membership from the previous scheme to the scheme sponsored by the new employer and the transfer value of the accrued rights will be transferred to the new scheme as well.

If the employer is undergoing any reorganisation or reconstruction and completes an arrangement with another employer to undertake the employee's rights and obligations under the scheme, the trusts of the scheme shall continue to have effect under the new employer.

21 Who is responsible for the investment of plan funds and the sufficiency of investment returns?

Fund managers are responsible for the investment of plan funds and the sufficiency of investment returns.

The Retirement Benefit Act defines a 'manager' as a company, the business of which includes:

- undertaking, pursuant to a contract or other arrangement, the management of funds and other assets of a scheme for the purposes of investment;
- providing consultancy services on the investment of scheme funds; or
- reporting or disseminating information concerning the assets available for investment of scheme funds.

Trustees are required to ensure that the scheme has appointed an independent fund manager that is registered under the Capital Markets Act, and the registration of which has been accepted by the Retirement Benefit Authority, constituting registration under the Retirement Benefit Act, subject to an agreement between the Capital Markets Authority and the Authority, to invest the scheme funds on their behalf.

The Retirement Benefit Act further provides that the fund manager appointed must not have a business relationship (eg, be a principal, owner, shareholder, director, employee, or consultant etc) with the Administrator.

The manager shall prepare, maintain and, after every three years, revise a written statement of the principles governing investment decisions for the purposes of the scheme or the pooled fund.

22 Can plan benefits be enhanced for certain groups of employees in connection with a voluntary or involuntary reduction in workforce programme?

Under a retirement benefit plan, neither a scheme nor the Authority can provide or approve of different pension factors and benefits where differentiation is based on wages, gender, race or any discriminatory factor. (See question 9 for a list of prohibited discriminatory factors.)

23 Are non-broad based (eg, executive-only) plans permitted and what types of benefits do they typically provide?

Non-broad based plans are not permitted, as plans must be open to all members of the public or all members of said group for which they were formed.

24 How do the legal requirements for non-broad based plans differ from the requirements that apply to broad-based plans?

Non-broad based plans and broad-based plans are not provided for legally in Kenya.

25 How do retirement benefits provided to employees in a trade union differ from those provided to non-unionised employees?

There is no difference between the benefits given to the two groups. Retirement benefit schemes in Kenya aim to show no difference or segregation when providing benefits. This is achieved by applying a uniform rate to all employees, regardless of their membership in a trade union.

26 How do the legal requirements for trade-union-sponsored arrangements differ from the requirements that apply to other broad-based arrangements?

There arises no difference legally between the two, as they are not expressly provided for under Kenyan law.

Enforcement

27 What is the process for plan regulators to examine a plan for periodic legal compliance?

Customarily, schemes are required, by law, to make various submissions that aid regulators in examining whether the scheme is compliant. Such submissions, as provided for by Retirement Benefits Act section 34(4), include annual reports and statements of audited accounts that must be submitted to the Authority's chief executive within three months of the end of each financial year. The scheme's record of contributions shall be submitted to the Authority by the 15th day of every third calendar month.

Actuarial valuations must be carried out on defined benefit schemes every three years and a copy of the valuation report must be submitted to the Authority within five months of the end of a financial year. Defined contribution schemes can also be valued, but only on decision of the Authority.

Customarily, plan regulators can also examine schemes for legal compliance by attending the meetings of a scheme, which must be held at least twice a year.

One of the Authority's functions is to regulate the management of retirement benefits schemes. This includes ensuring they are complying with the government policies relating thereto. The Authority's CEO can, if so directed by the board, cause an inspection to be made by an inspector of any scheme registered under the Retirement Benefits Act. In the course of the inspection, all the administrators of the scheme shall make available to the inspector all the documents of the scheme and relating to the scheme as required.

The inspector shall then submit his report to the Authority's CEO, indicating whether there have been any breaches of any of the requirements under the Retirement Benefits Act and regulations.

The period of payment of benefits has been reduced further to 30 days. This is in compliance with regulation 7(00) of the Retirement Benefits (Occupational Retirement Benefits Schemes) Regulations 2000.

28 What sanctions will employers face if plans are not legally compliant?

Various offences can result in an employer facing sanctions. For example:

- under section 22(5) of the Retirement Benefits Act, non-registration of a scheme or a manager shall result in an employer being liable to a fine not exceeding 500,000 shillings or imprisonment for a term not exceeding two years; and
- section 34(4A) provides that a trustee who fails to submit a copy of the audited accounts to the Authority is liable to a fine not exceeding 500,000 shillings, or a prison term not exceeding two years, and an additional fine of 5,000 shillings per day if it is a continuing offence.

In addition to the above, the general penalty provided under section 53 of the Retirement Benefits Act is that if an employer commits an offence it will be liable, on conviction, to a fine not exceeding 100,000 shillings or imprisonment for a term not exceeding one year.

If the scheme is not legally compliant, the Authority's CEO may appoint an interim administrator to assume control over the affairs of the scheme who will annually submit a report on the management and financial position of the scheme.

Under section 45(2b), the CEO may also remove any trustee, manager, custodian or administrator who has contravened any section under this Act.

Employers can also face sanctions under the Income Tax Act by:

- failing to register the scheme for tax purposes, where the penalty shall be 100,000 shillings per month, but not exceeding 1 million shillings;
- failing to retain records and documents, where the penalty shall be 10 per cent of amount payable; and
- providing a late submission of returns or avoiding tax payments altogether, which will result in a penalty of double the tax liability.

29 How can employers correct errors in plan documentation or administration in advance of a review by governing agencies?

The employer, on identifying an error, can liaise with the scheme's trustees to amend the trust deed and rules in accordance with a set procedure. The obligation is handed to the trustees to do the same under the trust deed and rules. The trustees must then prepare a deed of amendment and file it with the Authority. The amendments to the trust deed and rules require the consent of the employer and the Authority.

However, no such amendment will be valid if it reduces or invalidates the accrued rights and interests of the employer and members of the scheme, or purports to affect any right of a creditor of the scheme, other than as a member thereof, as outlined under regulation 16(1) of the Retirement Benefits (Occupational Retirement Benefits Schemes) Regulations 2000.

The employer is also mandated by section 34(3) of the Retirement Benefits Act to have an auditor audit accounts of the scheme's fund. The auditor will then prepare an opinion letter setting out the errors in plan documentation and the rectifications that should be made.

The trustees and managers of the scheme can also report to the Authority, in advance, any unusual occurrence that could affect the administration of the scheme, especially in relation to the rights of the members or sponsors, section 40(c) of the Retirement Benefits Act.

30 What disclosures must be provided to the authorities in connection with plan administration?

The disclosures that must be provided to the authorities are as follows:

- annual and audited accounts of the scheme within three months of the end of a financial year;
- annual reports containing statements of the scheme's assets and liabilities;
- actuarial reviews or reports of the scheme;
- statutory returns;
- a return indicating the number and amount of guarantees issued, including details of loans repaid and guarantees redeemed;
- a statement of all investments of the scheme fund;
- a record of contributions every quarter;
- the policy on the investment of scheme funds;
- a statement of the scheme's fund, investment portfolio and investment transactions; and
- a report reviewing investment activity and performance of the investments and the manager's proposals.

31 What disclosures must be provided to plan participants?

In normal practice, members are allowed to make any inquiries with regards to the scheme, as the trust exists for their benefit. This is contained in the trust deed and rules and any amendments made thereto. They are also entitled to receive a summary of the annual audited accounts and benefit statements within six months of the end of each financial year. This is as per regulation 30(3b) of the Retirement Benefits (Occupational Retirement Benefit Schemes) Regulations.

32 What means are available to plan participants to enforce their rights under pension and retirement plans?

Customarily, retirement benefit plans are required to have internal dispute resolution procedures in place. There is a multi-tiered dispute resolution mechanism in place which helps to resolve disputes amicably through conciliation, mediation and arbitration before litigation.

Plan participants have an option of engaging in alternative dispute resolution (ADR) with the party assumed to be at fault, after which the said party will issue a response to the complaint. Section 46(1) enables a plan participant dissatisfied by such a response to request, in writing, that the Authority's CEO review the decision and ensure it was made in accordance with scheme rules and the Retirement Benefits Act.

If the plan participant is still not satisfied with the Authority CEO's review, then he or she may appeal to the Appeals Tribunal within 30 days of receipt of the CEO's decision under section 48 of the Retirement Benefits Act.

Thereafter, every such dispute or question shall be referred for arbitration by a single arbitrator, appointed by agreement between the parties, or, in default of such an agreement, the chair of the Chartered Institute of Arbitrators, Kenya Branch, upon application by any of the parties.

If the plan participant is still not satisfied, then he or she may proceed to court. However, the ADR process must be followed first.

Plan changes and termination

33 What restrictions and requirements exist with respect to an employer's changing the terms of a plan?

Consent from the employer is required by the trustees to amend a scheme's rules. Approval from the Authority and the Commissioner of Income Tax must also be sought.

The amendments being made should:

- not vary the main purpose of the scheme;
- not authorise any payment to the employer, unless said scheme is being dissolved;
- not diminish or invalidate any pension already being paid, in accordance with the rules, or any rights or interests which shall have accrued to a member in respect of pension benefits secured under the scheme;
- not extend the operation of the scheme beyond the trust period of the scheme;
- not prejudice, cause the withdrawal of approval or registration of the scheme under the Income Tax Act or the Retirement Benefit Act;
- not purport to affect any rights of a creditor of the scheme, other than as a member;
- not purport to invalidate or reduce accrued rights and interests of the employer and members of the scheme;
- be approved by the Retirement Benefit Act; and

- be referred to an actuary, if the amendments will affect the financial position of scheme.

34 What restrictions and requirements exist with respect to an employer terminating a plan?

Customarily, an employer will be considered to have terminated a plan only in the following events.

Payments of contributions are discontinued if the:

- employer ceases to exist, or for any other reason ceases to operate, and some other statutory body has not been empowered to undertake the rights and obligations of the employer;
- employer is going into liquidation, other than for the purpose of reconstruction or amalgamation with any other company;
- contributions being paid by the employer and reasonably expected from it in the future are so low as to affect the long-term financial position of the scheme; and
- employer fails to remedy any breach of its obligations under the trust deed or the rules within the required number of days.

Some employers close their plans to future accrual and continue to fund the schemes. This option is available to defined benefit schemes which continue operating as closed schemes.

An employer must give written notice to trustees indicating intent to discontinue contributions. The trustees shall then take into account the relevant circumstances and ask an actuary to propose an arrangement providing for the benefits and contributions of the scheme. This agreement will be submitted to the employer and trustees to determine whether the scheme will be wound up.

The trustees must pass a resolution that is to be approved by the Authority.

A liquidator shall be appointed to wind up the affairs of the plan and to submit, to the Authority, preliminary accounts signed and certified by him or her as a correct record. This statement of preliminary accounts shall also be submitted to members. Fees payable to the liquidator shall be borne by the scheme.

A notice stating that the preliminary accounts above are open for inspection by interested persons shall be published in the Kenya Gazette.

35 What protections are in place for plan benefits in the event of employer insolvency?

The Retirement Benefits (Minimum Funding Level and Winding up of Schemes) Regulations govern the winding up of schemes.

Regulation 5(7) provides that, in the winding up of a plan, value of interests and benefits of the members shall be ascertained in such manner as a court directs. Benefits accrued will not be affected during employer insolvency. The total monies in the fund shall be applied to provide benefits for all members on an equitable basis. Members will have the option of transferring such benefits to another registered retirement benefit scheme.

Such benefits shall also include those assigned for purposes of providing for pension-backed mortgages. This has been made possible via regulation 9(4) of the Retirement Benefits (Mortgage Loans) Regulations, which provides that members will also have the option of being issued guarantees from the new scheme they are transferring to, if they were affected by the winding up of their previous one. The liquidator shall be required to provide for the distribution of surpluses under regulation 5(8A).

Pension schemes can also be established as irrevocable trusts, ensuring the assets of the beneficiaries are protected and cannot revert back to employer in instances of insolvency. Section 24(1) of the Retirement Benefits Act provides for this.

36 How are retirement benefits affected if the employer is acquired?

In practice, where an employer is acquired and the acquiring body does not undertake the rights of the employer, then the trust is considered to have been terminated and the benefits accrued become due in accordance with the trust's deed and rules.

If the new employer takes on the rights, it must prepare a deed of adherence, undertaking the rights of the previous employer. The deed sets out that the new employer takes on the years of service and will allow the old members to continue participating in the new scheme.

Members can transfer their benefits wholly to another scheme where their pensionable service under the previous employer will be regarded as service with the new employer.

It is important that a scheme contain provisions that are sufficiently broad to enable individual and bulk transfers to be made into the scheme. This will enable an employee to transfer accrued pension rights from a previous employer's pension scheme and also enable bulk transfers of members and assets in commercial transactions.

37 Upon plan termination, how can any surplus amounts be utilised?

The Income Tax Act prescribes certain requirements necessary for a registered scheme to be compliant with income tax provisions. Section 8(10)(b) and Section 22(A)(7) of the Income Tax Act provide that where a registered fund is wound up, any surplus funds shall be deemed to be the funds of the employer and shall be immediately withdrawn by the employer, unless the trust deed of the such-registered fund specifies otherwise. This provision, although permitting surplus funds to be withdrawn immediately by the employer upon winding up, subjects such a withdrawal to the provisions of the trust deed and rules of the scheme, confirming that the substantive law must always take precedence.

Consequently, under regulation 7(n) of the Retirement Benefits (Occupational Retirement Benefits Scheme) Regulations, every scheme must have rules that provide for a manner of determining surplus and deficit and disposing of such surpluses or providing for such deficits.

This regulation cannot be read in isolation. Reference must be made to regulation 32(1) of the Retirement Benefits Occupational Retirement Benefits Scheme Regulations, which provides that no surplus of a scheme's fund shall be directly or indirectly refunded to the scheme's sponsor, providing that:

- a contribution holiday for both the employer and the member, as shall be determined by the actuary, shall not be construed to mean a refund of the surplus of a scheme fund and shall be limited to the surplus above 10 per cent of the scheme's accrued liability;
- during a winding up for a defined benefits scheme, there shall be 50-50 sharing of surplus between members and the sponsor;
- if total accrued liabilities are being transferred to a different scheme, any surplus shall be allocated equally between the members and the sponsors;
- the portion of the sponsor surplus may be used as a contribution holiday in the new scheme; and
- where partial liabilities are being transferred to a different scheme, the portion of surplus transferred shall be proportionate to the value of liabilities being transferred.

Fiduciary responsibilities

38 Which persons and entities are 'fiduciaries'?

The term 'fiduciary' was originally used in the common law to describe the nature of the duties imposed on a trustee. The trustees of the scheme are therefore the fiduciaries as they are required to act in the best interests of members, and impartially. Their obligations to the employer are limited, unless stated otherwise in the trust deed and rules.

39 What duties apply to fiduciaries?

The fiduciaries have a duty not to benefit from the trust and not to delegate the trust.

They are to act in the best interests of the members and ensure the scheme is administered in accordance with the trust's deed and rules. In the course of discharging their duty they are not to put themselves in a position where their personal interests and their duties as a trustee conflict. Their duties are to:

- administer the scheme in accordance with provisions of the Retirement Benefits Act;
- keep all proper books of records of account;
- compute and prepare statements of payments of benefits made to members;
- liaise with the Authority and the other scheme administrators;
- collect and updating data with respect to each member;
- update the sponsor each quarter on all matters regarding the scheme;
- ensure contributions have been remitted to the custodian;

Update and trends

Recently, the Authority has partnered with the Micro and Small Enterprise Authority to increase its membership and assets held by pension schemes by targeting small-scale enterprises in the informal sector (eg, artisans, vegetable vendors, mechanics and other small entrepreneurs). Recent studies indicate that most jobs in Kenya are now found in the informal sector, where for long there was no defined pension arrangement.

Going forward, the Authority is planning on having automatic enrolment into pension schemes introduced so that all eligible workers and the self-employed are covered. One particular scheme that has generated global interest is the Mbao Pension Plan. It denotes that members save on average 20 shillings every day. To encourage establishment of this scheme, the Authority had to bend the law to allow flexibility that would befit people in the informal sector. In this scheme, contribution is voluntary and there are no strict deadlines on deposits and withdrawals.

Kenya has also introduced a new universal social security scheme. Under the plan labelled *Inua Jamii* (Swahili for 'Uplift Society'), more than 700,000 elderly will receive a bi-monthly stipend of 4,000 shillings and also get a National Health Insurance Fund. The stipend, considered a non-contributory social pension for the elderly, is being implemented by the Ministry of East African Community, Labour and Social Protection cover. This is an enhancement, given that the previous cash transfer initiated in 2012 targeted individuals above 65 years living in extreme poverty.

Recently, a fourth type of pension plan was introduced: the umbrella pension scheme. The scheme is provided for by the Retirement Benefits (Umbrella Retirement Benefits Schemes) Regulations. An employer who wants to participate in the umbrella scheme will look at the suitability of the scheme and through a deed of adherence, bind itself to the trusts of the scheme and participate in the provision of retirement benefits to its employees on the terms expressed in the scheme rules. Employers do not have to establish a fully-fledged pension scheme if they have few employees. This suits the informal sector, as members can now enrol in individual pension schemes under an umbrella scheme.

Schemes are also expected to venture into investing in alternative assets classes, given the broadening of the allowable investment categories. New products introduced recently include real estate investment trusts (development and income), private equity and venture capital, derivatives and exchange-traded funds. We now have more products where schemes can invest in through the capital market. The Authority undertakes regular reviews of investment asset classes to align them with market developments, enhance portfolio diversification, manage risks and boost returns.

The Authority has also proposed to the government that it allow for the 15th Investment Asset Class for debt financing of public-private partnership (PPP) projects approved under the PPP Act for infrastructure or housing to be utilised by schemes. This is expected to diversify investment opportunities for pension schemes.

- ensure scheme funds have been invested by a manager, appointed by themselves;
- communicate regularly with the members with respect to affairs of the scheme;
- ensure all documents binding the scheme are professionally prepared;
- convene annual meetings for members; and
- ensure all minutes, statements and resolutions are properly kept and maintained.

40 What are the consequences of fiduciaries' failing to discharge their duties?

The general penalty for breach of trust is sanctions imposed on the fiduciary, as given within the Retirement Benefits Act section 53. The sanctions may vary through the Act with regard to specific offences committed. Common law also sets civil penalties and prohibitions as consequences a trustee will face where they fail to impose due duty of care.

Most scheme rules contain provisions that indemnify the trustees when they exercise power on a matter where they had a personal interest in the result. However, they must disclose the same to other trustees and the sponsor.

This exclusion from personal liability does not extend to situations where the trustee has engaged in fraud or professional negligence.

Trustees shall also not be victimised, removed from office or discriminated against for having performed their functions under the scheme's trust deed and rules.

Legal developments and trends

41 Have there been legal challenges when certain types of plans are converted to different types of plan?

When it comes to conversion of plans, the stem of the problem is the lack of clear and specific legislation to govern the process. Conversion of schemes is mostly done as an amendment to a scheme's rules and not as a process.

The lack of these rules results in numerous challenges. In practice, the employer can exercise its discretion on how to fund the new scheme and force all members to transfer to the new scheme, a matter that should be decided by the member. The employer should operate the old scheme as a closed scheme up until all pending dues, to the members especially, have been paid.

Conversions of defined benefit plans to defined contribution plans have led to lower benefit levels and, as stated above, such matters are left to the discretion of the employee, thus members do not have an avenue to protest.

Recently, numerous schemes have been accused by former employees of miscalculating the benefits members will receive on retirement, resulting in the benefit being inadequate. This challenge is mainly in defined benefit schemes, as these schemes are based on final pensionable salaries, sums that are inadequate to support members comfortably upon retirement.

42 Have there been legal challenges to other aspects of plan design and administration?

Legal challenges mostly concern compliance with the Retirement Benefits Act, its regulations and all other legislation that governs schemes. Examples of such challenges include non-remittance of contributions, non-submission of requisite documents to the Authority and commutation of retirement benefits.

The office of the trustee has also resulted in legal challenges, especially with regard to their duties; so much so that it was recently legislated that trustees are not to be victimised for performing their powers in accordance with a scheme's rules.

There have been recent amendments making it possible for a member to allow for the transfer of part of accumulated benefits or additional contributions to be made for the purpose of post-retirement medical cover. Administratively, this has seen serious problems, as the Authority is yet to issue guidelines for the establishment and management of such funds.

43 How will funding shortfalls, changing worker demographics and future legislation likely affect private pensions in the future?

Funding shortfalls mainly affect defined benefit schemes.

If a problem befell a defined contribution scheme it would probably be the result of incorrect computing or entering of data during the actuarial valuation. These actuarial reviews can guide an employer in setting the contribution rate of the scheme. Within the three years, the scheme funds may not perform as expected, affecting the investment returns and the benefits funded by it.

The problem of funding shortfalls therefore affects both private and state pensions. In the future, most defined benefit schemes will be converted to defined contribution schemes, as per a government circular resolution. If a sponsor is faced with a funding shortfall, the burden will be eased on conversion, as the members' contributions will go towards the funding of the scheme.

Legislation always impacts the retirement benefits sector. The impact may be positive and result in better administration and governance of pensions, because the main aim of said legislation is to protect the beneficiaries of the scheme. It will also better protect a scheme's administrators. However, sometimes the impact may be negative and maybe not favour employers. Such laws will, in turn, not motivate employers and may delay the provision of benefits. Legislation should be of an impartial nature and be considerate of all parties. It should not be restrictive but instead be progressive. Recently regulation 7(g) of the Retirement Benefits (Occupational Retirement Benefits Schemes) Regulations was amended by Legal Notice 111 of 2015 to limit the re-election term of trustees to only one term of three years. This may negatively affect employers as the constant shift in trustees every six years may lead to delayed and disconnected decision-making.

Change in worker demographics will greatly expand the pensions and retirement benefits sector, as it will have to develop to accommodate all workers. An example is the Mbao Pension Plan, which is for persons employed in the informal sector. This plan's membership will increase in size with the development of the informal sector. The New NSSF Act, which is yet to be implemented, is considered a game-changer in the pensions industry as it aims to cover everybody, including members of the informal sector and the self-employed. It now encourages all employers and employees to contribute towards it.

This change will also result in more types of benefits being provided to various demographic groups such as the elderly and women. The New NSSF Act will introduce new benefits such as:

- a withdrawal benefit for members who opt to retire before attaining retirement age;
- an emigration grant that is paid to members of the scheme who permanently emigrate. This would be in accordance with globalisation and the increase in workers seeking international employment; and
- a funeral grant that is payable to a dependant of a deceased member nominated by the family and identified by the local administration.

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