VOLUNTARY PENSION CONTRIBUTIONS

RELEVANT LAWS:

A. Personal Income Tax Act (LFN) 2011 as amended (PITA).
B. Pension Reform Act 2014 (PRA 2014).

1. Introduction

The enactment of Pension Reform Act 2014 was principally to address noted gaps in the operation of the contributory pension scheme based on the legacy PRA 2004.

It has however become evident that in a bid to improve the capability of individuals to cater for their livelihood during old age/post retirement and increase the savings stock of the national economy through voluntary pension contribution, a loophole seems to have been inadvertently created in PRA 2014 with potential adverse fiscal effect.

2. Objectives

This Circular provides JTB's guidance with respect to claiming tax relief on voluntary pension contributions and to discourage abuse of the tax incentive based on the following:

I. Tax deduction cap for Voluntary Pension Contributions;

II. Lock-in Period for tax exempt payment of Voluntary Pension Contributions; and

III. Income earned on voluntary contributions

3. Observations

The Pension Reform Act 2014 does not specify a threshold for the amount that can be contributed by employees before the amount will qualify as tax free. However, a situation where an employee makes a voluntary contribution of a material portion of his/her salary in one month and withdraws almost the entire amount in the next month is clearly an abuse of the law and does not qualify as retirement benefit or a pension as envisaged in the Pension Reform Act. PRA 2014 Section 1(d) states that "*The objectives of this Act are to* "*assist improvident individuals by ensuring that they save in order to cater for their livelihood during old age*".

Such actions also clearly conflict with the provisions of the Personal Income Tax Act (PITA), Section 17 which states:

> *"Where a tax authority is of opinion that any disposition is not in fact given effect to, or that any transaction which reduces or would reduce the amount of any tax payable is artificial or fictitious, the tax authority may disregard the disposition or direct that such adjustments shall be made as respects the income of an individual, an executor or a trustee, as the tax authority considers appropriate so as to counteract the reduction of liability to tax effected, or reduction which would otherwise be effected by the transaction".*

4. Allowable pension reliefs for income tax purpose under the PRA 2014

Sections 10 and 16 of the PRA 2014 make the necessary guidelines for the application of tax exempt granted for pension contributions and withdrawals.

Below are the specific tax exempt provisions under the section 10:

I. Notwithstanding the provisions of any other law, contributions to the scheme shall form part of tax deductible expenses in the computation of tax payable by an employer or employee under the relevant tax law.
II. All interest, dividends, profits, investment and other income accruable to pension funds and assets under the PRA shall not be taxable.
III. Any amount payable as a retirement benefit under this act shall not be taxable

IV. Without prejudice to the provisions of subsection (2) of this section, any income earned on any voluntary contribution made under section 4 (3) of this Act shall be subject to tax at the point of withdrawal where the withdrawal is made before the end of 5 years from the date the voluntary contribution was made.

Section 16 states:

*"An employee shall not be entitled to make **ANY** withdrawal from his retirement savings account opened under Section 11(1) of this Act, before attaining the age of 50."*

The Section further stipulated the following provisions to guide withdrawals from the employees' RSA:

1. An employee shall not be allowed to make withdrawal from his RSA before attaining the age of 50 years.
2. The exception to 1 above is where the employee retires, disengages on the required advice that the employee is no longer capable of carrying out the function of his office , due to total or permanent disability before the age of 50 years in accordance with the terms of his engagement.
3. An employee, who disengages or is disengaged from employment before the age of 50 years and is unable to secure another employment within four (4) months, may make withdrawals from the RSA.

Based on the above, Section 16 of the PRA 2014 compels the employee to adhere to certain conditions within the law before withdrawals made on their RSA can be termed to be tax exempt.

5 Resolutions

On an annual basis, individuals claiming tax relief on voluntary pension contributions must submit to the RTA alongside their income tax return, a copy of their RSA (Retirement Savings Account) for the relevant tax year and statement of voluntary contribution to the scheme.

ANY payment made by Pension Fund Administrators [PFAs] to individuals that do not meet the relevant conditions specified in Section 16 of the PRA 2014 will be considered to fall outside the tax exemption granted in 10(3) of the Act.

Every Relevant Tax Authority [RTA] will:

a. Periodically audit withdrawals of voluntary pension contributions authorized by the respective PFAs.

b. Enforce the law with respect to recovery of any tax due which will include: applying interest and penalties on any resulting tax due on the employer under the PAYE scheme.

PS: This draft position paper is without prejudice to:

a. PENCOM's current effort at issuing guidelines to partially address the challenge of possible abuse of Voluntary Contribution provisions of PRA 2014.

b. The urgent need for legislative remedy through:
    i. An amendment of the PRA 2014 to engender adherence to basic objective of Contributory Pension Scheme articulated in Section 1 (d) of the Act. This can be achieved via adoption of the lock-in period for Voluntary Contribution to Contributory Pension Scheme as stated in the defunct PRA 2004 with some adjustments, if deemed necessary.
    ii. Introduction of a cap on Voluntary Contribution is also advisable as it would possibly free up transactional fund for consumption and investment at the household level thus contributing to growth of the national economy.
    iii. Enactment of an omnibus legislative provision that confers supremacy on taxation rules stipulated in provisions of extant Tax Acts/Laws over any contradictory tax rule provided for, under non-Tax Acts/Laws.