PENCOM REGULATIONS ON INVESTMENT OF PENSION FUND ASSETS (2017)

1. INTRODUCTION

The National Pension Commission ("**PenCom**") recently published the long anticipated "Regulation on Investment of Pension Fund Assets" (the "**2017 Regulations**") pursuant to the Pension Reform Act (2014) ("PRA") s. 85(2). The 2017 Regulations supercede the regulations on Investment of Pension Fund Assets, 2012 ("**2012 Regulations**") and expand the list of eligible investments for pension fund administrators ("**PFAs**") by including sukuk and other non-interest compliant instruments. The 2017 Regulations further provide the quality requirements of allowable investments and set out guidelines for the implementation of the multi-fund structure for the investment of pension fund assets in retirement savings accounts ("**RSA**") Funds. We have analysed the provisions of the 2017 Regulations hereunder:

2. THE 2017 REGULATIONS

2.1 *TAXES*

Pursuant to PRA s. 10(2), all interests, dividends, profits, investment and other income accruable to pension fund assets from allowable instruments under the PRA and the 2017 Regulations are exempt from taxes. PFAs are still liable to pay company income tax and other statutory contributions.

2.2 *EXPANSION OF ALLOWABLE INVESTMENTS*

2.2.1 **Sukuks –** Permissible investments for PFAs now include Sukuks issued by: (i) the Federal Government of Nigeria ("**FGN**"), its agencies and/or affiliates guaranteed by the FGN or the Central Bank of Nigeria ("**CBN**"); (ii) state or local governments or wholly owned companies of the state that fully implement the contributory pension scheme and which instrument is fully guaranteed by an irrevocable standing payment order or external guarantee by a multilateral development finance institution with a minimum credit rating of "A"; and (iii) eligible listed and unlisted corporate entities that fully implement the contributory pension scheme (2017 Regulations regs. 2.8 and 4).

2.2.2 **Non-Interest (Shariah) Compliant Investment Funds** - PFAs are now allowed to invest in non-interest compliant investment funds registered with the Securities and Exchange Commission ("**SEC**") (2017 Regulations reg. 4.6). Other non-interest compliant debt instruments issued by eligible listed and unlisted corporate entities are also permissible investments.

2.2.3 **Ordinary Shares of Public Companies to be listed on a Securities Exchange registered with SEC** – PFAs are now permitted to invest in the ordinary shares of public limited liability companies proposed to be listed on a securities exchange registered by SEC through an initial public offer (2017 Regulations regs. 4.4 and 5.2.4 (i)). There is no time-frame for concluding the listing of securities by way of an IPO and the 2017 Regulations are silent on steps to be taken by PFAs that have invested in a corporate entity that ultimately does not list its shares on a securities exchange.

2.2.4 **Naira-Denominated Depositary Receipts/Notes** – Naira-denominated depositary receipts and notes issued by foreign companies and listed on a securities exchange that is a member of the World Federation of Exchanges (WFE) are now allowable instruments for investments by PFAs (2017 Investment Regulations reg. 4.9). Depositary notes and receipts of foreign SPVs of Nigerian corporates listed on an approved securities exchange and denominated in Naira are eligible investments for PFAs.

2.4 *QUALITY REQUIREMENTS*

2.4.1 **Ratings –** Two (formerly one) rating agencies, one of whom must be incorporated in Nigeria and registered with the SEC, are now required to rate bonds, sukuk and commercial papers to be issued by eligible FGN, State, Local government and corporate entities. With respect to Eurobonds to be issued by Nigerian corporate entities, bonds, sukuk and other allowable instruments to be issued by eligible multilateral development finance institutions ("**MDFOs**"), the rating is required to be assigned by a rating agency recognised by SEC (2017 Regulations reg. 5.1.1 – 5.1.6). It is noteworthy that in the event that two rating agencies assign different rating grades to an instrument, issuer or issue, the lower rating grade will be applied for the purpose of determining the maximum investment limit (2017 Regulations reg. 5.1.8).

2.4.2 **Eurobonds** - Eurobonds issued by an eligible Nigerian corporate entity in which pension fund assets are to be invested must have a credit rating not lower than the sovereign rating of Nigeria (B and/or B-) at the time of issuance, by a SEC recognised rating agency (2017 Regulations reg. 5.1.5).

2.4.4 **New Company** – PFAs can now invest in a newly established quoted company that has evolved as a result of a merger, acquisition or any other combination arrangement of existing corporate entities subject to one of the erstwhile entities satisfying the minimum quality requirements for investment in ordinary shares (2017 Regulations reg. 5.2.4).

2.4.5 **Financial Statements** – Annual financial statements of an infrastructure fund shall be audited by an independent firm of chartered accountants registered by the Financial Reporting Council of Nigeria where a PFA intends to invest pension funds and assets in the infrastructure fund (2017 Regulations reg. 5.2.3(iii)(c)).

2.4.6 **Minimum Investment** – Unlike the 2012 Regulations which provides that a minimum of 75% of infrastructure funds and private equity funds are to be invested in companies or projects within Nigeria, the 2017 Regulations provide for a minimum of 60% and expands the categories to include bonds or Sukuks issued by MDFOs. This increases the flexibility of fund managers and issuers to invest the proceeds of the funds and bonds in other jurisdictions to maximise profits. (2017 Regulations regs. 5.2 (iii)(f), 5.2.11 (ix) and 5.2.12 (iii)).

2.5 *INTRODUCTION OF THE MULTI-FUND STRUCTURE*

2.5.1 All PFAs are now required to offer the Multi-Fund Structure ("**MFS**") for the investment of pension fund assets of RSA Funds. This structure replaces the single-fund structure that existed under the 2012 Regulations where all contributors to the pension scheme were allocated to one RSA Fund with no consideration for their age or risk profile. PenCom is, however, yet to provide the operational framework for the transition to the MFS structure. Once the framework is released, there will be clarity on when contributors can be assigned based on the default age classification. There shall be a transition period of six (6) months effective from the commencement date of the MFS for all PFAs to restructure their respective portfolios. Contributors will subsequently have the option to be assigned to a Fund of their choice depending on their risk tolerance.

2.5.2 The MFS splits the RSA Fund into Fund I – Fund IV. Fund I is an optional fund whose membership is strictly by request of a contributor. Fund II is the default fund for contributors aged 49 and below; Fund III is the default fund for contributors aged 50 and above and Fund IV is the retiree fund.

Fund Types	Contributors/Investors	Thresholds
Fund I	Strictly by formal request from a contributor and suitable for contributors who want to invest in high risk projects with higher rewards.	75% maximum and 20% minimum of Portfolio Value
Fund II	Active contributors who are 49 years and below as at their last birthdays.	55% maximum and 10% minimum of Portfolio Value
Fund III	Active contributors who are 50 years and above as at their last birthdays.	20% maximum and 5% minimum of Portfolio Value
Fund IV	Exclusively for retirees	10% maximum and 0% minimum of Portfolio Value

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