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| REGULATORY IMPACT ASSESSMENT REPORT  ON THE PENALTIES IMPOSED BY NAPSA ON LATE SUBMISSION OF MONTHLY CONTRIBUTIONS |

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# **INTRODUCTION AND BACKGROUND**

The Business Regulatory Review Agency is mandated to contribute to improving the business regulatory environment and reducing the cost of doing business. The Agency undertakes monitoring activities on the business environment. The Agency is also mandated to undertake Regulatory Impact Assessments on any regulation in any sector of the economy and advise Government as the need may be. The Agency through its monitoring activities received submissions from the private sector regarding the impact of NAPSA penalties on businesses. The contention by businesses is that the penalties imposed by NAPSA for late submission are punitive in nature and have caused closure of some businesses in some cases. Additionally, businesses are required to start making contributions upon registration as employers without consideration of when the business actually commences operations.

In view of the above, the Agency has commissioned a RIA to enquire into the imposition of penalties and their impact on businesses and how NAPSA can ensure business friendly administration of regulation on pension contributions without being overly burdensome on businesses.

The National Pension Scheme Authority (NAPSA) was established in 2000 under the National Pension Scheme Act, 1996. This followed the closure of the Zambia National Provident Fund (ZNPF) after the responsible Act under which it was formed was repealed.

The Act mandates NAPSA to provide income security against the risk arising from retirement (old age), death and invalidity with a focus on adequacy of benefits and monthly receipt of pension contributions. This is achieved through the payment of different kinds of benefits to its members

In order to ensure compliance on pension contributions, the National Pension Scheme Act provides for offences and penalties for avoidance and late submission of pension contributions. These include the following:

1. **Evading payment of contributions (section 51 (1) (a))** – This happens when employers do not pay the required social security contributions. It may also include late remittance of contributions.Section 12 of the Act defines who a contributing employer is and this includes any person, association, Institution, firm registered as a tax payer or a tax payer with a contract of service with an employee. It also includes the Government of the Republic of Zambia, Local Authority or Parastatal or Statutory Body.
2. **Failing to register within the period specified (section 51(1) (b)** – An employer should apply for registration within one month of commencing business. The period of one month begins on a date when the person/employee/member concerned becomes a contributing employee.

Section 13(13) of the Act obliges and empowers a contributing employer to register **every person**who becomes an employee in his service and also obliges him to provide the particulars of such employees. An employer is required to submit a duly completed Employer Registration Form number**NPS 411** and accompanied with Member Registration Forms. Section 15(2) of the NPS Act prescribes that penalties will be charged on all late or unpaid contributions. It states as follows:

“if any contribution is not paid within the time stated under subsection (1) a sum equal to twenty per centum of the amount unpaid shall be added as a penalty for each month or part thereof after the date the payment is due and the amount of the penalty shall be recoverable as a debt owing to the Scheme by the employer”. The foregoing section prescribes that a 20% cumulative penalty shall be charged on all unpaid or late contributions.

This penalty is charged on two major grounds:

1. It is compensation to NAPSA for the lost investment gains which would have been made and eventually passed on to the pensioner. At the time of retirement, the pensioner will have to be paid as though the money was received in the month it was deducted/due irrespective of whether NAPSA received it on time or not. In order to make it possible for such good payments to be sustained, NAPSA needs to invest all the funds received and to do so on time. Any delays may result in a situation where NAPSA’s obligations may outweigh its capacity to pay. The penalty therefore acts as compensation for the lost investment earnings; and
2. as a penal measure to deter would-be defaulters.

# **PROBLEM STATEMENT**

The National Pension Scheme Authority (NAPSA) was established to provide income security against the risk arising from retirement (old age), death and invalidity focusing on adequacy of benefits and monthly receipt of pension. This is achieved through the payment of different kinds of benefits to its members. The main source of funds for payment of benefits is pension contributions by members and proceeds from investments. NAPSA levies penalties on employers for late or none remittance of pension contributions. The penalty is intended to deter employers from defaulting on timely remittance of contributions.

However, the private sector has expressed concern regarding the administration of pension regulation. Particularly businesses are concerned about penalties charged by NAPSA for late remittance of pension contributions.

The contention by businesses is that the penalties imposed by NAPSA for late submission of contributions are punitive in nature and have caused closure of businesses in some cases. For example, one business complained that although their firm was regularly remitting contributions on time to NAPSA, it was treated with a heavy hand for delayed submissions caused by internet outage. Furthermore, the firm reported that, it was a good corporate citizen paying all statutory obligations including taxes and providing goods and services to society but one act of omission caused the business to lose a colossal sum of money in NAPSA penalties. There is also no distinction between a late contribution and avoiding to contribute.

Micro Small and Medium Enterprises (MSMEs) have also complained that, they are subjected to the same regulatory requirements as the large firms. They contend that due to their small size nature, uniqueness and limited capital outlay, they are susceptible to failure to meet statutory obligations regularly.

Currently, businesses are expected to pay penalties on pension contribution even when they have not met salary obligations to employees due to liquidity challenges. This situation pushes businesses into further debt and bankruptcy as chances of recovery diminish with passage of time.

# **Baseline**

Currently the penalty for late contributions is 20% of the total contributions overdue. Employers have up to the 10th of every month to remit contributions. The table below shows the number of companies defaulting per year and total penalties collected by NAPSA in the last five years.

|  |  |  |
| --- | --- | --- |
| Year | No. of Companies Defaulting | Penalties collected |
|  |  |  |
|  |  |  |
|  |  |  |
|  |  |  |
|  |  |  |

(NAPSA should complete the table)

# **POLICY OBJECTIVES**

# **General objective**

To reduce the compliance burden for pension contributions on businesses by 100% in order to assist businesses in financial distress to sustain themselves by 2022.

**Specific objectives**

1. To reduce penalties imposed by NAPSA on businesses in financial distress by 50% in order to assist them stay in business during crisis times by 2022;
2. To put in place a mechanism for MSMEs compliance to statutory requirements in order to promote their sustenance by 2023.

# **IDENTIFICATION OF OPTIONS**

1. Do nothing
2. Restructure the penalties imposed by NAPSA on businesses
3. Exemption of Micro, Small and Medium Enterprises from NAPSA

# **Do nothing**

This means, NAPSA continues to impose penalties as is being done currently. The current applicable penalties are 20% of outstanding contributions. The implication is that, businesses will continue to incur heavy penalties and deprived of finances for business growth. There will be no room for peculiar circumstances such as when a business fails or delays to meet its wage bill in a particular month due to liquidity challenges. The administration of the penalty regime will continue to be overly punitive with no regard to business continuity.

# **Amendment of National Pension Scheme Act**

Under this option NAPSA would continue to impose penalties for defaulting employers but restructure the penalties. This would require the National Pension Scheme Act to separate offenses and define them clearly. The restructured offenses and penalties will provide lower penalties or waivers for employers. The new law will provide for incentives to employers in order to encourage more businesses to be in line with requirements of the law.

In addition to the above, the option will provide for notifications to NAPSA of peculiar events at a business that may potentially lead to a default such as not being able to pay salaries. Consideration will be given to extenuating circumstances that may cause an employer to default on pension contributions.

The new law will also provide a mechanism for compliance to statutory requirements by MSMEs so that they are encouraged to grow.

# **Exemption of Micro, Small and Medium Enterprises from NAPSA**

The Pension system in Zambia is three tier. The first pillar is a basic mandatory scheme, which is NAPSA. The second tier includes private occupational pension schemes providing supplementary pensions to their respective employees. These private occupational schemes were established under trust in accordance with Land (perpetual) Succession Act, Chapter 186 of the Laws of Zambia, and are managed by different insurance and non-insurance companies. Lastly, the third tier covers individual accounts and voluntary pension plans. Previously some businesses such as Nkonkola and Mopani Mines had been excluded from NAPSA contributions. However, the National Pension Scheme Act provides NAPSA as the basic compulsory scheme.

The Agency considered the possibility of exempting MSMEs from NAPSA and only engaged themselves with private occupational schemes. However, the fact that MSMEs have challenges meeting statutory contributions with NAPSA means that for the same reasons they are not able to meet these obligations under NAPSA, they are unlikely to meet them under private occupational schemes.

Agency has considered the possibility of exempting MSME from pension obligations. However, while such a measure will reduce the cost of labour for the exempted businesses, employees will be disadvantaged as they will be without pension contributions

# **COMPARISON OF COSTS AND BENEFITS OF OPTIONS**

The overall objective of the National Pension Scheme is to ensure that working citizens enjoy a safety net (social security) after retirement. Penalties on none contributions and late contributions are imposed as a disincentive for defaulting. This Regulatory Impact Analysis used a multi criteria analysis to compare the options. Multi-criteria analysis was used because of the special nature of this impact assessment. Most impact assessment focus on the impacts and effects of a regulation itself. However, this impact assessment is focused on enforcement mechanisms (penalties). RIA methodologies such as Cost Benefit Analysis (CBA), Cost Effectiveness Analysis (CEA) and Standard Cost Model (SCM) are applied on regulatory costs and benefits that are predictable and known when they will be incurred and their size or magnitude unlike penalties that are on the enforcement end of regulation and imposed as and when a business defaults. This impact assessment is about finding an option that achieves the objective of the penalties while imposing the least burden or impact on businesses. Therefore, the report uses Multi-criteria Analysis (MCA). Each option was analyzed against the following:

1. Effectiveness at deterring employers from submitting contributions late;
2. Whether the option imposes the least regulatory burden on employers (businesses). This is the most important measure for the purpose of this impact assessment;

The above criterion was chosen on the assumption that any enforcement mechanism is supposed to encourage employers to register employees and make contributions on time.

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| --- | --- | --- | --- | --- | --- |
| **Options** | **Criteria** | **Impact on business** | **Weight** | **Score** | **Total** |
| Do nothing | Effectiveness at deterring employers from submitting contributions late | * The continuation of the current penalties will be effective at ensuring well performing businesses remit pension contributions on time; * The penalties will still not compel poor performing businesses to remit on time; * Businesses in financial distress require a different approach to regulation | 0.25 | 5 | 1.25 |
| Imposing the least regulatory burden on employers (businesses) | * Negative impacts as the penalties are fixed at 20% * Imposes high costs on poor performing firms | 0.75 | 1 | 0.75 |
| Restructure penalties | Effectiveness to deter employers from submitting contributions late | * Well performing businesses continue to remit pension contributions as per set timelines; * Businesses in financial distress are regulated in a manner that does not worsen their distress; * Flexibility to determine unwillingness to comply and failure to comply due to circumstances | 0.25 | 5 | 1.25 |
| Imposing the least regulatory burden on employers (businesses) | * Well performing businesses continue to comply; * Poor performing businesses or businesses | 0.75 | 2.5 | 1.875 |
| Private Pension Scheme/ 4.3 Exemption of Micro, Small and Medium Enterprises from NAPSA | Effectiveness to deter employers from submitting contributions late | * Well performing businesses continue to comply; * Poor performing businesses that are not able to meet NAPSA obligations will still not be able to self-regulate and meet their obligations | 0.25 | 2.5 | 0.625 |
| Imposing the least regulatory burden on employers (businesses) | * Imposes no regulatory costs for not remitting pension contributions; * However, businesses may be subject to litigation by their employees; | 0.75 | 2.5 | 1.875 |

Key: On a scale of 1 to 5 where 1 is poor and 5 is the best

Weights: 1 is the most important aspect and 0 is the least important

# **STAKEHOLDER CONSULTATION**

The Business Regulatory Review Agency had engagements with twelve Chambers of Commerce and Industry where it was informed of negative impacts of the penalties imposed on late submission of contributions to NAPSA. Further consultations will be required with businesses and NAPSA on how best the authority can guarantee contributions while minimizing negative impacts on businesses.

Proposed stakeholders

1. NAPSA
2. Businesses (micro, small, medium, large)
3. Private sector associations (ZACCI, ZAM, ZCSMBA,)
4. Government (PIA, MoF, MoLSS…)

# SELECTION OF PREFERRED OPTION

Penalties are imposed as an enforcement mechanism to deter businesses from defaulting on making pension contributions. This RIA document is based on preliminary consultations or views of businesses that came to the attention of the BRRA. Based on a preliminary assessment of the options, continuing imposing penalties regardless of reasons for default will be detrimental on businesses that are financially distressed especially small and medium enterprises. The alternative ie allowing businesses to work with private pension schemes does not guarantee that they will comply with their own commitments. They are likely to default for the same reasons that they are defaulting with NAPSA.

The Agency, therefore, recommends the restructuring of penalties to recognize businesses that are under financial distress or have a valid reason for default to allow them to operate without accumulating penalties. This would increase chances of recovery and allow businesses slipping into insolvencies and ultimately close. Labor is a key input of any business undertaking and labor laws have the potential to stifle businesses if not implemented with a clear understanding of circumstances prevailing in the internal life of businesses.

The final determination will be made after consultations.

# IMPLEMENTATION, MONITORING AND EVALUATION PLAN