G:ENESIS

DEVELOPING A BROAD-BASED EMPLOYEE PENSION SCHEME FOR BOTSWANA

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EXECUTIVE SUMMARY

The evaluation and reform of Botswana's system of pension provision is prompted by three main observations, namely high levels of poverty in old age which will persist unless broader pension participation is ensured; low levels of long-term household savings; and rapid economic development, which can make a broader-based pensions system affordable.

This research study identifies four main factors that support the need and viability of a broad-based pension scheme, and makes the case for moving to such an arrangement while taking account challenges such as high levels of unemployment and informality in the economy.

The report then evaluates the viability of such an arrangement, presenting evidence from some financial modeling undertaken for this study. Some broad institutional parameters, considerations and options are offered to inform the design and implementation process and, finally, recommendations are made on how best to move forward with this process.

The case for a broad-based pension arrangement

Four factors support the implementation of a broad-based pension arrangement:

1. **High levels of poverty and falling incomes await people in old age**

   Almost all Batswana above the age of 65 receive the universal Old Age Pension of P191 per month (approximately US$30), while some receiving additional grants. Despite this provision, peoples' incomes fall an average of 30-60% on retirement, with a third of elderly Batswana reporting that they are unable to afford food several times a year. Only 16% of the elderly currently receive a private pension that allows them access to an equivalent or better standard of living than they had before retirement.

2. **Limited provision for old age by working age people and limited access to pension arrangements**

   Within the working age population there is extremely low usage of individual, voluntary savings products such as retirement annuities, unit trusts or life insurance policies with large savings components. As a result, over 60% of employees can expect to rely primarily on either the state pension or non-pension sources (such as family, remittances or ongoing work) in their old age.

Out of a labour force of 790,000 workers, some 300,000 are formally employed and could potentially be covered by a pension arrangement. However, 84% of those in private formal employment and 33% of public sector employees are not covered by any scheme, indicating a large gap and an opportunity for pension cover in this space.

3. **The gratuity/severance scheme generates substantial sums of money, but this is used mainly on consumption**

   Under the Employment Act, gratuity/severance is a compulsory payment, due after every 5 years of continuous employment or on termination after at least 5 years of service. This gratuity is in lieu of a pension or provident scheme. It is usually provided to lower skilled, 'industrial' workers and is not made in response to any social security need. An estimated P115m in gratuity payments are made annually, the majority of which is spent on current consumption. There is therefore widespread recognition of the case for diverting the gratuity into long-term saving; with 90% of employers and 86% of employees surveyed for this study supporting the idea. Tellingly, almost all retired people who had received gratuity expressed a wish that they had saved more for their retirement.

4. **Providing costs are controlled, it can be financially viable and feasible to provide pension to low-income employees**

   Preliminary financial modeling work based on industry data suggests that it can be cost-effective to provide a pension of about 50% of final salary at retirement to someone earning P800 per month. When added to the state OAP this provides an income in retirement of over two thirds of pre-retirement income, assuming employer and employee contributions of 10 and 5% over working life without withdrawals. It also assumes, critically, low administration (P20) and investment management (1%) costs, which are at the low end of charges currently applied by the retirement fund industry in Botswana. These costs are not unreasonable provided that the retirement fund industry and government work together.

   The above factors provide a strong motivation for a broad-based national pension system. The case is based on recognition of current low levels of provision for old-age and the prospect of descent into poverty for retirees. There is also the realisation of an opportunity given the expressed willingness of employers and employees to divert gratuity payments into a pension arrangement and contribute to such a fund. Finally, financial feasibility analysis confirms that such an arrangement is viable.

Further considerations

This study presents some further considerations concerning the choice of benefit structure and the institutional framework for delivery of the benefits which will have to be determined under the proposed model. Most Botswana schemes have moved towards a defined contribution structure. While this has both advantages and disadvantages relative to defined benefit structures, it is possible to overcome many of the challenges presented by these defined contribution arrangements. For example, a lifestage investment approach could be adopted, together with regular projections to ensure the benefits will be sufficient. This report recommends that the benefits should be paid out in the form of income, with only limited access given to accumulated funds on early withdrawal from the scheme due to death, disability and involuntary unemployment.

Consideration is given to the institutional framework which will have to be set up to deliver the envisaged benefits. This will have to involve combinations of public and private sector actors arranged to capture the economies of scale achievable by government together with the efficiencies of competition delivered by the private sector. It is likely that existing private sector expertise can be cost-effectively utilized by wholesale tendering of sections of activity such as interface with scheme members, administration of accounts and investment of contributions. Contribution collection is probably done most effectively and cheaply by the Botswana Unified Revenue Service (BURS), while benefit payment expertise exists both in the private sector and in the Department of Social Benefits.

Recommendations

The key recommendation is to proceed with the process of extending access to pensions for low-income formally employed workers. This should be done by firstly diverting amounts currently put aside for gratuity to pension schemes instead. These contributions can be supplemented by employee contributions and gradually increased over time.

Involvement of key stakeholders needs to be secured to build support at all levels, including the private sector administrators and fund managers, BURS, Department of Social Benefits, the trade unions, employer groups as well as the Ministry of Labour and Home Affairs, and Ministry of Finance and Development Planning.

In parallel, it is important to quantify in more detail the existing costs of benefit delivery in the public and private sector in order to inform development of the most cost-effective institutional model.

The results of this review and the dialogue between the parties can feed into a substantive discussion about the optimal institutional structure for this pension arrangement.

1. INTRODUCTION

1.1. CONTEXT OF THE STUDY

Botswana is a relatively well-off country by sub-Saharan African standards, though it has a relatively high rate of unemployment (20-25%), particularly high HIV prevalence (24% of adults) and a correspondingly low average life expectancy, with estimates ranging from 35 to 50 (World Bank, 2007 & FinMark, 2004).

Botswana private domestic savings stand at roughly 26% of GDP, which is high relative to other sub-Saharan countries (IMF, 2003). Relative to other countries in the region, savings products show high usage levels in the 2004 Finscope survey (FinMark Trust, 2004). Some of this relates to long-term private savings, and there has been some public sector activity too which has driven an increase in savings. For instance, the Botswana Public Officers Pension Fund (BPOPF) was formed in 2002, and now accounts for the majority of pension assets. At the same time, private provision by companies for their employees has grown from P40m in 1985 to P14500m today (Mmegi/The Reporter, November 2007). However, coverage by private pension schemes has been reported to be patchy and limited to higher income employees, while also delivering poor replacement rates[1].

Apart from this type of contributory saving, on the non-contributory side retirement security is also provided through the universal, low level state Old Age Pension (OAP). Other forms of saving in Botswana are investment in housing, small businesses, cattle, and individual retail products.

Finally, the projected growth in the total population, and specifically the population over 60 (HIV notwithstanding) suggests that resources should be dedicated to increasing saving for retirement and modifying the current arrangements to ensure greater access to retirement provision.

In the context of these features and dynamics in the Botswana savings environment, the broad aim of this study is to supply knowledge about the current coverage of public and private schemes in Botswana. The study also evaluates the

[1] The replacement rate is defined as the ratio of income received in retirement to income received just before retirement.

desirability and feasibility of a long-term contractual savings scheme in the country, potentially to be grown out of the severance/gratuity payment scheme created by the Employment Act (EA).

The specific terms of reference of the study are summarised below:

- Provide an overview of pension provision in Botswana, covering the state OAP scheme and private (mostly employment based) schemes under the Pension and Provident Funds Act.
- Review the operation of the gratuity and severance schemes provided for under the EA.
- Analyze the need and potential for using existing EA provision as the basis for a mandatory national retirement saving arrangement.
- Comment on the possible management and administration arrangements and costs if a scheme based on the EA provision is implemented.
- Provide policy recommendations of relevance to the Botswana Government.

The study was initiated and financed by FinMark Trust, a not-for-profit organisation dedicated to making markets in Southern Africa work better for the poor.

1.2. METHODOLOGY

The study used a combination of methodologies which included a review of existing data and literature; discussions with key industry players; and a survey. The review of existing literature included official annual reports from the Registrar of Insurance and Pensions[2]; Central Statistics Office publications[3]; annual reports from the Ministry of Labour and Home Affairs; data from the Department of Social Services; and Finscope survey data collected in 2004.

Discussions were held with key government officials (Ministry of Finance and Development Planning; Ministry of Labour and Home Affairs; Department of Social Services in the Ministry of Local Government); key market players in the pension industry (pension funds; insurers; brokers; administrators, fund managers); and the broader economy (trade unions; businesses and their representative organizations). In total 30 interviews with the key industry players were undertaken.

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[2] Pension and Provident Funds Report for the year 2006; Eighth Annual Report of Registrar of Insurance for the year 2006

[3] 2001 Census report; Labour Statistics; Household Income and Expenditure Survey Reports.

Three separate surveys, employee, pensioner and employer, each involving 80 persons were undertaken to supplement the existing data sources. The samples for the three surveys were taken from Gaborone city and neighbouring towns.

- *Employee survey:* employees entitled to receive gratuity/severance pay under the employment act were surveyed to understand how gratuity payments are utilized and to assess the willingness to transform gratuity payments into long-term savings for retirement. Sampling criteria was employment in the public or private sector on non-pensionable terms and eligibility to receive gratuity under the Employment Act.

- *Pensioner survey:* The survey assessed the welfare of people in retirement, specifically comparing those who had employment-related contributory pension arrangements with those who were on gratuity arrangements. Sampling criteria was that they must have previously worked in the public or private sectors and are now in retirement.

- *Employer survey:* The survey captured information on compliance with Employment Act provisions for gratuity payments and willingness to have the gratuity payments transformed into a contributory pension scheme for the employees. The employers sampled were well-established formal firms, of a range of sizes and industries, and from both the public and private sectors.

1.3. STRUCTURE OF THE REPORT

Section 2 of the report reviews the circumstances of the elderly in Botswana, and demonstrates the gap between the OAP and their needs. Section 3 presents findings on how the working age population plans to provide for old age, while section 4 outlines the gratuity/severance scheme and provides insights into its functioning and implementation.

Section 5 goes on to consider whether there is scope for a broad-based pension scheme in Botswana, and what form this could take. In particular, the extent to which the cash flows currently directed to regular gratuity payments could be directed to longer term savings is explored. Section 6 offers some pension fund design parameters, and section 7 offers some concluding remarks and recommendations to move this process forward.

2. CIRCUMSTANCES OF THE ELDERLY

Botswana has a population of approximately 1.7 million, of which the elderly (that is those over 65 years) account for at least 65,000 (CSO, 2005).

2.1. SOURCES OF INCOME

The primary source of income for the elderly is the universal, non-contributory pension scheme funded through tax revenues where all Batswana aged 65 and above are paid P220 per month (as at April 2008). Approximately 90,000 people are currently on the state OAP roll. (This exceeds the number who would be expected to be age-eligible according to demographic projections, as for many old people there is uncertainty about their age.)

In addition, some of the elderly receive other social benefits such as destitute benefits and food grants that are not exclusively directed or provided to them. These benefits are means-tested. A small number of eligible elderly receive a veteran's pension for past military service, while others are self employed. Only an estimated 11,000 elderly Batswana are currently in receipt of private pensions being paid out by a pension fund or insurance company.

These sources of income in old age are illustrated diagrammatically, below:

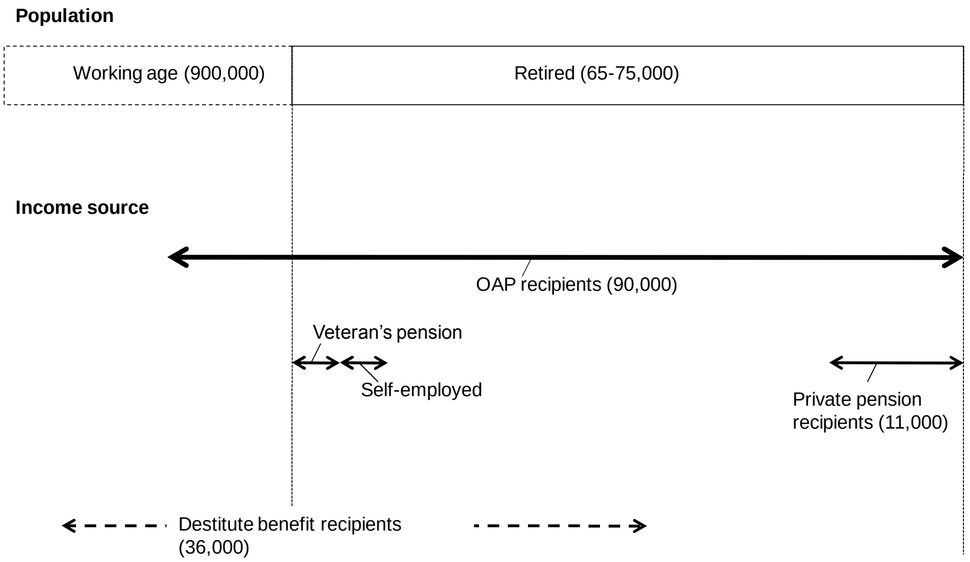

Figure 1: Schematic representation of sources of income of elderly population in Botswana
Source: Botswana. Central Statistics Office (CSO). 2005. Population Projections for Botswana 2001-2031; Consultations with insurers & Department of Social Benefits

2.1.1. SUBSTANTIAL FALL IN INCOME IN OLD AGE

Our research findings suggest that people experience a drop in income on retirement. For households located in cities/towns, the average drop in income when the household head retires (from its maximum lifetime level) approximates 32%; while for those located in urban villages the average reduction is 43%. Households located in rural areas experience an average drop in income of 56% when the household head retires (CSO, 2004).

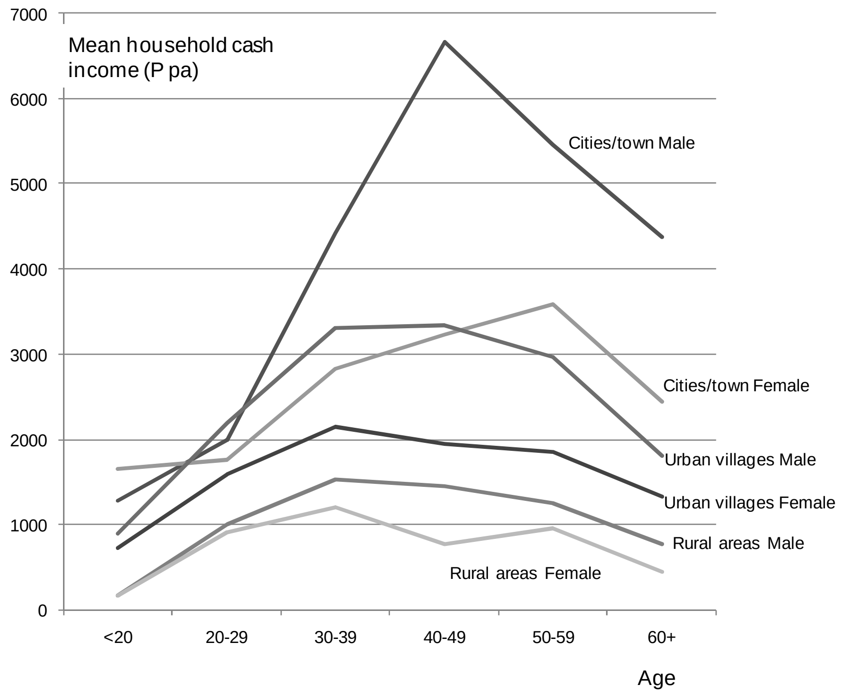

Figure 2:Average fall in retirement income by age
Source: CSO, 2004

Evidence from the survey conducted shows that the elderly who were eligible to receive gratuity under the Employment Act (i.e. did not have contributory pension arrangements when in active employment) experienced a 55% drop in income, from approximately P1,349 per month when in active employment to P601 per month in retirement (see Table 1).

In contrast, those who had a contributory pension scheme arrangement while in active employment actually reported an increase in income while in retirement[4].

[4] The increase can be attributed to pension payouts as well as income from other sources, and includes any increases in pensions since retirement e.g. 5% increase in annuity.

Status	Mean Employment Income (Pula)	Mean Retirement Income (Pula)	Percent Change
Elderly who had Contributory Provident/Pension Fund	5,225.6	5,433.5	4.0
Elderly who Received Gratuity under Employment Act	1,349.3	601.9	-55.4

Table 1: Percentage Drop in Mean Income on Retirement
Source: Pensioner survey, 2008

2.1.2. HIGH LEVELS OF POVERTY

For the elderly who did not contribute to a pension fund, this fall in income can leave them below the poverty line. According to the Household and Income Expenditure Surveys, at the national level the proportion of the population below the poverty line (approximately US$ 1 a day) increased from 19.9% in 1993/94 to 23.4% in 2002/03. Poverty is highest among the elderly and in rural areas, where the elderly are disproportionately represented (CSO, Household income and expenditure survey 2002/03).

Further evidence from the Finscope 2004 data suggests that as many as a third of elderly people are unable to afford food several times a year, which further underlines the desperate situation in which many Batswana find themselves in retirement (Finscope 2004).

2.2. CONCLUSION

The conclusion from this analysis is that working people experience a severe drop in income on retirement, especially if they have not built up long-term savings during their working life. In addition poverty tends to be more severe among the elderly and in rural areas. This therefore calls for strategies to enable the working age population to save for retirement.

3. PROVISION FOR OLD AGE IN BOTSWANA

This section uses survey data to outline the sources of income working-age people expect to rely on after retirement. A discussion of the labour market structure follows, to understand people's ability to save for the long-term. Finally, there is a review of the provision made for old age and the various channels people expect to rely on, contributory or otherwise.

3.1. EXPECTED SOURCES OF INCOME IN OLD-AGE

The employee survey conducted for this study suggests that approximately 60% of employees expect to rely primarily on the state old age pension or non-pension sources (such as income from assets, work in old age, or family & friends) in their old age. However 41% of employees currently under the gratuity scheme hope that they will shift to a contributory pension scheme to provide for their old age. It should be noted that the employees surveyed were those entitled to receive gratuity under the employment act, hence this response highlights their wish to move from the current gratuity payout environment to a contributory pension scheme (see Figure 3). This is highly unlikely to happen unless access to pension schemes is actively encouraged or made compulsory for some workers in place of the gratuity scheme.

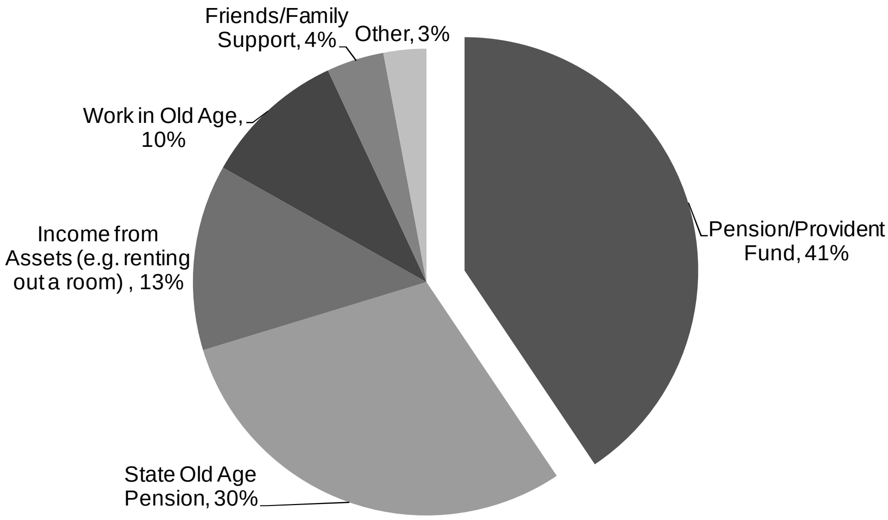

Figure 3: How Employees Expect to Provide for Old Age
Source: Employee survey, 2008

3.2. LABOUR FORCE AND UNEMPLOYMENT[5]

In 2005/06 industry market analysis showed that the labour force numbered around 790,000, with a labour force participation rate of 68.7% (CSO Stats Brief, 2007). The total unemployment rate, using a broad definition, was estimated at 31.6% (Labour Force Draft Report, 2005/6)[6]. For all age groups except above 50 years of age, females have higher unemployment rates than males. Most of the unemployed (57%) are found in the urban areas. Of the 540,000 who were

[5] Unemployed persons are defined by the Labour Force Draft Report 2005/6, as those individuals who did not do any work in the last 7 days either for payment in cash or in kind or who were not in self employment for profit or family gain. A narrower definition (as used by the ILO) counts unemployed persons as those actively seeking but unable to find work, which gives a lower rate of 18%.

employed in 2005/06, 56% were employed in the formal sector. Of the 300,000 employed in the formal sector, 40% were in the central and local government employment. In summary, the labour force is characterised by high unemployment, high levels of informality and dominance of public sector employment (shown pictorially in Figure 5).

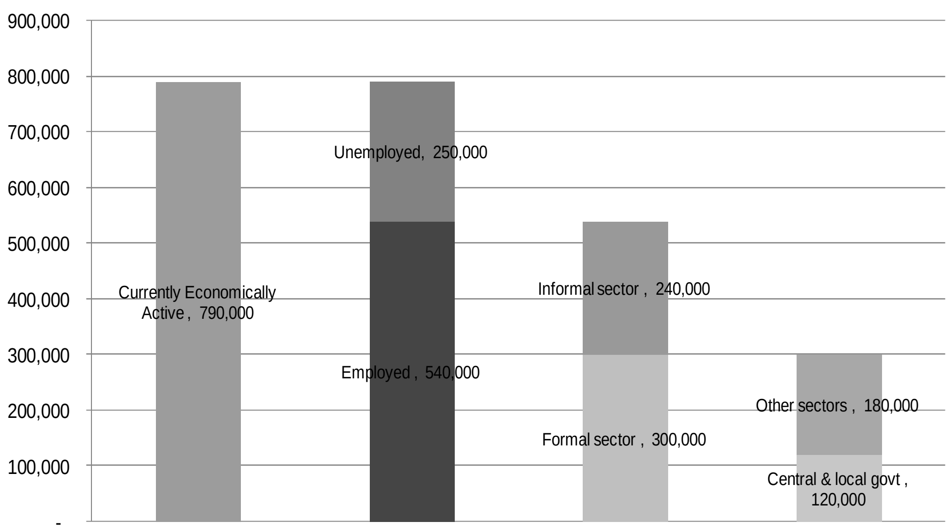

Figure 4: Labour Force and Unemployment in Botswana
Source: CSO Stats Brief, 2007

3.3. OCCUPATIONAL PENSION COVERAGE

The low rates of formal employment suggest limitations on the proportion of the population for whom long-term savings is attractive, feasible or available through channels such as occupational pensions.

Employment related provisions for old age can include defined contributory pension or provident funds, and defined benefit pension funds (under the Pensions and Provident Fund Act). Under defined contribution pension and provident fund schemes, both the employer and the employee contribute. The occupational provision space in Botswana is overwhelmingly dominated by defined contribution pension funds[7]. However, even within the formal sector identified in Figure 5 above, there is still a substantial gap in occupational provision, with 33% of government workers and 84% of the formally employed workforce having no cover. This is shown in Figure 6 below.

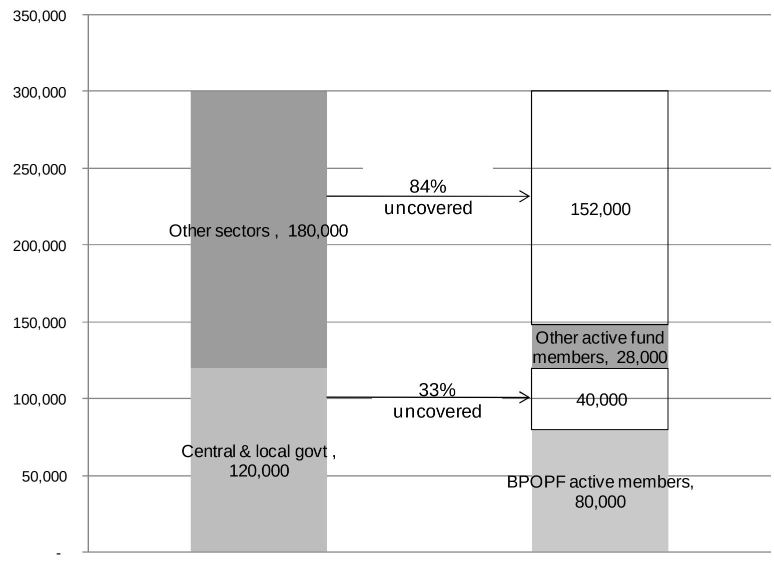

Figure 5: Coverage of private and public sector formal workforce by pension fund arrangements
Source: CSO, 2007, Stats Brief; Registrar of Pension Funds Annual Report for 2006, Finscope, Genesis estimates

3.4. INDIVIDUAL SAVINGS PRODUCT COVERAGE

The gap in formal provision for retirement outlines above does not seem to be made up by provision through private, individual retirement provision. The figure

[7] There are a total of 123 funds, of which 94 are active and only 13 are defined benefit.

below shows that take up of individual products with a long-term savings component, such as retirement annuities or long-term life insurance policies is low[8]

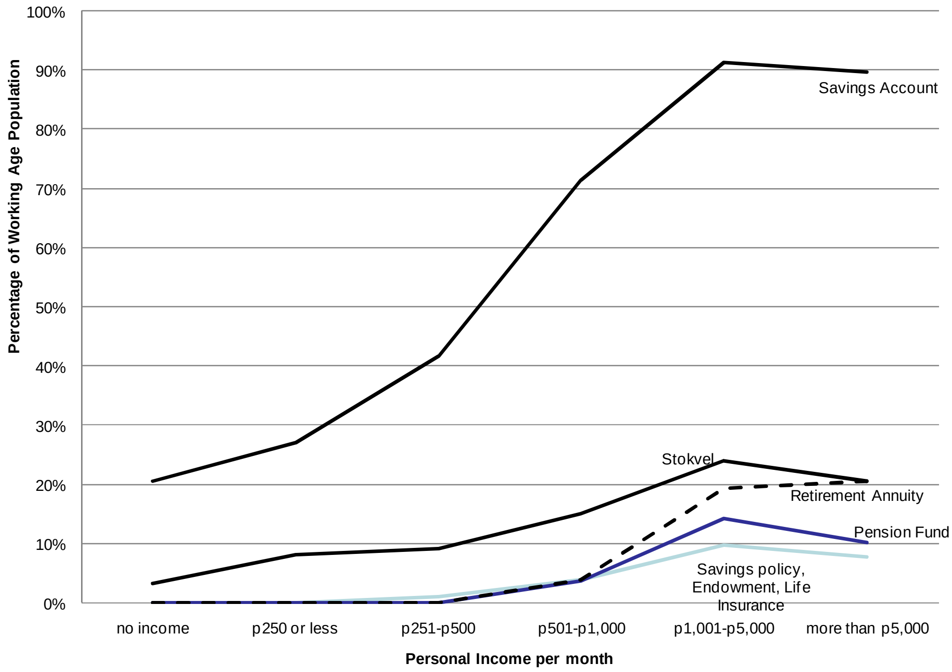

Figure 6: Percentage of working age population using different financial services
Source: Finscope 2004

3.5. OTHER PROVISION FOR OLD-AGE

Evidence from primary research suggests that people utilise other forms of provision to supplement the OAP grant in retirement. Survey work indicates that

[8] A savings account is anyone with a bank account, Stokvel refers to an informal group savings account, a retirement annuity is an individual, tax efficient vehicle offered by insurance companies and savings policy/life endowment and life insurance refer to individual long-term insurance policies with a high savings element.

investment in housing is the most commonly cited form of long-term investment. The housing asset can be added to incrementally, and this seems to be a common occurrence in Botswana, with 90% of pensioners surveyed indicated that they lived in a self-built structure. A housing asset is attractive as it can be used immediately once an initial structure has been completed. In addition to the social value a house carries, it can be rented out to provide an income, or it can be used to house a small business. Housing is also attractive in that it can be passed on as inheritance. In fact,.

Another form of provision for old-age mentioned by survey participants was investment in or start-up of a small business in old-age (such as a kiosk or cattle post). Some respondents indicated that they would rely on family support, particularly remittances received from children. A few also indicated that they would try to carry on working into old-age or accumulate cattle as a store of value for their retirement.

3.6. SUMMARY

In conclusion, most working age people are likely to have to rely on the old age pension as their primary source of income in old age. There is minimal take up of formal financial products and instruments, although some form of saving does takes place through various channels such as housing and education.

4. GRATUITY/SEVERANCE SCHEME

This section starts with a detailed description of the gratuity/severance scheme followed by insights about how the payout is used. It then turns to compliance and other issues related to the scheme before ending with a financial summary which outlines the costs of the scheme and an estimate of the annual amount of funds generated and paid out.

4.1. DESCRIPTION OF THE SCHEME

The gratuity/severance benefit started purely as a severance benefit to tide workers over for periods while they are in between jobs, i.e. where they have lost a job for whatever reason and currently unemployed. This meant that the benefit was paid on termination of employment. (Henceforth in the document the benefit is referred to as the gratuity scheme.)

However, problems and complaints arose when the benefit was not paid, for instance if the employer was in financial difficulty. Partly as a result of this, the Employment Act of 1992 made the gratuity payable every five years, irrespective of whether employment has been terminated or not. Termination in this context covers resignation, retrenchment and retirement.

In the first five years of service, the gratuity is set at a level corresponding to one day of pay for every month worked (with no pro-rating for termination before the end of the five year period). This equates to approximately three times the employees monthly salary at the end of the five-year period.

For every subsequent five years of service the benefit accrues at a rate of two days for each month worked and the benefit is pro-rated on termination.

In terms of the Employment Act, the gratuity scheme is meant to apply to any continuous employment relationship, including informal work, though it can be waived if a pension or provident scheme is provided to workers instead.

4.2. USAGE OF THE BENEFIT

Employees receiving a gratuity instead of a pension, would need to manage gratuity payments themselves if they so chose to provide for their old age. There is no centralised collection of data on the gratuity/severance scheme, and there is no obligation on employers to report these payments (except as a part of aggregated taxable income), or for employees to disclose what they used their gratuity on. As a result there are no records of the numbers of employees receiving this benefit or the total amounts paid out, and this study therefore relied on survey information and consultations to estimate these figures. The surveys conducted investigated the uses to which employees put their gratuity payments and their willingness to allocate these payments into long-term savings.

Of the 58 employees surveyed who received gratuity, 60% used it for consumption purposes, dominated by expenditure on durable goods and day-to-day expenses. 60% of respondents used it for repayment of loans, mainly in respect of loans taken to purchase household and durable goods and debts from money lenders[9]. 41% invested the gratuity in housing, largely building a new house or adding rooms to an existing house[10]. A smaller proportion of gratuity was invested in businesses (for either start-up or expansion) or used for the education of either the recipient or their children.

Use of Gratuity	No. respondents confirming use of gratuity	As a percentage of total respondents
Consumption	35	60
Loan Repayment	35	60
Housing	24	41
Education	4	7
Cattle	3	5
Business	10	17

Table 2: Uses of gratuity by employees[11](The percentages add up to over 100% because a respondent can use gratuity for multiple purposes.)
Source: Employee Survey, 2008- 58 respondents

None of the employees reported investing the gratuity in financial assets such as fixed deposits, bonds and equities. There is therefore some evidence that the

[9] Discussions with stakeholders revealed that some employees contracted new debt in anticipation of receiving gratuity.
[10] This is consistent with our findings that a large proportion of elderly live in self-built and owned houses.
[11] Source: Department of Labour and Social Security, Annual Report 2006

gratuity is not channeled towards long-term savings for old age, except through the formation of a housing asset.

4.3. COMPLIANCE PROBLEMS WITH THE SCHEME

In consultations with private sector and unions, it was suggested that a major problem with the gratuity/severance payment system is the poor level of compliance, particularly by businesses in the textile, wholesale, retail and services sectors[12]. This non-compliance can take the form of unfair dismissal just before payment is due as well as outright non-payment of the benefit due[13]. Table 3 shows that non-payment of the benefit is the fifth highest source of trade disputes in Botswana. It also shows unfair termination as the fourth highest source of disputes, with many of these instances reported as termination just before payment is due.

Trade Dispute	Number	% of total
Failure to pay notice	2,533	24.1
Failure to pay wages	2,340	22.3
Failure to pay leave	1,179	11.2
Unfair termination	1,140	10.8
Non-payment of severance	498	4.7
Other	2,821	26.8
Total	10,511	100.0

Table 3: Trade Disputes[14]
Source: Department of Labour and Social Security, Annual Report 2006

4.4. OTHER PROBLEMS

While non-compliance is the most common problem, there are several other operational problems that can occur in the implementation of the gratuity scheme. Gratuity is paid every five years and for this to be effectively done firms need to make provisions in their accounts. However, firms are not obliged under the

[12] It is also believed from consultations that compliance is very low in respect of informal, domestic service and subsistence agriculture sectors.
[13] Early dismissal is a strategy used by employers to save themselves the cost of paying gratuity. Plans are underway to amend the employment legislation to pro-rate the benefit on dismissal before the end of the five year period.
[14] Source: Department of Labour and Social Security, Annual Report 2006

existing law to make mandatory provisions for future gratuity payments in their accounts. Most employers do not make any provisions for gratuity payments before they are due and hence wait for the gratuity to fall due and then source money to pay the amount as a direct expense.

As a result of this, smaller firms may face cash flow constraints due to lump sum gratuity payments falling due. Non-accrual by a firm also means that no investment returns can be earned on the accruing entitlements. No tax benefit or relief is earned by the employer for providing the gratuity other than when actual payments are made (as they are a tax-deductible expense for the firm, like salaries).

Overall, the gratuity scheme (with the exception of the severance component) has little justification from a social security point of view. The gratuity component does not meet needs that social security benefits typically aim for, such as those arising from a change in circumstances with negative financial repercussions, for example unemployment, ill-health or retirement.

4.5. COSTS OF THE GRATUITY

Costs of the gratuity in practice vary widely by employer. For instance, new firms will not have to pay any gratuity until the first five year period has expired. Non-compliant, or partially-complying employers may pay very little. Consultations with private sector indicated that the average employer pays approximately 5% of annual payroll on gratuity. Employers with high staff turnover will probably pay less than 5% on average per year on gratuity, as many of their employees will leave before 5 years of service. The higher the proportion of long-serving staff on the payroll the higher the amount the company will be obliged to pay, up to a maximum level of 10% of salary. This is represented illustratively by the graph in Figure 8 below.

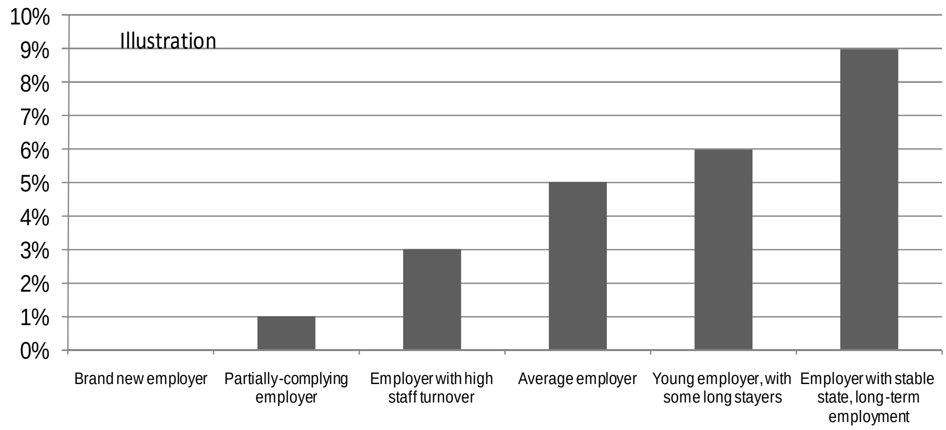

Figure 7: Illustration of the range of possible costs to employers of gratuity payments, expressed as an annual percentage of payroll
Sources: Registrar of Pension Funds Annual Report, Genesis estimates

4.6. SUMS GENERATED BY THE GRATUITY

In total the amounts paid out from the gratuity system are significant, and are estimated to be in excess of P100m per year (Calculation of the estimate is given in the table below).

	Amount
Formal workers not in pension scheme	192,000
Average salary *	P1,000 pm
Payroll	P2,304m pa
Total gratuity amount (approx 5% of payroll)	P115m pa
* Assumed at the low end of industrial class wages in public sector: P800-P3400pm	

Table 4: Estimated amount of gratuity paid in the economy
Source: CSO Stats Brief, 2007; Genesis estimates

This can be compared to an estimated total payment of P237m in respect of the OAP per year, and P717m in respect of private pensions.[15]

4.7. SUMMARY

The gratuity system is an unfunded benefit that is only available to employees who do not have access to pension or provident funds. In theory, at least, it is compulsory and therefore an existing obligation for the employer. While the gratuity generates substantial sums, these amounts are typically not paid, except in the case of severance, in response to any social security need. The payout is generally applied to consumption rather than to long-term saving or towards provision for old age.

[15] OAP payments estimated as P220 x 12 x 90 000; private pensions as P5434 x 12 x 11 000

5. PROSPECTS FOR A BROAD-BASED PENSION SCHEME

This section presents evidence that points towards the need for a national pension arrangement. It considers four underlying factors that contribute to this need and which can be leveraged to create the opportunity for a broad-based pension scheme. These are the following:

- Increasing numbers of elderly with inadequate provision through current schemes
- Willingness of employers and employees to contribute more towards provision for old age
- Utilisation of gratuity payments towards pension contributions
- Financial viability of a broad-based pension arrangement

These are factors where evidence has been gathered to support the implementation of a broad-based pension arrangement in principle. Section 6 raises further considerations to be taken account when turning this arrangement from principle into practice.

5.1. INCREASING NUMBER AND PROPORTION OF ELDERLY

The absolute number of the population over the age of 65 is expected to increase, from approximately 63,000 at present to 114,000 in 2026. As a proportion of the total population it is also expected to increase, rising from 7.1% of the adult population at present to 8.6% of the adult population.

	2006	2016	2026
Total age 65+	63,000	83,000	114,000
Total adult population	894,000	1,102,000	1,332,000
% of adult population age 65+	7.1%	7.5%	8.6%
Estimated elderly people without access to private pension	41,000	54,000	74,000

Table 5: Projected elderly and working age populations

Source: CSO, 2005, Population Projections for Botswana 2001-2031; Genesis estimates

If current rates of participation in occupational schemes and reliance on the OAP continue, many of these elderly people in the future will experience the same declining incomes and risk of poverty currently experienced by the elderly in Botswana.

This clearly indicates that there is a need to engage with the current working population and create channels of saving for them in order for them to be able to retire without the risk of sliding into poverty.

5.2. EXPRESSED WILLINGNESS TO CONTRIBUTE MORE TOWARDS OLD-AGE PROVISION

A question on willingness to divert current gratuity payments to pension schemes was put to both employees and employers. The elderly in retirement were also asked whether they would have been able to save more for retirement if they had been given another chance.

5.2.1. FIRMS/EMPLOYERS VIEW

Two thirds of the 40 employers surveyed recognize that their employees are probably worse off in retirement than in working age. Approximately 90% of the employers are supportive of directing gratuity payments into a pension scheme, and an overwhelming majority of the surveyed employers were supportive of the introduction of a national compulsory contributory pension scheme

In terms of contribution, the surveyed employers expressed their willingness to contribute on average a total of 10-15% of the employees' basic pay towards the pension scheme.

5.2.2. EMPLOYEES VIEWS

Among the 80 respondents eligible to receive gratuity under the EA, 86% were willing to direct at least some of their gratuity payments towards old age savings. The employees further reported that they would be willing to direct as much as 50% of the gratuity payments into a pension arrangement if one was made available and accessible to them.

In terms of their own contribution to the pension scheme, the employees reported that they will be willing to contribute on average 6-7% of their basic pay towards the pension scheme. In consultations with union umbrella bodies, a similar employee contribution level was expressed by union leaders.

With regard to the potential for introducing a compulsory national contributory pension scheme, 84% of the employees were supportive of this view. Several employees advocated government financial support for the creation of a mandatory pension scheme and introduction of new pension products.

5.2.3. PENSIONERS VIEWS

While they would be unable to benefit from such a scheme, 93% of the surveyed pensioners supported the introduction of a compulsory contributory pension scheme. In addition 86% of the pensioners expressed a wish that they had saved more for retirement and 60% expressed that they would have saved more than they did had a contributory pension arrangement been available.

These retrospective views emphasise the need to enhance savings mechanisms for old age and enable workers to save proactively for their old-age within a pension arrangement.

5.2.4. COST IMPLICATIONS

In the table below, we summarise the suggested total contribution rates employers and employees expressed they were willing to make during consultations. These estimated contributions are shown in Pula terms based on three low-income salary points.

	% of salary	Salary (Pula per month) 800	2000	3000
Employee contribution	6-7%	52	130	195
Employer contribution	10-15%	100	250	375
Total contribution		152	380	570

Table 6: Prospective contribution rates and Pula amounts

Source: Consultations with unions and businesses; Employer survey; Genesis estimates

For comparison, Table 7 below shows the current average levels of contribution in percentage and Pula terms in the pensions environment. The percentages of payroll suggested in Table 6 above are similar to those currently in place for pensionable workers, however, due to the smaller contributions, the Pula amounts can be substantially lower. The implications of low contributions in Pula terms on financial viability is taken up in Section 6.

	Range: % of payroll	Pula pm
Employer contribution	8-16%	637
Employee contribution	4-7%	176
Total contribution	15.5% on average	813

Table 7: Current average contribution rates and Pula amounts

Source: Registrar of Pension Funds Annual Report for 2006; Genesis estimates

5.2.5. SUMMARY

While the contributory percentages given above are derived from questions about a hypothetical pension arrangement, and percentages expressed here may not be strictly translatable into reality, it is relevant to note strong support and willingness to contribute across the spectrum of stakeholders.

5.3. ABILITY TO OFFSET COST OF PENSION CONTRIBUTIONS BY DIVERTING GRATUITY AMOUNTS

Compulsory contributions can have the effect of increasing overall labour costs for employers, and therefore increasing unemployment, or at least the facilitating the informalisation of employment. This is particularly true for competitive and price-sensitive sectors where labour costs are a high proportion of total cost, retail, wholesale, services, textiles for example, or for industries under international pressure to keep costs low in order to remain competitive like the textile industry. It is also particularly true in the short term, and less so in the medium to long term.[16]

In a country where unemployment is already a problem, compulsory savings which increase labour costs can be less compelling. While employers surveyed expressed willingness to contribute 10-15% of basic pay towards a pension arrangement, the question was asked hypothetically and the actual willingness to contribute may be somewhat weaker when the time comes to actually make the payments.

To offset this effect, it is proposed that the estimated 5% of payroll currently being paid by employers as gratuity could be redirected to a pension arrangement, and the contribution level built up over time to 10%. This will moderate the impact on employer's payroll and reduce the likelihood of the employer turning to the informal market in the short run.

5.4. FINANCIAL VIABILITY OF A BROAD-BASED SCHEME

Employers are willing to contribute a percentage of salary on a sustained basis towards a pension fund. The research highlights the gap between government provision and requirements in old age. Using the contribution margins derived from the research as a starting point, some models have been constructed to test the feasibility of a pension plan based on these contribution levels.

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[16] Theory and empirical evidence suggests that compulsory savings have relatively little impact on total labour costs in the medium to long-term. The impact in the short-term may initially increase labour costs for employers by adding a compulsory contribution to existing take home salary. However, in the medium term, over a few rounds of wage negotiation it is the *total cost to company* of the employee (the take home pay plus the contributions) which returns to an equilibrium level (ILO, 1996). Overall, the cost to company returns to its previous level, and ultimately most of the real cost of the contributions is born by the employee. However, it can still be valuable for the employer to be perceived to be contributing to workers' retirement.

Early modeling work based on industry figures suggests that it could be cost-effective to provide a pension of about 50% of salary at retirement to someone earning P800 per month. When added to the state OAP this provides an income in retirement of over two thirds of pre-retirement income. This assumes the employer contributes 10% and the employee 5% of income over working life, with no withdrawals. It also assumes, critically, that total administration costs in the system are being kept to P20 per member per month, and total investment management costs can be held to 1%. These are at the low end of the charges currently applied by the retirement fund industry in Botswana. It will be challenging to serve low-income individuals with charges at this level but with scale this could be feasible.

5.4.1. ILLUSTRATIVE MODEL

The illustrative model can be depicted visually as in the diagram below. The solid line represents real total income assuming receipt of a gratuity over the working life according to current rules and assuming uninterrupted lifetime employment. Income is assumed to start at P800 per month and increase modestly above inflation over the lifetime. At age 65, income falls significantly to the level of the OAP.

The dotted line illustrates an income profile over the lifetime assuming the individual contributes 5% of their salary to a pension scheme, with the employer contributing 10%. These contributions are paid over the whole working life, and net of the charges described above, roll up in a fund at a rate of return above the rate of inflation. Critically, the model assumes no early withdrawal of funds before retirement. A third of this fund is then assumed to be paid out as a lump sum and the rest converted at current market rates into an annuity with a fixed escalation. [17]

[17] Relaxing the assumption of uninterrupted lifetime employment will reduce the payments provided by both the gratuity and pension scheme, but will not change the relative attractiveness of each.

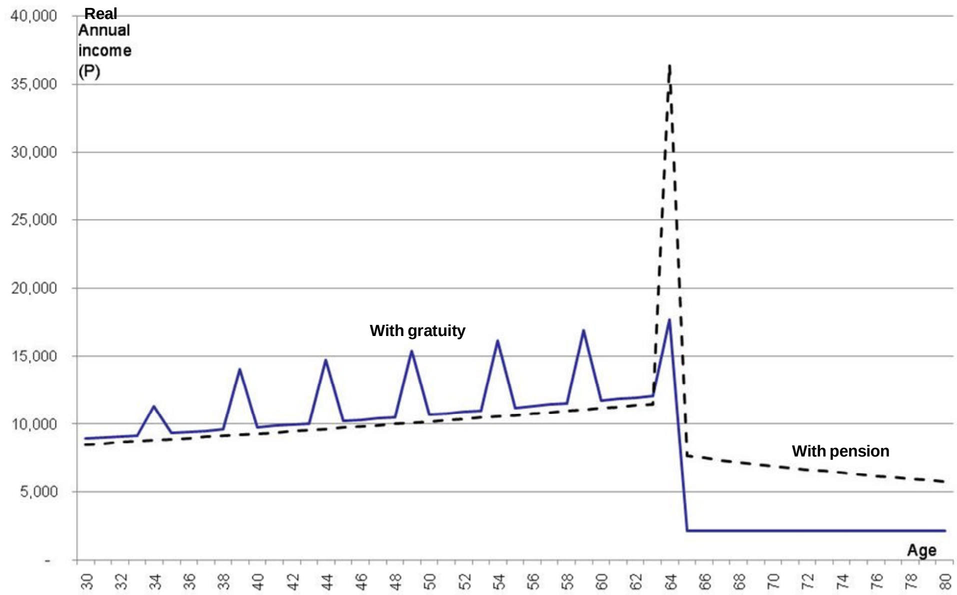

Figure 8:Projected lifetime incomes assuming gratuity and pension

Source : Genesis illustrative model

5.4.2. SENSITIVITY OF PENSION TO ADMINISTRATIVE COSTS AND CONTRIBUTION RATES

Two critical elements of the model are the levels of employer contributions and administrative costs. A decrease in employer contribution from 10% to 5%, or an increase in administrative costs from P20 to P40 would result in a significant decrease in the payout to pensioners, making the pension plan a less attractive option than other methods of providing for old age. This decrease is in the order of 30-40% for individuals on a P800 per month salary. A combination of the two effects could result in an even higher drop.

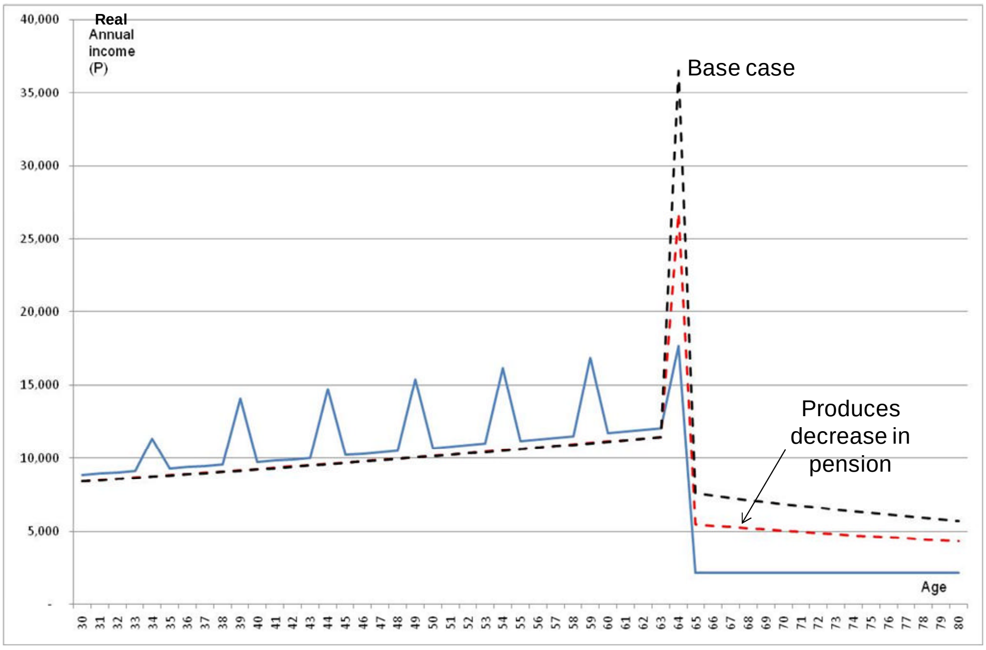

Figure 9: Projected lifetime incomes showing 1) gratuity, 2) base case pension and, 3) decreased level of pension assuming higher costs or lower contribution

Source: Genesis illustrative model

Administration costs tend to be fixed relative to the size of the contribution being made into a pension scheme. Many of the costs are determined by the number of people on the scheme, rather than the size of the contributions they make. Examples of scale dependant costs include distribution, client communication, contribution collection, benefit payouts and the costs of handling queries.

Unfortunately this means that costs make up a higher proportion of the contributions of low-income individuals. This means that the level of the expected benefit is particularly sensitive to the level of charges. The illustrative modelling shows how small changes in administration costs relative to contributions can significantly reduce benefits, highlighting the need to control costs in a broad-based pension scheme.

5.5. SUMMARY

The projected increasing numbers of elderly and the drop in income they will face on retirement and the expressed willingness of key stakeholders to provide more for old-age and contribute to a pension arrangement if one is made available suggest underlying support for a broad-based pension arrangement. This is further strengthened by the possibility of diverting gratuity payments into such an arrangement, making it a relatively cost-effective transition for employers. Finally, preliminary modelling suggests that such an arrangement could be financially feasible if costs are controlled.

6. INSTITUTIONAL OPTIONS AND CONSIDERATIONS

It is possible, in principle, to make pension cover in Botswana more broad-based, starting with formally employed, low-income workers. This could mean that up to 200,000 workers transfer from gratuity to pensionable status. The challenge is to create an institutional framework, made up of a combination of public, private and regulatory entities, to deliver such an expansion cost-effectively. Such a framework will not be designed on a blank slate. Rather, the starting point is an existing environment of partial pension coverage through a set of occupational schemes and universal state provision of a low level poverty relief benefit.

This section does not attempt to present final views on the institutional framework for delivery but makes suggestions where possible and outlines considerations for making the choices involved. This is an extraordinarily complex area involving administrative, ethical and economic choices, and is covered briefly here as an introduction to these issues. The section proceeds by outlining some possible coverage and benefit models and the pros and cons implied by each. It then presents the value chain of activities that the institutional framework will have to deliver and suggests some models for these, involving both public and private sector participation. Finally the section outlines a number of regulatory and governance principles that will have to be in place to monitor and assess the interaction of parties involved in delivery of broad-based pensions.

6.1. COVERAGE OPTIONS

There appear to be four key coverage options available to Botswana to achieve this goal of more broad-based access, varying according to the type of compulsory involvement in the scheme for members.

1. First is compulsory membership of the current occupational schemes, but extended to all formally employed workers. This approach would not necessarily ensure low costs, as a fragmented set of schemes will not be able to achieve the economies of scale required to drive down administration costs. Furthermore, it would require measures to ensure that workers could transfer easily from fund to fund as they change jobs. Mandated membership may also create additional obligations on the regulator to supervise the governance and operations of the schemes more closely.

2. A second option is a centralised, compulsory scheme with contributions made by all workers as a percentage of income. It would only be compulsory for workers earning above a threshold level (above a minimum wage benchmark) and up to a cap. Members earning more than the cap would be free to top-up pension provision in respect of income above the cap through other schemes or products. While achieving scale economies, this approach would probably have the consequence of removing many members from the current occupational pension fund industry. It would also create duplicate costs for members who are both part of the centralised fund and have some additional top-up provision.

3. A third option is as 2 above, but with the ability to opt out of the centralised scheme into a scheme provided by an accredited entity. This would mean that people opting out would have all their pension provision provided through one entity and so avoid duplicating costs. It would however mean that the centralised scheme would be smaller than otherwise, with potential negative cost implications from losing economies of scale. It would also mean that the scheme would lose the ability to ensure that higher income contributors subsidise some of the costs in respect of lower income contributors[18].

4. A final option is to allow voluntary participation in a centralised scheme, potentially with incentives from the public purse, such as matching contributions from the treasury for those who contribute, or a direct, fixed subsidy for members. However, given low take-up in the current voluntary environment it is unlikely that take-up would be much higher. Incentives would also obviously constitute an ongoing cost to the fiscus which would have to be weighed up carefully against other uses of public money.

From brief discussion of these options it would seem that options 2 and 3 are the most promising for the Botswana environment. They are flexible, in that they allow inclusion of low-income workers in a relatively low cost system, but can also integrate well with higher levels of top-up participation for higher-income workers.

[18] This would be achieved by allocating a percentage of contributions to covering administration costs. Higher income individuals would therefore contribute more to administration than lower income contributors even though the actual expenses associated with administering them are likely to be very similar.

6.2. BENEFIT STRUCTURE OPTIONS

A choice of benefit structure is firstly between that of a defined contribution and a defined benefit system. In Botswana there has been a strong move (as in the rest of the world) towards defined contribution plans and these now dominate the market including, significantly, the government employees fund. While defined benefit structures should not be dismissed out of hand, this section concentrates primarily on defined contribution structures. It outlines some of the relative advantages and disadvantages and how the key disadvantages of defined contribution arrangements can be overcome. The section proceeds to discuss how investment, benefit payments and early withdrawals of funds could be handled.

6.2.1. DEFINED CONTRIBUTION RELATIVE TO DEFINED BENEFIT

The key advantage of defined contribution relative to defined benefit is the certainty of cost to employer and employee, as the contribution amount is set and the level of benefits depends on how they accumulate (rather than the benefits being set and the contributions depending on what level is required to generate them). The downside of this arrangement is that the member is exposed to the risk of the accumulated fund being insufficient to provide for sufficient benefits in retirement. This could arise either because contributions have proved to be inadequate to produce the sorts of benefits expected, or because market movements have reduced the value of the fund below that which was originally anticipated.

Under a defined contribution structure, since benefits are not guaranteed, it is essential to make sure that projections are performed regularly to estimate likely benefits that the scheme would generate. It is also important that contribution levels are pitched at a level to ensure that members' benefit expectations are met and that members are aware of their projected benefits so they can increase contributions if these are expected to be insufficient.

6.2.2. LIFESTAGE INVESTING

Many defined contribution schemes offer members a choice of investments for their funds. As well as being confusing for people without sufficient financial literacy, this can increase actual costs for the administrator, and so it is likely to be simpler and more cost-effective to adopt a lifestyle investment approach. By this is meant an investment strategy where younger people's investments are automatically heavily weighted towards higher risk and return assets such as equities as they can benefit from the additional returns, and the higher volatility of the investments is unlikely to be a problem as they are less likely to draw on the fund in the short-term. As people age, their portfolio is shifted to lower risk, more liquid assets whose values are less likely to be volatile as the member approaches retirement when the fund will have to be converted into an income stream. While such an automatic approach is useful to apply to individuals without the financial literacy to make these choices themselves, it may not be appropriate for every individual's savings preferences.

6.2.3. INCOME BENEFITS

The objective of the scheme is to provide income security in old age and it is therefore important that income benefits are paid rather than lump sums. Payment of income streams below a certain amount (currently about P400 per month in the private sector) becomes difficult to achieve in a cost-effective manner, as the expenses of payment and administration then make up a larger proportion of the payment. In this case it could be feasible to pay benefits in larger but less frequent tranches, for example annually.

Annuitisation at retirement is required for defined contribution funds to be converted into guaranteed lifetime income streams. This could be done by purchasing annuities from private providers. However, these can be expensive, particularly because of the risk the provider takes of individuals living longer than expected. In addition the price of annuities can vary significantly with changes in the yield curve and so people retiring at slightly different times with similar lump sums could find themselves with very different income streams. Finally, the way annuities are priced means that rich, long-lived annuity recipients tend to be subsidised by poor, short-lived recipients, which is undesirable from a social equity point of view. Annuitisation, by the state, at a set of smoothed rates may be a solution to these problems, though this has not been a widely adopted approach internationally. Deeper and more competitive annuity markets, with plenty of information to price longevity risk and plenty assets to match the annuity cash flows (i.e. long-dated government bonds) could make for a better approach.

6.2.4. PRESERVATION

There should be some limits on accessibility to the funds built up before retirement, with access given only in cases of genuine life emergency, such as involuntary unemployment, disability or death of the member. If this is not ensured, it is likely that members will withdraw funds in cash when they leave a job and subsequently undermine the whole intention of retirement provision. There needs to be sensitivity to the fact that members of the scheme will be relatively poor and vulnerable to the financial impact of life shocks, and it makes no sense for them to build up an asset they are unable to access to mitigate such shocks.

6.3. INSTITUTIONAL VALUE CHAIN

Irrespective of the coverage and benefit structure choices, the institutional framework needs to fulfil a set of basic functions. This can be expressed as a 'value chain' of activities that the whole system has to perform. In the next section we outline the conditions that have to be met for these functions to be performed well, and then which players exist in the environment and how they can work together to perform these tasks.

- *Public interface function*. This involves educating members and potential members about how the scheme works, its rules, etc. It also involves administering enrolment on the scheme, handling enquiries, complaints, and ongoing communication about entitlements.

- *Administration of accounts*. This involves updating changes in the entitlements of members, updating and tracking personal information about members and beneficiaries and contact details, and managing the tracking of choices in the scheme.

- *Administration of contributions*. Collection of contributions, ensuring compliance with mandated membership, tracking contributions so that corresponding benefit entitlements can be determined, passing money to the investing institutions.

- *Investment*. This involves setting the investment policy, usually to maximise returns subject to meeting certain risk management requirements. (There may also be some social investment objectives to take into account.) Procedures, governance and auditing requirements need to be developed and followed, as well as regular investment benchmarking, monitoring and reporting. Quantification of any liabilities of the scheme will also have to be done and compared to the assets held.

- *Payment of benefits*. This entails quantification, authorisation and disbursement (either directly or through other institutions) of benefits to members. Benefits may be paid electronically or in cash. They may be in the form of income streams or paid out in lump sums or regular tranches for smaller sums.

In the subsequent sections we will consider what objectives the fulfilment of these functions needs to achieve and how this can be done given the current private and public sector institutional infrastructure and expertise in Botswana.

6.4. OBJECTIVES FOR THE INSTITUTIONAL FRAMEWORK

Whatever mixture of public and private participation is selected needs to meet the following criteria in respect of performing the above functions.

- It needs to do these at low cost. This can be achieved by optimally combining the economies of scale achievable with a centralised scheme and the efficiencies generated by competition between private sector entities. It is also important to minimise costs to government and ensure that spending is good use of public money. Subsidies could be limited to up-front costs to set up infrastructure, rather than ongoing contributions.
- The framework should use available public and private sector expertise, infrastructure and institutions to minimise additional expenditure and also to reduce the implementation risk of setting up new capabilities. Private sector players include the current pension fund administrators and fund managers. Public sector players include the Botswana Unified Revenue Service (currently collecting tax from employer payrolls), the Department of Social Benefits (currently paying the universal old age pension), the administration behind the OMANG national identity cards.
- The service and administration provided needs to be quick, simple and responsive, in terms of updating entitlements and communicating with members and employers.
- It has to ensure portability, so that employees can move between jobs without penalty on their retirement funds.
- This system must be structured to produce high compliance. As well as being simple it must be enforceable and have government sanction behind it.

These objectives can conflict and trade-offs will need to be made, for instance, a more responsive administration system may be more costly to set up and run.

However, the models for achieving these objectives involve a mixture of state and private provision, with the state tending to bring enforcement, scale and reach to low-income individuals. In addition to bringing existing systems and expertise geared to providing occupational linked benefits, the private sector can bring beneficial cost saving dynamics in two main ways:

- By competing to provide administration and fund management services based on a competitive wholesale tender. (It tends to be undesirable for the private sector players to be allowed to compete at a retail level for this business as costs are then driven up by their marketing expenses, as was found to happen in Chile.)
- By contracting to provide services to a government scheme on a public-private partnership basis.

6.5. PRELIMINARY RECOMMENDATIONS ON INSTITUTIONAL OPTIONS

Given the relative expertise and capacity of the public and private sector in Botswana in the provision of occupational benefits it makes sense for many of the value chain functions identified to be outsourced to the private sector. These will probably include the public interface function, administration, and investment of contributions. These roles could be most cost-effectively outsourced through a wholesale tender or auction process with a limited number of players involved to ensure sufficient economies of scale are achieved.

Public sector entities like the Department of Social Benefits have experience in delivering small, regular, universal payments to low-income people and so could be usefully involved in the benefit payment aspect of delivery. Similarly, the Botswana Unified Revenues Service has experience in collecting tax in the form of payroll deductions from employers which is likely to be the most cost-effective way of collecting and tracking contributions before the information and money is then passed on to the administrators. It is important to note that the broad-based system will entail the inclusion of workers who do not currently pay income tax and will therefore mean the addition of many new records to the tax system.

6.6. REGULATION AND GOVERNANCE

Regulation and governance requirements become particularly important if it is made compulsory for segments of the population to use services provided by the combination of state and private providers. This section highlights some of the broad principles that should apply to this.

Final responsibility for the working of the scheme should rest with a board of appropriately selected individuals. This board should be drawn from the set of stakeholders, including government departments, elected representatives, groups like trade unions and employer associations, as well as independent experts. The executive of the scheme will be accountable to this board. For all of these individuals there should be requirements that they are fit and proper, not beholden to conflicts of interest, have limited tenure and are nominated and appointed in a process that allows for review of decisions.

Regulatory requirements, such as accreditation rules, on outsource participants in the scheme should apply on a level playing field basis to public and private players to ensure that the whole value chain is delivered effectively.

6.7. IMPLEMENTATION

The process for the construction of this scheme involves several considerations.

In order to spread the impact of the change it is proposed that the new scheme be phased in on a 'next gratuity is the last' basis, so that from a certain date individuals will receive their next gratuity and thereafter be moved into the pension scheme. This will mean that the impact of the change on low-income workers will be spread over a five year period.

It is important to note that older workers may only have a few years to contribute to the scheme before they retire and so will not have built up significant retirement funds. Whatever the size of these funds, they are however still likely to be larger than provision they would make otherwise and may be paid out cost-effectively in tranches rather than income streams.

The design of the system should allow for possible later expansion, for instance to universalise the scheme to include self-employed and potentially informally employed individuals. It is most feasible to start by targeting formally employed workers to prove and bed down the scheme before extending it to members who are more difficult and expensive to include. The scheme could also ultimately be used to provide access to other valuable social security benefits, for instance, unemployment insurance, medical cover, workers compensation, death and disability benefits.

7. CONCLUSION

There are significant positive factors in favour of implementing a broad-based pension scheme in Botswana.

- A wide and deep gap in provision exists: up to 192,000 formally employed workers are without private pension arrangements.
- There is widespread recognition and support for further long-term savings.
- It is possible to use the money currently paid out in gratuity, to offset the contribution burden for employers.
- Much of the expertise and infrastructure exists in Botswana to provide these benefits to low-income formal sector workers cost-effectively.

There are also, however, several challenges that need to be addressed in the process of creating a broad-based national pension fund.

- Firstly, it is critical to keep administrative costs low. It will be important to include large numbers of people in the broad-based scheme in order to spread costs as broadly as possible.
- Measures to enforce compliance will have to be carefully crafted given that enforcement is difficult especially in the poorer section of the formal sector. Given the state of current non-compliance with the gratuity payment, this is an issue that needs to be deeply examined and studied. Collection through the tax system could help to alleviate of this problem.
- In step with non-compliance is the challenge of preventing employers from reacting to the pension fund by reducing their demand for labour, or turning to the informal labour market. With already high unemployment and a large informal sector, this would be an undesirable outcome of the pension fund, and steps must be taken to mitigate this effect, by working with employers to ensure a smooth transition and not too much of a strain on employers, especially on smaller sized organizations. Building up the contribution rate from a starting level of 5% in respect of the current gratuity scheme employees is one way of achieving this[19].

[19] In this regard, it will be important to ensure that employers do not reduce their contributions in respect of currently pensionable employees to 5% from their current average level of 10%.

8. RECOMMENDATIONS

With the objective of improving retirement provision for low-income workers, the following recommendations for the Botswana government and FinMark Trust flow from the conclusions above:

1. Overall, look to redirect gratuity payments for low-income, formally employed workers into a pension arrangement
2. Build political support for such a move from the unions and employers
3. Review disclosure and costs of provision of administration and investment management services in the private retirement fund industry
4. Review the administration and delivery costs of providing the state benefits such as the OAP
5. Begin dialogue with key public sector players likely to be involved in such a pension arrangement, particularly Botswana Revenue Services
6. Use results of the reviews and the dialogue to feed into a substantive discussion about the optimal institutional structure for this pension arrangement, combining the expertise and systems of the private sector and public sector to provide the most cost-effective system. This will involve making decisions on benefit structure issues as well as the design of the best institutional framework for cost-effective delivery.

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- South African Revenue Service. *Shaping social security for South Africa: Early perspectives on the operational design.* Working draft. 31 August 2007.

MEETING LIST

WHO	POSITION	ORGANISATION
Mr M B Palai	Permanent Secretary	Ministry of Labour
Mr Claude Mojafi; Ms Sissy Seemule	Commissioner of Labour and Social Security; Deputy Commissioner of Labour	Ministry of Labour and Home Affairs,
Mr D Gaseisiwe, Ms Nancy Diphupu, Mr Stanley Makosha	Director of Economic Affairs (Employment and Manpower Planning)	Employment Policy Unit in the Ministry of Finance
Ms K.O. Mogotsi, **Ms. Eunice Thupeng**	Commissioner of Social Benefits	Department of Social Benefits
Ms Elaina Gonsalves, **Mr Wilbrod Eluru,** **Mr Dineo Khame**	Director, Insurance and Pensions	Ministry of Finance and Development Planning
Mr Simon Ipe, Mr Seagiso Ramatshaba	COO, Portfolio Manager	Botswana Insurance Fund Management (BiFM)
Mr Martinus Seboni	Managing Director	Investec Asset Management
Dr Paul Okwii	Consultant	Department of Social Benefits

Mr Chiliboy Sechele	Business Consultant	Metropolitan Botswana Employee Benefits
Mr Paul Masie	Managing Director	Alex Forbes
Ms Tefo Lionjanga, Mr Lemogelang Ebineng	Business Development and Operations Manager, Senior Employee Benefits Consultant	Glenrand MIB
Mr Phillip van Rooijen, Mr Gaffar Hassan & Mr Kathiresan Subbaraj	Actuary, COO, Assistant General Manager	Botswana Life
Mr Ephraim Letebele, Mr Baboloki Reetsang	CEO/Principal Officer, Director of Benefits Administration & Communications	Botswana Public Officers Pension Fund
Ms Tiny Kgatlwane	Principal Officer	Debswana pension fund
Mr Oteng Yezo	HR	Metsef
Ms Ivy Ramolohlanye	General Manager Corporate Services	Botswana Telecomms
Ms Kamogelo Chisiwa	Head of HR	Standard Chartered Bank
Mr Peter Hikhwa, Mr Alexio Dzidzwa	Senior Account Executive	AON Insurance Brokers and Risk Managers
Mr Johnson Motshwarakgole	National Organizing	Amalgamated Union (industrial class)

	Secretary	
Mr Gadzani Mhotsha	Secretary General	Botswana Federation of Trade Unions
Prof Happy Siphambe	Associate Professor, Head (Department of Economics)	University of Botswana
Mr Hiram Mendis	CEO	Stock Exchange
Mr L Ketlaaleka	Membership Services Manager	BOCCIM
Mr Norman Moleele	Deputy Executive Director	BOCCIM