As the income from the sale of crude oil dwindles, adding to the paucity of funds the government has to allocate to both maintaining and financing new infrastructure, there is urgent need for innovative means of financing infrastructure to bridge the present infrastructure deficit.

The need to diversify from the traditional approach of financing infrastructure projects – public finance- and seek new sources and instruments of finance is now imperative. Perhaps, one veritable means of financing this infrastructure deficit is through the use of contributory pension funds estimated to be about N5trn (five trillion naira).

The Pension Reform Act (“the PFA”)¹ and the Regulation on Investment of Pension Fund Assets (“the Regulation”)² both regulate the investment of pension funds in infrastructure projects in Nigeria.

The PFA and the Regulations provide the modalities, requirements and thresholds for such investments.

Section 86 of the PFA expressly provides for the modes of investment of pension funds subject to the provisions of the guidelines prescribed by the National Pension Commission (“PENCOM”). The modes include but are not limited to Federal government bonds, bills and other securities, state and local Government bonds, bills and other securities, banks deposits and bank securities and real estate developments.

Whilst the PFA makes no express reference to any instrument for investment in infrastructure projects such as roads telecommunications and or power, reference is made to “specialist investment funds and other financial instruments as the Commission may, from time to time approve.”

In addition to the PFA, the Regulations also provide guidelines for the investment of pension funds. The Regulation is more definitive on the form of investment for pension funds infrastructure projects. The Regulations define “Specialist Investment Funds” as infrastructure and Private equity registered by the Securities and Exchange Commission (“SEC”).³

The Regulations prescribe two main routes through which pension funds asset can be invested in infrastructure projects - eligible bonds or debt instruments and infrastructure funds.⁴

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¹ Cap A27, LFN 2014
² 17 December 2012.
³ Section 3.5(c) of the Regulations
⁴ Section 5.2.3 of the Regulations
It should be noted that a draft set of regulations on investment of pension funds has been circulated but yet to be adopted by PENCOM. Once adopted, there will be some slight modifications to the requirements for the investment of pension funds through bonds and infrastructure funds in infrastructure projects. The modifications are as follows:

(a) The requirement that the infrastructure fund have a satisfactory pre-defined liquidity/exit routes, has been extended by the draft regulations. The draft regulation accepts Initial Public Offer, sale to other Private Equity Funds and sale to a strategic Investor as satisfactory exit routes for investors.\(^5\)

(b) The threshold percentage of infrastructure fund to be invested in projects in Nigeria is reduced from 75% in the current regulations to 60% under the draft regulations.

Presently, only 5% of the total pension fund assets can be invested in infrastructure funds and these assets are also held in a single fund.

However, under the proposed draft regulations, a multi-fund structure is established. The multi-fund structure categorizes assets into four tranches based on the overall exposure to variable income instruments. The age of the contributor, work status and the risk exposure elements are also considered in determining which of the tranches the pension funds’ assets will be invested in. The tranches are as follows:\(^6\)

Fund 1 - suitable for contributors who want to invest in high risk projects with higher rewards;

Fund 2 – suitable for contributors aged 49 and below;

Fund 3 – suitable for contributors aged 50 and above; and

Fund 4 – strictly for RSA retirees.

Under the multi-tiered system, a PFA is also allowed to invest a maximum of 5% of the pension fund assets in Fund 1 and Fund 2. While the draft regulations stipulate 0% for Fund 3 and Fund 4.

Though there exists a robust legal and regulatory framework in place for the investment of pension funds in infrastructure projects, there appears to be reluctance by the PFAs to invest in the much needed infrastructure projects that are likely to yield significant profits.

The factors inhibiting the growth of investment of pension funds in infrastructural projects in Nigeria are multi-faceted. While there are factors arising from the lapses in the legal framework and operational environment; there are also other social, economic and political factors that could have impeded the growth of pension funds investment in infrastructure projects in Nigeria.

The reluctance of the PFAs to invest in infrastructure projects may therefore be attributed to the following factors such as:

(a) Bias in the allocation of pension fund assets

The regulatory framework expressly allows for the investment of pension funds in infrastructure. However, there is huge bias in the allocation of pension funds’ assets allowable for investment in infrastructure.

The regulatory framework limits the proportion of pension funds that could be invested in infrastructure to a maximum of 5% of the total pension funds’ assets; compared to other investment allocation, where pension funds can invest up to 80% in Federal government bonds and 35% in Money Market instruments.

(b) Transparency in the Competitive Bidding Process

The Regulations require that for pension fund assets to be invested in infrastructure projects, such project must be awarded to a concessionaire with a good track record; and must be through an open and transparent bidding process conducted in

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\(^5\) Section 5.2.3 (c) of the Draft regulations

\(^6\) Section 7.4 of the Draft regulations

“The safe way to double your money is to fold it over once and put it back in your pocket”

-Frank Hubbard
accordance with the requirements of the Infrastructure Concession and Regulatory Commission Act ("ICRC Act").

Section 4 of the ICRC Act requires that where any project or contract or maintenance of any infrastructure has been approved, the Federal Government Ministry, Agency, Corporation or body concerned shall publish in at least three national newspapers having wide circulation in Nigeria or such other means to invite open competitive bids for such project or contract.

The requirement to publish approved project or contract is limited to three national newspapers in Nigeria. Publication in international newspapers or other international media that could attract foreign prospective concessionaires to participate in the competitive bidding process is not considered.

The ICRC Act sadly, is riddled with loopholes which could significantly impact pension funds invested in infrastructure projects. The loopholes are as follows:

- Section 11 of the ICRC Act stipulates that an agreement made pursuant to the ICRC Act shall not be arbitrarily suspended, stopped, or cancelled except as provided for in the ICRC Act.

However, the ICRC Act does not expressly make provisions for the payment of compensation to the concessionaires in the event that the contract is suspended, stopped or cancelled except as may be provided for in the concession agreement. A case in point is the Lagos-Ibadan expressway concession which was suspended and/or cancelled. If a PFA had invested in such venture, it would be in difficulty in recouping its investment.

- The ICRC Act does not make provisions for the protection of the concessionaires in the event of any change in regulatory framework or polices which might adversely affect the concessionaires.

- The ICRC Act does not make provisions for the event of substitution of concessionaires.

- There is also no clear provision on confirmation by the government to abide by the governing law and dispute resolution mechanisms adopted.

Though the loopholes can be addressed in concession agreements; there would be greater investor confidence if they were addressed in a statute.

(c) Lack of knowledge of the infrastructure sector

An in-depth knowledge of the infrastructure sector is critical to pension fund investment in any country. According to the OECD Survey (2011), “infrastructure investment involves a steep learning curve given the unique nature of each investment.” Most of the PFAs in Nigeria, do not have a deep understanding of the infrastructure sector to conduct comprehensive due diligence and perform risk assessments. This major challenge has constrained investors in making an informed decision as to whether or not to invest in infrastructure sector in Nigeria.

(d) Shortage of data

The PFAs stands in a fiduciary relationship to fund owners. This relationship requires the PFAs to safeguard the security of the funds under their management. In carrying out this duty, adequate information, historical facts and figures are required for proper assessment of the various risks involved in infrastructure transactions. Unfortunately, in Nigeria, the PFAs do not have adequate data to conduct due diligence and access the various risks involved in infrastructure transactions. This has slowed down the active participation of pension funds in infrastructure.

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7 Section 5.2.3 of the Regulations
8 Infrastructure Concession in Nigeria: Challenges and Opportunities – Uche Ohio
9 Legal & Regulatory issues in Infrastructure Finance in Nigeria by Asue Ighodalo 29th October 2008
10 ibid
11 ibid
(e) Lack of effective engagement with stakeholders

Effective engagement of all stakeholders in the infrastructure sector is important to propel pension funds investment in infrastructure in Nigeria. There has been very little engagement and collaboration between the government, pension funds managers, construction companies and suppliers and other institutional investors to identify and discuss the constraints accountable for the slow evolvement of pension funds’ investments in infrastructure; and developing workable solutions.

In other jurisdictions pension funds have proved to be a veritable means of financing infrastructure projects. In Australia, the Australian government has been able through collaboration with the various levels of government, financial, construction and supply industries, and asset owners to identify key constraints to optimal investment in infrastructure assets. A stakeholder forum, known as Infrastructure Australia was set up in 2008 to identify and develop key infrastructure projects in the seven key sectors of the Australian economy. This metamorphosed into the funding of seven of the nine priority projects through the Building Australia Fund.

In the United States, Infrastructure projects such as water -ways, toll roads, bridges, airports, and power plants are carried out by various municipal governments through revenue bonds. Institutional investors took up 25% of the Build America Bonds for infrastructure projects and the bonds enjoyed 35% rebate on interest cost from the US treasury.

In Europe, “the Europe 2020 Project Bond initiative” was set up to provide technical and financial support for companies engaged in large scale infrastructure projects. This initiative was launched to attract institutional investors like pension funds.

Similarly, in Chile and Peru, the government was able to encourage pension funds to invest in infrastructure by designating sponsored programs aimed at risk reduction.

Despite all the constraints mentioned above, a pioneering US$250 million Specialist Private Equity Infrastructure Fund (“ARMHIF”) was recently introduced as the first indigenous, developed and managed Fund in Nigeria.

The investors in the fund include: Asset & Resource Management Company (“ARM”) committing the sum of US$25 million to the ARMHIF; the African Development Bank with a commitment of US$20 million, Nigerian pension funds, including Chevron Contributory Pension Fund Administrator (“CPF”), Progress Trust CPF, and Total E & P CPF. The investment of the Nigerian pension funds in the ARMHIF is the first infrastructure investments made by Nigeria Pension Funds through the private equity routes.

The ARMHIF subscribed for an equity stake in the pioneering Azura-Edo IPP, a US$890 million 450 MW gas –fired power generation plant project being developed in the outskirts of Benin City, Edo State.

Given the reluctance of the PFAs to invest in infrastructure funds, what were the key elements that perhaps made the Azura IPP attractive to the pension fund administrators above?

These elements are as follows:

- The project had full federal guarantee;
- Partial Risk Guarantees (“PRG”) from the World Bank;
- DFI investment of US$292.5million; and

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12 Pension Fund Investment in Infrastructure: Lessons from Australia and Canada – George Indest
14 Ibid
15 Ibid p. 19
16 Ibid
17 Asset & Resource Management Company (ARM) -
18 Ibid.
Certainty in the supply of gas; as the project sponsors were able to agree to a fifteen years gas supply agreement with the Seplat Petroleum Development Company.

Conclusion

Despite the legal and socio-cultural factors inhibiting the growth of investment of pension funds in infrastructure in Nigeria, several lessons can be learnt from the Azura project and the experiences of other countries with developed pension markets to create enabling environment for pension funds investment in infrastructure, in Nigeria.

The following are however recommended:

i. The government should consider issuing bonds (For example, Build Nigeria Bonds) specifically dedicated to infrastructural projects and duly backed by full government guarantee similar to the one issued in the Azura project; and other technical and financial support to attract pension funds;

ii. A structure needs to be developed for incentivizing PFAs particularly tax incentives, and rebates to encourage PFAs to invest in infrastructure projects;

iii. An upward review of the percentage of the total pension funds asset that can be invested in infrastructure should be considered. This will give the PFAs the opportunity to consider investing more in infrastructure;

iv. The ICRC Act should be reviewed to incorporate provisions that will guarantee transparency in the appointment of a concessionaire with good track record.

v. The Infrastructure Concession Regulatory Commission (ICRC) must be independent in conducting a fair, transparent bidding process in the concessioning and award of infrastructure projects;

vi. There is need for increased transparency in the project implementation process and provision of quantitative data to enable pension fund managers conduct due diligence; to access the risks involved in investing in infrastructure. The ICRC should review their project data base by including other vital information that would enable PFAs make an informed decision on investment in infrastructure projects; and

vii. There has to be more active engagement of the government with all stakeholders involved in infrastructural development in the country to generate ideas towards active involvement of pension funds in infrastructure.