



SOMALILAND CIVIL SERVANTS' PENSION LAW



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Abbreviations and Acronyms

CSC	Civil Service Commission
CSSP	Somaliland Civil Service Strengthening Project
DB	Defined Benefit
PAYG	Pay-As-You-Go
GDP	Gross Domestic Product
GoSL	Government of Somaliland
ILO	International Labour Organization
MESAF	Ministry of Employment, Social Affairs and Family
MTO	Money Transfer Operator
OECD	Organization for Economic Cooperation and Development
SNDP	Somaliland National Development Plan I
SNDPII	Somaliland National Development Plan II

1. Introduction and Current Economic Context

1.1 Background

Somaliland's unique development trajectory has evolved over three decades of grassroots peacebuilding and institutional building. The political settlement in Somaliland is founded on a deep-rooted commitment to maintain peace, sometimes at the expense of other priorities. It has been a haven of peace and remained relatively stable since it seceded from the rest of Somalia on 18 May 1991. Somaliland is now about to come out of its post-rehabilitation stage. Democratic governance is gradually taking root. There are now Democratically Elected and Functioning state structures. The House of Representatives, the president, and the local councils have been elected democratically in a free and fair election. In recent years Somaliland has made significant progress in many fields. Public order and security have been strengthened and institutional reforms have made strides ahead and the civil servants are managed well to provide various public services. However, there are still challenges in the pension schemes of public servants.

There is currently no social security system in Somaliland. The system that existed during the colonial administration has not been in use for several decades. As a consequence, elderly public servants have three options of receiving income in retirement: (i) continue to work until they cannot work anymore – their salary effectively serves as their social security benefit; (ii) stop working and become financially dependent on other family members; and (iii) stop working and live in poverty. The reality of the situation, however, is that most civil servants continue to work beyond what should be regarded as retirement age because their salary supports a significant number of extended family members. The overall problem that the Somaliland Civil Service Strengthening Project (CSSP) seeks to respond to is GoSL's absence of a pension system to support the retirement needs of its employees who are retiring. The Somaliland National Development Plan I (SNDPI 2012-2016) concurs that the absence of government pension and social security systems and the supporting legislation and policies are among the policies and laws that need to be developed further to promote social development and protect citizen's rights. The Somaliland National Development Plan I (SNDP) states that Somaliland people rely mainly on traditional, social protection structures (e.g. inheriting public sector jobs) rather than setting up a national social security fund and introducing a pension scheme for public and private workers.

Though the Civil Service Law No. 7 of 1996 has provisions for civil servants to retire at age 60 and 55 for men and women, respectively, this is not being enforced. The Law also provides for a generous but inconsistent retirement benefit package for some categories of civil servants. The priorities and strategies of the Somaliland Civil Service Commission (SL CSC) for the current Somaliland National Development Plan I (SNDPII) period include, amongst others, introduction and adoption of pension and welfare schemes for retirees and incapacitated staff. In addition, the SNDP II envisions that there will be the introduction of a civil service pension and welfare contributions scheme to a pension fund and introduction of a pension system for retirees. Prior to the conclusion of the HR Data Audit exercise, there was no reliable data to enable meaningful pension projections related to payroll. The now finalized HR Audit exercise has resulted in cleaned payroll data including biometric registration of civil service employees. The payroll

data provided will be used to make clearer and meaningful data projections relevant to the pension policy as well as the projected costing of funding for the scheme. The absence of a public sector pension policy continues to have a negative impact on reforms in the civil service, particularly where staff beyond the retirement age continue to occupy their positions but not report to work and even when they do, are unable to satisfactorily perform their functions. There is evidence to show absence of pension system prevents large numbers of elderly staff from retirement, therefore impacting negatively efficiency and effectiveness of the civil service and prevents young entrance of new recruits, further distorting the dynamics of the labor market.

The increasing alarms about the sustainability of public pension systems have led to reforms that have tended to increase the degree of uncertainty over the amount of pension that individuals will receive when they retire. The changes in question include, in particular, linking contributions to benefits, building in annuity factors to take account of longevity, and introducing funded schemes to link pensions to the performance of the economy. In Somaliland, there is no social security system. Therefore, most civil servants continue to work beyond what should be regarded as retirement age because their salary supports a significant number of extended family. And such a public pension policy was required and adopted. The adopted pension policyⁱ is expected to resolve many challenges facing the GoSL civil service and provide details of the type of pension plan suitable for adoption by the GoSL and provide a roadmap for implementation including legislation.

1.2 Macro-Economic Outlook

Somaliland is one of the poorest nations in the world with a GDP per capita of USD444 in 2012. Economic production and trade are dominated by the livestock sector and this has led to macroeconomic volatility. In the short term, growth is likely to fall and the current account deficit to rise as the drought and livestock ban both reduce output and exports. Inflation is also likely to rise as the currency continues to devalue. The fiscal position is strong with approximately no outstanding debt. In the medium and the long term, Somaliland is in a relatively strong position to take advantage of its peace dividend and secure economic and human development.

Somaliland has progressed rapidly after independence due to the security and stability that the country enjoys. Building upon its long tradition of pastoralism, Somaliland has developed a strong livestock sector that accounts for around 30% of GDP and the vast majority of its exports. However, the country requires critical reforms and investments to diversify its economy and reduce dependency on primary production. The government's role in the economy has been limited since independence in 1991. In 2013, central and local government spending was around 8.5% of GDP and, although public spending has increased, levels of public investment remain low. Somaliland is one of the most difficult places in the world to do business with Hargeisa ranking 174 out of 183 in the Doing Business Index in 2012.

1.3 Gross Domestic Product

Somaliland's GDP per capita was amongst the lowest in the world in 2012. Its production structure is heavily dependent on livestock and imports. The economy will face significant short-term challenges as the result of the drought as well as a new Saudi Arabian ban on livestock exports restrictions.

However, in the medium-term Somaliland's continued safety and stability should allow it to reap a "peace dividend" that encourages further investment into the country. In the long-term the country will need to address its low level of human capital and the damaging effects of climate change.

Somaliland's GDP in 2012 was estimated at USD1, 558.4 million. Somaliland's GDP per capita stood at USD444 and is considered one of the lowest in the world. Somaliland's economy is dominated by low-productivity sectors with livestock and retail trade making up over 50% of GDP. Livestock has been traditionally the backbone of Somaliland's economy contributing 28.4% of its GDP. The wholesale and retail trade (21.9%), real estate activities (7.6%) and crops (7.0%) are other important sectors. On the other hand, sectors that are key for economic growth such as energy (1.0%) and finance (0.3%) have meagre participation. Table 1 below presents a breakdown of GDP by economic sector in 2012.

This is version 3 of the GDP-estimate for 2012. It brings the estimates forward to 2013 and beyond. The same sources and methods can be applied to compile estimates for 2010 and 2011 as well. The intention was to keep the document updated as the methods were being developed and modified. The data sources are scarce and the estimates are to a large extent based on assumptions and inferences from other countries in the region. The assumptions have been made explicit, discussed and validated. The estimates have been organized as follows:

- The GDP estimates have been derived by the production approach (GDP by activity) as well as by the expenditure approach.
- The GDP estimates are based on the Somaliland Business Survey (SBS); the Somaliland Household Survey (SHS); and the Population Estimation Somaliland Survey (PESS).

Table 1: GDP Activity, 2012

Description	Contribution	USD million
Growing of crops	7.00%	109.8
Livestock industry	28.40%	443.1
Forestry	4.60%	71.9
Fishing	0.30%	3.9
Mining and quarrying	1.20%	18.7
Manufacture of food and beverages	1.20%	18.9
Other manufacturing	0.50%	8.3
Electricity supply	1.00%	16.2
Water supply; sewage; waste management	0.30%	4.3
Construction	2.20%	33.9
Wholesale and retail trade; repair of motor vehicles	21.90%	341.7
Transportation and storage	1.90%	28.9
Accommodation and food service activities	3.10%	47.5
Information and communication	2.00%	31.2
<i>Financial and activities</i>	<i>0.30%</i>	<i>4.5</i>
Real estate activities	7.60%	117.8
Professional and support services	1.70%	26.2
Public administration and defense	3.00%	46.7

Description	Contribution	USD million
Education	3.30%	50.7
Human health and social work activities	1.70%	25.9
Other service activities	0.50%	8.2
Sum of values added at basic prices	93.60%	1, 458.4
Taxes and subsidies on products	6.40%	100
GDP at purchasers' prices	100.00%	1, 558.4
GDP per capita, SLS thousand / USD		444

Source: Ministry of Planning

1.4 Exports and Imports

The Somaliland economy is a pastoral economy. Livestock contributes 65% of the GDP hence livestock constitutes the principal export from Somaliland. The second biggest export is hides and skins with approximately 4.8 million exported in 2010. Frankincense and other natural gum and resins constitutes the third largest export (see Table 2 for details).

1.5 Remittances

The Somaliland economy is highly dependent on remittances, which are a significant contributor to family income and investment with implications for poverty reduction. Remittances constitute nearly 40% of income for urban households in Hargeisa and Burco towns (Dr. Saad Shire 2005). Dahabshil is the largest of about a dozen Somali MTOs active in Somaliland. Between them they handle about \$500-600 million annually. This is the money that pays for most of the imports into Somaliland.

Table 2: Exports through Berbera Port (2005-2010)

Year	Livestock (No)	Hides & Skins (No)	Gums (kg)
2005	1,183,225	3,123,723	272,720
2006	1,321,1107	2,090,620	423,011
2007	1,452,442	2,609,375	614,706
2008	1,332,077	4,041,121	883,677
2009	1,675,410	3,522,565	-
2010	2,747,120	4,784,041	3,070,005

Source: Ministry of Planning

1.6 Central Government Revenue

- a) Domestic revenues have grown significantly over the years for the period 2011 to 2015. Customs duties accounted for nearly 76% of total revenue and constitute the largest source of revenue for the government of Somaliland. Sales tax accounted for 2.5% of the government's tax revenue. Unlike most of the Sub Saharan countries, income tax and corporation tax account for less than 10% of government revenue (see Table 3).

Table 3: Actual Government Revenue (2011-2015) (in Sl.Sh and percentage of total)

Indicator	2011	2012	2013	2014	2015
Import	407,014,668,334	238,411,970,931	595,872,909,682	678,159,660,269.7	903,683,377,456
Direct taxes	13,840,197,999	33,979,991,447	44,284,084,918	96,879,951,467.1	30,593,083,329
Indirect tax	60,468,821,140	377,349,005,029	160,985,498,317	193,759,902,934.2	247,127,892,546
Total	481,323,687,473	649,740,967,407	801,142,492,917	968,799,514,671	1,181,404,353,331
Percentage of total revenue					
Import	85%	37%	74%	70%	76%
Direct taxes	3%	5%	6%	10%	3%
Indirect tax	13%	58%	20%	20%	21%
Total	100%	100%	100%	100%	100%

Source: Ministry of Finance

1.7 Central Government Revenue & Expenditure Projections

- b) The Government currently forecasts a slowdown in revenue growth in 2018 (due to the livestock ban and current drought) with greater revenue growth in 2019 and beyond. As part of the PFM Reform program, the government has utilized its new forecasting model to give a projection of central government revenue over the implementation period of the Somaliland National Development Plan II (SNDPII) (2017-21). The table 4 below gives the results of this modelling. A slowdown in revenue growth in 2018 is projected as the aftereffects of the drought and livestock ban take hold before a marked improvement in revenues in 2019 and beyond. The Central Government is projected to receive around USD 315 million in 2021 (from the central scenario). All revenue forecasts have been made using conservative assumptions to ensure that in the case of a negative shock to the economy or revenue collection efforts, the government will not have to make sudden, unplanned cuts to expenditure that would damage policy delivery in future years (Table 4).

Table 4: Central Government Revenue Projections 2017-2021

	2017	2018	2019	2020	2021
Optimistic		271,979,000	299,415,000	322,491,000	347,345,000
Central	258,867,000	271,979,000	273,511,000	293,194,000	314,293,000
Pessimistic		259,463,000	268,864,000	282,723,000	297,296,000

Source: Government estimates

1.8 Central Government Budget Allocation 2015

- c) Central Government's estimated budget for the year 2015 reveals a budget leaning more towards security at the expense of all other sectors. The second largest beneficiary of the 2015 budget is the economic sector. This is the sector that is poised to drive the agenda of government as envisioned in the National Development Plan 2012-2016. Table 5 below indicates the sectorized budget estimates for 2015:

Table 5: Government 2015 Budget Allocation

Sector	Budget
Economic	312,849,736,128
Good governance	172,274,047,877
Infrastructure and natural resource	60,641,089,248
Security	386,008,429,577
Social	148,226,697,170
Total	1,080,000,000,000

Source: Ministry of Finance

1.9 Public Sector Expenditure

The budget appropriations are predominantly for staff salaries and recurrent administrative costs based on annual expenditure plans submitted by MDAs. The Government has been experiencing a budget surplus over the last five years with only one year i.e. 2011 when they had a budget deficit. The government has been able to meet consistently its statutory obligations of payment of salaries and pensions in payment without delay. This pattern is unlike other Somali States like Puntland where the salaries are delayed, and the levels of revenue are lagging. Table 6 gives a breakdown of the Government's expenditure against revenue for the period 2011 to 2015:

In all the years since 2011, the growth in revenue has been steadily rising enough to cover the government's expenditure needs (Table 7). What the government collects is almost exactly what it spends, leaving a modest surplus. This is a demonstration that there is still room for both revenue expansion and further expenditure expansion and still maintain a modest budget surplus.

This pattern of revenue growth and expenditure has been replicated across all the major six districts of Somaliland and local authorities. In all years under consideration, the expenditure is lagging revenue albeit all of them on the increase.

d) Table 6: Central Government Revenue Vs Expenditure 2011-2015 (Sl.Sh)

Year	Revenue	Expenditure	Surplus/Deficit
2011	481,323,687,473	494,493,147,825	-13,169,460,352
2012	649,740,967,407	618,779,267,104	30,464,404,054
2013	801,142,492,917	740,772,622,951	60,369,869,966
2014	968,799,514,671	900,126,181,367	68,673,323,304
2015	1,181,404,353,331	1,072,963,812,985	108,440,540,346

e) Source: Ministry of Finance Accountant General

Table 7: Total Local government revenue and expenditure 2011-2015 (Sl.Sh)

Year	Revenue	Expenditure	Surplus/deficit
2011	60,292,718,930	56,944,955,022	3,347,763,908
2012	50,857,600,517	57,976,363,503	-7,118,762,986
2013	69,947,893,770	74,296,275,454	-4,348,381,684
2014	113,527,920,858	108,899,007,629	4,628,913,229
2015	142,549,750,417	124,317,429,201	18,232,321,217

Sources: Ministry of Finance.

1.10 Public Sector Salaries

The Government spending on public sector wages for the central government amounts to 56% of the total budget of USD90million, with the salaries and benefits budget at approximately USD50.4million (2012). Any upward shift on this budget will further increase the cost of wage bill. It is however worth noting that other areas of the government are underfunded and so the surplus available would be competing with other priority areas of government. The spread of salaries per grade is as shown in Table 8 below:

Table 8: Salary Structures & Allowances by Job Group (Mean Salary, SL Sh)

Job Grade	What is the amount of the current salary				How much are these allowances and benefits			
	Minimum	Mean	Maximum	Range	Minimum	Mean	Maximum	Range
A	300,000	1,169,648	4,280,000	3,980,000	0	4,209,316	1,800,000,000	1,800,000,000
B	300,000	877,672	4,200,000	3,900,000	0	1,121,753	235,000,000	235,000,000
C	300,000	714,106	4,000,000	3,700,000	0	1,624,316	120,000,000	120,000,000
D	200,000	548,332	4,115,650	3,915,650	0	573,872	13,500,000	13,500,000

Source: ??

The spread of salaries is higher in grades A and lower in grade D which is lower grade. The allowances are higher than basic salaries in all grades. A huge fraction of total remuneration is attributable to allowances. Allowances across the grades differs from ministry to ministry, hence are not harmonized within job groups. The resultant impact on pensions will be significantly disproportional since pension benefits will be based on basic salary as opposed to gross pay, thereby creating a pension benefit illusion in retirement if the allowances are not harmonized and members not sensitized.

1.11 Current Employment Levels in the Civil Service

The levels of employment are low. The spread of employment levels for Government employees for the period 2012-2015 as well as 2019 per gender and grade is as shown in Table 9 below.

Table 9: Distribution of Employment levels per grade and gender

Year	Gender		Grades				Total
	Female	Male	A	B	C	D	
2012	2,588	8,998	1,611	6,591	1,587	1,538	11,327
2013	2,800	9,989	1,824	7,466	1,785	1,727	12,802
2014	3,381	10,931	7,900	7,900	1,977	2,323	14,301
2015	3,552	11,803	2,586	8,271	2,271	2,380	15,384
2019	4,690	12,883	4,887	8,191	2,326	1,178	17,573

Source: Civil Service Commission

The number of the civil service employees has been on a steady upward trend since 2012 to 2015 with the majority of the employees being at grade B, the largest increase being in 2013/2014 and then decreased. Male employees dominate the staff of Government service.

The Government has been maintaining a pensioner's payroll for the last four years since 2012 as shown in Table 10 below. Individuals above retirement age are given the option of taking a pension equal to 50 percent of basic salary and retiring.

Table 10: No of Government Pensioners per grade 2012-2015

Grades	No of Pensioners				
	2012	2013	2014	2015	2016/17
A	58	58	72	70	63
B	107	107	98	97	92
C	91	91	78	76	74
D	77	77	75	74	73
Total	333	333	323	317	302

Source: Ministry of Planning

The number of pensioners declined from 333 in 2012 to 302 in 2016/17. No information was available to explain the reduction in numbers as well as the amounts payable to them.

1.12 Monetary Policy

The Bank of Somaliland established in 1994 is responsible for monetary policy. It acts as the Central

Bank (CB) and a commercial bank at the same time. It currently operates eight branches. Some of the CB instruments to affect the policy are still at the infancy stage. The development of the bond market and government securities is still not established and the Central Bank's main instruments of printing money and buying and selling the dollars are so far the ones in use. The bulk of the Central Bank work is yet to be realized as the number of commercial banks in Somaliland hopefully will grow.

1.13 Financial Sector Development

The National Development Plan I (2012-2016) has identified the absence of financial institutions such as commercial banks, investment banks and other lending institutions as one of the weaknesses in Somaliland that require attention during the term of the strategic plan. The absence of a formal financial sector for a long time created room for an informal sector to come in and fill the void. The latter has traditionally been comprised by remittance companies. The remittance sector dates back many decades. Even though the remittance sector plays a vital role in the current Somaliland Economy; the existing financial sector is characterized by the following:

- a) Virtual lack of intermediation; i.e., deposit taking and lending through financial intermediaries, albeit some informal lending taking place through nongovernmental organizations in form of microfinance
- b) The economy is predominantly cash based;
- c) Very limited banking services, including those such as money transfers, foreign exchange and deposit facilities, which are provided by remittance companies;
- d) Banking sector comprises an active informal sector dominated by remittance companies and a virtually non-existent formal sector which includes the central bank;
- e) The central bank operates as a commercial bank. This operation undermines its supervisory and regulatory authority.
- f) The lack of international recognition of the Government of Somaliland affects the Government's international banking relations;

Despite these challenges, a few micro finance institutions have established operations and are a main source of employment for the urban and rural population through the micro- and small enterprises. The microfinance survey of 2013 puts these micro small enterprise institutions at 100,000 MSEs. Up to 33% of the population is employed by these MSEs. Even with this growth, the baseline survey showed that provision and delivery of credit and other financial services to the sector by formal NGOs and non- financial institutions has been inadequate. Some of the Micro Finance Institutions set up include Salaam Financial Services (a subsidiary of Telsom) and Kaaba Microfinance Institution. (*Source: SNDPI 2012-2016*)

The year 2017 has seen some international banks set up operations in Somaliland e.g. Premier Bank which opened its operations in May 2017, the Dahabshil International Bank associated with the Dahabsil remittance Company has also opened operations in Hargeisa. All these are signs of confidence in the financial sector in Hargeisa which will help address the access to finance challenges that have been there before as regulated by the Central Bank.

2 Pension Policy Objectives and Proposed Solutions

2.1 Overview

The Government of Somaliland is seeking to introduce an affordable and adequate pension system for public sector workers. Although The Constitution of the Government of Somaliland guarantees retirement benefits for all employees of the public service, currently Somaliland does not operate a traditional pension system and instead relies on informal measures, such as hiring the children of the deceased public sector workers to enable the family to maintain an income, and allowing voluntary retirement at half salary to those above the retirement age. The SNDP II 2017-2021 underscores the absence of a pension policy and outlines how it inhibits the exit from and recruitment of staff into the civil service.

The purpose of this policy note is to discuss a package of pension policies that, through consultations with the Government and analysis of the socio-economic situation in Somaliland, have been identified to most effectively fulfill the objectives set forth by the Government of Somaliland with respect to establishing a fiscally affordable and adequate pension system for public sector workers.

This policy note recommends that a Defined Benefit (DB) Pension System financed on a Pay-As-You-Go (PAYG)¹ basis is the most appropriate arrangement given the Somaliland context. Namely, opting for a DB system would permit for a straightforward calculation of pension benefits to be paid to individuals above retirement age, resolving the challenge of how to address the issue of acquired rights. In addition, PAYG financing eliminates the need for external financing as contribution revenue from current workers would be used to finance current pension expenditures. While PAYG financed DB systems can accumulate some reserves when immature, reserves are likely to be small since pension contributions from active public sector workers are used to pay the pensions of current retirees. This is a preferred outcome in the absence of limited domestic investment opportunities and the lack of adequate oversight structures.

2.2 Key Policy Goal and Objectives

The main policy goal is to meet the pension needs of Somaliland civil servants in a sustainable, cost-effective, and socially acceptable manner for social and economic development while the key pension policy objectives are as follows:

- 1) Developing a fiscally affordable and sustainable pension system that delivers adequate and equitable old age, disability and survivor's pensions to public sector employees.
- 2) Ensuring public sector workers who are already above retirement age begin receiving pensions.
- 3) Minimizing the need for external financing of pension expenditures.
- 4) Serving as a blueprint for developing a private sector pension system, including provisions for the informal sector.

¹ A system in which retirement benefits are financed by contributions levied from current workers, as opposed to a funded system in which contributions are invested to pay for future benefits.

2.3 Guiding Laws and Policies

2.3.1 Civil Service Law No. 7 of 1996

The Civil Service Law no 7 of 1996 article 23 (1) states “Social Security, compensation for service incurred death, illness or injury, pensions and other related benefits, subsistence allowance for special services shall be established by separate laws “ which is a demonstration that the government is keen on providing these benefits albeit through separate pension laws.

The retirement age for the public service is as stated in the Civil Service law no of 7 of 1996 under article 38 (1) and (2) which states as follows:

- i) An official shall retire from the service on attaining the age of 60 years for male and 55 years for female.
- ii) However, for exceptional exigencies of service, the President, with the consent of the official concerned, may extend his/her service beyond the age of sixty, provided that the official's service shall not be extended beyond 65 years of age.

2.3.2 The Somaliland National Development Plan I 2012-2016

The Somaliland National Development Plan I (SNDPI) stipulates country’s short to medium term strategic direction, development priorities and proposed implementation mechanisms including the use of development aid. The Plan provides an analysis of Somaliland’s current development status, challenges and opportunities.

2.3.3 Somaliland National Development Plan II (2017-2022)

During the development cycle of the Somaliland National Development Plan II (SNDP II), the Social Protection Sector focused on the following:

- a) Strengthening existing institutions such as orphanages, and community-based support services
- b) Institutionalizing child protection services
- c) Establishing family centers and promoting equity within societies
- d) Setting up a national social security fund, and
- e) Introducing a pension scheme for public and private workers

The social protection pillar is also amplified in the Somaliland National Vision 2030 as a key pillar focusing on the above subsectors as enablers to the realization of this pillar.

Just like the SNDPI, SNDPII recognizes that the absence of a functioning pension scheme has limited the government’s capacity to retire staff and thus create the space for recruiting fresh talent into the civil service.

2.3.4 Draft Military Pension Law

One of the attempts to put in place a pension law was through the Ministry Established Military Pension Law. This law was in draft form and was a translation of the same from the Somali

language. It borrowed heavily from the draft Civil Service Draft Pension Law which was also developed. These laws were all in draft form and because they lacked a policy framework on which they could be anchored, they were never operationalized. The same pension laws i.e. the Military and the Civil Service lacked key components of an ideal pension framework such as financing, governance and regulations all of which ought to have been provided for under law or policy. The Government could therefore not properly enforce these laws. There has however been development in military law and a draft law has been drafted and presented for discussion. If enacted into law, the affected employees will therefore be covered under the proposed Somaliland Armed Forces Retirement and Pension regulations no 6 of 2018 (under development).

2.4 Pension Policy Development Process

The development of this pension policy is informed by the need for the Government of Somaliland to provide for financial freedom for the staff who have attained the retirement age but are still in office. Through the World Bank supported CSSP program, the pension policy was earmarked as one of the projects to be implemented to address the issues of an aging public service.

The process commenced with participation of the key senior Government officials led by Ministries of the Government and key Government agencies' officials. The information obtained from these processes was consolidated into a policy framework source document from which this policy was drawn. The policy development process was also informed by various studies published by various writers with respect to development of pension policies in developing countries under the OECD. The rich experiences learnt from comparator countries who have undergone similar experiences like the Government of Somaliland were also taken on board to inform this policy. Key lessons were picked from countries such as Eritrea, Rwanda, South Sudan as well as the larger Sub Saharan Countries' pension arrangements.

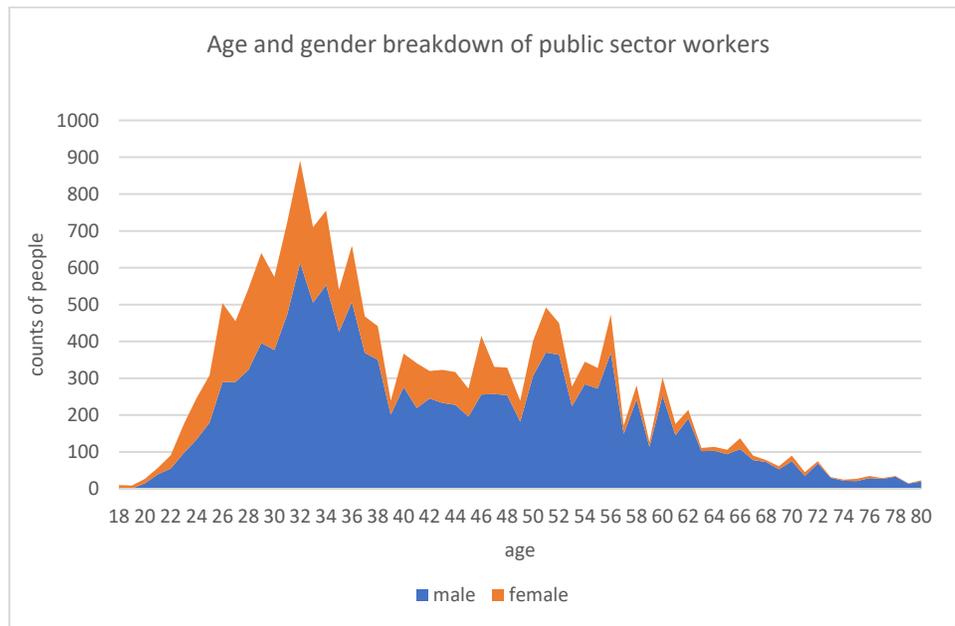
Linkages with all stakeholders was undertaken through the various meetings held and the trainings undertaken during the validation process. At all levels of stakeholder's consultations, all Government officials were given opportunity to participate and give their views by completing a questionnaire and feedback in the workshops held. Analysis arising from the completed questionnaires contributed to the development of this policy.

The policy takes cognizance of the synergy and co-operation of the various roles the different stakeholders played in shaping this pension policy.

2.5 Profile of Public Sector Workforce

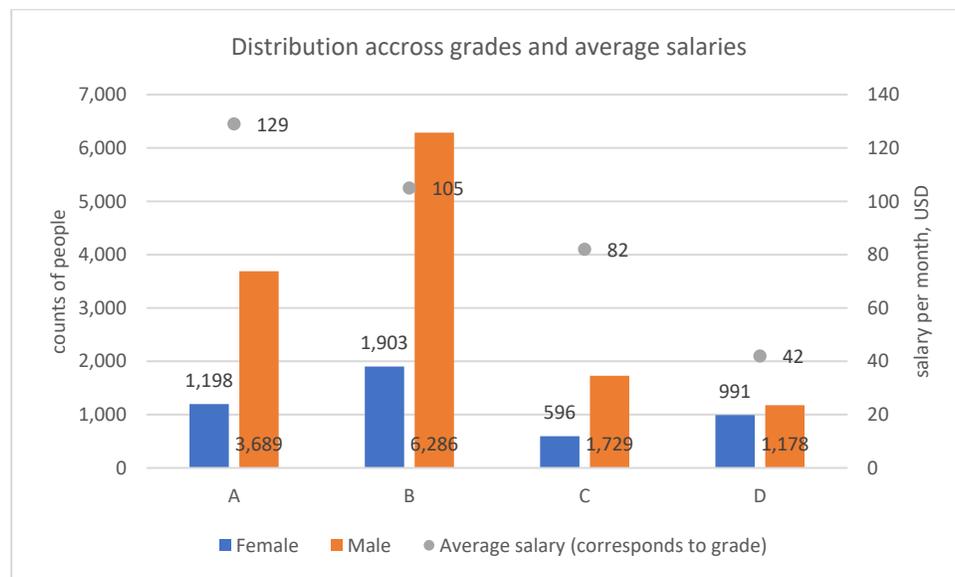
In 2019, there were 17,570 public sector employees, 73% of whom were male (see chart 2.5-1 for age/gender breakdown details). Most public sector workers are at grade B. Women earn markedly lower wages than men. The average monthly salary was \$101 USD (see chart 2.5-2 for grade/gender/salary details). The basic salary wage bill amounted to \$21,420,353 USD.

Figure 2-1: Age and Gender Breakdown of Public Sector Workers



Source: Somaliland Administrative Data

Figure 2-2: Distribution of Workers Across Grades and Average Salaries



Source: Somaliland Administrative Data

2.6 Proposed Policy Solutions

Arriving at the right set of pension policies for a country usually requires that the proposed package be modelled actuarially to ensure the system can not only meet its objectives today but that it can continue to do so decades into the future. Long-term projections are typically needed to enable a

more complete assessment of proposed pension policies because pension systems are long-term contracts and their true fiscal needs might not appear until many years after they begin.

To help inform an appropriate set of pension policies for the Somaliland public sector, a World Bank team has developed a PROST model (Pension Reform Options Simulation Toolkit) for Somaliland to facilitate informed policy making and help ensure the selected parameters meet the stipulated objectives, namely to introduce a fiscally sustainable and fair pension system that delivers adequate retirement income and income protection against disability and loss of a breadwinner and pays pensions to public sector workers above retirement age with limited reliance on external financing. The next section discusses the rationale and expected impact of the proposed pension policies.

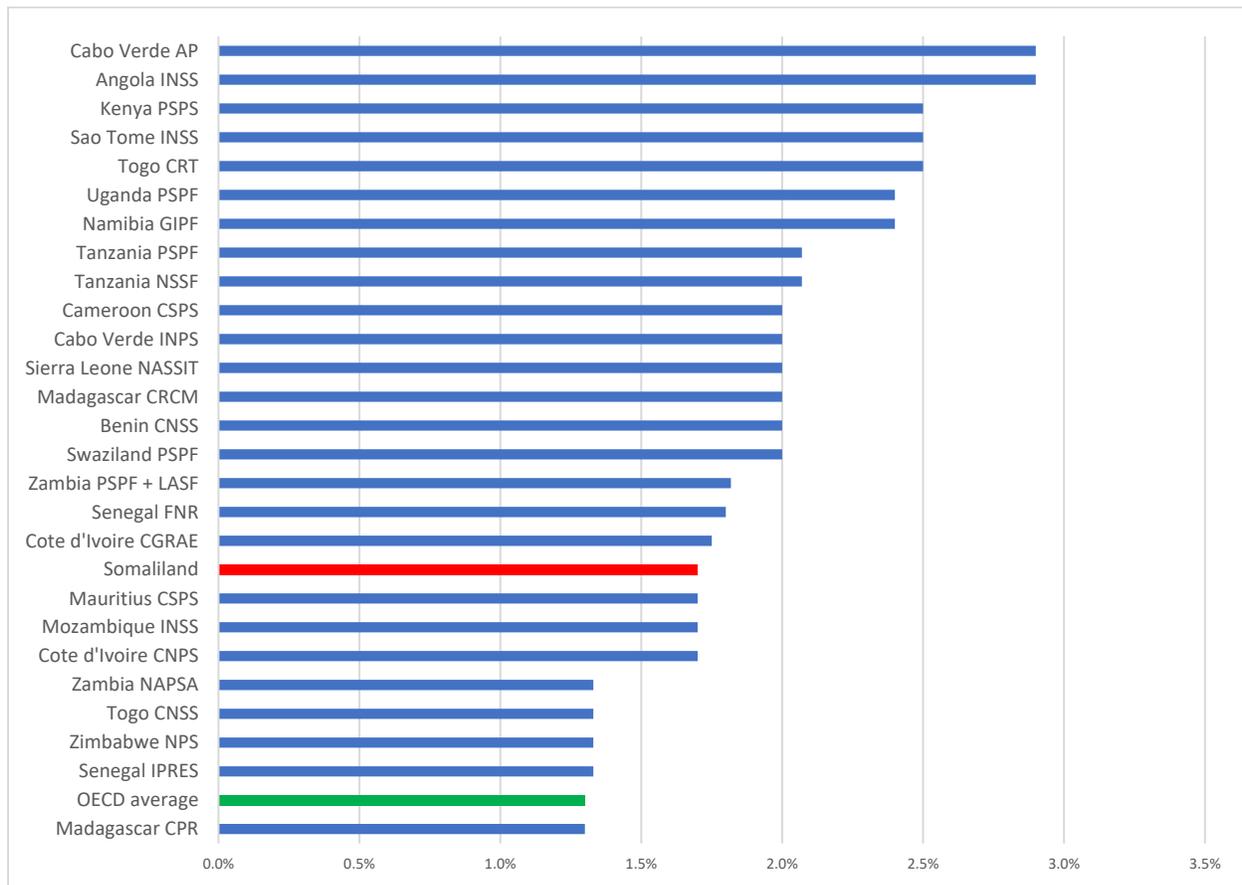
2.6.1 Proposed pension system parameters

- a) **The proposed defined benefit pension system has an old age pension benefit rate of 50% of reference wage after 30 years of service which is equivalent to a 1.7% accrual rate per year.** This rate exceeds the minimum threshold for pension adequacy under defined-benefit plans set forth by The ILO Social Security (Minimum Standards Convention, 1952 No. 102). The ILO minimum standard for old age income security recommends a replacement rate of 40% after 30 years of contributions. The proposed accrual rate also exceeds the average accrual rate observed in high income countries of 1.3% per year. Accrual rates in high income countries are generally considered fiscally sustainable and international best practice. (Source: OECD Reviews of Pension Systems, 2019). Although the proposed replacement rate of 50% after a full career is higher than in OECD countries, it is still considered appropriate for Somaliland because the retirement age of 65 for men and women is equivalent to retirement ages observed in the OECD despite lower life expectancy which would result in shorter duration of retirement for Somaliland pensioners.
- b) Figure 2-3 below provides an overview of accrual rates across national and civil service pension systems in Sub-Saharan Africa. Pensions in Sub-Saharan Africa accrue at higher rates compared with rates across OECD countries, but they also are less likely to be fiscally sustainable. Higher accrual rates are usually seen in countries where civil service systems are generating fiscal deficits and where pension system contribution rates are markedly higher. Figure 2-3 also shows that in some countries accrual rates in civil service schemes are higher than the accrual rates in the national pension systems, creating a disparity between civil servants and private sector workers. This is an important caveat for Somaliland since eventually the newly designed public sector pension system may be used as a blueprint for the development of a national pension system. In summary, the proposed benefit for Somaliland is adequate while not overly generous as are some of the plans in African countries that will require major fiscal adjustments in the future.
- c) **With respect to survivors' pensions, surviving families will receive 70% of old age pension if the employee had retired and 70% of old age pension entitlement if the employee is still working. Similarly, to old age pensions, survivor pensions are indexed to inflation.** Drawing from regional experience, the Somaliland public sector pension system can expect the number of surviving families in the long run to represent 20% of contributors and retirees. In order to estimate the fiscal needs of a survivor pension program, survivors are assumed to draw a survivor's benefit for 15 years on average (children reach maximum age, widows either remarry or survive on average 15 years).

- d) **Regarding disability pensions, disability pensions will be 50% of average basic salary paid as monthly pension. However, rather than being indexed to inflation, 50% of current average wage is expected to be paid to all disabled employees, resulting in a more generous indexation.** Disability pensioners are assumed to be 4% of contributors after 15 years.
- e) **The reference wage for the calculation of the pension will increase from final basic salary in the first year to an average of last five annual basic salaries at the rate of 1 year per year,** given the lack of full Government records on past wages. Basing pensions solely on last salary can be a more costly approach for instance relative to basing pensions on a career average wage, but it is also much less complicated as it eliminates the need to index historical wages. As a result, opting to base pensions on the average of the last five years of wages seems like an appropriate compromise as it more closely aligns benefits with contributions paid (*if a worker has paid contributions on earned wages over a lifetime, then aligning benefits with contributions would imply that pensions should be based on the average lifetime wage*) without introducing added complexity with respect to the need to valorize² historical wages.
- f) **The proposed system calls for a retirement age of 65 for both men women.** Based on population statistics for Somalia, the life expectancy – or expected duration of retirement – at age 65 about 13 and 14 years for men and women respectively. International best practice for duration of retirement is 15 years, though national life expectancies often underestimate the life expectancies of civil servants who typically have better access to healthcare and safe work conditions.

² Historical wages are typically adjusted upward to reflect changes in price levels or average economy wide wages – also known as valorization - when the reference period for the calculation of pensions is comprised of five or more years.

Figure 2-3: Pension System Accrual Rates in Select SSA Economies

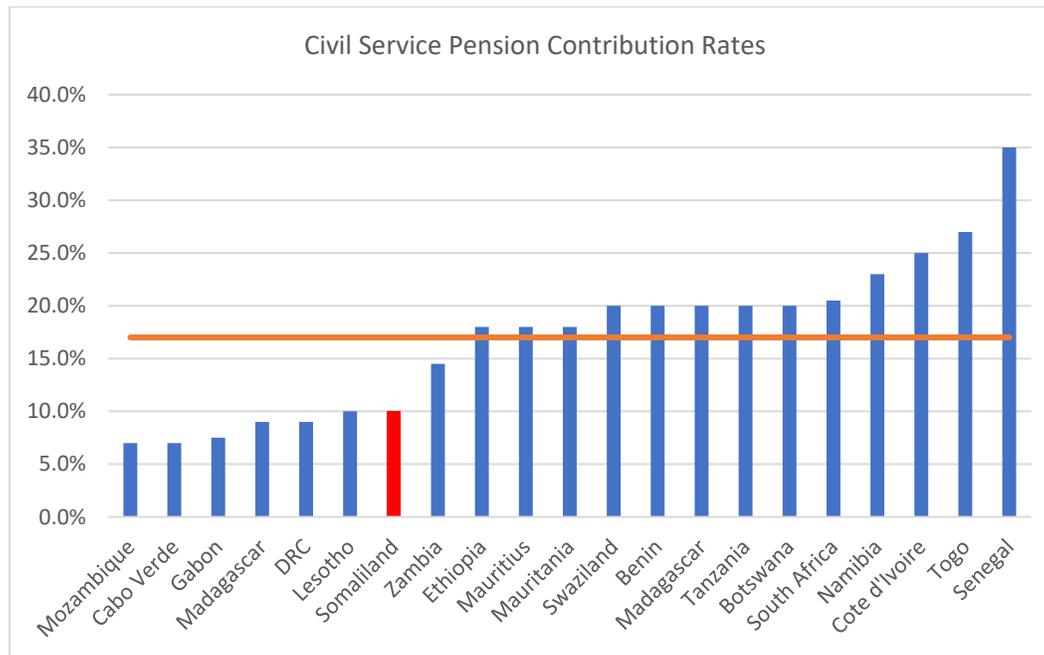


Source: Social Protection and Jobs Africa Pensions Database, December 2019 Update

- g) **Pensions after retirement are assumed to be adjusted according to inflation.** International best practice suggests indexation post-retirement should be by inflation only, with the logic that an individual's purchasing power should be maintained from the first day of retirement throughout retirement, however long it lasts.
- h) **The system is financed on a PAYG basis from employees and employer contributions at the rate of 5% and 5% of basic salary for a total contribution rate of 10%.** The average civil service pension system contribution rate in SSA is 17% (see Figure 2-4). While the proposed contribution rate falls below the SSA average, projections of the fiscal needs of the Somaliland public sector pension system presented in the next section show that a 10% contribution rate is sufficient to fully finance pension expenditures over the next decade under the proposed set of pension system parameters. Many African countries have attempted to accumulate a reserve in their pension system with higher contribution rates to allow them to cover future pension deficits. However, in the absence of deep financial markets and adequate regulatory oversight, these reserves are often squandered, after the workers and their employers have spent funds on higher contribution rates in order to accumulate those reserves. Most high-income countries started with low contribution rates, like what is being proposed in Somaliland, and only raised them over time.

- i) **The recommendation for Somaliland is, therefore, to run the system on a pay as you go basis with only limited reserves and to gradually consider raising the contribution rates in the future when the financial status of the pension system requires it.** The projected financial flows under the proposed set of parameters, including a 10% total contribution rate, are presented in the next section.

Figure 2-4: Pension Contribution Rates in Select Civil Service Pension Systems



Source: World Bank Africa Pensions Database

2.7 Projected Pension Policy Outcomes Using World Bank's PROST Model

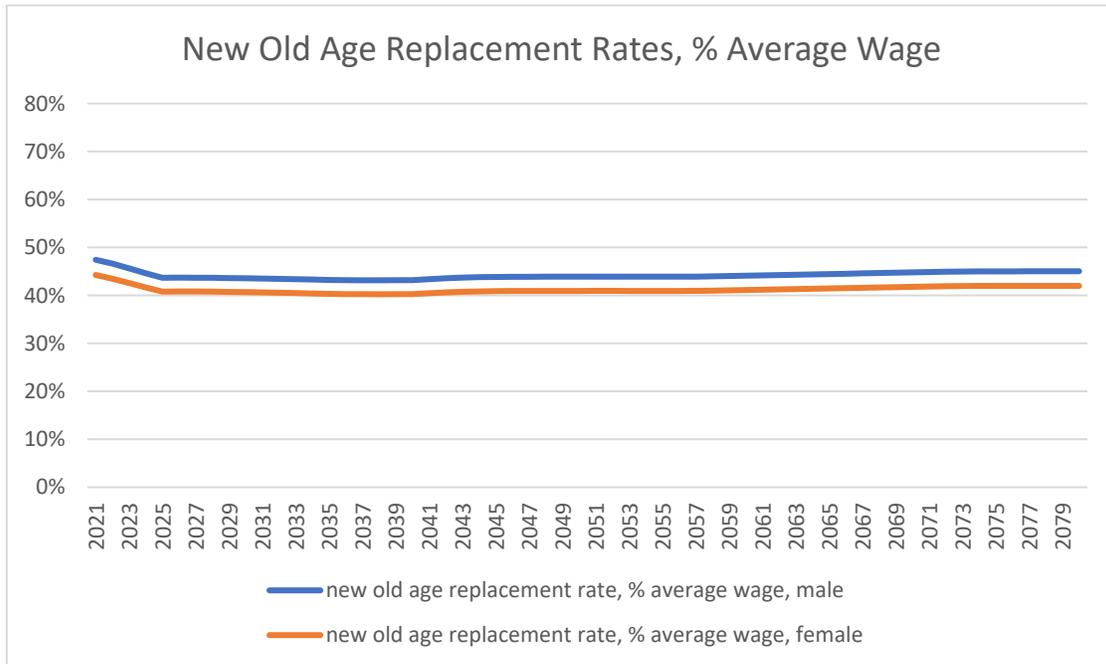
2.7.1 Adequacy of pension income

Projected new old age replacement rates exceed ILO's minimum standards of pension adequacy.

The proposed defined benefit pension formula provides 50% of the average last five year salary after 30 years of service – equivalent to an accrual rate of 1.7% per year. Figure 2-5 below shows that the proposed pension parameters will provide an adequate pension based on ILO standards. It is assumed all newly retired in year 2021 are awarded pensions based on a 30-year career according to Government decision; subsequently both men and women are assumed to have 30 years of service. The projected replacement rates shown below indicate new women's pensions as a percentage of the average wage, not the average women's wage. Since women earn less than men, their pensions are also expected to be lower.

Average benefits for existing pensioners are lower relative to average wage than starting benefits. This is because pensions after retirement are increased according to inflation whereas wages of active public servants are assumed to increase in line with average real wage growth.

Figure 2-5: Projected pension system replacement rates, new retirees

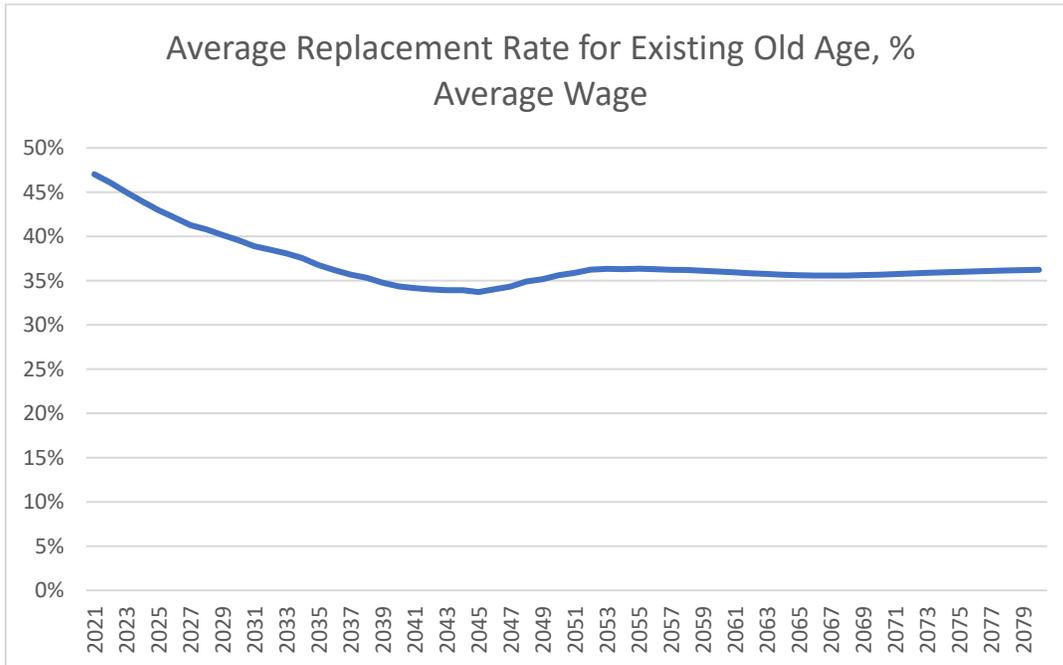


3

Source: PROST Projections using Administrative Data

³ Projected new old age replacement rates show below 50% replacement rate because new pension amounts are expressed as a percentage of current civil service wide average wage (due to the way PROST pension model produces results), not the average 5-year salary after 30 years prescribed by the pension formula.

Figure 2-2: Projected pension system replacement rates, existing retirees



Source: PROST Projections using Administrative Data

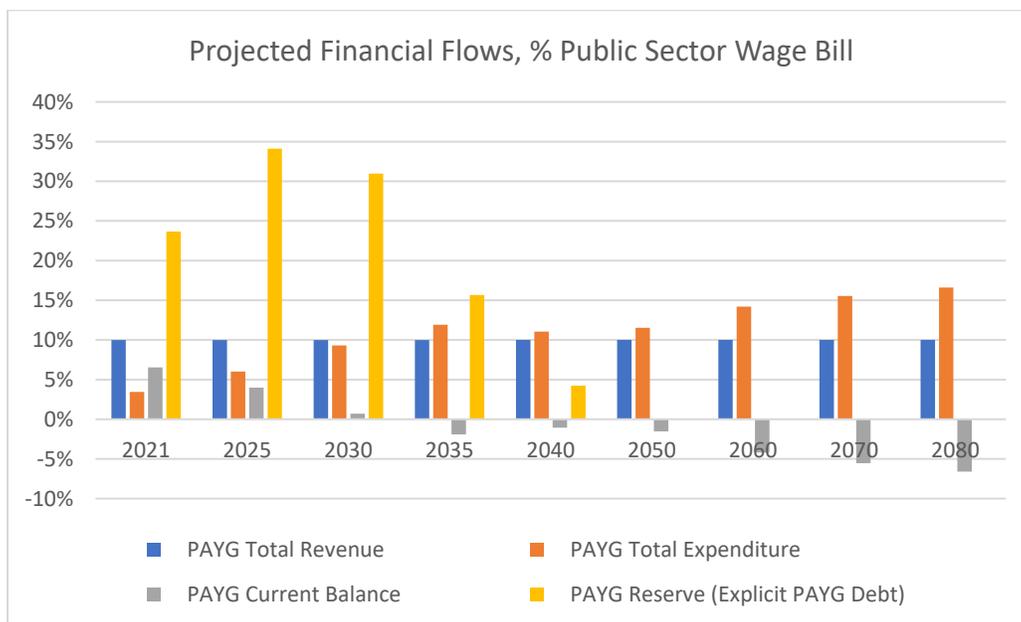
2.7.2 Fiscal affordability

Projections show that under the proposed PAYG pension system parameters, contribution revenue from employees and employer will be sufficient to cover projected pension system expenditures until 2031 and accumulated reserve funds will lengthen the sustainability of the pension fund until 2045. Initially, a contribute on rate of 10%, evenly split between employees and employer, is enough to cover pension expenditures through 2031, while also generating a reserve fund in the initial years because contribution revenue will exceed pension expenditures. It is important to note that expenditures may be higher than shown below because Somaliland currently has around 300 pensioners which were not included in the simulation due to lack of data on them. Once data on the 300 pensioners becomes available, the projections can be amended to include the added costs. Figure 2.7.2 1 below shows the projected fiscal flows as a share of the public sector wage bill under the proposed pension system parameters. There is an initial reserve because Somaliland has had a 1% employee contribution for some time. While the current account will begin to show deficits in 2031, the accumulated reserve fund can then be accessed to balance the fiscal flows. Projections show the reserve fund will be able to supplement the current deficits until 2045, as shown in Figure 2.7.2-1 as the yellow bar which remains positive until 2045. The projections shown in this note assume that the reserve fund is accumulated purely as cash and thus earns a zero percent nominal interest rate or profit-sharing rate. Should the fund be able to be invested to earn better returns, the fund will last longer. Furthermore, when pay and grading reforms are implemented, wages are expected to rise. This will immediately raise contribution revenue for all those experiencing a wage increase, but the full wage increase will only be reflected in higher

pension benefits for those workers who have paid contributions on the basis of the higher wages for 5 years, thus raising contribution revenue immediately, but only raising pension benefits for new retirees gradually for the first 5 years and then fully thereafter. This will also lengthen the sustainability of the pension fund.

Due to steadily increasing pension expenditures as the pension system matures, it is recommended that the Government periodically reassesses key pension system parameters to ensure they continue to support a fiscally sustainable pension system. For example, most countries expect to pay total pension contributions of 20 percent of wage in order to finance an adequate pension. Somaliland, while starting with low contributions initially when wages are low and the Government has financing constraints, should expect to pay higher contributions in the longer term. When the reserve is depleted in 2045, the Government could consider the following policy options: (i) raising contribution rates; (ii) raising retirement ages in line with life expectancy changes; (iii) increasing the number of wage years used in the calculation of the benefit; or (iv) reducing the benefit rate slightly (assuming most public sector workers start working at age 25, with a retirement age of 65, replacement rates will approach 68% which is relatively high compared to international experience which means that as expenditures begin to increase, benefits could be adjusted down slightly to ensure the fiscal balance of the pension system).

Figure 2-1: Projected Fiscal Flows, % Public Sector Wage Bill



Source: PROST Projections using Administrative Data

3 Implementation Framework

3.1 Institutional Framework

The Government is committed to implementing the policy objective strategies and ensuring that it provides for old age pensions and attracts and retains the skills needed in the public service.

The Constitution has provided for retirement benefits for all public service employees as an earned right. In view of this, the Government, through the Ministry of Employment, Social Affairs and Family, Ministry of Interior, Office of the President, and the Civil Service Commission, will collaborate with all stakeholders to implement this policy.

The collaboration mechanism will be developed through consultations between the Government entities, preventative of beneficiaries and representatives of the broader civil society. The agreed mechanism will become a part of the final policy document to be approved by the Government and other stakeholders.

To give effect to this policy, a legislative framework will be developed to regulate and institutionalize mechanisms and procedures for administration, management, custody of the assets of the pension fund and regulation of the public-sector pension arrangements.

3.2 Monitoring and Evaluation

A monitoring and evaluation framework will be developed to evaluate progress made in the implementation of this policy in line with the SNDPII of 2017-2021. Annual monitoring and evaluation will be carried out by the Ministry of Planning and a report will be prepared and shared with all stakeholders on the implementation progress and coordinated with the Civil Service Commission. The implementation plan of this policy will be a key framework to use for regular reporting at least on a quarterly basis from the date of implementation.

3.3 Transition mechanism to this policy

Any existing pieces of guidelines affecting this policy will cease to be operational upon establishment and implementation of this policy. All past service liabilities will be transferred into the new public sector pension arrangements to form part of the member's balances.

The CSSP, World Bank, MESAF and the Civil Service Commission to support the Transition and implementation of the policy in line with the implementation road map.

3.4 Policy Review

This policy will be reviewed as at and when circumstances change to warrant its review. The periodic reviews will be triggered by socio-economic factors and as guided by Government.

3.5 Other Policy Reviews

Another policy issue that emerged during the course of the policy development that require addressing by the Government, and which will affect the pension policy, is the review of the current salaries and allowances. To this end, a pay and grading reform of the current civil service pay policy is being undertaken alongside the implementation of the pension policy.

The benefits of the pay and grading policy reform will be a transparent and equitable system of pay and grading and, by extension, pensions in retirement.

Annex 1: Projected Performance of the Pension System Using the World Bank's PROST model

Background

The cost projections in this Annex were produced using the World Bank Pension Reform Options Simulation Toolkit (PROST). The PROST model has been used to project pension system benefits and fiscal costs in more than 130 countries, and takes into account macroeconomic projections and life expectancy changes in producing cost estimates for all three types of benefits included in a typical pension system: old age, disability, and survivors.

The modeling covers the period 2019⁴ to 2080. While policymakers may wonder why it is necessary to model out to very distant years like 2080, it is important to determine whether the pension promises being made today to newly joined public sector workers at the age of 21 in 2020, for example, can be kept. Today's 21 year old will not retire until 2064 and will expect to spend some 13 or 14 years in retirement and then might leave a spouse and children who will collect benefits for some years after his death. As the Government makes promises to these workers today, it is important to know whether these are promises that the Government will be able to keep.

The macroeconomic assumptions used are included in Figure 1 below. While 2020 is not a normal year due to the impact of the coronavirus pandemic and perhaps 2021 will not be either, pension policy is being set for the long term. Therefore, the projections are maintaining what had been the growth trajectory. Once the growth implications of these extraordinary years become clear, the projections can be updated. No interest is assumed to accrue on any pension reserves in line with the lack of interest-earning financial instruments in Somalia.

Modelling parameters and assumptions

- The newly designed public sector pension system is assumed to begin in 2021.
- Individuals already above retirement age, but currently employed in civil service are all given pensions assuming they had 30 years of service.
- Length of service is maintained at 30 years for both men and women.
- Only those currently working will be eligible to receive a pension or generate a survivor or disability pension, aside from those who are already receiving a pension
- Pension reserves earn a nominal interest rate equal to zero in line with the limited participatory investment instruments in Somaliland.
- Administrative costs will be paid by the Government.
- Macroeconomic assumptions used for the projections are shown in Figure 1 below. While 2020 is not a normal year due to the impact of the coronavirus pandemic and perhaps 2021 will not be either, pension policy is being set for the long term. Therefore, the projections are maintaining what had been the growth trajectory. Once the growth implications of these extraordinary years become clear, the projections can be updated.

⁴ The projections are based on counts of contributors in year 2019 as provided by the Government of Somaliland.

Projected demographic composition of the pension system

Life expectancies at the retirement age of 65 are derived from the UN Population Projections for Somalia⁵ and are shown in Figure 2 below.

Figure 3 below shows the projected evolution of pension system participants. The first cohort of old age pensioners is in year 2021 when everyone currently over pensionable age is retired along with the cohort reaching retirement age in 2021. In year 2019 there were about 1,100 public sector workers over retirement age. Similarly, if the system were to begin in 2022, old age pensioners will be comprised of everyone over retirement age in 2020 plus those reaching retirement age in 2022. The disabled are assumed to roughly equal 4% of contributors, based on data from similar countries and survivors are assumed to be equal to about 20% of the sum of contributors plus retirees, based on the experience of other countries and the number of expected deaths each year. Projections show that counts of contributors will exceed the number of beneficiaries throughout the simulation horizon. The total number of contributors are assumed to grow with the working age population. While the cadre of those who work in central offices will not necessarily be affected by the growth in population, those who provide services like teachers and health workers will need to increase in number as the population who consumes those services grows.

The financial projections are shown below in Figure 5 as a percentage of the wage bill and in Figure 6 in millions of US dollars. The pension system contribution rate is set to 5% each for employer and employee. Due to expected increase in pension expenditures overtime, it is recommended that the total contribution rate be correspondingly increased in order to ensure fiscal balance. Most countries expect to pay total pension contributions of 20 percent of wage in order to finance an adequate pension. Somaliland, while starting with low contributions initially when wages are low and the Government has financing constraints, should expect to pay higher contributions in the longer term.

If the PAYG contribution rate starts at 5% each for employer and employee in 2021 and remains unchanged throughout the simulation horizon, the pension system is projected to run into a fiscal deficit around year 2032 as shown in Figure 7. The accumulated reserve fund – resulting from contribution revenue exceeding pension expenditures in the initial years – is projected to supplement the current deficits and lengthen the sustainability of the fund until 2045. When the reserve is depleted in 2045, the Government could consider the following policy options: (i) raising contribution rates; (ii) raising retirement ages in line with life expectancy changes; (iii) increasing the number of wage years used in the calculation of the benefit; or (iv) reducing the benefit rate slightly (assuming most public sector workers start working at age 25, with a retirement age of 65, replacement rates will approach 68% which is relatively high compared to international experience which means that as expenditures begin to increase, benefits could be adjusted down slightly to ensure the fiscal balance of the pension system).

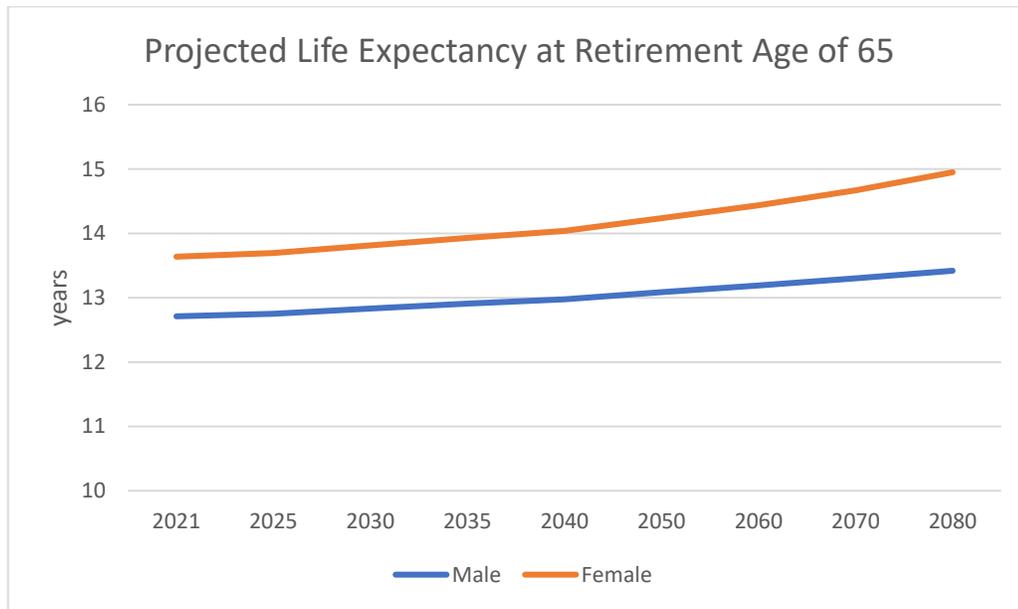
Figure 1: Macro-economic assumptions used for PROST modelling

	2020	2021	2025	2030	2035	2040	2050	2060	2070	2080
Real GDP Growth	3.2%	3.5%	3.5%	4.0%	4.5%	4.5%	4.0%	4.0%	3.5%	3.4%
Inflation Rate	3.0%	2.5%	2.2%	2.2%	2.2%	2.2%	2.2%	2.0%	2.0%	2.0%
Real Wage Growth	2.5%	2.5%	2.4%	2.8%	3.4%	3.4%	3.0%	3.0%	2.5%	2.4%

⁵ Since long-term population projections for Somaliland itself were not available, the pension simulations rely on population projections for Somalia. However, if the Government of Somaliland feels that the population structure of Somaliland is closer to that of another country covered in the UN statistics rather than Somalia itself, the World Bank pension tram would be happy to use that country as the basis of the demographic projections.

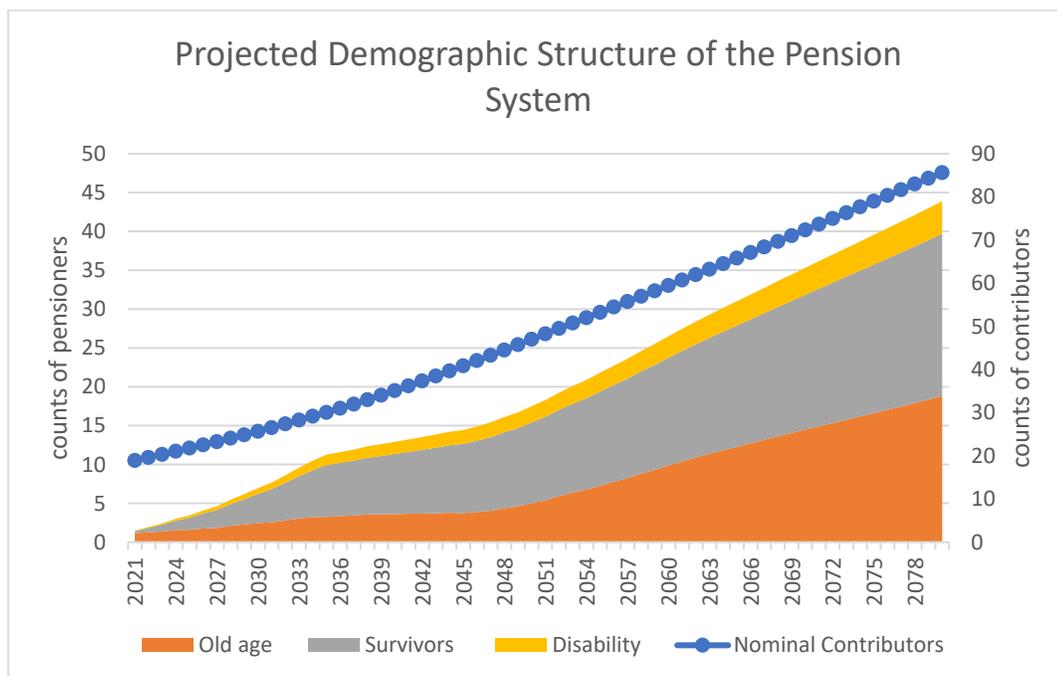
Source: Government of Somaliland and World Bank Estimates

Figure 2: Projected Life Expectancy at Retirement Age



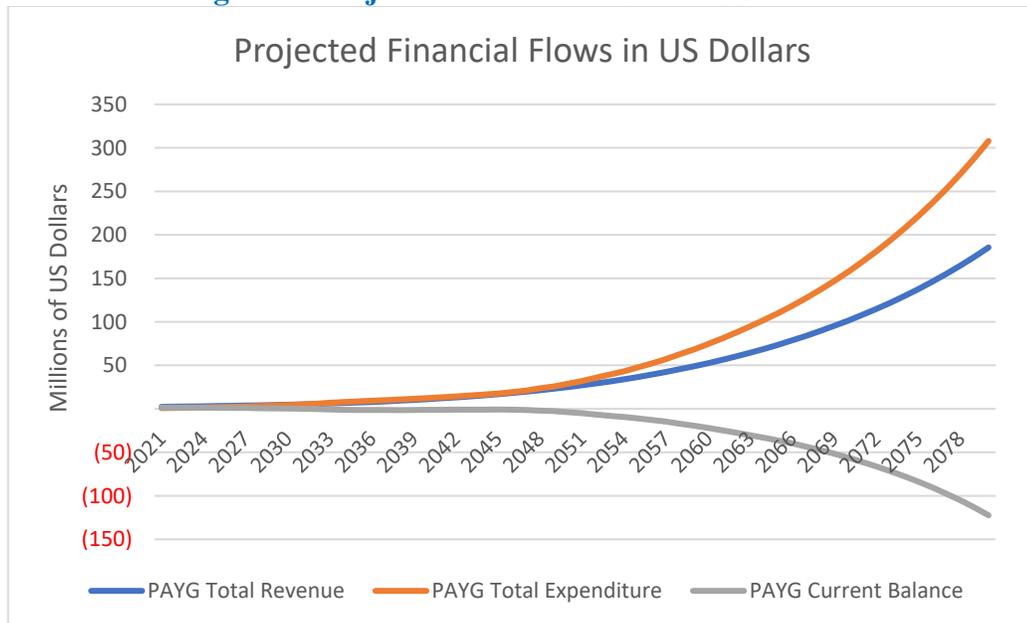
Source: PROST Projection using United Nations, Department of Economic and Social Affairs, Population Division (2019). World Population Prospects 2019, Online Edition. Rev. 1

Figure 3: Projected Demographic Structure of the Pension System



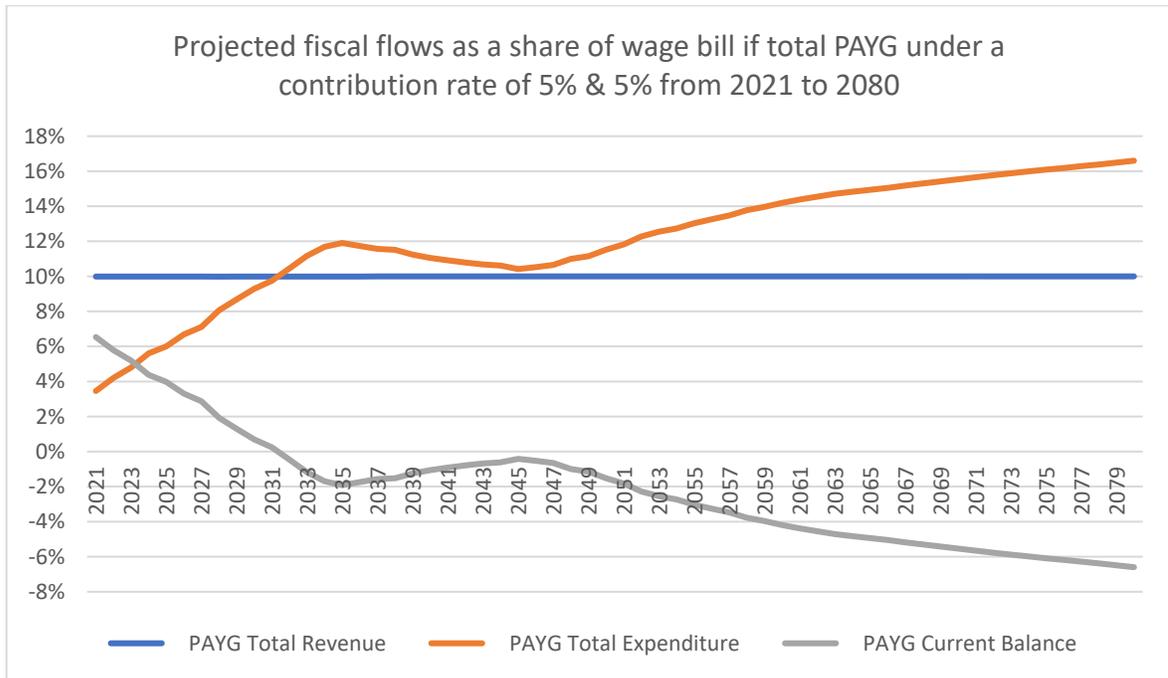
Source: PROST Projections using Administrative Data and UN population projections

Figure 6: Projected Financial Flows in US Dollars



Source: PROST Projections using Administrative Data

Figure 7: Projected fiscal flows under PAYG contribution rate of 5% each for employer and employee during the entire projection horizon



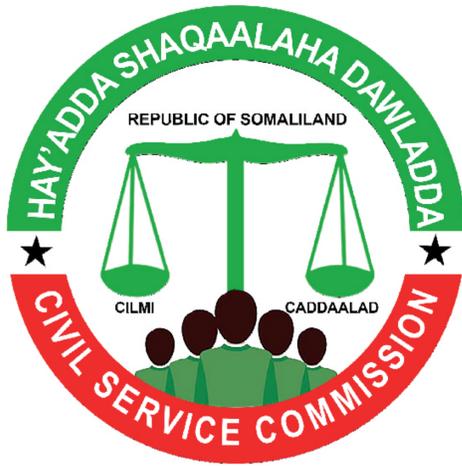
Source: PROST Projections using Administrative Data

Annex 2: Proposed Implementation Plan

Launching Somaliland Civil Service Pension System (number of month)

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	Comments
Modelling and forecasting of needs, deductions, size of benefits																		This activity is in progress, the Army data is not yet complete
Review of current Pension Policy and the Bill Include the pension policy analysis of fiscal implication and means of addressing them.																		Terms of Reference were drafted and shared with the TTLs to review.
Government internal discussions																		
Approval be the Cabinet																		
Ratification by the Parliament																		
Preparation and enactment of by-laws (if needed)																		
Development of regulations and procedures																		Detailed instruction (Guidelines) and regulatory documents to guide launch and operations
Public awareness campaign																		Public must be aware of the reform; retirees must know where to go and what to do.
Creating a database of retirees and connecting it to other Government databases																		Database has to be created before registering the Retiree
Registering retirees																		
Approval of regulations and procedures																		
Finding and fitting the premises for housing the Civil Service Pension Unit																		Room, computers, connectivity, etc.
Hiring and training relevant staff, technical advisors for the Civil Service Pension Unit, other ad hoc preparations																		CSC/PCU are working the JDs for the senior positions to the Office of the Pensions.

ⁱ This policy covers all public servants of the GoSL on permanent or terms contract of employment and state-owned agency employees.



SOMALILAND CIVIL SERVANTS' PENSION LAW