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Theme 237

THE NEW PENSION SYSTEM

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THEME 237 : THE NEW PENSION SYSTEM

A well informed customer will make the policy makers as well as organisations which produce goods and services more responsive to the customer needs. This will also result in healthy competition among organisations and improve the quality of goods and services produced.

The "SIB Students' Economic Forum" is designed to kindle interest in economic affairs in the minds of our younger generation. We highlight one theme in every monthly meeting of the "Forum". This month we discuss on the topic "The New Pension System".

What are the different pension systems prevalent in our country?

1. Defined benefit system – applicable to employees who have joined on or before December 31, 2003- where the onus of providing for pension benefits lies solely with the employer.
2. Defined Contribution system- applicable to employees joining service on or after January 1,2004 – even though the employer is making a contribution, the extent of liability is capped.
3. New Pension system- applicable to all Indian Citizens – the full fund comes from contributions made by subscribers.

What do you know about the New Pension System?

The Central Government introduced the New Pension System (NPS) with effect from January 01,2004 . The scheme originally covers the employees of Central Government and certain state government services, excluding Armed Forces. NPS is now made available to all citizens of India from May 01,2009. The system is an important milestone in the development of a sustainable, efficient and voluntary defined contribution pension system in India.

How does the new system differ from the benefit schemes?

1. Under the new system the pension will be fully funded.
2. The new system does not depend on the employer or the Government for making pension payments.
3. The full fund under the system will come from contributions made by the subscribers.

Who is the regulator of the New Pension system?
The New Pension Ordinance, promulgated by the President of India, calls for establishment of a Pension Fund Regulatory and Development Authority (PFRDA) as the regulator of the NPS. It is an autonomous body set up by Government of India to develop and regulate the pension market in India.

What is the major objective in introducing the ordinance?
By introducing the ordinance, the Government wants to bring down the financial burden and at the same time protect the interests of the subscribers. The pension pay outs and other commitments of the Government in this sector may significantly come down within a decade or two.

What are the objectives of PFRDA?
PFRDA was established by Government of India on October 10, 2003. The broad objectives of PFRDA are

1. Provide old age income
2. Provide reasonable market based returns over the long term
3. Extend old age security coverage to all citizens.

What are the major features of the NPS?
1. High yield 2. Tax benefits 3. Low charges 4. Protection

How does the System work?
The System is based on a unique individual Permanent Retirement Account Number (PRAN) created for each individual subscriber with nomination facility. A subscriber can periodically contribute savings into his /her Permanent Retirement Account and may utilise the funds accumulated to procure pension, on retirement, for the rest of the life. The above services are offered by PFRDA through eligible institutions, registered as Point of Presence –Service Providers (POP-SPs). The minimum annual contribution to NPS has been fixed at Rs.6,000 with minimum one yearly instalment. There is no upper limit on the contribution per instalment or on the number of instalments. A default charge of Rs.100 per year would be charged for default in instalment or in the minimum contribution of Rs.6,000 per year. A dormant account can be renewed by paying the charges and minimum contribution of Rs.6,000 per year.

The scheme has generated an average return of 12% in the first year of its operation, outperforming most of the long term savings schemes.

What are the operational guidelines of NPS?
There are two types of accounts namely Tier 1 and Tier 2 accounts available to

subscribers. Under tier 1, subscribers between 18 and 60 years can contribute their savings as retirement plan into a non- withdrawable account with income tax benefit under section 80 CCD. Tier 2 is a voluntary savings account, for those who maintain an active Tier 1 account, without any limit on the number of withdrawals. The minimum account balance at the end of financial year should be Rs.2,000 and one way transfer of savings to Tier 1 is available.

What are the minimum contribution requirements for Tier 2 accounts?

1. Minimum contribution at the time of opening should be Rs.1,000
2. Minimum amount per contribution should be Rs.250
3. Minimum number of contributions a year is 1.
4. Minimum number of contribution is one even in the case of a subscriber joining in the last quarter.

What are the charges prescribed?

- New account opening charges is Rs.60 for Tier 1 & Tier2
- Tier 11 activation charges for existing subscribers of Tier1 is Rs.40.

How is the corpus of the new pension scheme maintained ?

The corpus of the new pension scheme is equally divided amongst the six fund managers namely SBI Pension fund, UTI retirement solutions, IDFC Pension fund, ICICI Prudential fund, Kotak Mahindra pension fund, Reliance capital pension fund.

How does the new system differ from the traditional provident fund system?

Under the provident fund system, the contributions are invested under a rigid pattern with comparatively low returns. Under the new system, the subscriber can change the investment pattern based on the risk taking ability such as equity investments, balanced portfolios and risk free debt instruments.

What are the basic features of the new pension system?

1. Each subscriber will have an individual PRAN.
2. The Central record keeping agency will perform the functions of record keeping, accounting and switching over options of a subscriber.
3. The subscriber has a choice of multiple pension schemes and pension managers.
4. No explicit or implicit assurance of benefits except the market based guarantee.
5. A subscriber can exit from the system only as specified in the Central Government notification.
6. A subscriber shall purchase an annuity from a life insurance company (appointed by PFRDA for NPS) at the point of exit.

What are the functions of a Central Record keeping Agency (CRA)?

The PFRDA may appoint one or more central record keeping agencies by issuing certificates of registration. The agency will be responsible for receiving funds under the new system. The instructions from the subscribers shall be transmitted by the agency through the POPs. The agency helps to keep the administrative costs down, thereby enabling the subscribers maximise their savings. The Government ensures that millions of low value transactions are undertaken by the agency quite efficiently and effectively.

Explain the term "Point of Presence"?

The PFRDA may authorise one or more persons to act as Point of Presence for receiving contributions and adhering to the instructions from the beneficiaries. The contributions along with instructions are passed on to the Central Record keeping Agencies from time to time. The Point of Presence is the one appointed by the PFRDA to act in accordance with the terms of certificate of registration and the regulations made under the ordinance. Commercial banks are allowed to act as POPs on approval by PFRDA.

Who is authorised to act as" Pension Fund Manager"?

Generally the POPs may be allowed to act as Pension fund Managers. They are allowed to operate one or more pension funds as prescribed by PFRDA.

What is the "Swavalamban scheme"?

The scheme was launched on September 26,2010 for the benefit of the citizens in the unorganised sector who join the NPS with a minimum contribution of Rs.1,000 and maximum Rs.12,000 per annum. The Central Government will contribute Rs.1,000 every year upto 2013 - 14 to each NPS account under the scheme opened from April 1, 2010 to March 31, 2014.The benefit of the scheme has been made available to all NPS accounts opened during 2009-10 also within the above eligibility criteria.

What are the terms and conditions for exit from the scheme?

The exit from the scheme would be on the same conditions applicable for Tier 1 accounts subject to the overriding condition that the amount of pension to be annuitized should be sufficient to yield a minimum amount of Rs.1,000 per month. If the annuitized pension wealth does not yield an amount of Rs.1,000 per month, the percentage of pension wealth to be annuitized would be increased proportionately to yield pension amount of Rs.1,000 per month.

1. Exit at age 60 with 40% minimum annuitisation of pension wealth
2. Exit before age 60 with 80% minimum annuitisation of pension wealth.

Functions of POPs

- Addressing queries of potential subscribers regarding NPS.
- Providing and displaying PFRDA approved information/material on NPS.
- Verification of KYC documents.
- Collection of NPS applications with initial contribution and issuing receipts to the subscribers.
- Forwarding the application forms on a daily basis to CRA.
- On receipt of PRAN, uploading the contribution details into CRA system.
- Remitting the initial contribution to the trustee bank on receipt of PRAN allotment intimation.
- Carrying out changes in subscriber details on a regular basis.
- Receiving switch request for change in Pension fund manager or investment option from subscribers and transmitting the same to CRA.
- Receiving subscriber grievances against POP /other NPS intermediary in PFRDA prescribed format and uploading the same to Central Grievance Management System (CGMS) of CRA on a daily basis.

Your comments and feedback on this publication may be sent to Staff Training College, The South Indian Bank Ltd., Thrissur 680 001 or by E.mail: ho2099@sib.co.in

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