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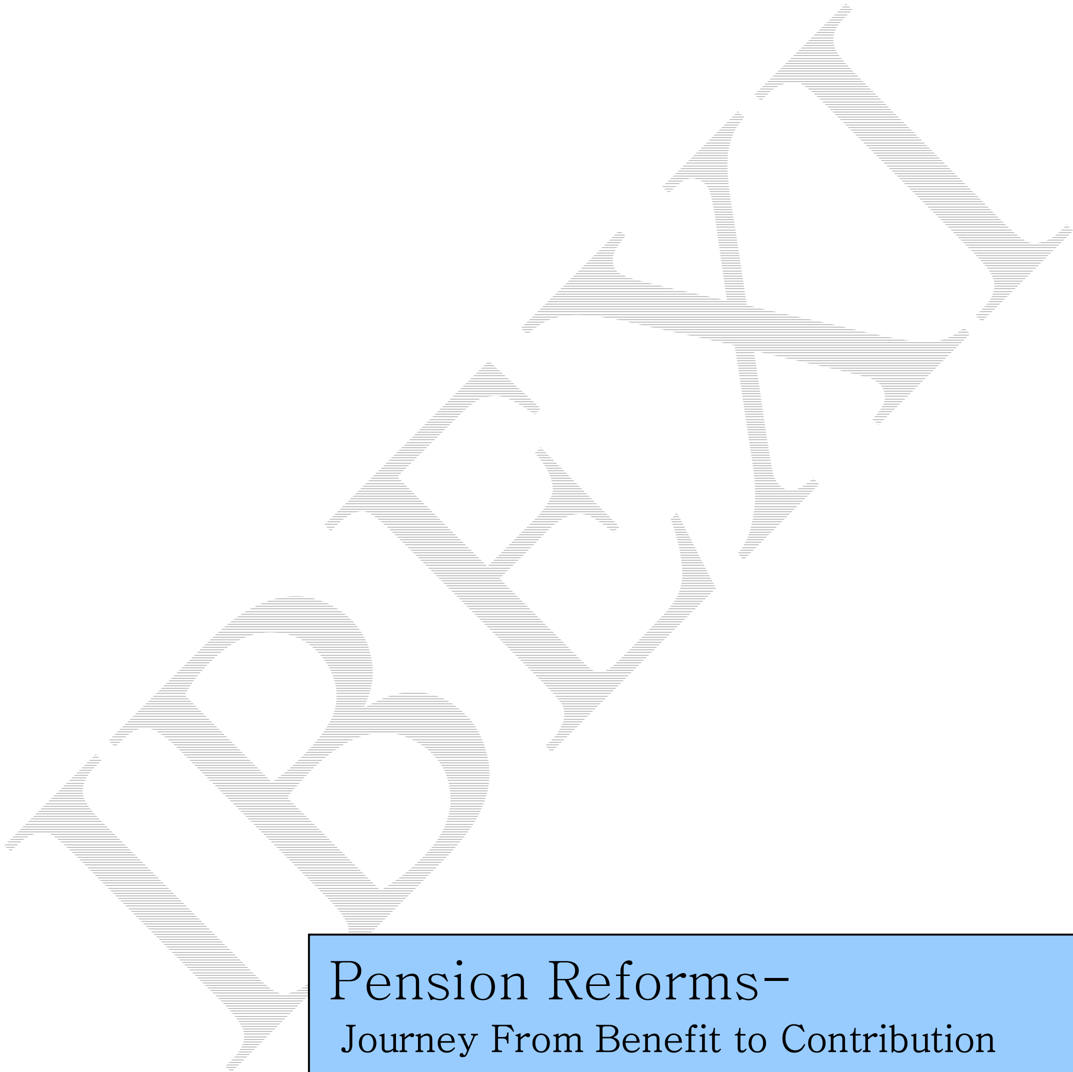

Pension Reforms-

Journey From Benefit to Contribution

Surajit Basu
Saiprasad Janakiraman

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Executive Summary

India has all the symptoms of the disease that has afflicted most countries – the financial problems of retired citizens. Meanwhile, Indian society is going through a transition. Consequently, people are increasingly looking at formal pension schemes to support themselves beyond retirement.

From 1998, there have been several efforts in thinking about reforming the Indian pension system. The pioneering effort was Project OASIS, set up by the Ministry of Social Justice and Empowerment in 1998. As they say, the winds have started blowing and more importantly in the right direction. It is a landmark decision in the area of pension reforms in India.
Reforms have been the buzzword for long, but what is the significance of these reforms?

The individual will have a concern about the safety of his funds and other concerns. Therefore like the IRDA, a regulatory authority called the PFRDA- Pension Fund Regulatory and Development Authority has been entrusted with this task under the New Pension Scheme.

One has to just wait and watch if these winds of change are accepted and channelised or just allowed to pass on and pass on….

The paper is a peek at the past, an analysis of the present and an expectation from the future. Reforms, Reforms and Reforms, the buzzword is in the air…..

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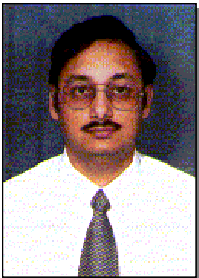
About the Authors



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Emerging environment

A growing problem

India has all the symptoms of the disease that has afflicted most countries – the financial problems of retired citizens. Thanks to better health-care, people live longer than before, and life expectancy continues to grow. Population is increasing, but the rate of increase has slowed down, the fertility rates are coming down. While India's total population is expected to rise by 49 per cent by 2016, the number of senior citizens aged 60 and above is expected to soar by 107 per cent to 113 million. A majority of them will need retirement security.

Meanwhile, Indian society is going through a transition. The traditional system where the parents lived with children is gradually collapsing. Thus, the traditional dependence on children as a means of support in old age is reducing. Consequently, people are increasingly looking at formal pension schemes to support themselves beyond retirement.

A formal pension system allows people to plan for a few decades of old age based on financial instruments instead of children. In such a scheme, there would be two phases: an "accumulation phase" and a "reduction phase". In the "accumulation phase", the individual is working, and makes steady contributions (i.e. payments) into the pension system. Upon retirement, the individual finds himself with a stock of wealth. This wealth can be used to buy an annuity, a life insurance product that gives a monthly payment until death.

Currently in India, pension schemes cover only a small fragment of the citizens. It is available to government staff, and to employees of large firms- typically industrial. Citizens in the large number of smaller firms, in the vast unorganised sector, in self-employed businesses, in the agricultural community are not

covered by any pension schemes. Typically, they depend on their children, and on their savings invested in regular income schemes.

Existing pension schemes are an unsustainable fiscal crisis. For example, the pensions for civil servants, and the EPS program, involve large liabilities for the government. The government does not have the fiscal strength to deal with these claims. Indian railways is another institution that is suffering from huge pension payouts, which currently amount to over 20% of the employee cost.

Most existing pension schemes were an extremely bad deal for participants. As the incomes of pensioners need to keep pace with inflation, the investments in the pension schemes must generate returns significantly in excess of inflation. The investment strategy across the pension system has been extremely restrictive, giving low returns. Often, the pension and provident funds have been used to finance the fiscal deficit. It is estimated that the real rate of return on provident fund assets is 2.5 per cent. The long-run average rate of return on the equity index in India is 18.5 per cent, far beyond the rate of return generated by Indian pension and provident funds. Artificial rates of return (e.g. for PPF) not in line with the generated returns of the investments have resulted in many schemes having liabilities which cannot be met out of their assets.

Additionally, there has been a history of very low standards of customer service, making it highly inconvenient for individuals to know where they stand, or exercise any control upon their assets. In some cases, morbid jokes of people dying before they could receive their overdue pensions have turned out to be tragic reality.

The problem of pension reforms consists of creating a pension system that can be accessible to all citizens of India, as opposed to a tiny group of organised

sector workers, and provide for old age at the price of the smallest possible pension contributions without the government paying pensions. It is expected that it would be possible to reform the pension system so that there would be

- Increased domestic savings
- Better management of domestic savings
- Reduction of poverty among the lower-income classes
- Improvements in customer service
- Additional external financial capital
- Greater strength in financial markets

Winds of change- First Signs of Reforms

From 1998, there have been several efforts in thinking about reforming the Indian pension system. The pioneering effort was Project OASIS, set up by the Ministry of Social Justice and Empowerment in 1998. The reforms World Bank and the IMF have prepared reports on Indian pensions. Also, a reforms project has been funded by the ADB to study the operations of the Employees Provident Fund (EPF).

The Old Age Income and Social Security (Oasis) project report of 1998 has been the cornerstone of thoughts of pension reforms. Led by Dr. S A Dave, a former chairman of UTI, the committee of experts recommended allowing pension funds and reforming the existing Employees' Provident Fund (EPF) and Employees' Pension System (EPS). Inspired and influenced by the 401(K) schemes in the U.S. and the experiences in other countries, the report focused on individuals planning on their own retirement and separating pension schemes from government. There should be transparency, and accountability in managing these funds. The government should desist from using the funds for infrastructure developmental purposes, and financing the fiscal deficit. Instead,

the funds should be allowed to go through insurance companies and private pension companies to the capital market, where they can generate better returns. Professional fund management, declarations of daily net asset values (NAV), and individual access to funds were essential elements of the report. Project OASIS also suggested that, for monitoring and control, an independent body - Indian Pensions Authority (IPA) be set up on the lines of the Indian insurance regulator.

Internationally, privately managed pension systems have resulted in high costs for sales, marketing, administration and fees of pension fund managers. Since each of these brings down the overall rate of return, and are extremely large, they cannot be ignored.. Since the total pension funds in India were expected to grow to extremely large amounts (estimated at 400,000 crores), Project Oasis made some recommendations for bringing down costs. The primary approach suggested was having two different methods for administration and fund management. Since administration is low-value-adding and works purely through efficiency of scale, the report recommended the creation of a single public agency for record-keeping functions, and the use of depository offices, bank branches, post offices for distribution and collection. For fund management, it suggested a finite list of six pension fund managers based on a bidding system; they would have to pre-commit to fees and expenses in a national auction. The OASIS report recommended that like mutual funds, pension funds would offer at least three types of schemes — safe income, balanced income and growth. It had also suggested fund management fees of 0.25 per cent for all types of schemes.

Other important recommendations included shared costs for training and education between the pension fund companies and the IPA. There was also suggested, a disincentive for withdrawal. Under the 401(k) plan of the USA, savings are taxed only when there is a withdrawal. Similarly, Project Oasis also

recommended a 10 per cent tax on premature withdrawals from the retirement account.

Players in the market- More takers to the pie

The Indian pension market has been restricted, and limited by regulation. Only the Life Insurance Corporation (LIC) is allowed to administer pension funds on behalf of organizations. It is possible to outsource the pension member administration to companies such as India Life Pension Services. However, private life insurance companies, private pension companies and mutual fund companies are not yet allowed into the pension market.

The life insurance market has been opened with the first batch of licences being issued in late 2000. This has led to a flood of new life insurance companies. These include
HDFC Standard Life, ICICI Prudential, OM Kotak Mahindra (OM-KM), ING Vysya Bank, Max New York Life, Birla Sun Life, Reliance, SBI Life and Allianz Bajaj. A few other companies are also planning to join the growing list. These companies can offer life insurance products – both traditional and unit-linked, as well as single premium products and annuities.

The key attractions for the life insurance business have been growth – estimated at 18-20 per cent – availability of funds, and synergy with other financial operations (banks, mutual funds, loans). The attractions for the pension business are similar, though much more magnified. The growth is forecast at 30 per cent; and the amount of funds available would be staggeringly large (400,000 crores).

Therefore, all the new life insurance companies are potential players in the pension fund business. Mutual funds and banks are also eyeing the huge market and claim to be equipped to manage the pension funds.

Companies such as HDFC and ICICI have been repeatedly announcing their intention to enter the pension fund business on pension reforms.

It is worth noting that none of the players suggested the creation of the depository-style national administrator envisaged by Project Oasis. Each of them so far planned to administer their own products, and service their own customers, with a view to create a differentiation based on customer service, sales and marketing. Also, each believed that one of the strengths they would bring was their existing customer base, and their sales and marketing skills. Internationally, the margin in pension administration businesses has been very low; the profits typically come from fund management. While Project Oasis recommended 0.25 per cent fund management fees, AMFI has suggested a 1 per cent fee for safe income, 1.25 per cent for balanced fund and 1.5 per cent for growth-funds.

Another contentious point was about portfolio management, mainly in the composition of pension funds. Countries such as the United Kingdom and the USA largely follow the prudent man concept: the pension fund manager has investment freedom and can decide prudently where to invest. Mutual fund industry experts in India are of the opinion that the same practice should be followed. Once the fund manager is selected, choice of assets should be left to him and true, investment quality, investment merit and returns should be the considerations for designing a pension funds portfolio.

Arguing that regulatory chains should be replaced by market forces such as elasticity of demand and supply, these experts also claimed that the market forces should be the arbitrator for deciding the number of players, fee structures, costs and distribution. The government should define norms for capital adequacy, transparency, disclosure and delivery standards and create a powerful regulator. The players should compete in the marketplace and the fittest will survive. Only those who provide competitive products with adequate distribution and marketing will survive. Life insurers, banks, and post offices will be driven by market forces to create networks for the points of sale and collection.

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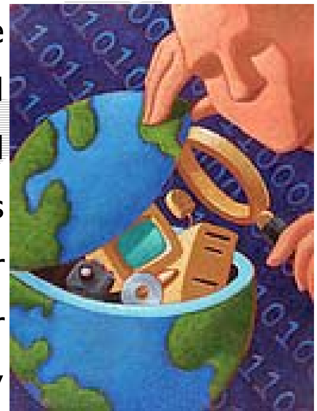
Current products

The current products, which will continue and grow in the short term - are the current schemes for gratuity, superannuation, and annuity. The first two are currently offered only by LIC. UTI was allowed to enter the annuity market in 1997. All the new life insurance companies under the file-and-use product scheme can currently offer annuities.

Annuity products are useful for retirement benefits. They offer periodic payments (usually monthly) for the lifetime of an individual (the annuitant) or the individual and his or her designated beneficiary. An annuity may be a fixed or varying amount, and may continue to be paid for a period after the annuitant's death. Annuity products – variable and fixed – may also offer provisions for premature withdrawal. These are useful for deposits for retiring citizens, who have a fixed sum of money to invest. The source of this money may either be the pension amount built up over the working period, the savings maintained in a retirement fund, or a special amount available as part of a Voluntary Retirement Scheme.



One of the advantages of the annuity product is that these products do well even in a falling stock market. For instance, in third quarter 2000 in the U.S, almost all the insurance companies reported large increases in annuity products. American General, John Hancock Financial Services, the Hartford Financial Services Group, Jefferson Pilot and Nationwide Financial were among the companies reporting growth.

In India, LIC offers an Immediate Annuity Plan (Jeevan Akshaya). This offers annuity for life, ceasing on death or payable for fixed periods (5,10, 15 or 20 years) and thereafter as long as the policyholder is alive. It also offers as an option a return of purchase price on death of the annuitant to a beneficiary. Another option is a variable annuity amount, increasing at a simple rate of 3% per annum, which is extremely low, given the inflation rate in India, and the fact that the inflation is a compounding factor, while the increase offered is a simple interest rate. Thus, on a real rate, there is a very large drop in annuity amounts payable each year; over 10 or 20 years, this drop is substantial. A variation that LIC offers is a deferred annuity (Jeevan Dhara), which allows the individual to pay in instalments over a period of time to build up his balance. However, returns in this scheme are also not comparable with returns in capital markets. (See Appendix 2: LIC Immediate Annuity Scheme, Appendix 3: LIC Deferred Annuity Scheme).

Since annuities and single premium policies are not - strictly speaking - pension products, they are already open to the life insurance companies under the file-and-use policy. Many of the new private insurance companies are beginning to offer annuities, especially targeting those who have opted for VRS, or have access to a large lump sum, and can therefore pay a large single premium policy. With increasing competition, it is expected that competition in the annuity market will push up the rates of return offered.

Gratuity is a statutory benefit for employees of organizations above a pre-defined size. For every year of service (above a minimum period), the employee is entitled to 15/26 of the last drawn monthly salary. This is distributed on the employee's retirement, resignation or death. However, the liability to the employer accrues every year. From the point of view of sound accounting practice, it is desirable to provide for this liability before the profits are

determined. The Group Gratuity Scheme offered by LIC provides an actuarial method for funding gratuity liability as the premiums paid by the employer are based on actuarial principles. Additionally, life insurance cover to every employee is bundled in the same product; in the event of the premature death of an employee, his dependants become entitled to substantially higher benefits than the statutory gratuity amount. The funding of the Gratuity benefits can also be made on Cash Accumulation basis; in such a case, the fund is accumulated at an attractive rate of interest. Advantages of tax are available to both the employer and the employees.

Several private companies plan to introduce a similar product. Though this product has grown slowly in India (pension products currently are estimated to account for a mere 3% of LIC's revenue), it has high growth potential. This is a defined benefit product, typically with long-term liabilities which are unmatched by the fund's assets. The low rate of return on pension funds caused by the constraints on investments has also not helped in managing such products. This product could have a few risks, especially in a scenario where the employee salaries rise fast. In India, in many sectors, especially those that are more global in nature (e.g. financial services, IT), the salary increases have been quite dramatic, leading to a very high rate of increase in gratuity amounts. If the insurance companies were to absorb such risks instead of just managing the funds, this product can have damaging long-term impact on a new insurance company's portfolio. So, it is likely that private companies will offer a product structurally similar to the one offered by LIC with marginally better returns, offering better customer service.

Superannuation: LIC's Group Superannuation Scheme is designed to provide pension to the employees on their retirement. The scheme may be financed by the employer alone or jointly with the employees. A decreasing group insurance

cover in conjunction with superannuation benefits may also be provided under the scheme. There are two variations within this: a Money Purchase scheme and a Benefit Purchase scheme. In the former, the contributions are fixed generally as a percentage of salary. The accumulated value of such contributions is utilised to purchase the pension of appropriate amount. In the latter, the employer fixes the amount of pension in advance generally in relation to the salary drawn by the employee at the time of exit. LIC determines the contributions payable for funding of pension benefits. Different types of pension are available under LIC's scheme such as Pension payable for life, guaranteed for 5, 10, 15 or 20 years and thereafter for life, Joint life last survivor pension, Pension payable for life with return of Purchase Price on death of the pensioner etc.

New products

While the current products fall largely under the category of defined benefits, the new products expected to emerge will fall largely under the category of defined contribution. In all of these, the deposited amounts / contributions for each individual (employee/ scheme member) will be used to purchase units of the scheme. The funds will use a combination of government papers, bonds, and equities. The individual's retirement account will depend on the returns of the fund in which it is invested. There are likely to be 3 forms of such products; it is likely that there will be a set of companies, each offering similar products. The individual will be able to choose how much to invest into each product and also be able to choose the specific company for each type of fund.

Safe Income: In this scheme, the investment will be largely in the government paper (>50%), with investments allowed into corporate bonds (around 30%),

and very limited amounts in domestic equity (<10%). Equity investments are likely to be only in Stock exchange index-linked funds, and not in any specific sector (e.g. FMCG, Tech) or specific companies.

Growth: This will be a high-risk, high-return scheme, where the equity exposure may be as high as 50%. Even foreign equity may be allowed, probably up to 10%. All forms of equity exposures – index-linked, sector-linked, specific companies – will be allowed over a period of time. Initially, investments into equity may be based only on index-linked funds. Corporate bonds and government bonds will be used to ensure a limit to the risk; each such investment class will probably be limited to 25%.

Balanced Income: Between the two schemes, the Balanced Income scheme will provide less risk than the Growth scheme with an almost uniform spread between domestic equity, government bonds, and corporate bonds. There is likely to be a cap of 30% on equity investment of less than 30%. Minor exposures into international equity may be allowed, say 5%.

In summary, the defined contribution schemes may be represented as follows:

Investment Class	**Safe Income**	**Balanced Income**	**Growth**
Government Paper	>50%	>30%	>25%
Corporate Bonds	>30%	>30%	>25%
Equity	<10%	<30%	<50%
International Equity	Not allowed	<5%	<5%

Features across all products- Expectations during the first phase

One of the key features of all these schemes will be portability. It is likely that there will be full portability across schemes, and across companies. Thus, if the individual is transferring funds from one scheme to another, or from one company to another, the full amount will be transferable. Also, the rules governing such transfers will be different from withdrawals/ deposits, even though from the perspective of the fund manager, the two types of transactions are similar. Thus, there will probably be no entry or exit loads as mutual funds typically have. Early withdrawals will be subject to taxes on withdrawals, probably tax deductions at source; transfers will not be taxed. Similarly, deposits into a scheme will not get tax breaks if they are merely transfers. To meet the costs of the transactions for transfer, it is possible that there will be fixed charges for transactions for transfer of funds across schemes. In order to ensure that the lower-earning citizen is not affected, these will probably come into force only for the high-growth scheme; also a few transactions will probably be allowed at no cost. Thus, there may be conditional clauses for charges such as "charges apply if there are more than 3 such change transactions in one fiscal year" or "1 charge per quarter is available at no cost".

One of the related issues for portability would be member tracking. Members need to be tracked if they move across schemes, employers (who may be contributing to the pension account), or even across fund managers. Since this would be related to the income-tax deferred and payable by the individual, a unique member id would be required for managing this. This is likely to be the PAN number given by the income tax department. For non tax payers, a new

number will have to generated and used across all the systems whenever the individual moves across schemes or fund managers.

Statutory reporting will be a critical requirement for all the pension fund managers and the depositories. Since one of the requirements for each company in the pension system will be full computerisation of individual accounts, it is likely that systems implemented have to provide all the statutory reports; this may be driven either by business efficiency or regulation. These reports include those for tax accounting and for compliance reporting for investments. There is likely to be a much stricter implementation of these rules than currently for banks, mutual fund companies, and current EPF and PPF accounts. It should be noted that portability and compliance reporting are some of the key criteria for pension systems worldwide, and it is likely to have the same importance in India.

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Market Segments

The first wave

Pension schemes tend to be ambitious in their sweep; the aim is to cover the entire citizenry of the country. The Oasis scheme, which is the basis for the reform process, targeted everyone from the daily wage earner to the self-employed to the employed. Reaching out to the Indian masses with a mix of distribution channels, with a strong emphasis on the existing network of post offices and bank branches, it sought to cover everyone.

As the private sector will be entering pensions, it will first focus on the more profitable segments of the market where the expenses of sales and marketing, consumer education, and administration will be low, and where the availability of funds will be high. This may seem like an unsocial attribute of what is primarily a social security solution; but we can see the reality of the situation by looking at related sectors and their expansions. Private sector banking started with a focus on the metro areas, and has largely focussed on the urban populace. New private sector insurance companies have focussed on urban centres and industrial areas. Similarly, it is expected that the first wave of pension segments will be the existing market: corporate employees and the self-employed in the urban areas. While there may be some element of rural savings in the first wave, the rural poor will largely be unaffected.

The immortals versus the mortals: The OASIS report talks about the retirement age (60) and the minimum total contribution by an individual (Rs.2 lakhs). It does not mention any upper age limit other for the accumulation phase other than 60. The minimum annual contribution is Rs 500 at current rates, which would mean a 20-year accumulation period. This figure of Rs.500 could be

assumed to be indicative of daily wage earners in the unorganised sector and dependant persons. Hence in this sector entry level customers are not likely to be over 45 years old. (Typically in the daily wage sector incomes peak around 35 and start falling after 45). As income levels rise this entry age moves upwards. The Dave Committee also recommends that the tax-free limit for accretions into the IRA should continue to be a maximum of Rs.60,000 per annum. Which indicates an age limit of 56.

Where do we draw the lower line? Thanks to the decimal system, people tend to consider the age of 30 as a cut off between immortal youth and worrisome middle-age. However given the immature dependency of Indians on their parents there still could be enough 25 year olds- especially those who work in large safe corporations- who would let themselves be influenced to subscribe to pension plans Early marriages would also motivate younger people to look for pension plans. With similar reasoning we could arrive at the following table:

Market segment	Minimum age of entry	Most likely age of entry	Maximum age of entry
Employed	25	30	56
Self-employed	25	30	56
Unorganised sector	20	25	45

The earlier the entry age, the more risk the person will be ready to take. Pension schemes have to be appropriately designed and targeted.

Gender bender

The failure of current pension systems to provide an adequate income for women in later life

- the 'pensions problem' for women - emerges starkly from virtually every report on pension

income. The high risk of poverty that women pensioners face has been well documented.

The World Bank, in its 1994 report *Averting the Old Age Crisis* stated that old age means
something quite different and more troubling for women than for men (World Bank,
1994: 29). Pensions problem for women stems from their different life course experiences in combination with a pension system that was not designed to meet women's needs. Governments have been quick to identify how behavioural differences between women and men, in labour market participation and in the division of caring labour, impact upon income in old age. They are, however, more reluctant to examine those features of pension systems that perpetuate the economic advantages and disadvantages experienced during the working life into inequality in old age.

Women's participation in the labour market is distinct from men's in **several** respects.

Overall, women are less likely to be in paid employment. Where women are in the labour
market they are more likely to be working part-time, especially if they have young children or care for a dependent adult. The pay penalty experienced by women includes both a gender gap (affecting all women) and a family gap (which results from women' s experience of motherhood)

Men' s earnings profile is humpbacked, suggesting that men benefit from an age/experience premium in their middle years, whereas women have a much flatter earnings profile which reflects the impact of interrupted employment patterns and labour market segmentation

Women are concentrated in parts of the labour market with less access to occupational pensions. Where occupational pensions are a major part of overall pension provision, occupational segregation of women is important. Small

firms and those in certain sectors such as personal services are less likely to offer occupational pension coverage. Further, where

employers limit the membership of schemes and exclude part-time workers or those on short-term contracts, women are disproportionately affected

Women live longer than men Women' s greater longevity means that women are more likely to be widowed in later life and to live alone, losing the spouse' s contribution to household income *and* the principal source of care-giving. Greater longevity means income is needed to cover a longer period, recognised by insurance companies who use sex-based annuity rates.

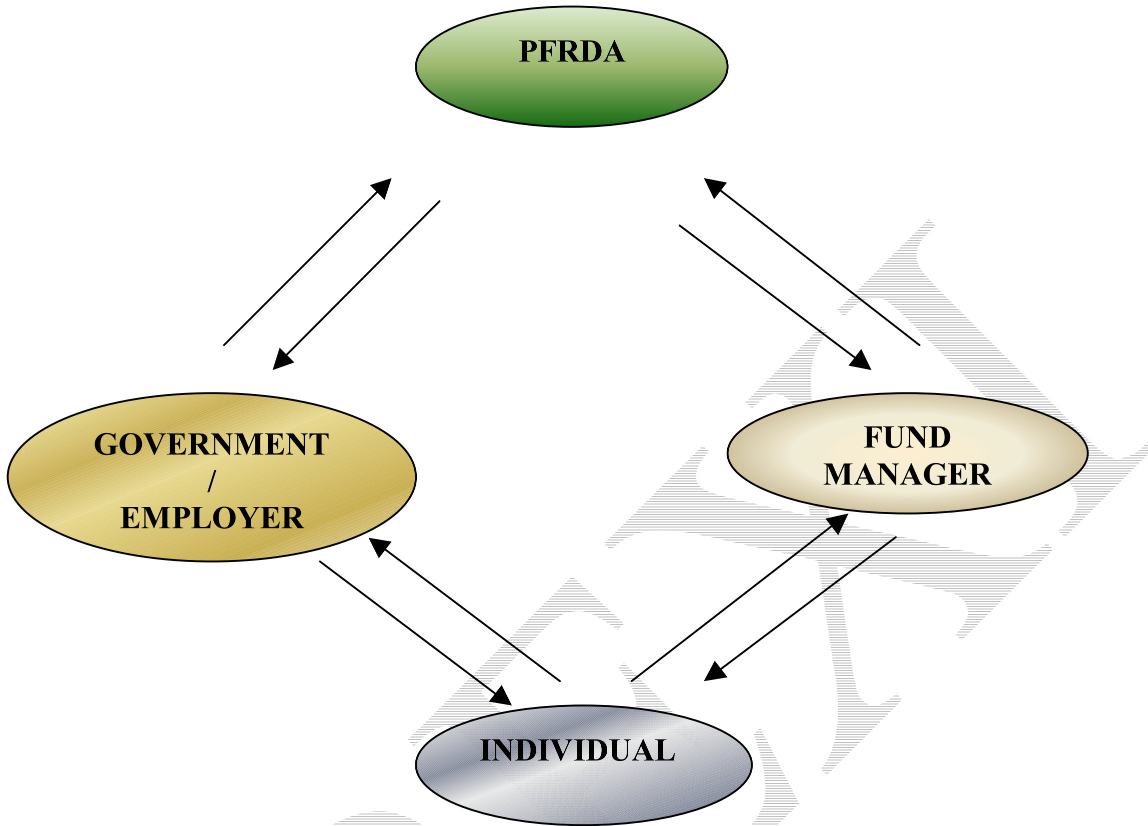
Oasis-like schemes would ideally suit women as the flexible annual contribution would suit them in the years when they are out of employment. Under current tax schemes a person can obtain tax benefits for insurance premier paid by on behalf of dependants. If this facility is extended to the pension market, more women would enter the market as subscribers.

Varnashram

Will the tinker, the tailor, the soldier and the spy back the same horse? Most unlikely not. Given the same annual income levels, a wage-earner is less likely to subscribe to a high risk fund than a businessman, especially in low to medium income levels. Self-employed professionals like doctors would maybe subscribe to a balanced fund.

Again place determines risk taking ability. People living in metropolitan and urban areas are normally the first victims of rampant consumerism, which tends to increase their liabilities and hence their risk-taking ability. This works for the unorganised sector also. People who are on the fast track and fear middle age burnout would also be willing to gamble on their old age funds. This would include frequent job-changers and yuppies- but however it is likely that they might be late entrants into the market.

Winds of change- Milestone 1….



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As they say, the winds have started blowing and more importantly in the right direction. It is a landmark decision in the area of pension reforms in India. Reforms have been the buzzword for long, but what is the significance of these reforms? It is the first time that any such reforms have been tried on government employees. Pension for government employees was based on their last drawn salary. As reiterated in this article, there was a tremendous burden on the fiscal reserves of the nation as a result of such appeasement policies. Recently, the decision to hike PF interest rates to 9.5% has not been appreciated by a lot of economists. This is because, the government plans to dig into the PF reserves in order to fund the deficit caused. So the step of this reform is seemingly the right step.

Starting January 1st 2004, all new entrants to the central government service will not get a fixed, inflation-indexed pension on their last drawn salary. But according to the new pension scheme, 10% of their salary would be directed towards a privately managed pension fund. The individual resumes responsibility for his / her savings and thus becomes his or her own fund manager in some ways. In the yesteryears, the retirement savings grew at the administered rate announced by the government. In this new pension scheme, the returns that an individual may get would depend upon the performance of the retirement funds .i.e. the performance of the private fund managers who would be handling the fund. Unlike the fixed returns scheme, the individual in this case would know the amount he would contribute, but not the amount that he would get eventually as returns.

Like mutual funds, the individual would get three options or three types of funds, to be more precise three sets of standardized options. The growth option wherein

the major chunk of the individual's funds would be invested in equity, the balanced option which would mean equitable investment in equity as well as debt and finally the conservative option which would be dictated by a major portion invested into debt.

The individual has the funds and makes the contribution. The logical question that would arise is who would handle the funds? The funds would be typically handled by private pension fund managers. These companies would be typically established names in the insurance and mutual fund industry like LIC, HDFC, Templeton, etc. These companies would be in a position to operate and service once they would have obtained PFRDA- Pension Fund Regulatory and Development Authority. The PFRDA as a body would be discussed later in this paper.

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One can look at the **advantages to the subscriber** in terms of the following;

Manage one's own funds: the individual will have the freedom to invest in any of the options mentioned and hence choose which way his returns would go depending upon his objectives of saving, growth or balance.

Portability: the individual would have one reference number throughout his life which would mean that he would be operating the same account irrespective of how many jobs he would change throughout his life. A central record keeping agency would keep a track of all the transactions that the individual would make regarding the same.

Access: the individual would be able to access all his records very easily. All transaction would be enabled through the internet and hence checking one's investment scenario and other concerns would be beyond time and spatial constraints,

Switching loyalties: It would be necessary for the fund manager o provide the individual with regular updates on the Net Asset Value (NAV) of the individual's funds. Since the individual's transactions would be maintained in a certain placed, he would be able to switch fund managers if he finds any issues with their performance.

Retail outlets: the individual would also be in a position to make contributions through post offices, banks, etc.

Change Pension Options: At a nominal cost, the individual would be allowed to make a certain number of changes (during a stipulated time period) in his fund options.

The next issue that arises is who is covered under the term **"individual"**

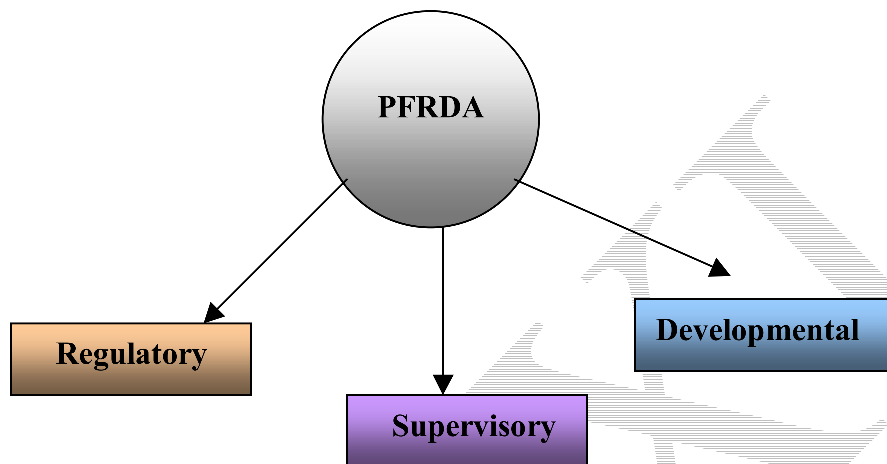
New government employees joining work from 1 January 2004 would be mandatorily covered by the scheme. They will now have two accounts: mandatory and voluntary. In the former account, their mandatory pension contributions will be lodged along with a matching contribution from the government. Contributions to the voluntary account will be flexible but the government will not match the contribution—something like the GPF.

Non-government employees like those in the private sector, the self-employed, and unorganised sector workers will also be able to participate in this scheme by having the same dual accounts, but with no government contribution—employer contribution in the voluntary account will depend upon the employer.

The individual will have a concern about the safety of his funds and other concerns. Therefore like the IRDA, a regulatory authority called the PFRDA-Pension Fund Regulatory and Development Authority has been entrusted with this task.

IBEXI

PFRDA : Pension Fund Regulatory and Development Authority



The **objectives of the PFRDA** would be typically:

- Protection of the rights and interests of consumers.
- Formulation of policies and legislations to ensure not regulation and supervision but also tap opportunities that would benefit the consumer.
- There would also be a developmental objective for the PFRDA to ensure that the transition from a government managed pension scheme to a self managed pension scheme is a smooth and successful one.
- The PFRDA would also look at fixing the roles and responsibilities of different facets of the pension scheme i.e. the pension fund members, the pension fund managers, trustees, etc.

Role of PFRDA

- License, regulate and supervise the functioning of the pension fund managers.
- Supervise and regulate personal, group pension and gratuity based funds.
- Ensure protection to all by ensuring that security of pension funds is not put to risk and also press upon sound management practices.
- Unlike previously, PFRDA as a regulatory authority has top pay a more proactive role rather than a passive role. This would mean anticipating problems in the system and solving them, don the developmental role aggressively and clamp down heavily on bad governance and inefficiencies,

Immediate Task before the PFRDA

- The interim PFRDA would - draft the Bill for establishment of the PFRDA by an Act of parliament. The act would have to cover aspects such as the powers, roles and responsibilities of the PFRDA, finances, etc.
- With regards to the fund managers the Act would need to specify the eligibility criterion for the promoters for pension fund managers, specify their roles and structures, if Pension Fund Manager is a separate entity, its shareholding structure, minimum capital requirement and ceiling on foreign equity.

Conclusion

Well winds of change may also indicate **rough weather**:

The conservatives have always wondered what the role of the government was in the modern era. If they are sure of one thing, it is always that government is paternalistic and hence, responsible for long term provider of stability and equity. The present system they feel is a nice way for the government to absolve itself of this role in providing social security. What is the role of the PFRDA when the IRDA already exists? With more and more financial companies moving into insurance offerings, the portfolio of these entities is ever widening. Hence, there are some cynics who feel that there is just a duplication of what the PFRDA would do when he IRDA is capable of doing the same. Separation of pension funds from insurance may result in greater "foreign interference".. in financial terms we refer to it as FDI. Though the limit is 49% in insurance, this separation may mean a hijacking of one's social security funds. The risk of losses due to exposure may mean no pension payable, loss of all future earning, etc…

The cynics keep saying, they keep protesting. If democracy means coalition pressures dictating economics, then the proposed reforms would stay as just proposed. One has to just wait and watch if these winds of change are accepted and channelised or just allowed to pass on and pass on..

The world is closing in
Did you ever think
That we could be so close, like brothers
The future's in the air
I can feel it everywhere
Blowing with the winds of change

- The Scorpions