

**MINISTRY OF FINANCE**  
**DEPARTMENT OF ECONOMIC AFFAIRS**

**PRESS RELEASE**

**SUBJECT: Operationalisation of the budget announcement 2003-04 on new pension system.**

The Government approved on 23<sup>rd</sup> August 2003 the proposal to implement the budget announcement of 2003-04 relating to introducing a new restructured defined contribution pension system for new entrants to Central Government service, except to Armed Forces, in the first stage, replacing the existing system of defined benefit pension system. The new system will also be available, on a voluntary basis, to all persons including self employed professionals and others in the unorganised sector. However, mandatory programmes under the Employee Provident Fund Organisation (EPFO) and other special provident funds would continue to operate as per the existing system under the Employee Provident Fund and Miscellaneous Provisions Act, 1952 and other special Acts governing these funds.

2. The Government approved the basic features of the new pension system; and setting up of an interim pension fund regulatory and development authority (PFRDA).

3. The main features of the new pension system are given below:

- The new pension system would be based on defined contributions, which will use the existing network of bank branches and post offices etc. to collect contributions and interact with participants allowing transfer of the benefits in case of change of employment and offer a basket of pension choices.
- The system would be mandatory for new recruits to the central Government service except the armed forces and the monthly contribution would be 10 percent of the salary and DA to be paid by the employee and matched by the Central Government. However, there will be no contribution from the Government in respect of individuals who are not Government employees. The contributions and investment returns would be deposited in a non-withdrawable pension tier-I account. The existing provisions of defined benefit pension and GPF would not be available to the new recruits in the central Government service.
- In addition to the above pension account, each individual may also have a voluntary tier-II withdrawable account at his option. This option is given as GPF is proposed to be withdrawn for new recruits in Central Government service. Government will make no contribution into this account. These assets

would be managed through exactly the above procedures. However, he would be free to withdraw part or all of the 'second tier' of his money anytime. This withdrawable account does not constitute pension investment, and would attract no special tax treatment.

- Individuals can normally exit at or after age 60 years for tier –I of the pension system. At exit the individual would be mandatorily required to invest 40 percent of pension wealth to purchase an annuity (from an IRDA-regulated life insurance company). In case of Government employees the annuity should provide for pension for the lifetime of the employee and his dependent parents and his spouse at the time of retirement. The individual would receive a lump-sum of the remaining pension wealth, which he would be free to utilise in any manner. Individuals would have the flexibility to leave the pension system prior to age 60. However, in this case, the mandatory annuitisation would be 80% of the pension wealth.

### **Architecture of the New Pension System**

- It will have a central record keeping and accounting (CRA) infrastructure, several pension fund managers (PFMs) to offer three categories of schemes viz. option A, B and C.
- The participating entities (PFMs and CRA) would give out easily understood information about past performance, so that the individual would be able to make informed choices about which scheme to choose.

### **Regulatory Authority**

- An independent pension fund regulatory and development authority (PFRDA) will regulate and develop the pension market. PFRDA will develop its own funding stream based on user charges.
- Till such time when a statutory PFRDA is established, an interim PFRDA, on the pattern of SEBI and IRDA, should be appointed by an executive order.
- The interim PFRDA is to be headed by a Chairman with a status of not less than a Secretary to the Government of India and would be appointed by the Central Government. Other members of the interim body, not exceeding four in number, of whom not more than two shall serve full time, shall be selected by the Central Government from amongst persons having experience and knowledge in economics, finance, legal and administrative matters with one person from each discipline.

### **Investment strategy**

- There will be different investment choices such as option A, B and C. The option A would imply predominant investment in fixed income instruments and some investment in equity. Option B will imply greater investment in equity. Option C will imply almost equal investment in fixed income and equity.

- Pension fund managers would be free to make investment in international markets subject to regulatory restrictions and oversight in this regard.
- It is proposed to evaluate market mechanisms (without any contingent liability) through which certain investment protection guarantees can be offered for the different schemes.

### **Tax treatment**

- Pension contributions and accumulation would be accorded tax preference upto a certain limit, but benefits would be taxed as normal income

### **Scope of the New Pension System**

- The option of joining the new system would also be available to the State Governments and as and when they decide, the new system would be capable of accommodating the new participants.
- Mandatory programmes under the Employee Provident Fund Organisation (EPFO) and other special provident funds would continue to operate as per the existing system. However, individuals under these programs could voluntarily choose to additionally participate in this scheme.

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**New Delhi, dated August 27<sup>th</sup>, 2003.**

The Press Information Bureau is requested to give wide publicity to this Press Release

**(U.K. Sinha)**

**Joint Secretary to the Government of India**

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