## Pension reforms

2.43 In India, retirement benefits, in one form or the other, are currently available to only about 11 per cent of the working population, including Government employees. This leaves 89 per cent of the working population in the unorganised sector uncovered by any formal pension provision. Unfunded pensions have been a major fiscal drag worldwide. The pressure of pensions on Central and State finances is becoming increasingly burdensome. The total pension outgo in respect of Central Government employees as a proportion of GDP, after rising from 0.38 per cent in 1990-91 to 0.74 per cent in 1999-2000, declined to 0.56 per cent in 2003-04 (RE). The outgo in absolute terms increased from Rs.2,138 crore in 1990-91 to Rs.15,367 crore in 2003-04 (RE). As a proportion of net revenue receipts, expenditure on pensions after increasing from 3.9 per cent in 1990-91 to 7.9 per cent in 1999-00, started declining from 2001-02 to reach 5.8 per cent in 2003-04(RE). The compound annual average growth rate of the pension outgo of the Central Government was 21 per cent during the 1990s. Pension payments at the State Government level have also risen sharply during the last 10 years. The annual average increase in pension outgo for States during the late 1990s was 27 per cent. Pension expenditure of States as a proportion of revenue receipts rose from 5.4 per cent in 1990-91 to more than 10 per cent in 2000-01.

2.44 In the Budget for 2003-04, Government announced the introduction of a new restructured defined contribution pension system applicable, in the first stage, to new entrants to Government service, except armed forces. Accordingly, the New Pension System (NPS) was introduced from January 1, 2004 for Central Government employees recruited on or after that date. The NPS will be available, on a voluntary basis, to all persons including self-employed professionals and others in the unorganised sector. However, mandatory programmes under the Employees' Provident Fund Organisation (EPFO) and other special provident funds continue to operate as per the existing system under the Employees' Provident Fund and Miscellaneous Provisions Act, 1952 and other special Acts governing these Funds, such as the Coal Mines Provident Fund and Miscellaneous Provisions Act, 1948, the Assam Tea Plantations Provident Fund and Pension Fund Scheme Act, 1955, the Jammu and Kashmir Employees' Provident Funds Act, 1961 and the Seamen's Provident Fund Act, 1966.

2.45 It was announced in Budget 2004-2005 that a suitable legislation providing for a regulatory framework for NPS would be introduced in Parliament. The Union Cabinet recently approved a proposal to introduce a legislative framework for the NPS. An ordinance was promulgated on December 29, 2004 for the establishment of a statutory regulatory body called the Pension Fund Regulatory and Development Authority (PFRDA) to undertake promotional, developmental and regulatory functions in respect of the pension sector. The ordinance empowers the PFRDA to regulate the NPS, including authorizing and regulating intermediaries and protecting the interests of subscribers.

2.46 Tax treatment for contributions to the scheme was also announced in Budget 2004-05. The universally accepted formula of exempt exempt tax (EET) has been adopted, that is, the contributions will be excluded from income for tax purposes; the accruals will also be exempt from tax; and only the terminal benefits will be taxed at the applicable rate in the year of receipt. The Finance Act 2004 gave effect to this announcement by inserting a new section 80CCD in the Income Tax Act.