

PENSION REFORMS- A PANACEA FOR FINANCIAL FREEDOM

Independent India will celebrate its 60th anniversary on 15th August 2007 and it will be time once again for us to look back and count our achievements and think of the future.

Sixty years may not be a long period in the history of a nation but 60 years is a long period in the life of an individual. A nation may be considered young at 60 but for a citizen, 60 years has been recognised as the time to retire from active service. It also happens to be a point at which a subscriber can exit the New Pension System (NPS).

NPS promises to provide a solution to the problem of inadequate income after retirement. For new government employees, for whom the scheme is mandatory, it marks a shift from defined benefit to a defined contribution regime.

NPS is based on the principles of defining upfront the liability of the government, giving choice to subscribers, facilitating portability of labour and ensuring transparency and fair play in the industry within a regulated and secure environment for investment. In due course, NPS will be made available to every citizen on a voluntary basis.

Individual choice and portability of pension accounts are two distinguishing features of the NPS. Under the NPS, a subscriber will not only have the option of choosing her fund manager and investment pattern, but also have the choice of switching between fund managers as well as investment options. No other pension scheme offers this flexibility and freedom. There are no entry and exit loads.

Apart from availability of individual choice to account holders under the NPS, the centralized accounting and administrative infrastructure based on a specialized and custom-built IT platform will facilitate quick and seamless movement of funds across fund managers. The costs will also be highly competitive as NPS is designed to ride primarily on the existing infrastructure. The cost of record keeping

and management of funds will also decline gradually due to competition and economies of scale to bring about a sea change in financial intermediation. Growth of the pension sector will also render depth and stability to the capital and debt markets and provide funds for infrastructure development.

The government intends to allow investment of pension money of government employees as per the pattern available to non-government provident funds, such as EPFO. The EPFO investment pattern allows investment up to 5 per cent in stocks. But, actually up to 10 per cent can be invested in equity-linked mutual funds. This comes to a total of 15 per cent.

A word of caution, however. Mere availability of a right to exercise individual choice is not a sufficient condition for unshackling the pension sector. The prerequisite for translation of this vision into reality is that the freedom to choose is exercised in an informed manner.

This, in turn, will depend upon the level of financial literacy, especially the advantages of regular savings in a pension scheme. The need for public awareness and education about the pension sector is even more compelling as we transit from an assured return regime to a market oriented one under the NPS. The enormity of the challenge of creating awareness and educating the subscribers should not be underestimated. Undoubtedly, our biggest challenge would be extending the scheme to the rural areas.

Political freedom was won 60 years ago. NPS will provide an opportunity to every senior citizen to achieve financial freedom.