National Pension Scheme

The National Pension System (NPS) is a pension scheme sponsored by the government that was started in 2004 for all government employees. The scheme was made open to all citizens in 2009. It is a voluntary and long-term retirement scheme. It is regulated by the **Pension Fund Regulatory and Development Authority (PFRDA)** and Central Government. In this article, you can read about the National Pension Scheme (NPS) for the civil services exam.

Why is National Pension Scheme in the news?

PFRDA has recently announced that the National Pension System (NPS) will no longer compel investors to convert 40% of their accumulated retirement corpus into an annuity, as poor yields on annuities and high inflation are translating into negative returns. [Source - The Hindu]

It has also announced that the retirees will be able to take out the entire Rs.5 lakh savings in the NPS against Rs. 2 lakh at present.

National Pension System Latest News

In March 2023, the Finance Minister announced a committee to propose changes to improve the National Pension System (NPS).

About the panel:

- The panel will recommend changes to improve the existing NPS for government employees in a way that takes care of the aspirations and concerns of common citizens with fiscal prudence.
- The new approach will be designed in such a way that both Central and State Governments can adopt it for their employees.
- The committee will be headed by Finance Secretary T.V. Somanathan.

Need to relook the National Pension System:

- Five Opposition-ruled States such as Rajasthan, Chhattisgarh, Punjab, Himachal Pradesh, and Jharkhand already switched to the Old Pension Scheme (OPS). And more states may likely follow the same.

What is the old pension scheme?

- The old pension scheme is an old scheme of providing pensions which is a “pay as you go” scheme which was operational till 2004.
- According to analysts, it poses an intergenerational disparity.

- Under it, contributions from the current generation of workers were used to pay for the pensions of current pensioners, making it an unfunded pension scheme because it represented a direct transfer of resources from the current generation of taxpayers to fund the pensions.
- OPS assured benefit to the retirees that is fixed at 50% of the last drawn basic pay.
- Salaries and pensions also increased with hikes in dearness allowance, essentially to accommodate inflation.
- OPS is politically attractive but not fiscally sustainable as it is not contributory in nature and the burden on the exchequer keeps on increasing.
- According to Soumya Kanti Ghosh, Chief Economic Adviser of the State Bank of India, the old system was fiscally ruinous and any return to the old scheme will not be fiscally viable. Again sharp increase has been noticed in the pension liabilities of state governments in the long term. The compounded annual growth in pension liabilities is 34% for all state govt for the 12-year period ended 2021-22. As of 2020-21, 13.2% of revenue receipts was pension-related expenditure.

New Pension Scheme

During Atal Bihari Vajpayee's regime, NPS was brought and rolled out on January 1, 2004.

- It has been implemented for all central government employees except those in armed forces joining central government on or after 1 st of January 2004.
- Most of the state/Union Territory governments also notified the NPS for their newly employed employees.
- In 2003, the government created PFRDA (Pension Fund Regulatory and Development Authority) to regulate and develop the pension market. It was initially designed to cater for the needs of government employees only, but later its services were expanded to include all Indian nationals and NRIs.
- According to PFRDA, except for West Bengal and Tamil Nadu, all 26 state governments notified and implemented NPS for their employees.
- NPS has been made available to every Indian citizen such as public, private and even the unorganized sectors can opt for this, from May 1, 2009, on a voluntary basis.
- Tax benefits are also offered on the scheme post-2014 by the government to make it popular.
- The total assets being managed under the National Pension System and Atal Pension Yojana stood at ₹8.81 lakh crore as on March 4, 2023.

Who can join NPS?

Any employee from public, private and even the unorganised sectors can opt for this. Personnel from the armed forces are exempted. The scheme is open to all across industries and locations.

The other eligibility criteria for opening an NPS account:

1. Must be an Indian citizen.
2. Must be between the ages of 18 and 65.
3. Must be KYC compliant.
4. Must not have a pre-existing NPS account.

NPS Benefits

- NPS offers returns higher than traditional instruments like the PPF (Public Provident Fund).
- It offers many investment options to subscribers who also have a say in where their funds are invested.
- The NPS reduces the retirement liabilities of the government.
- If the subscriber has been investing for at least three years, he/she can withdraw up to 25% for certain purposes before retirement (age 60). This withdrawal can be done up to 3 times with a gap of at least 5 years between each withdrawal. These restrictions are only for tier I and not tier II accounts.
- The entire amount cannot be withdrawn by the account-holder on retirement [Changes to be introduced]. As of April 2021, 60% can be withdrawn which has now been made tax-free. The rest 40% has to be kept aside so that the subscriber can receive a regular pension from an insurance firm.

There are two types of NPS accounts. They are briefly explained below:

NPS Account Types

NPS Tier 1 Account

There are tax benefits under this account. But the withdrawals are subject to certain conditions and restrictions as explained above.

NPS Tier 2 Account

Account holders can invest an additional amount under the tier-II account. Here, they are free to withdraw the whole corpus at any point in time. There are no tax benefits associated with this account type.