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COMMENT

New Pension Bill

FORMER FINANCE MINISTER Yashwant Sinha had initiated a New Pension Scheme (NPS) in 2004 to limit the ever-increasing financial burden while hoping to reduce the fiscal deficit through the new mechanism. All Union Government employees recruited after 2004 are to get pension under this scheme. They have to contribute 10 percent of their salaries towards their pension fund with the Union Government providing a matching amount. The NPS makes a radical departure from the past practice. Previously the amount of pension was determined by the present salary structure as advised by the Pay Commission. The NPS does away with a determined amount of pension. The amount accumulated in the pension fund of the individual is used to provide pension. This varies with the amount accumulated.

There are some shortcomings in the NPS, however. First, that it covers only government servants. Ninety-five percent of the citizens are outside its coverage. Second, the pension fund is wholly being invested in Government Bonds which provide a low rate of return. Chairman of Pension Fund Regulatory Authority, D Swamp says that the cost of managing these funds is high while the return is low. The UPA Government has now made a Bill to remove these shortcomings with the pre-conceived notion that they could control fiscal deficit by bashing the employees.

The new Bill provides flexibility in investment of the fund. The beneficiary can choose a management agency from among many that may be registered for the purpose. Presently the entire corpus is managed by the State Bank of India. A beneficiary does not have the option of assigning management to another agency which may be able to garner better returns. Private as well as foreign entities are allowed to register themselves as fund managers under the new Bill. And Foreign investors want the Bill to be passed expeditiously because they want to enter this huge market. The crux of the matter is foreigners are coming in a big way to control pension funds and they call it 'reforms' in the right direction.

The Bill apparently enables the beneficiary to take a higher risk and earn higher amounts as well. Pension Funds are allowed to invest up to 60 percent in equities in the UK. But pensioners in the US have lost about one-third of their payouts to the global recession. And it cannot be otherwise in India where regulations are slack. Even the main accused in the Bhopal gas tragedy-Anderson-had his way because India can hardly punish any foreigner in real life even if he violates laws of the land.

The Bill also allows private citizens to invest in the NPS. However, they will not be entitled to a matching grant by the Government. There is provision for a small incentive to those investing less than Rs 12,000 per year. On the negative side the returns from the NPS are taxable. This

makes NPS less attractive than the Public Provident Fund which is tax free. Therefore, this provision in the Bill is likely to be a non-starter.

Commentators have suggested that the Bill will help control the fiscal deficit of the Government. In reality it is unlikely to happen. The budget has already been firewalled from pension liability of new recruits to the government by the NPS. They are not to be paid pensions from the budget. Therefore, the Bill will have no impact on fiscal deficit. If at all, it may have a negative impact. The Bill will lead to diversion of part of the fund from Government Securities to equities. That will reduce the demand for Government Securities and the government may have to offer higher interest rates to meet its borrowing targets. That will in fact worsen the fiscal deficit due to increasing interest burden. □□□ *[contributed]*