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Proposals approved by Government to streamline National Pension System

The Government of India has issued a press release[1] on 10 December, 2018 to streamline the National Pension System (NPS). The Union cabinet has approved the proposals to extend benefits to the Central Government employees and on enhancing the tax exemption at the time of exit from NPS.

The key proposal are as follows:

- Enhancing the Central Government's contribution for its employees from 10% to 14%;
- Providing freedom of selection of pension funds and pattern of investments for Central G overnment employees;
- Enhancing the tax exemption on exit from NPS from 40% to 60% of the accumulated corpus; and
- Introducing deduction from gross total income for Government employees for contributions to the NPS Tier II account.

Background

The NPS is a defined contribution pension scheme launched by the Government of India with effect from 1 January 2004. The NPS is regulated by the Pension Fund Regulatory and Development Authority (PFRDA). It was first introduced for government employees as a defined contribution pension scheme, and then extended to all the citizens of India at the end of 2009.

Summary of proposals approved

Existing	Proposed
Employer contribution to NPS scheme under Tier-I was 10% for Central Government employees.	Employer contribution to NPS under Tier-I to be enhanced to 14% from 10% for Central Government employees. Employee contribution remains unchanged.
The Fund Managers specified for the Central Government employees till now includes: - SBI Pension Fund - LIC Pension Fund - UTI Retirement solutions Pension Fund There is only a default investment pattern for Central Government employees wherein allocation to equity investment is capped at 15%.	Central Government employees will have choice of selection of Pension Funds and pattern of investment. This is expected to be aligned with the options available to corporate employees and self-employed individuals.
40% of the total accumulated corpus utilised for purchase of annuity is tax exempted. Out of remaining 60% of the accumulated corpus withdrawn, 40% is tax exempt and the balance 20% is taxable.	40% of the total accumulated corpus utilised for purchase of annuity is tax exempted. This remains unchanged. The remaining 60% of the accumulated corpus withdrawn will be exempt from tax.
No tax benefits were available for contribution to the NPS Tier II account (voluntary account).	Deduction under section 80C of the Income-tax Act, 1961 (within overall limit of INR 0.15 million) will be available to Government employees for contribution to NPS Tier II account with a lock in period of three years.

As per the Press Release, the above proposed changes will be effective immediately upon approval of the other concerned Ministries/ Departments.

Key takeaways

Although the proposed changes would have an impact on the exchequer, the Government of India has definitely made the pension scheme attractive, especially by extending the tax exemption limit.

While the above proposals are expected to give an impetus to the NPS, the private sector employees, self-employed persons and the State Government employees may feel left out, as the deduction under section 80C of the Income-tax Act, 1961 for contributions made to the NPS tier II account has been proposed only for employees of Central Government.

Currently, these are only proposals approved by the Union Cabinet. For operational details, respective amendments by PFRDA and the Central Board of Direct Taxes are awaited.

[1] Press release by the Ministry of Finance on streamlining of NPS on 10 December, 2018

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