Old Pension Scheme Vs New Pension Scheme

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Why is in news? Govt. staff seek restoration of old pension scheme

Thousands of employees of the Union government and Central public sector undertakings, including the defence establishments, marched to Ramlila Maidan demanding the restoration of the old pension scheme (OPS).

After the protest rally, organised by the Joint Forum for Restoration of Old Pension Scheme, a platform of some 60 unions, the employees sent a memorandum to Prime Minister stating that if the existing National Pension Scheme (NPS) is allowed to continue, employees recruited on or after January 1, 2004, will be “left in the lurch” after retirement.

The memorandum said that under the OPS, 50% of the last basic pay drawn by the employees was straightaway given as pension and the dearness allowance was revised twice based on inflation.

Old Pension Scheme (OPS):

OPS offers pension to **government employees on the basis of their last drawn salary**.

The attraction of the Old Pension Scheme **lay in its promise of an assured or ‘defined’ benefit** to the retiree. It was hence described as a **‘Defined Benefit Scheme’**.

Eg., If a government employee’s basic monthly salary at the time of retirement was Rs 10,000, she would be assured of a pension of Rs 5,000.

Also, like the salaries of government employees, the monthly pay-outs of pensioners also increased with hikes in dearness allowance or DA announced by the government for serving employees.

The **entire amount of the Old Pension was paid by the government**. The budget for pensions used to be announced during the Budget announcement every year. Furthermore, the federal and state government were responsible for the payment of the yearly DA increase in the pension as well.

OPS was the **financial liability for the government without any source to derive income** from the corpus collected as savings of the government employee. Though the announcement would be made every year, the carrying forward capacity of the scheme was not certain.

The OPS was **discontinued** by the Central government **in 2003**.

Concerns with the OPS:

The main problem was that the **pension liability remained unfunded** — that is, there was **no corpus specifically for pension**, which would grow continuously and could be dipped into for payments.

The Government of India budget provided for pensions every year; there was **no clear plan** on how to pay year after year in the future.

The **'pay-as-you-go' scheme** created inter-generational equity issues — meaning the present generation had to bear the continuously rising burden of pensioners.

New Pension Scheme (NPS):

As a substitute of OPS, the NPS was introduced by the Central government **in April, 2004**.

The scheme encourages people to **invest in a pension account at regular intervals** during the course of their employment.

All citizens **between 18 and 65 years** are eligible for NPS.

NRIs (Non-Residential Indians) are also eligible to apply for NPS.

After retirement, the subscribers can take out a certain percentage of the corpus.

The beneficiary receives the remaining amount as a monthly pension, post retirement.

Nodal agency: Pension Fund Regulatory and Development Authority (PFRDA)

Concerns with NPS:

Deductions from salary: The NPS, in contrast to the OPS, mandates that employees deposit 10% of their base pay in addition to the dearness allowance.

The amount of the pension is not set in stone, and there is **no GPF benefit**.

Linked to market returns: The scheme's major flaw is that it is return-based and linked to the market. Simply put, the payout is speculative.

Key differences between OPS and NPS are in the following:

OPS:

The old pension scheme used to give a fixed monthly income **to government employees** after retirement.

It **provided 50 per cent of the last drawn salary** as a pension.

No tax benefits are applicable to the employees.

Income under the old pension scheme **doesn't attract tax**.

Only government employees are eligible to receive a pension under the OPS after retirement.

NPS:

It is **open to employees from the public, private and even the unorganised sectors** except those from the armed forces.

State governments also follow the NPS for their employees.

In NPS, employees **contribute money from their salary during their employment tenure**. The amount is invested in market-linked instruments.

Investment in NPS **up to Rs 1.50 lakh is tax-deductible** under Section 80C of the Income Tax Act, 1961. Additional annual investments up to Rs 50,000 are tax-deductible under Section 80CCD (1B) of the Act.

According to the rule, **60 percent of the corpus on maturity is tax-free**, while the remaining 40 percent is taxable and must be invested in annuities for a regular income or pension.

Under the NPS, employees make a monthly contribution at the **rate of 10 per of their salary**. A matching contribution is also made by the government.

Starting April 1, 2019, the employer's contribution rate has been enhanced to 14 per cent for the central government employees.

Some common issues with the Pension system in India:

Insufficient coverage: Any pension plan leaves a lot of the Indian population out of pocket. The unorganized sector typically includes those who remain uncovered.

Insufficient sums: The sums received by those who are covered by various pension plans are insufficient to ensure their continued existence.

Insufficient pension amount: The Parliamentary Standing Committee on Rural Development observed that the various components of the National Social Assistance Program (NSAP) provided insufficient assistance. It cost between 200 and 500 rupees per month.

Disparate Coverage: In addition, the implicit rate of returns and benefits minus contributions vary among programs, occupations, industries, and other contexts. and as a result, the pension benefits become unequal.

Financial viability: The government's fiscal plan is further strained financially by the pension industry. According to a number of studies, the amount of money spent on pension payments is rising faster than taxes and duties.

Ineffective management: The issuance of annual statements and the delays in processing and crediting claims are the subject of criticism. The structure of organizational governance also needs to be improved. Additionally, government regulations prevent retirement benefit systems from being transferred to other industries.

Way forward:

The government can **optimize pension schemes** by reviewing the benefits and eligibility criteria of the pension schemes. This can **help identify areas** where the benefits can be reduced without impacting the employees.

The government can also **work towards increasing efficiency in its operations** and reducing the overall workforce.

This can **help reduce the pension burden** and **improve the fiscal health** of the country.

This does **bring state governments some short-term gains**, they save money since they will not have to put the 10 percent matching contribution towards employee pension funds.

For employees it will result in higher take-home salaries, since they too will not set aside 10 percent of their basic pay and dearness allowance towards pension funds.

Bad politics: Contrast this with the bulk of the workforce which has no old age income security, but which also does not have much electoral salience.