# Operationalizing the NPS for corporates

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**Retirement is a topic that the majority of companies in India tend to ignore. The general consensus seems to be that it is not an employer's responsibility to help an employee prepare for retirement, but rather, it is the individual's 'self-obligation.' However, financial wellness of an employee is a serious issue that affects employee morale and productivity. When offered as an employee benefit, it can help companies improve recruitment, potentially stem the steady flow of employee turnover, and provide a reward of financial security for long-term employees when their employment comes to an end.**

This is Part 2 of a three-part series on the National Pension Scheme. Our intention is to provide useful information for employers who would like to operationalize NPS in their organization. Most of the content has been derived from information which is publically available. For more information, please contact the author.

The first part of the series focused on basic information for employees and individuals about NPS and can be accessed here. Part 3 of the series will compare returns of NPS and other retirement funding products generally used by Indians.

Employers already assist in retirement planning for their employees in the form of contributions to the mandatory provident fund scheme run by the Employees' Provident Fund Organisation of India (EPFO). However, the list of complaints from both employers and employees are numerous. As a voluntary, market-linked, and transparent system, the New Pension System (NPS) has the capability of changing the paradigm of retirement financing in India.

The NPS was opened to the general public on a voluntary basis in 2009 whereby individuals initiated the arrangement and paid the contributions. However, it was soon realized that offering the NPS through corporates would not only result in reaching critical mass for the scheme but also help solve the retirement puzzle for many people in India. Seeing this opportunity, the Pension Fund Regulatory and Development Authority (PFRDA) announced 'NPS for Corporates,' a version of the NPS directed toward companies in the organized sector with a few 'additional' benefits, such as:

- The employee receives tax benefits over and above the Rs. 1,00,000 limit when making contributions through an NPS for Corporates arrangement.
- The employer is able to deduct the contributions made on behalf of its employees as an expense before determining taxable profits.
- The employer has the option to decide the investment manager and the investment approach for its employees. Such an option is not available under any other NPS scheme.
- The employer was given the freedom to negotiate fees with Point of Presence (POP), an option which is not available to the retail subscriber.

Before we discuss NPS for Corporates, it is important to understand the role of intermediaries in the NPS architecture. The NPS follows an unbundled architecture concept, where each function is potentially performed by a different entity:

1. **Point of Presence (POP)**
   POP-Service Providers (POP-SP) are the designated branches of a registered POP that extend the reach of the NPS. POP and POP-SP are the interface between the customers and the NPS architecture. They perform functions relating to registration of employers and subscribers, undertaking Know Your Customer (KYC) verification, and receiving contributions and instructions from employers and transmission of the same to designated NPS intermediaries. The documents for KYC verification for employees and employers should be as prescribed under the Anti-Money Laundering (AML)/Combating of Financing of Terrorism (CFT) Act of 2002 by the government of India for customer identification. A list of POPs as at September 15, 2013, is available here.

2. **NPS Trust and Trustee Bank (TB)**
   PFRDA established the NPS Trust under the Indian Trusts Act, 1882, and appointed the NPS board of trustees who oversee the administration of the NPS. The Trust is responsible for taking care of funds under the NPS.

   Trustee Bank (TB) manages the pension fund banking transactions in accordance with the applicable provisions of the NPS, and from time to time guidelines and notifications issued by the PFRDA, Ministry of Finance, and government of India. As of July 1, 2013, Axis Bank has taken over the responsibility of TB from Bank of India.

3. **Central recordkeeping agency (CRA)**
   The main functions and responsibilities of the CRA include:

   - Recordkeeping, administration, and customer service functions for all the subscribers of the NPS (both Tier I and Tier II accounts[1]).
   - Issuing permanent retirement account number (PRAN) to each subscriber, maintaining a database of all PRANs issued and recording transactions relating to each subscriber's PRAN.
   - Acting as an operational interface between PFRDA and other NPS intermediaries such as pension funds, annuity service providers, TB, etc.

   The current CRA is National Securities Depository Limited (NSDL).

4. **Pension fund managers (PFMs)**
   PFMs manage the retirement savings of the subscribers. PFMs are required to invest strictly in accordance with the guidelines issued by the government of India and PFRDA. A participant or an employer selects a particular PFM for managing the contributions. The list of PFMs as on September 15, 2013, is available here.

5. **Custodian**
   A custodian is responsible for the safekeeping of the underlying assets and must be a custodial services provider registered with the Securities and Exchange Board of India (SEBI). Currently Stock Holding Corporation of India (SCHIL) performs the role of custodian for NPS.

6. **Annuity service provider (ASP)**
   ASPs are responsible for delivering a regular monthly pension to subscribers as per the selected choice of annuity by the subscriber. A list of ASPs as of September 15, 2013, is available here.

Under the NPS for corporates model, there are a few more aspects to consider.

## ELIGIBILITY OF CORPORATES

The NPS for Corporates model is available to any of the following entities:

- Entities registered under the Companies Act
- Entities registered under various cooperative acts
- Central public sector enterprises
- State public sector enterprises
- Registered partnership firms
- Registered limited liability partnerships (LLPs)
- Anyone incorporated under any act of Parliament or state legislature or by order of central/state government
- Proprietorship concerns
- Trusts or societies

A corporate interested in joining the NPS is required to go through any one of the existing POPs. The NPS for Corporates model facilitates employees working under various organizations to come on board the NPS within the purview of their employer-employee relationship, subject to the norms prescribed by PFRDA.

- Once the desired paperwork is complete, the corporate can offer the NPS to its employees and get them registered in the NPS.
- Once the employee's registration is complete, he or she is issued a PRAN.
- Once employees are issued PRANs, they can start contributing to the NPS.

It should be noted that the corporate, along with POP, is also required to comply with the provisions of the 2002 Prevention of Money Laundering (PML) Act.

## SUBSCRIBERS

The employees enrolled by the employer will be registered as subscribers under the NPS. Each subscriber will have a separate individual pension account. If the *employer* does not make a choice of the pension fund manager (PFM) or scheme preference, then each *subscriber* will be able to select from the pension fund managers registered under the NPS. Subscribers also have the option to switch savings between investment schemes, subject to such conditions and charges as prescribed by PFRDA from time to time.

## HOW CAN A CORPORATE JOIN THE NPS?

As stated earlier, corporates interested in extending the NPS to their employees would need to contract with any of the approved POPs under the NPS by establishing a memorandum

1 For details on Tier I & Tier II accounts, please review our first article in this NPS series here.

of understanding (MOU). The mutually acceptable MOU is written by the POP subject to the maximum charges as prescribed by PFRDA. There is a minimum compliance standard called 'service level requirement/turnaround time' (SLR/TAT) that needs to be adhered to and communicated by the POP to employer and employees. It should be remembered that the participating corporate is free to negotiate charges with the POP.

The interested corporate is required to complete Form CHO-I [2] and submit it to the POP along with the details of its corporate branch offices (CBOs), if any. The CRA registers the corporate in the system and allots an entity registration number, which would be reflected in each employee's registration form (CS-S1).[3]

Once the company registration is complete, any eligible corporate entity may enroll their employees. The POP ensures that the necessary due diligence as required for KYC verification is carried out and submits the CS-S1[4] forms to the recordkeeper.

The POP, in consultation with its corporate client, will develop an in-house mechanism and processes for accepting the consolidated data and aggregated funds to be uploaded to the CRA and TB, respectively. The branch of the POP or POP-SP will undertake the data upload.

The POP should ensure that all the required forms are received from the contributing employees, and that they are registered and issued a PRAN *before* receipt of contributions from the corporate. An agreed maximum turnaround time (TAT) as prescribed under NPS would be applicable for receipt of money.

## HOW TO RAISE GRIEVANCES

There is a multi-layered Central Grievance Management System (CGMS), which is easily accessible, simple, quick, fair, responsive, and effective. Subscribers have the option of registering a grievance or complaint through the following options:

- **Call centre/Interactive voice response system (IVR)**
  Subscribers can contact the CRA call centre via a toll-free telephone number, 1 800 222080, and register grievances. On successful registration of the grievance, a token number will be allotted by the customer care representative for future reference.

- **Web-based interface**
  Subscribers can register grievances at a website, https://cra-nsdl.com, with the use of the 'I-pin' allotted to them at the time of opening a permanent retirement account. On successful registration, a token number is displayed on the screen for future reference.

- **Physical forms**
  Subscribers can also submit grievances in a prescribed format to employers and/or POPs, which should forward it to the CRA Central Grievance Management System.

2 Available at the NSDL e-Governance Infrastructure Limited website, here.
3 Ibid.
4 Ibid.

## HOW TO GET CORRECTIONS OR CHANGES DONE

Subscribers can submit Form CS-S2 [5] to request correction of personal details or a reissue of their I-pin, T-pin, or PRAN card. They can use Form CS-S3 [6] to request a change in employer or scheme preference. All these forms are to be submitted to employers and POPs, which will update the change on the relevant CRA platform or forward it to the CRA.

Corporates can submit requests for a change in investment choice in Form CHO-2 [7] and requests for a change in POP in Form CHO-3.[8] Corporates should forward the form to their POPs, which would update the change on the relevant CRA platform or forward it to the CRA.

## BENEFITS OF THE NPS TO EMPLOYERS

The NPS is an attractive framework to manage the contributions of employees ahead of their retirement. Almost all companies contribute to the EPFO. While the interest rate declared by the EPFO has been reasonable in the context of government bond yields, members have not benefited from the growth opportunities associated with the growth in the economy (normally associated with equities). Meanwhile, payment of the benefit as a lump sum under either the provident fund scheme or any other pension products sold by insurance companies leave retirees with the challenge of managing the money throughout an unpredictable period of retirement. The NPS has the possible answer to most of these issues. Individuals can choose the degree of investment risk to take if they wish to take advantage of high-return-seeking investment options (or choose a low-risk strategy if they so wish). The annuity conversion means that the lump sum is managed professionally during the remainder of the employee's retirement.

Before the introduction of the NPS for Corporates, if a company wished to help its employees for their retirement, it had to either buy a group insurance product or establish its own self-administered fund. Both these options had various costs for services, such as recordkeeping, investment management, annuity, etc. Within the NPS framework, through a combination of regulations and economies of scale, the costs have been brought down to a very low level.

We mentioned earlier that the EPFO investment strategy is the same for all members, and it has essentially been to deliver returns in line with the yield on long-term government bonds. With a simple, single investment strategy, it is not unreasonable that there is one fund manager–the EPFO.[9] The NPS offers choice within investment strategies. It is therefore natural that there should also be choice among the managers that deliver the investment strategies. The NPS permits this. It must also be remembered that an employer may choose the pension fund managers for its employees. Alternatively, the employer can allow the employees to decide on the pension fund manager selection themselves.

From April 1, 2012, contributions of up to 10% of the salary (basic and Dearness Allowance) can be deducted as a business expense from profit and loss accounts under the NPS for Corporates model.

5 Ibid.
6 Ibid.
7 Ibid.
8 Ibid.
9 Even though investment management is currently an 'outsourced' function to numerous asset managers, they all are required to follow a single investment policy.

Finally, the contribution formula in the EPFO leaves many with relatively small amounts that will be insufficient to support them in retirement.[10] The NPS is flexible in the level of contributions that the employee may pay and indeed in the amount that the employer pays. This provides the opportunity to enhance contributions from time to time. The NPS platform allows all three variations of contributions from employer and employee:

- Equal contributions by employer and employee
- Unequal contributions by employer and employee
- Contributions from either employer or employee

As an extension to this, there is a useful tax-saving option where employees may sacrifice their bonus (or a part of it), which can then be contributed into the NPS as an employee contribution. The employee's take-home salary is not affected.[11] Note that there is a limit to the amount of this sacrifice such that the total of employee contributions for the year cannot be more than 10% of basic salary.

While offering access to the NPS to its employees, an employer needs to remember that the NPS is not without its flaws.[12] This is a defined contribution (DC) program, and as past global experience has proved, success of such DC arrangements is based on participation in smart investment choices. Another important aspect to remember is employee communication. Well-thought-out and planned communication programs are needed to assist employees so that they can make smart investment choices. Even though NPS looks like a very simple plan that is easy to implement, it is still in its infancy phase. Early adopters of the scheme had to face some challenges, especially in servicing the subscribers. However, those issues and hurdles are being resolved by PFRDA and other involved stakeholders. With PFRDA and the NPS Trust coming together to specify deadlines and enforcing turnaround times, it looks like a road map is being created for setting the NPS as a primary retirement funding vehicle in India.

Below is an example of how participating in the NPS can help employees reduce their income tax liability.

## Annexure 1

Below is an example of how participating in the NPS can help employees reduce their income tax liability.

| | | | |
|---|---|---|---|
| Total Annual Salary | | 1,200,000.00 | |
| Personal Income Tax Slab | | 30% | |
| **Particulars** | **Comments** | **Without NPS** | **With NPS** |
| Basic Salary | Assumed as 40% of CTC | 480,000.00 | 480,000.00 |
| NPS Contribution | Maximum at 10% of basic salary | - | 48,000.00 |
| Other Taxable Allowances | Total salary *less* basic salary | 720,000.00 | 672,000.00 |
| Gross Total Income | | 1,200,000.00 | 1,200,000.00 |
| Less: Deductions | | | |
| Section 80C | Maximum allowable deduction | 100,000.00 | 100,000.00 |
| Section 80CCD(2) | Newly introduced section for NPS | - | 48,000.00 |
| Taxable Total Income | | 1,100,000.00 | 1,052,000.00 |
| Tax on Total Income | See breakup below | 164,800.00 | 149,968.00 |
| Tax Savings | | | 14,832.00 |

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10 Of the 24% of the total contribution, 12% of employee contribution is made towards the provident fund. Of the employer's 12%, 8.33% is made to the provident fund and 3.67% is for the pension scheme.

11 See Annexure 1 for more details.

12 See NPS Part 1 article, page 4.