

India

India: Pension system in 2020

Workers are covered under the earnings-related employee pension scheme and defined contribution employee provident fund administered by the Employees Provident Fund Organization (EPFO) and other employer managed funds. Civil Employees of Central Government who have joined services on or after 1 January 2004 are covered under the Defined Contribution based New Pension System (NPS).

Key indicators: India

		India	OECD
Average worker earnings (AW)	INR	150 000	2 903 303
	USD	2 024	39 178
Public pension spending	% of GDP		7.7
Life expectancy	at birth	69.3	80.6
	at age 65	14.6	19.7
Population over age 65	% of working- age population	11.3	30.4

Qualifying conditions

The normal pension age for earnings-related pension benefits from the Employees' Pension Scheme is 58 years with a minimum of ten years of contributions. The pension age for the earnings-related Employees Provident Fund scheme is 55 years.

About 12% of the workforce (or approximately 58 million people) are covered under various pension systems according to the 2011 census. Covered individuals belong to the organized sectors and are employed by the government, government enterprises, public and private sector enterprises, which are mandatorily covered by the Employees Provident Fund Organization (EPFO). Employers with 20 or more employees are covered by EPFO.

The remaining 88% of the workforce are mainly occupied in the unorganized sector (self-employed, daily wage workers, farmers etc.) and some are in the organized sector, but are not mandatorily covered by the EPFO. For this share of the workforce the Public Provident Fund (PPF) and Postal Saving Schemes have traditionally been the main long-term savings instruments but these have only catered to a relatively small section of this population.

Benefit calculation

Employees Provident Fund Schemes (EPF)

The EPF scheme is mandatory for employees with a 'Basic Wage' of less than or equal to INR 15 000 per month. Basic Wage does not include many allowances and therefore ranges from 30-50% of total remuneration on average.¹ The employee contributes 12% of the Basic Wage and the employer contributes 3.67%. This combined 15.67% accumulates as a lump-sum.

For employees with a Basic Wage greater than INR 15 000 per month, the employee generally contributes 12% of the Basic Wages and the employer also contributes 12%. This combined 24% accumulates as a lump-sum. However, the mandatory obligation on employer contribution of 12% is only with respect to the Basic Wage up to INR 15 000 per month. Therefore, the employer can choose to contribute only up to INR 1 800 i.e. 12% of INR 15 000 instead of the actual Basic Wage, which may be higher.

There is no annuity and full accumulations are paid on retirement after attaining 55 years of age. For comparison with other countries, for replacement rate purposes the pension is shown as a price-indexed annuity based on sex-specific mortality rates.

Employees' Pension Scheme (EPS)

Starting from September 2014 new members with basic wage above INR 15 000 per month no longer have the option of contributing to the EPS. Existing participants who have until now been contributing over the earlier INR 6 500 wage cap have an option to continue contributing over the increased wage cap of INR 15 000 but they would also have to contribute the government subsidy of 1.16% on the excess amount.

For the existing and new subscribers who are within the new basic wage cap of INR 15 000, the employer contributes an amount equal to 8.33% of the basic wage to the EPS fund and the Central Government contributes a subsidy of 1.16% of the salary into the EPS. This accumulation is used to pay various pension benefits on retirement or early termination. The kind of pension a member gets under the scheme depends upon the age at which they retire and the number of years of eligible service.

$$\text{Monthly pension} = (\text{pensionable salary} \times \text{pensionable service})/70$$

The pensionable salary will be calculated on the average monthly pay (Basic Wage) for the contribution period of the last 60 months (as against 12 months earlier) preceding the date of exit from the membership.

The maximum possible replacement rate is roughly 50%.

With effect from September 2014, a minimum pension level of INR 1 000 per month has been provided under the scheme.

Targeted Social Safety Net

There is no population wide social safety net.

In 2020, India has replaced its existing labour laws with three labour codes. Under this, the new Code on Social Security, 2020 (“Code”) has replaced nine legislations which provided social security to the employees like Maternity Benefit Act, Employees’ Provident Fund Act, Employees’ Pension Scheme, Employees’ Compensation Act, among others. The Code bring uniformity in providing social security benefits to the employees which were earlier segregated under different acts and had different applicability and coverage. The Code has recognised and covered workers working in the unorganised sector through new concepts such as gig workers, platform workers, fixed term employee etc.

Earlier, the labour laws did not provide for any social security benefits to the unorganised workers. The new Code empowers the Central Government to frame welfare schemes for the workers in the unorganised sector on the matters related to:

- Life and disability cover;
- Accidental insurance;
- Health and maternity benefits;
- Old age protection;
- Crèche; and
- Any other benefit as may be determined by the Central Government

The Code provides that these schemes may be wholly funded by the Central Government or partly by the Central Government and partly by the State Government or wholly funded by the contributions of the aggregators (eCommerce platforms) or partly by the Central Government and partly by the State Government

and partly funded by the beneficiaries of the scheme or the aggregators or wholly funded by the contributions of the aggregators or funded from corporate social responsibility fund (within the meaning of India's Companies Act, 2013) or through any other source.

The rules under the new Code are being finalised.

Variant careers

Early retirement

The EPS can be claimed from age 50 with ten years of contribution and the benefits are reduced by 3% per year of early retirement. If a member leaves his job before rendering at least ten years of service, he is entitled to a withdrawal benefit. The amount he can withdraw is a proportion of his monthly salary at the date of exit from employment. This proportion depends on the number of years of eligible services he has rendered. No pension is payable in cases where there is a break in service before ten years.

When a member has not rendered 10 years of pensionable service on the date of exit or on attaining the age of 58 years, then the member is entitled for a lump sum withdrawal or the member may opt to receive scheme certificate provided on the date of exit if age is below 58 years. A scheme certificate is issued to members who withdraw their EPF contribution but wish to retain their membership with EPFO, to avail pension benefits on attainment of retirement age. Upon joining a new job, Scheme Certificate ensures that previous pensionable service is added to pensionable service rendered with the new employer thereby, increasing the amount of pension benefits. Further, Scheme Certificate is also useful for family members to avail family pension, in case of untimely death of the eligible member.

In case of EPF, there are multiple scenarios, which allow for early access to the accumulation. Partial withdrawals relate to marriage, housing advance, financing life insurance policy, illness of members/family members, withdrawals are also permitted one year before retirement etc. In addition to various permitted partial withdrawals, employees can close their account and withdraw the full corpus in case they move from one employer to another or decide to retire early. No gratuity can be claimed before five years of service.

Late retirement

It is not possible to delay claiming pension after the normal pension age.

Personal income tax and social security contributions

Taxation of workers (for Financial Year 2020-21)

Contributions to the provident fund and pension scheme of EPFO and NPS are allowed as deductions from income while computing one's tax liability. A total deduction up to INR 150 000 is applied to social security contributions. This limit also includes other contributions like life insurance premium and Public Provident Fund (Voluntary Scheme) among others.

Workers under NPS also get an additional tax deduction for their employer's contribution into their account subject to a limit of 10% of their salary (Basic Salary + Dearness Allowance). This benefit, provided exclusively to NPS, is over and above the deduction of up to INR 150 000 mentioned above and is available from financial year 2011-12. However, this provision is more beneficial to workers in higher income groups as they are likely to be better placed to lock additional savings into their NPS account and would save a higher amount of tax at the maximum marginal rate of 30%.

Health insurance premium up to INR 15 000 is deductible (not included in the model). Transport allowance of INR 800 per month is exempted from taxation (included in the model).

Additional deduction (not included in the model): Mediclaim premium paid for parents. Maximum deduction INR 15 000. In case any of the parents covered by the Mediclaim policy is a senior citizen, deduction amount is enhanced to INR 20 000.

In 2020, the tax laws were amended to put a cap on the maximum amount of contribution made by an employer towards EPF, NPS and superannuation scheme to INR 750 000 beyond which the same is taxed as perquisite in the hands of the employee. Moreover, the amendment provides that any interest attributable towards the excess contribution beyond INR 750 000 was also to be treated as perquisite in the hands of the employee.

Taxation of worker's income

India's financial year begins in April. The following rates apply for 2020:

Annual income from all sources (INR)	Income tax Rates for Male and Female below 60 years
Up to 250 000	Nil
250 001 – 500 000	5%
500 001 – 1 000 000	20%
1 000 001 and above	30%

Additional Surcharge:

- a) 10% of Income tax where total income exceeds INR 5 million
- b) 15% of Income tax where total income exceeds INR 10 million
- c) 25% of Income tax where total income exceeds INR 20 million
- d) 37% of Income tax where total income exceeds INR 50 million

Health & Education cess: 4% of income tax plus surcharge

A resident or Resident but not Ordinarily Resident individual is entitled to rebate under section 87A if his total income does not exceed Rs. 5, 00,000. The amount of rebate shall be 100% of income-tax or Rs. 12,500, whichever is less.

Taxation of pensioners

Health insurance premium of up to INR 50 000 is deductible for senior citizens over 60 years.

For super citizens (age 80 years and above), the deduction for the payment of medical premium as well as the actual expenses incurred on their treatment are allowed.

The senior citizens (age 60 years and above) are exempt from income tax on their interest income up to INR 50 000 in a financial year. This applies to interest earned in the savings bank account, deposits in a bank, and/or deposits in post-office.

Senior citizens get a deduction limit of INR 100 000 if they undertake any treatment for specified disease/critical illness in a financial year. This deduction is INR 40 000 for persons below 60 years.

A senior citizen may reverse mortgage any of his accommodation to make monthly earnings. The ownership of the property remains with the senior citizen and they are given monthly payments for it. The amount paid in instalments to the owner is exempted from Income Tax.

Senior citizens are allowed a standard deduction of INR 50 000 on account of their pension income. This deduction is generally available to all salaried tax employees.

Taxation of pension income

Maturity benefits on account of provident fund and pension from EPFO are fully tax exempt. Lump-sum benefits and Periodic Annuity in case of NPS are taxable when the same is received. EPFO enjoys an EEE (exempt, exempt, exempt) regime where it is tax free during contribution, growth and withdrawal phase. NPS, on the other hand is under an EET (Exempt, Exempt, Taxed) regime where maturity benefits are taxed. As NPS is still in infancy, the rule for taxation on withdrawal does not really have any impact as the withdrawal stage is still some years away even for the first set of subscribers. The following income tax rules apply to senior citizens over age 65. An education cess of 4% is charged on the total tax amount.

Annual income from all sources (INR)	Income tax Rates for Senior Citizen	
	Age between 60 - 80 years	Age Above 80
Up to 300 000	Nil	Nil
300 001 – 500 000	5%	Nil
500 001 – 1 000 000	20%	20%
1 000 001 and above	30%	30%

Additional Surcharge:

- a) 10% of Income tax where total income exceeds INR 5 million
- b) 15% of Income tax where total income exceeds INR 10 million
- c) 25% of Income tax where total income exceeds INR 20 million
- d) 37% of Income tax where total income exceeds INR 50 million

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A resident or Resident but not Ordinarily Resident individual is entitled to rebate under section 87A if his total income does not exceed INR 500 000. The amount of rebate shall be 100% of income-tax or INR 12 500, whichever is less.

Under the NPS, once a subscriber reaches 60 years of age, he or she has to compulsorily purchase an annuity for an amount equal to a minimum of 40% of the accumulated balance in the NPS account. The balance amount can be withdrawn as lump sum at 60 years or can be deferred and withdrawn at any time before reaching age 70. Annuity purchase can also be deferred for a maximum period of 3 years.

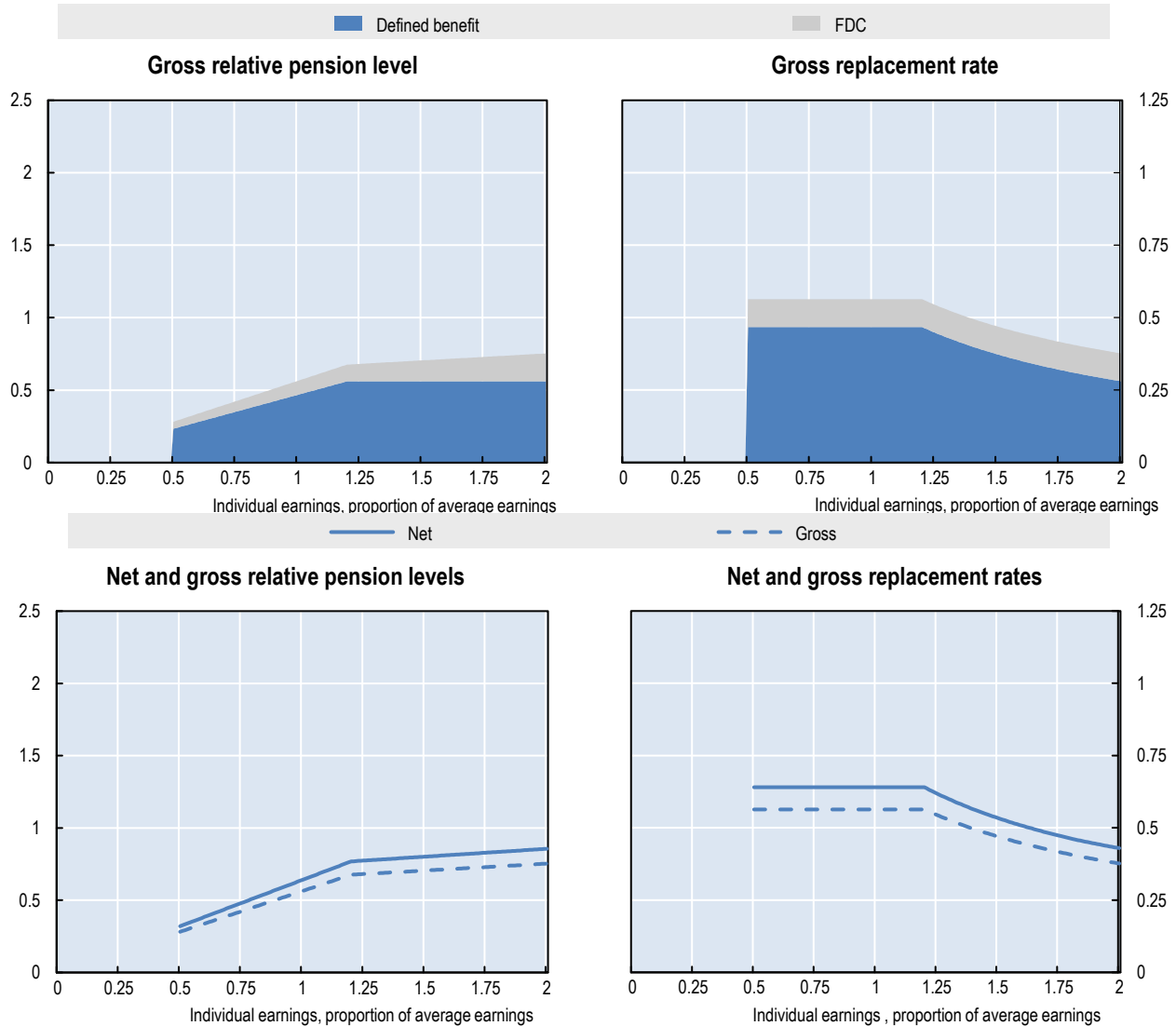
One can also withdraw the money before reaching 60 years of age, but in that case one will have to purchase an annuity utilising minimum of 80% of the accumulated corpus at the time of withdrawal.

In case of the untimely death of a NPS member before completion of 60 years of age, the nominee may withdraw the corpus accumulated at the time of death of the account holder. The money received by the nominee or legal heirs is fully exempt.

Social security contributions payable by pensioners

Pensioners do not pay any social security contribution.

Pension modelling results: India in 2056 retirement at age 58 (men)



Men	Individual earnings, multiple of average					
	0.5	0.75	1	1.5	2	3
<i>Women (where different)</i>						
Gross relative pension level	28.2	42.3	56.4	70.5	75.3	84.9
(% average gross earnings)	27.8	41.7	55.6	69.3	73.7	82.5
Net relative pension level	32.0	48.0	64.0	80.1	85.6	96.5
(% net average earnings)	31.6	47.3	63.1	78.8	83.8	93.8
Gross replacement rate	56.4	56.4	56.4	47.0	37.7	28.3
(% individual gross earnings)	55.6	55.6	55.6	46.2	36.9	27.5
Net replacement rate	64.0	64.0	64.0	53.4	43.0	32.8
(% individual net earnings)	63.1	63.1	63.1	52.5	42.1	31.9
Gross pension wealth	9.7	9.7	9.7	8.1	6.5	4.9
(multiple of individual gross earnings)	10.5	10.5	10.5	8.7	6.9	5.2
Net pension wealth	11.0	11.0	11.0	9.2	7.4	5.7
(multiple of individual net earnings)	11.9	11.9	11.9	9.9	7.9	6.0

Assumptions: Real rate of return 3%, real earnings growth 1.25%, inflation 2%, and real discount rate 2%. All systems are modelled and indexed according to what is legislated. Transitional rules apply where relevant. DC conversion rate equal 90%. Labour market entry occurs at age 22 in 2020. Tax system latest available: 2020.

ⁱ Section 2(b) of The Employees' Provident Funds And Miscellaneous Provisions Act, 1952 defines "basic wages" to mean all emoluments which are earned by an employee while on duty or on leave or on holidays with wages in either case] in accordance with the terms of the contract of employment and which are paid or payable in cash to him, but does not include—

(i) the cash value of any food concession;

(ii) any dearness allowance (that is to say, all cash payments by whatever name called paid to an employee on account of a rise in the cost of living), house-rent allowance, overtime allowance, bonus commission or any other similar allowance payable to the employee in respect of his employment or of work done in such employment;

(iii) any presents made by the employer;