

The New Pension Scheme (NPS)

***Administrative arrangements  
for central recordkeeping  
of personal retirement accounts***

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**Disclaimer:** *While the inputs and ideas from the above institutions have provided an input in preparing this document, this document does not necessarily represents their views.*

## **Glossary of terms**

<b>ARA</b>	Authorized Retirement Advisor
<b>CAMS</b>	Computer Age Management Systems Limited
<b>CDSL</b>	Central Depository Services Limited
<b>CRA</b>	Central Recordkeeping Agency
<b>DDO</b>	Drawing & Disbursing Officer
<b>DP</b>	Depository Participant
<b>DRF</b>	Data Recovery facility
<b>IIEF</b>	Invest India Economic Foundation
<b>IRDA</b>	Insurance Regulatory & Development Authority
<b>NAV</b>	Net Asset Value
<b>NSDL</b>	National Securities Depository Limited
<b>P&amp;AO</b>	Pay & Accounts Office (or Officer)
<b>PFM</b>	Pension Fund Managers
<b>PFRDA</b>	Pension Fund Regulatory & Development Authority
<b>POP</b>	Point of Presence
<b>PRA</b>	Personal Retirement Account
<b>PSU</b>	Public Sector Undertaking
<b>SEBI</b>	Securities and Exchange Board of India

## 1. Executive Summary

1. The central government has introduced a new pension system with effect from 01 January 2004. The new pension system will initially target new entrants to central government service (excluding Armed Forces) and will thereafter be available to all other citizens of India.
2. This new pension system is based on *Personal retirement accounts* (PRAs) created by individual members. In this system, a member will accrete savings into his PRA while he is working and use the accumulations at retirement to procure a pension for the rest of his life. Members in this system will enjoy a variety of important benefits including portability across jobs and locations, rights and choices regarding fund managers and schemes, freedom to switch between service providers, low transactions costs, nationwide access, and protection against fraud and malpractice through a dedicated regulator.
3. The efficient implementation of these features necessitates a centralized recordkeeping and administration facility by a centralized recordkeeping agency (CRA) which will enable reconciliation and administrative efficacy as well as economies of scale. The CRA will be required to electronically interconnect with the PFRDA, service providers (banks, post offices, DPs, etc), pension fund managers and life insurance firms. It will also offer a number of services directly to members including consolidated account statements. This centralized recordkeeping and administration facility will need to be flexible to future changes in technology and system specifications including number of members, number of fund managers and schemes, service and functional obligations, etc.
4. The choice of the agency which is entrusted with the task of central recordkeeping should be of paramount importance and interest to policymakers. The full operational

and member service framework, as well as the core principles of this pension system rest on the ability of the CRA to efficiently and accurately discharge its responsibilities and enforce the service and functional obligations on service providers over multiple decades.

5. The PFRDA proposes to invite a suitable agency to serve as the CRA for this new pension system. In this regard, the PFRDA proposes to publish a set of eligibility and pre-qualification criteria on the basis of which interested and eligible entities will be able to submit an expression of interest to serve as the CRA.
  
6. The applicants shortlisted after the EOI will be invited to submit technical proposals and financial bids to a special Evaluation and Selection Committee set up for this purpose. One agency will be selected to (a) build and operationalize the CRA facility, and (b) perform the system management and service delivery functions as the CRA for an initial license period of ten years.
  
7. The implementation of the administrative arrangement will be divided into three phases and will be based on milestones and functions specified by the PFRDA. It is expected that Phase-I will be completed within 8 months from issue of the License to the CRA and the remaining two phases will be completed within the next 7 months.

## 2. System Overview

1. The new pension system announced by the government will initially target new entrants to central government service (excluding Armed Forces). After a few months, it will be available to all other citizens of India. Each member of the new pension scheme will be allotted a unique *personal retirement account* (PRA) number. This pension system will initially be based on two types of sub-accounts created by individual members:
  - (a) a Tier-I non-withdrawable and tax deferred *pension* account (for all individuals), and
  - (b) a Tier-II withdrawable *savings* account with no tax advantages (for all individuals subject to minimum deposits per year in the Tier-I account).

The number of such sub-accounts may be altered as the system evolves and depending on the needs and performance of the pension system.

2. A member will accrete savings towards his retirement into his PRA through his working life. This PRA will stay with the member regardless of where he stays or works – including spells of unemployment, self-employment, changes in jobs or location. He will be able to use a nation-wide network of competing pension service providers (POPs) to access this system for opening a PRA, accreting new contributions, receiving account or system information and for obtaining retirement benefits.
3. A member will have complete control on how his contributions and savings in his PRA are managed. He will be able to select a professional Pension Fund Manager (PFM) from a pool of competing pension fund managers. Each PFM in this system will offer a choice of three simple and standard pension schemes with different risk and return profiles. If he desires, the member will be free to allocate his savings across multiple PFMs and schemes. If a member is unable to select a PFM, his savings will be directed to a 'Default' scheme. He will also be free and seamlessly able to switch his savings between fund managers and products as and when he desires. With individual accounts

and complete freedom of choice, a member will be able to easily alter his risk profile in an optimum fashion over time – he will be able to move from a high return scheme with relatively higher risk at a young age, to a low or near zero risk, modest returns portfolio when approaching retirement if he desires. The member will receive periodic, consolidated statements of his PRA which will reflect his wealth in his PRA across various products and PFMs. This will be the sum total of his contributions at that point in time and the returns that these contributions have earned.

4. On retirement, the member will be able to use a part of the savings accumulated over the years in his PRA to buy an annuity as a way to obtain consumption for the rest of his life.
5. In this process of accumulating retirement savings, the Pension Fund Regulatory and Development Authority (PFRDA) will provide the members of this scheme with a sound regulatory framework and an umbrella of safety with respect to prevention of fraud and malpractice.

## **2.1 Roles of participants in the new pension system**

1. This scheme will target two categories of participants (**members**):
  - a) It will be applicable to all employees of the central government (excluding Armed Forces) who join service after 01 January 2004. For these employees, participation and contributions to the Tier-I (pension) account will be *mandatory*. Every month, the government will deduct 10% of the salary (basic plus DA) of these new employees, match it with an identical contribution from its side, and transfer this full 20% contribution into the relevant employee's Tier-I pension account. The employee will select the PFM(s) and scheme(s) to which this 20% monthly contribution will flow. The cost of opening this account and the fees and charges levied by the CRA / PFMs on all twelve depositions in a year may be borne either by the employer or by the employee as per the terms of employment.

Every employee may voluntarily invest either in Tier-I (non-withdrawable) or in Tier-II (withdrawable) subject to certain stipulations. The Tier-II account will allow deposits / withdrawals at any P&AO / POP location on a voluntary basis. The fees and charges levied by P&AOs / POPs /CRA /PFMs for all transactions on Tier-II will be borne by the employee. The amount and periodicity of contributions into this Tier-II account will be decided by the employee and will be over and above the mandatory contributions into the Tier-I pension account. The government will not contribute to this account. If a government employee decides to resign from service, his pension wealth and his PRA will be unaffected.

However, once he ceases government service, he will obviously no longer be eligible for the 10% government contribution and will thereafter be free to contribute voluntarily into his Tier-I account. The status of tier-II account, however, shall not change.

- b) The second category of members will include all other citizens of India including non-resident Indians (NRIs) who will participate in this scheme on a *voluntary* basis. This category of members will also be allowed to operate the Tier-I and Tier-II accounts. These members will be free to decide the amount and periodicity of contributions into these accounts. For these members, there will be no matching contribution by the Government. However, employers will be free to make contributions into the PRAs of their employees if they wish. Unlike in the case of the government, these contributions by employers may not be mandatory<sup>1</sup>. The members who choose to open Tier-II accounts may do so after they have invested at least Rs. 3600 (2003-04 prices) into their Tier-I accounts (implying a contribution of Rs.10 per day).

Once an account has been opened, the transaction logic would be the same for both categories of members. In both categories of members and account types, the members will receive a unique account number, accrete contributions into this account, select a PFM and product, switch between PFMs and products, and receive consolidated

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<sup>1</sup> *The tax treatment of contributions by employers to the voluntary Tier-I accounts of their employees and whether this can be treated as a deductible expense from the employer's income may be examined in a separate note.*

account statements.

2. **Points of presence** (POPs) will be the service providers for members and will offer a host of services. POPs will assist members in opening new PRAs and issue PRA I-Cards; collect, verify and transfer contributions and/or instructions regarding PFMs and schemes to the CRA with relevant and correct member account information; collect and transfer complaints from members to the CRA; provide performance data as well as account information and statements to members; and communicate changes in personal information of members to CRA. Once a member retires, the CRA may use this same network to deliver the lump sum terminal accumulations to the bank account of relevant member. Banks, post offices, depository participants and other secure entities which are capable of electronic connectivity with the CRA will serve as POPs.

For central government officers including Civil Services, Railways and Department of Posts, the relevant Pay & Account Offices (P&AOs) which manage the government's payroll process, will perform some of the POP functions. The P&AOs will be responsible for the initial services to government employees including (a) handing over of a system information brochure on joining service, (b) account opening, (c) deducting and transferring the 10% employee contribution and 10% government contribution to the CRA on behalf of each employee as per the choice of PFM and scheme, and (d) deduction and transfer of employee contributions to Tier-II accounts to the CRA as per the choice of PFM and scheme. Once this initial contribution reaches the PFM and the units are credited into the PRA of the relevant employee, he will be able to avail of all other services (switching PFMs and schemes, account statements, NAV information etc.) by opening a *service account* with a POP or by directly accessing the CRA over the Internet or phone. The transaction and service charges of this service account will be borne by the employee. The details of the operation of P&AO under the interim arrangement is described in section 2.2.

3. The recordkeeping, administration and customer service functions for all members of this pension system will be centralized and performed by the **Central Recordkeeping**

**Agency** (CRA). The CRA will issue a unique account number to each member, maintain a master database of all personal retirement accounts and record the transactions related to each member's PRA. The CRA will receive and consolidate member contributions and instructions and transmit them to the relevant PFM and scheme on a daily basis. The CRA will periodically provide consolidated PRA statements to each member. The CRA will also enforce operational guidelines of the PFRDA (on service providers) as well as report compliance on mandatory contributions by government employees.

4. An initially limited number of competing, specialized professional **pension fund managers** (PFMs) will manage the retirement savings of members. Every day, the CRA will receive payments and/or instructions regarding (a) new contributions to PFMs and schemes, (b) changes (switches) in PFMs or schemes, and (c) terminal withdrawals. The CRA will reconcile and collate all such instructions and funds received from members through the POP / P&AO / bank network or the Internet. For each scheme of each PFM, the CRA will arrive at a single amount which will include the sum of fresh contributions as well as incoming transfers from other schemes. From this, the CRA will deduct the total outflow from the specific scheme (which may be on account of transfers or terminal withdrawals) to arrive at a *net* amount payable or receivable from each scheme of each PFM. Once all such balances are determined, the CRA will remit a single, netted amount to the PFM (which be the sum total of the netted amounts across all three schemes of the PFM) along with a statement specifying the exact amount to be invested under each of the 3 schemes on a daily basis. PFMs will comply with the investment guidelines issued by the PFRDA for allocating these assets under each scheme. Firms with requisite fund management experience and which satisfy the eligibility criteria specified by PFRDA will be eligible to apply for a PFM license.
5. When a member retires, he will be mandated to use a specified part of his terminal accumulations in his PRA to buy an annuity from a pool of competing **annuity providers** who will be responsible for delivering a regular monthly pension to the

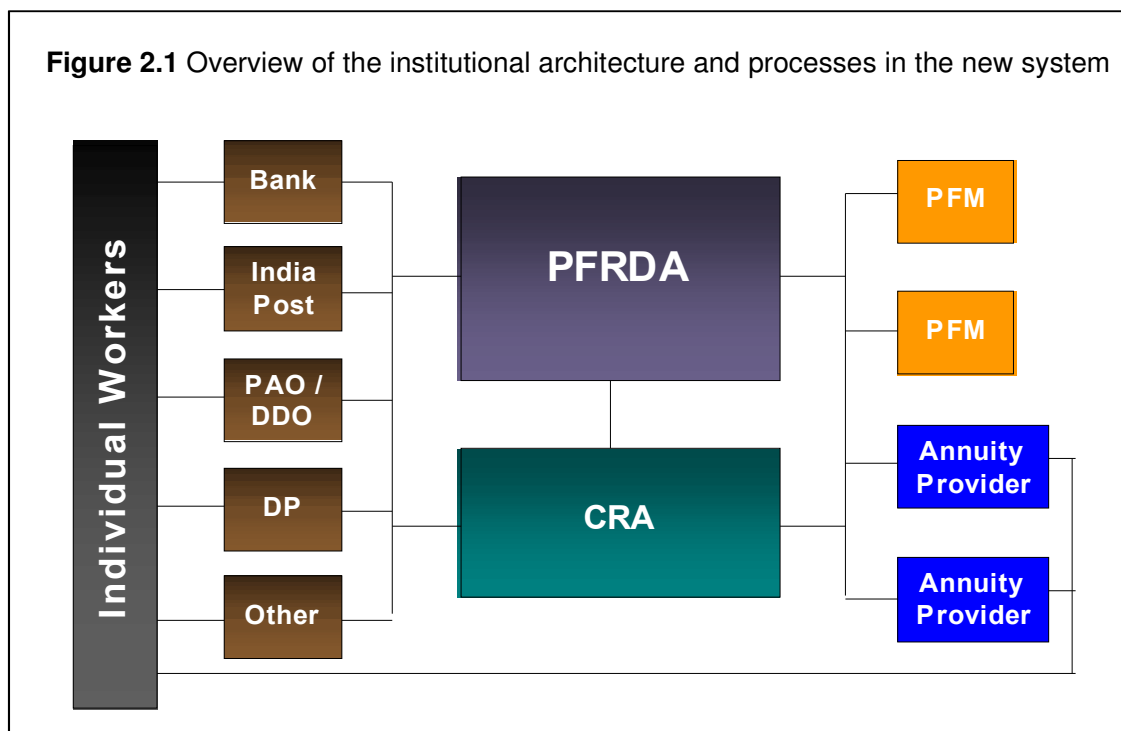
member for the rest of his life. Life insurance firms which are registered with the IRDA will serve as annuity providers. The retirement age for non-government employees, which is the age at which they will be able to withdraw their savings and buy an annuity will be decided by the PFRDA<sup>2</sup>.

6. **Authorized Retirement Advisors (ARAs)** will help in marketing the new system to potential members. They will advise and assist members with opening retirement accounts, as well as with selecting appropriate pension fund managers and products. The ARAs will conform to a uniform code of conduct and ethics and will have to pass a certification examination prescribed by the PFRDA in order to obtain a periodically renewable work license. The ARAs may be affiliated to specific PFMs, POPs or may work as independent advisors. Existing agents and financial intermediaries of mutual funds and insurance firms will also be able to serve as ARAs by passing this certification examination. The transaction forms filled by the members of the new pension scheme and deposited through an ARA will bear the latter's certification number. Using this, the CRA will keep a track of the all the ARA transactions and the volume of transactions transacted through each ARA. The PFRDA shall determine the cap on the charges to be paid to the ARAs by the POPs/PFMs. The PFRDA can use PFM-wise / POP-wise ARA data generated by the CRA and compare the same with ARA disbursements reported in the PFM/POP annual statement of accounts. A malpractice detected in this regard shall be construed as contravention of the license conditions and may lead to cancellation of the PFM/POP registration as well as the ARA certification.
  
7. In this entire process of accumulations and withdrawals, a sound **regulatory framework** would give individuals an umbrella of safety with respect to problems of risk management and prevention of fraud. The PFRDA will regulate the charges, entry and exit, quality and provision of service of POPs, ARAs, CRA and PFMs during the accumulation phase of this pension system. The PFRDA shall also approve periodic

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<sup>2</sup> A further discussion on Exit Rules is provided in Section 4.8.1, page 28

investments on account of CRA system upgrades. The process of delivery of pensions to members by annuity providers will be regulated by the IRDA. However, if a member chooses to not withdraw his savings as a lump sum and decides to instead phase out his withdrawals from his PRA, he will continue to interact with the POPs, CRA and PFM and will thus remain the responsibility of the PFRDA as well.



**Note:** A detailed description of the various transactions in this system are provided in subsequent sections.

## 2.2 The Interim arrangement for new central government employees

1. The New Pension Scheme became operative from 1.1.2004. The scheme is applicable to all new entrants to Central Government including central government civil ministries, non-civil ministries and departments and armed forces (civil) which are paid a pension from the Consolidated Fund of India.
2. The DEA is setting up the institutional framework for the New Pension Scheme which is expected to be in place in a few months. Meanwhile, the CGA and the CPAO are jointly

managing the 'Interim Arrangement' of collecting contributions, issuance of unique account numbers, administration and recordkeeping for persons who join central government service on or after 01 January 2004.

3. In the interim arrangement, only contributions into Tier-I accounts (@ 10% of basic+DA), are recovered from the salary bills of new government employees every month. The Government matches this with an identical contribution into the employee's Tier-I account.
4. Deductions and contributions to Tier-I accounts begin only from the 2<sup>nd</sup> month after the government employee joins service. No deductions from salary or contributions by Government are effected for the month of joining service.
5. No deductions are made towards GPF contribution from these new government employees as the GPF scheme is not applicable to them.
6. Voluntary contributions to Tier-II (withdrawable) accounts are not permitted during under this interim arrangement.
7. The Central Pension Accounting Office (CPAO) is functioning as the 'Interim CRA' for the new pension scheme and is responsible for central recordkeeping and reconciliation of pension contributions by new central government employees.
8. The Pay & Account Offices (P&AOs) under the CGA are partly performing the role of the CRA (of allotting unique account numbers) and partly that of POPs – they are responsible for monitoring salary deductions and reporting of contributions to the CPAO.
9. The CGA has developed software which captures information on new employees and their contributions. The CGA has delivered training to most P&AOs on this software and on handling the accounting and information processes of the New Pension Scheme. The P&AOs have also instructed the relevant DDOs to provide information on new

employees.

10. The Departments of Railways and Posts have decided to issue unique account numbers to their new employees.

**(a) Allotment of Permanent Pension Account Number (PPAN)**

11. The CGA has developed and distributed a new form<sup>3</sup> for new employees to all P&AOs. The DDOs have been requested by their relevant P&AO to provide information on new employees in the prescribed format.

12. On joining service, the concerned DDO instructs a new government employee to fill up the form prescribed by the CGA and provide particulars such as his name, designation, scale of pay, date of birth, nominee(s) for the New Pension Scheme, relationship to the nominee etc. Consolidated information for all those who have joined service in the month (say January) is to be submitted by the concerned DDO in the prescribed format to his P&AO by 7<sup>th</sup> of the following month (February).

13. On receipt of the above form from the DDO, the P&AO allots a unique 16 digit Permanent Pension Account Number (PPAN) to the new employee. The first four digits of the PPAN indicate the calendar year of joining the scheme, the next digit indicates whether it is a Civil Ministry or a Non-civil Ministry, the next six digits represent the P&AO's code and the last five digits indicate the running serial number of the individual government servant in a particular calendar year. Each P&AO maintains an Index Register for the purpose of allotment of PPAN to new government employees.

14. The P&AO returns a copy of the statement indicating the PPAN number allotted to each new employee by the 10<sup>th</sup> of the same month. The DDO intimates the account number to the individuals concerned and also notes the same in the Pay Bill Register.

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<sup>3</sup> A copy of this Form is in Appendix '1'

15. The particulars of all new government employees (including the details provided by them in the prescribed format and their respective PPAN) received from various DDOs across the country are consolidated by the relevant P&AOs and forwarded to the Principal Accounts Office by the 12<sup>th</sup> of every month.

16. The Principal Accounts Office in turn consolidates this information and forwards the same to the CPAO by the 15<sup>th</sup> of the month. The CPAO feeds this information in its database.

**(b) Deductions towards the New Pension Scheme and its accounting**

17. An office memorandum regarding interim accounting procedures for these deductions was issued by the CGA on 24 February 2004. All principal CCAs/CAs were requested to instruct the P&AOs and the DDOs of their ministries / departments for compliance.

18. The DDOs/CDDOs prepare separate Pay Bill in respect of Government servants joining service on or after 1.1.2004. The CDDOs then prepare pay bills but do not make any payment to the new employees. All such bills for new employees are sent by them to the respective P&AOs on or before 20<sup>th</sup> of the month to which the bills relate for pre-check and payment.

19. Along with the salary bill for the government servants who join the service on or after 1.1.2004, the DDO/CDDO also prepares a separate bill for the matching contributions to be paid by the government and credited to the PPAN.

20. On receipt of the salary bills of the new employees, the P&AOs exercise usual checks and pass the bill and make the payments to the DDOs.

21. The P&AO consolidates the information on new employees received from various DDOs and forwards the same in a floppy to the respective Principal Accounts Office by the 12<sup>th</sup> of the month following the month to which the credit pertains. The Principal

Accounts Office consolidates the information and sends the same in electronic form to the CPAO by 15<sup>th</sup>.

22. CPAO on receipt of this information from all Principal Account Officers (including from the non-civil ministries) updates the database and generates exception reports on missing credits, mismatches etc. which are sent back to the P&AOs concerned through the Principal Account Officers for further action.

**(c) Transfers and promotions**

23. Whenever any government servant is transferred from one office to another either within the same accounting circle or to another accounting circle, balances are not transferred to another accounts office. However, the DDO indicates the unique account number and the month up to which the employee's contribution and the matching government's contribution has been transferred to the Pension Fund in the Last Pay Certificate of the individual.

24. The CGA is drafting rules regarding treatment of contributions in the event of a transfer or promotion of an employee covered by this scheme. In principle, if the basic pay of an employee covered by the scheme changes in the middle of the month, the change in the contribution amount to the PPAN will be effected only from the subsequent month. The CGA will shortly finalise the rules regarding responsibility for effecting the deduction and transfer to the PPAN – i.e. whether the earlier or new DDO will be responsible for this transaction.

**(d) Withdrawals**

25. No withdrawal of any amount is allowed during the interim arrangement. Provisions regarding terminal payments in the event of untimely death of an employee or in the event of his leaving the government service during the interim period are yet to be notified.

**(e) Reconciliation**

26. At the end of each financial year the CPAO will prepare an annual account statement for each employee showing the opening balance, details of monthly deductions and government's matching contributions, interest earned if any, and the closing balance. The CPAO will send these statements to Principal Account Officers for onward transmission to the DDOs through the P&AOs.

27. After the close of each financial year CPAO will have to report the details of the balances (P&AO-wise) to each Principal Accounts Offices, who will forward the information to each P&AO for the purpose of reconciliation. The P&AO will reconcile the figures of contributions posted in the ledger account of the individuals as per their ledger with figures as per the books of the CPAO.

After the New Pension System is in place the CPAO shall hand over the member identification information, salaries, deduction and accumulation to the new CRA. The P&AOs shall send the member information and contribution details to the CRA after verification.

### 3. CRA Responsibilities

The CRA will serve as the central administrative and recordkeeping agency and will be directly responsible to the PFRDA and members for the following:

- 1. Recordkeeping:** The CRA will be the single source for issuance of the unique account number to a member. Once this number is issued, the CRA will be responsible for capturing and recording personal details of the member, as well as all actions by the member including the date and amount of each contribution, instructions related to choice of PFMs and schemes, number of units credited to the member, changes in NAV and account values, etc<sup>4</sup>. The CRA will be expected to maintain this account information till a member retires and withdraws his full terminal balance from PFMs.
- 2. Reconciliation:** The CRA will accurately reconcile all instructions and information received from POPs and P&AOs with the exact funds that are received by it. The CRA will act on member instructions and allocate the funds to the selected PFMs and schemes only when the instructions and funds received from POPs and P&AOs match. It will also be responsible for accurately converting new contributions or transfers into units and for timely credit of these units (reconciled at prevailing NAVs obtained from PFMs) to relevant member accounts as also for speedy rectification of any errors in this regard. However, the calculation of NAV shall be the responsibility of the PFMs and not the CRA and carried out as per the methodology specified by the PFRDA. In this process, the CRA may receive a large number of documents, letters, requests or complaints in a non-electronic format. The CRA will be required to digitize and electronically store all such information / documents.
- 3. Netting and funds transfer:** The CRA will receive member contributions and instructions and transfer a lump sum, netted amount to each PFM for allocation under

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<sup>4</sup> The POPs and P&AOs will be responsible for the accuracy of the data that they capture and transmit to the CRA. This responsibility will be specified by the CRA in its service contract with these entities.

each scheme on behalf of the members on a daily basis. When a person retires and selects an annuity provider, the CRA will withdraw the funds from the relevant PFM(s) and transfer the same to the relevant annuity provider. If a member chooses to withdraw his savings in a phased manner after he retires, the CRA will be responsible for withdrawing the sums from the relevant PFM and transferring them to the designated bank account of the member.

4. **Customer services:** The CRA will provide members with a periodic, consolidated account statement and a facility to submit instructions for switches between PFMs and/or schemes. It will be responsible for standardizing information on account balances, fees and charges, performance, system operations, etc. Customers will be able to access the CRA for these facilities as well as for filing complaints against POPs or reporting errors in statements directly through the Internet, telephone or a POP. The CRA shall be mandated to maintain digitized records of all complaints for six months after these have been resolved by the CRA/PFRDA. A log of all the complaints shall however always be maintained.
5. **Interconnectivity and access:** The CRA will be directly responsible for enrolling and training a geographically widespread and appropriate set of agencies to serve as POPs to enable easy access to the pension system. It will provide the software specifications<sup>5</sup> and data formats to enable the PFRDA, POPs, P&AOs and PFMs to interconnect with it.
6. **Enforcement and compliance:** The CRA will be responsible for supervising the process of collection and timely transfer of member contributions by POPs. It will capture, report and act upon irregularities and impose penalties for delayed or inaccurate transfers by POPs. Importantly, the CRA will be able to monitor and report errors or delays in mandatory contributions by P&AOs on behalf of government employees. The CRA shall be responsible for effecting Tax Deduction at Source (TDS) for all withdrawals from Tier-I accounts at the time of retirement, as well as for periodic

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<sup>5</sup> More details on the software protocol and format is provided in Section 4.3 on page 24

withdrawals from Tier-II accounts. In addition, the CRA will be responsible for enforcing limits (if any) on member actions related to the number of PFMs or schemes that can be selected, the number and periodicity of inter or intra PFM switches as also limits on contribution values. The CRA will reconcile and debit (standard or differential) asset management fees or loads (if any) imposed by PFMs on terminal exit or switches between schemes or PFMs from member accounts.

In short, the CRA will be responsible for efficient collection and timely transfer of member contributions by POPs and P&AOs, timely allocation of these funds by PFMs, and accurately crediting and reporting allocation of units into each PRA.

### **3.1 CRA inter-linkages with other service providers**

In order to carry out its functions, the CRA will need to interact with the following entities:

1. **POPs:** The POP network (including banks, post offices, depository participants, P&AOs and all other entities which serve as service providers) will be electronically connected to the CRA (either directly or indirectly through their internal networks). The POPs will serve as the interactive service delivery channel of the CRA and will be provided a license, cryptographic keys and interlinking format and system specifications by the CRA. If required, the CRA should be able to provide relevant software to each POP. POPs will use this software/formats, electronic connectivity and their keys to access the CRA and to transmit member instructions and the amount of contributions to the CRA. Bank POPs will use their existing infrastructure and permissions to also channel member contributions. If a POP is not a bank, it will use the banking channel to transmit the funds to the CRA. If India Post serves as a POP, their current capabilities including the dedicated V-SAT-based network of around 4000 branches which are capable of electronic transfer of funds and instructions, can be harnessed into service delivery.

In the case of government employees (mandatory participation), each relevant Pay & Accounts Office (P&AO) which manages the government's payroll process, will be

registered with the CRA and will also obtain a unique access code by the CRA. The P&AOs will be electronically connected to the CRA using the Internet. These P&AOs will use their respective access codes to access the CRA and the bank or Post Office which is used for payroll related transactions, to transfer the mandatory (10%+10%) contributions (funds). The P&AOs which are not automated, will access the CRA either through a conveniently located POP or through telephones / fax. In this case, the P&AO will use the POP or telephone / fax to transmit member instructions regarding PFMs or schemes but will use the banking channel to transmit funds to the CRA. For instructions through the telephone or fax, the CRA may demand some additional verifications and checks.

2. **PFMs:** Firms designated as PFMs by the PFRDA will be electronically connected to the CRA and will be provided with access codes and system software specifications/format. The PFMs will use this access code and communication formats to confirm receipt of netted assets and instructions regarding investments, confirm allocation of funds and communicate the NAV of each scheme to the CRA on a daily basis. This information will enable the CRA to credit the relevant number of new units to the account of a member based on his new contributions or switching instructions.
3. **Annuity Providers:** Annuity providers will also be electronically linked to the CRA and will receive a unique access code and system software. Once a member selects an annuity provider, the CRA will transfer the specified sum along with the accurate personal information and banking details of the member to the annuity provider on behalf of the member. Annuity providers will use their access codes to confirm receipt of this amount.
4. **PFRDA:** The CRA will be electronically linked to the PFRDA using the Internet and system software formats developed by the CRA. This connectivity will be used by the regulator to regularly access a variety of MIS reports. These may include reports on member activity and preferences (flows to specific PFMs and schemes including the

default option), errors and penalties on POPs, member grievances, complaints and redressal status, NAVs and PFM performance, changes in charge structures, etc. The PFRDA can use this channel for ongoing operational review of the institutional arrangements. In the course of regulatory proceedings or at other times in public interest, the PFRDA may require the CRA to submit any information in any form that it requires.

5. **Members:** For some transactions, the CRA will interface with members (government employees, other individuals and NRIs) only through its service network of POPs or P&AOs. These will include transactions related to account opening and transfer of new contributions. However, for non-financial transactions (switching between PFMs or schemes, viewing account balances or statements, reporting changes in employment status or contact information, registering a complaint, or ordering information on the system), members will be able to interact with the CRA through the Internet and telephone. Importantly, CRA will offer a facility for local language communication on its website as well as on telephones. Internet or telephone access will be protected by issuance of a unique user ID (which can be the unique account number) and a password (I-PIN for Internet access and a T-PIN for access through telephone) by the CRA to each member. Issuance of a *numerical* unique account number (instead of an alpha-numeric number) will be essential – especially for telephone access. In the future, members may also be able to undertake other (financial) transactions using the Internet, ATMs or smart cards (like switching funds from their bank accounts to their retirement accounts).

### 3.2 System Objectives (the rationale for CRA)

- a) **Lower transactions costs:** Global evidence clearly shows that administrative costs and charges have a very significant impact on benefits and can dramatically reduce terminal accumulations. In some developed countries (like the UK and Australia), administrative charges have resulted in a reduction of benefits by as much as 55%. By

centralizing the administration and recordkeeping process, pension systems can harness the benefits of lower transactions costs. Several new reforms (Argentina, Mexico, Sweden, Croatia, etc.) have chosen to adopt a central recordkeeping model. Central recordkeeping allows several benefits including economies of scale with a large base of members. Importantly, a CRA will be easily able to deal with millions of low value transactions and small account balances (which we will certainly face in India) at costs which are comparable to those witnessed in our equity markets. The facility of 'netting' where the CRA also serves as a central clearinghouse is only possible with this model. With a CRA and a non-proprietary service network, we also avoid the costs and limitations of each PFM building a proprietary distribution capacity.

- b) **Efficient customer services:** A central recordkeeping facility is essential for implementing several critical features of the new pension system – the facility of a unique account number for portability across jobs and locations (which is only possible with central recordkeeping). This helps reduce the incidence of multiple accounts; enables members to seamlessly switch between PFMs and schemes without the necessity of withdrawing from their accounts to affect such transactions; offers a single, consolidated account statement to customers; enables the facility and benefits of a 'default' option; offers wider and easier access (not possible if PFMs build proprietary distribution mechanisms); and provides a uniform quality of service to all customers regardless of location or PFM choice.
- c) **Regulatory efficiency:** A central recordkeeping agency (CRA) is directly responsible to the regulator for the quality of services and efficiency of operations of the network of service providers. In this way, the CRA can play an essential role in ensuring operational efficacy of the system. The CRA will be able to efficiently monitor compliance of mandatory contributions by P&AOs, ensure efficient and timely transfers between schemes and PFMs, capture information on delays or errors in transfers by POPs and P&AOs, minimize fraud and malpractices by service providers and efficiently redress complaints and grievances.

## **4. Functional and Service Obligations of the CRA**

The CRA will be responsible for seamless and error-free system operations involving POPs and PFMs, enabling nation-wide, portable outreach and access to the system, as well as for recording and maintaining accurate and updated information on all transactions by all members across multiple decades. The CRA will be expected to set up the required capacity and provide the service network with electronic access to meet these functional obligations. In addition, the CRA will be responsible for customer services and communication (either directly or through the POP network) as well as for monitoring and reporting mandatory contributions. Therefore, its capacity will need to include its service obligations to individual members and employers. Over the years, as a result of advances in technology as well as growth in the number of member accounts, POPs, PFMs and other service providers, this pension system is likely to undergo several improvements and changes. It will be necessary for the CRA system and its functional and service obligations to be flexible to absorb future changes and improvements. The functional and service obligations of the CRA as well as member actions which will drive the system specifications and architecture are described in this section.

### **4.1 Unique identification number**

A key feature of this system is its ability to offer a portable account which is achieved by allotting a unique retirement account number to each member. This unique account number will be essential for account reconciliations and will counter the problems with account duplication. The CRA will be required to provide the technology for generating and issuing a unique account number to over a billion members located across 3.3 million square kilometers. This number should be generated keeping in mind future changes in technology, new applications for this number in the future (including integration with other identity numbers like tax, voter ID, etc.), increases in membership, security of member accounts, and remote customer transactions using a variety of media including the Internet, telephones, ATMs and electronic cards. It may be necessary for this unique

number to be numerical (and not alpha-numeric). This (numerical number) is essential for secure transactions using telephones, occupies less space in the hardware and can be used by illiterate persons. This number, coupled with member specific information fields (date of birth, father's name, place of birth, etc.) will be used to validate member instructions and account ownership.

A temporary unique ID is being currently issued by the CGA under the present (temporary) 'interim' arrangement to new central government employees who join service from 01 January 2004. This temporary number allocation will be discontinued and each of these new employees covered in the interim phase will be allotted new unique IDs by the CRA. The unique account numbers issued to these employees by the CRA, coupled with information on their employment status will be essential to calculate and monitor mandatory contributions by employees and the employer.

Importantly, there are already some efforts in India to generate and allot unique numbers (for example the SSN number by the EPFO) which may satisfy the above criteria. The PFRDA will evaluate the merits of adopting this technology. If the PFRDA decides to use this existing capacity for issuing unique account numbers, it may be technically possible for the CRA to connect to the EPFO for accessing this capability. In the event that the government decides to license additional recordkeeping agencies in the future, the process of generating unique account numbers should continue to be managed by a single agency to avoid account duplications.

## **4.2 Support for corporate, self-employed and government employees**

The system designed by the CRA should allow for differential contributions into a large number of investment accounts for a variety of members and member preferences:

- Discretionary (voluntary) contributions by individuals
- Discretionary (voluntary) contributions by employers
- Mandatory employee contributions (government employees)
- Mandatory employer contributions (government employees)

- Contributions to the 'default' option
- Phased / lumpsum withdrawals at exit
- Participant loans (if any)
- Lump sum withdrawals and transfers to annuity providers

The CRA will issue individual account numbers to self-employed workers, government employees and private sector employees. Crediting contributions from the government into the PRA of its employees would require the system software to have the capability of matching the PRA number of each government employee with the employer. This will be necessary for government employees since the mandatory matching contributions by the employer would cease if a member leaves government service. Other employers may also choose to contribute to their employee accounts on a voluntary basis – the CRA would need to relate and credit such contributions into employee IRAs. There could also be an instance, where the Government privatizes a government undertaking while maintaining the service conditions of employees. Here, the employees may continue to be recipients of the matching employer contributions. The corporate accounts under this condition would change, while the PRA would remain unchanged. There could also be a condition in which there is a merger of two entities with different matching contributions for different employees. The system should be able to handle all such foreseeable conditions.

The PFRDA may prescribe certain ceilings for fees and charges by service providers. All fees and charges will be transparently reported to the PFRDA. Importantly, 'rebating' or sharing of fees with members will *not* be permitted. The system should provide for advanced tracking and reporting of withdrawals from Tier-II accounts and for transfers from Tier-II to Tier-I accounts. Accurate vesting calculations (including TDS liabilities) when prior distributions have occurred should also be provided.

### **4.3 Open architecture for software**

The CRA software system is required to be an open architecture, in the sense of having fully documented interfaces. While encryption would be used for security, the full details of

the protocols, encryption procedures, and feed formats would be available in the public domain, so as to foster innovative and low-cost software development. The client site should not be forced to use proprietary software through the technology choices of the CRA. There would be no role for 'security through obscurity'.

POPs, PFMs and other service providers who have to electronically connect to the CRA would have the option of either using/buying software from the CRA, or developing their own software or buying software from some third party. If these service providers decide to not use software from the CRA, they will not require any permissions or approvals or empanelment procedures. The CRA would be free of 'security through obscurity'.

The CRA website will be required to freely disseminate the following documents and files to the public: (a) the full document of the interface language / data formats / file formats, (b) sample source code of a skeletal working application that utilizes this feed format. The CRA would be required to depute staff to process questions and problem reports that would be received by email, from external software developers.

The CRA would be free to choose whether to conduct (paid) training programs on how to build software that speaks to it.

#### **4.4 System flexibility for future changes**

The system should be flexible and have the capability to handle future changes including:

- Introduction of new (additional) schemes by PFMs
- Increase in the number of PFMs
- Termination of a PFM license or takeover of an existing PFM by a competitor
- Increase in the number of accounts
- Increase in the number of sub-accounts, i.e. beyond tier-I and tier-II
- Increase in the number of POPs
- Integration with additional CRAs in the future (if any)

- Changes in technology
- Changes in regulations or government policies (including those on taxation)
- Changes in fees and loads as in the limits (if any) prescribed by the PFRDA

## **4.5 Reports**

The CRA system should enable the PFRDA to obtain on-demand reports and information on performance, compliance, fees and charges (and changes therein), errors, complaints, members actions and behavior, etc. The system should enable the PFRDA and members to perform benefit simulations<sup>6</sup> based on discretionary or mandatory contributions, current account balances, age, and other criteria. The system should also have the capability to store date-wise information of transactions, PFMs or schemes selected, NAV data, etc. to facilitate periodic valuations on any user-selected frequency. The system should be able to generate accurate, periodic reports indicating the same. The system should allow allocation of earnings to a PRA based on a variety of choices exercised by the user. Some of these choices could be user-defined – fixed percentage, pro-rata of existing holdings, unit value, predefined user-input. The system should be able to generate reports which illustrate plan and participant values by investment. The system should be able to calculate earnings on accounts since the last valuation (taking into account contributions, withdrawals, transfer, loan payments, premium, dividend and compensation). The system should support transaction based compensation to allow for the prior valuation compensation without rerunning the valuation. The system should be able to generate reports in formats with user-controlled content and design. A complete report generator should be made available for users to create and save their own report formats. And finally, the system should enable reconciliation of allocation to schemes and IRAs at all times.

## **4.6 Inter-linkages**

The CRA system architecture should allow PFRDA, POPs, PFMs and members to electronically access information, and transmit instructions and funds in a secure manner

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<sup>6</sup> *All simulations by CRA or service providers (POPs, PFMs, ARAs, etc.) will be based on standard measures prescribed and approved by the PFRDA.*

and using a variety of media (V-SAT, Internet, telephones, ATMs, etc.) with strict reconciliation features and safe-guards to avoid duplications, delays, errors and fraud. The CRA must provide the necessary software specifications and file formats to POPs, PFMs and PFRDA. The software procured from the CRA or developed by the service providers should be able to determine the identity of the member in each situation and especially at the time of issue of a new PRA number, and also at the time of vesting / exit.

#### **4.7 Clearinghouse functions**

The CRA's process architecture should allow it to reconcile and transmit (or receive) netted amounts from PFMs using its bank.

#### **4.8 Member transactions**

This section outlines (a) some restrictions and rules for member actions, and (b) the flow of transactions (instructions, information and funds) and operational roles of the CRA, POPs, PFMs and the PFRDA for delivering a variety of identified customer services. The CRA will define a standard set of account opening processes using a standard file formats for all POPs and P&AOs. These would include verification criteria and standardized forms for opening new accounts and future account transactions including requests for statements, etc. In addition, each POP and P&AO registered with the CRA will provide full contact information to the CRA. These entities will be allotted a unique access code which will help the CRA in tracking transactions which originate from these entities. This information will also assist the CRA in tracking and reporting mandatory contributions by government employees. Information regarding procedures, functional and service obligations of the POPs and P&AOs and the permissible time for transfers will be articulated in the Operations Manual for POPs prescribed by the CRA. In addition, the CRA will specify the formats for information display and distribution.

##### **4.8.1 Operational rules and restrictions for Members**

a) **Minimum amount per contribution:** Each contribution by a member into his PRA and

the process of its collection, transfer and deployment will be subjected to transaction costs and fees levied by service providers including ARAs, POPs, CRA and PFMs. While the system should not exclude persons with potentially low value contributions and account balances, it is important for the PFRDA to prescribe a minimum amount that can be accreted per transaction to ensure that the value of the contribution is not significantly eroded by these transaction costs. The value of each monthly mandatory contribution by a central government employee is already defined (20% of basic salary plus DA). It is proposed that the PFRDA prescribe a minimum of Rs.300 per contribution by all other members. This implies a contribution rate of Rs.10 per day for a monthly contribution. While no concept of monthly contributions by this segment may be imposed, this will ensure that a significant part of the voluntary contributions into Tier-I accounts is finally invested. For workers who can only contribute much lower amounts (and may perhaps prefer more frequent accretions due to a daily or weekly wages), some mechanisms for frequent 'pooling' of contributions and transfers may be encouraged using self-help groups, NGOs and micro-finance institutions (MFIs).

- b) **Minimum annual contribution:** For this DC system to achieve its core objective of providing adequate old-age income security to members, it may also be necessary for the PFRDA to consider mandating a minimum annual contribution into a PRA (Tier-I) – for members who participate on a voluntary basis. It is proposed that this minimum annual contribution be pegged at Rs.3600 (i.e. Rs.10 per day) (2003-04 prices). This annual contribution is likely to result in an annuity of roughly Rs.800 per month at age 60 after 25 years of uninterrupted contributions. Non-government employees will however be free to decide the periodicity of their contributions provided that each contribution is at least Rs.300 and that the sum of contributions per year totals Rs.3600. Investments in Tier-II accounts shall be allowed for voluntary members only if they invest a minimum amount of Rs. 3600 in tier-I. The PFRDA may change the minimum contribution requirement from time to time.
- c) **Nomination facility:** The CRA will provide each member a facility to specify a nominee

(wife, children, parents or any other person) to whom the Tier-I account can be transferred in the event of death of the member before he/she retires. If the nominee is already a member in the pension system, the two accounts will be merged. If the nominee is not a member, he/she will be able to own and operate this account till retirement and draw benefits from it. A similar nomination facility will also be available for the Tier-II account. In this case, the nominee will be able to withdraw the balance from the Tier-II account or transfer the same to the Tier-I account.

- d) **Exit rules:** Premature withdrawals from Tier-I accounts will not be permitted. However, if a member decides to close his Tier-I account and exit from the system before retirement, he will be required to annuitize a majority of his terminal accumulations. This facility will be especially useful and relevant for informal sector workers who may not work under any prescribed retirement age. Such members will be able to exit earlier (than say government employees who will retire at age 58 or 60). Mandatory additional annuitization will ensure a steady, monthly income to these members during their lifetime and help them in staying above poverty during retirement<sup>7</sup>.
- e) **Restrictions on inter or intra-PFM switches:** It is proposed that the system architecture be developed in *phases*<sup>8</sup> to reduce the time-to-market for the CRA. In the initial phase of system implementation (of 8-12 months), members will not be permitted to exercise any options to switch between PFMs or schemes. They will however be free to specify their preferences for PFMs or schemes at the time of contribution. This restriction will be relaxed and lifted in a phased manner by the PFRDA in consultation with the CRA. However, all transfers (new contributions or switches) may be subjected to some specified 'loads' – the ceilings for such loads will be prescribed by the PFRDA.
- f) **Restrictions on portability:** In the initial phase of system implementation (of 8-12 months), each member will be required to transact only through one POP or P&AO. This restriction will be lifted by the PFRDA once the system stabilizes and members will

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<sup>7</sup> The extent to which annuities will be useful for poorer persons will need to be examined in more detail

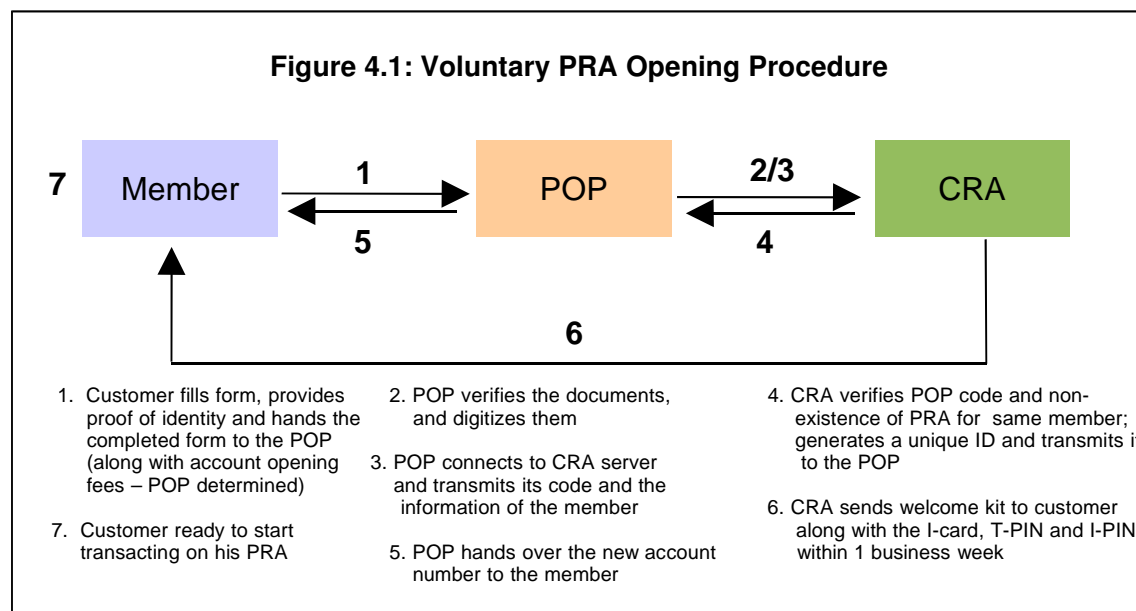
<sup>8</sup> The implementation process is described in more detail in Section 7 on page 62

thereafter be able to enjoy full portability and will no longer be 'tied' to any POP or P&AO.

#### 4.8.2 Opening a new personal retirement account (mandatory and voluntary)

##### (i) Process for opening a voluntary PRA

Only POPs will be authorized to open a new personal retirement account and allot the unique account number to a member due to identity verification needs. The member will walk into a POP location, complete and submit a standard form along with a proof of identity to the POP. Once the identity is verified, the POP will correctly record the details in the form and electronically transmit the full data to the CRA. The CRA will reconcile this new account request and data with its existing member database to ensure the relevant person does not already have a PRA to avoid duplication. If at any time, the CRA finds that two CRA accounts exist for the same person, the CRA will undertake prescribed reconciliation actions.



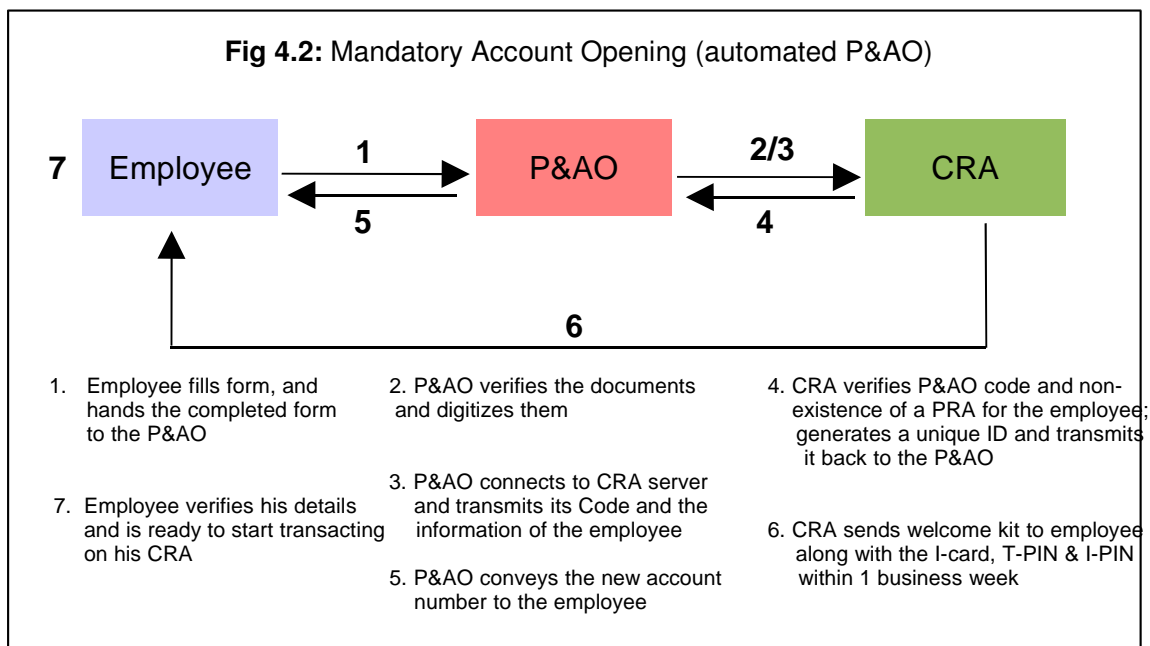
Thereafter, the CRA will communicate the new unique account number allotted to the new member to the relevant POP. The POP will issue a PRA I-Card to the member. This card will include a photograph, account number and other information unique to the member. A

member will be able to obtain a new I-Card from a POP by paying a fee if the earlier card is misplaced or damaged or if the member's personal details (name, address, etc.) change. If the card is misplaced, the POP will carry out some strict identity verification before issuing a new I-Card.

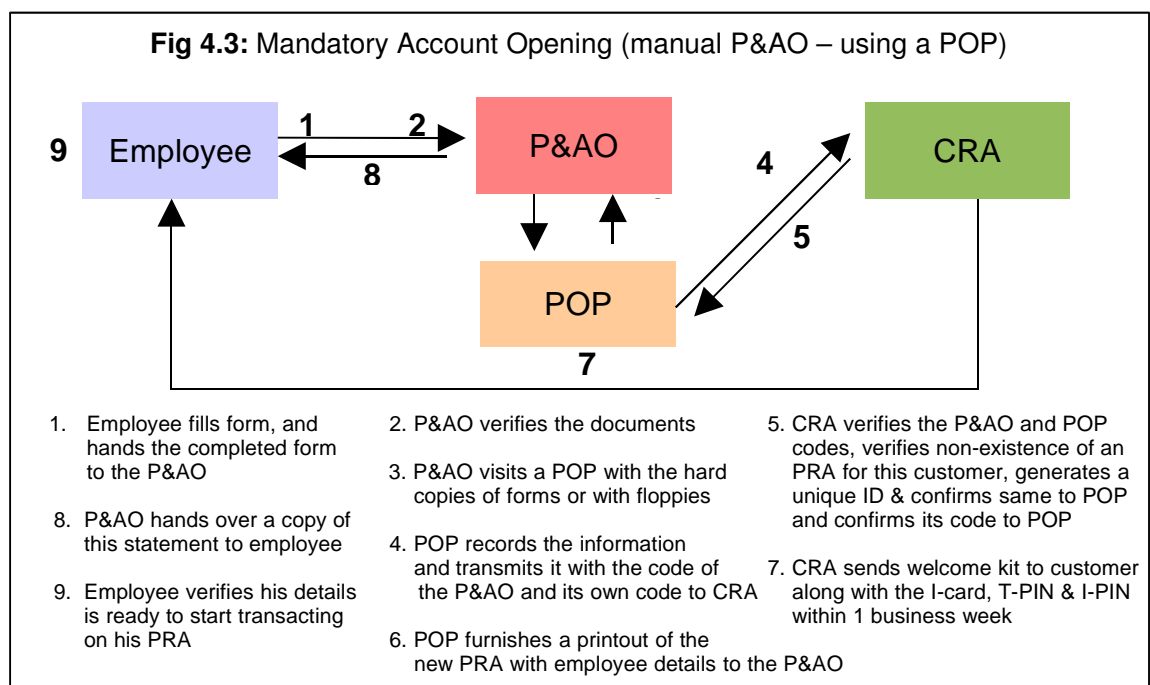
A few days after this account is opened, the member will receive a new account informational packet from the CRA which will include a T-PIN for secure telephone access and an I-PIN for secure Internet access to their accounts, generic information on the system, account operations and member rights and obligations. The activation of services through telephone access and Internet access using T-PIN and I-PIN will be allowed by the CRA only on receipt of a written confirmation from the member that T-PIN and I-PIN have been received. This process is outlined in Figure 4.1.

*(ii) Process for opening a mandatory PRA*

When a new employee joins government service, he will receive a pension information docket from the relevant P&AO or DDO. This will contain simple information on the system operations, member services and rights as well as forms for services and transactions. For P&AOs which can be electronically connected to the CRA, the process for opening a new PRA will be relatively simple and very similar to the one followed by POPs. Such P&AOs will be able to use the Internet to log into a secure server of the CRA, register new employees and transmit the relevant information (including salary, specified contributions by employee and government, date of joining, etc.) to the CRA. After this information is received, the CRA will allot the unique account number to each registered employee. The CRA will courier the PRA I-Card, T-PIN and I-PIN directly to each new member. The activation of services through telephone access and Internet access using T-PIN and I-PIN will be allowed by the CRA only on receipt of a written confirmation from the member that T-PIN and I-PIN have been received. This transaction is outlined in Figure 4.2.



If a P&AO is not automated, it can use the services of a designated POP for transmitting employee information and obtaining account numbers. This transaction is outlined in Figure 4.3.



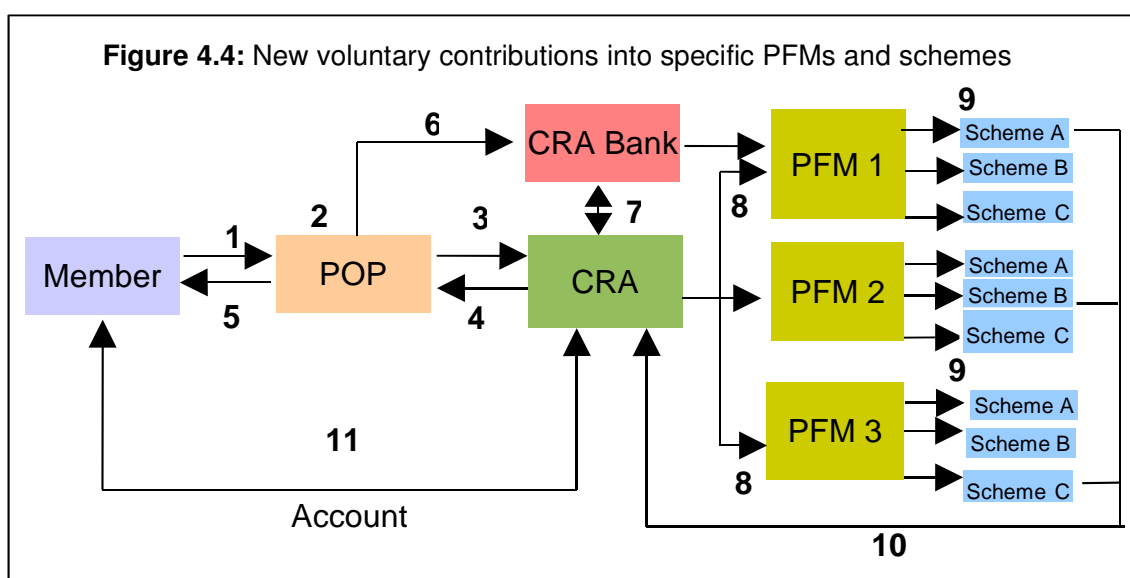
#### **4.8.3 New contributions and PFM/scheme selection**

a) **Voluntary accounts:** Once a member has received a unique PRA number and his I-Card, he will be able to use any convenient POP to accrete fresh contributions into his PRA. The member will be required to fill a form and specify his choice of PFM and scheme. The member will be able to use a single form to allocate this contribution across multiple PFMs and/or schemes. The POP will verify the identity of the member and enter the details of this transaction – account number as well as the amount allocated for each PFM and scheme. It will accept the contribution and transmit the verified instructions to the CRA along with its unique access code. The CRA will verify the POP access code and reconfirm the allocation and PRA number to the POP. The POP will handover a printout of this verified transaction to the customer. The POP will then use the banking channel to transfer the funds to the CRA. The flow of instructions and contributions is mapped in Figure 4.4.

b) **Mandatory accounts:** In the case of government employees, the initial (monthly, mandatory) contributions will flow through the P&AO network in a similar format. Here, the employee will fill out a standard form specifying his choice of PFM and scheme, and submit it along with his PRA number to the P&AO. The P&AO will access the CRA using the Internet or a convenient POP, verify its access code and communicate the amount being transferred. The CRA will verify this transaction and reconcile it with the mandatory amount due from this employee. This transaction is outlined in Figure 4.5. The Tier-II accounts for the Government employees are opened automatically along with the allotment of the PRA number.

In future, a member may be able to accrete new contributions, select the PFM(s) and scheme(s), verify this allocation and the credit of units in his PRA through the Internet or an ATM. In these cases, the member will be able to electronically transfer funds to the CRA and verify this transaction by logging onto the CRA's website and using his account number and the I-PIN. This contribution may be through a cheque or in cash. If the

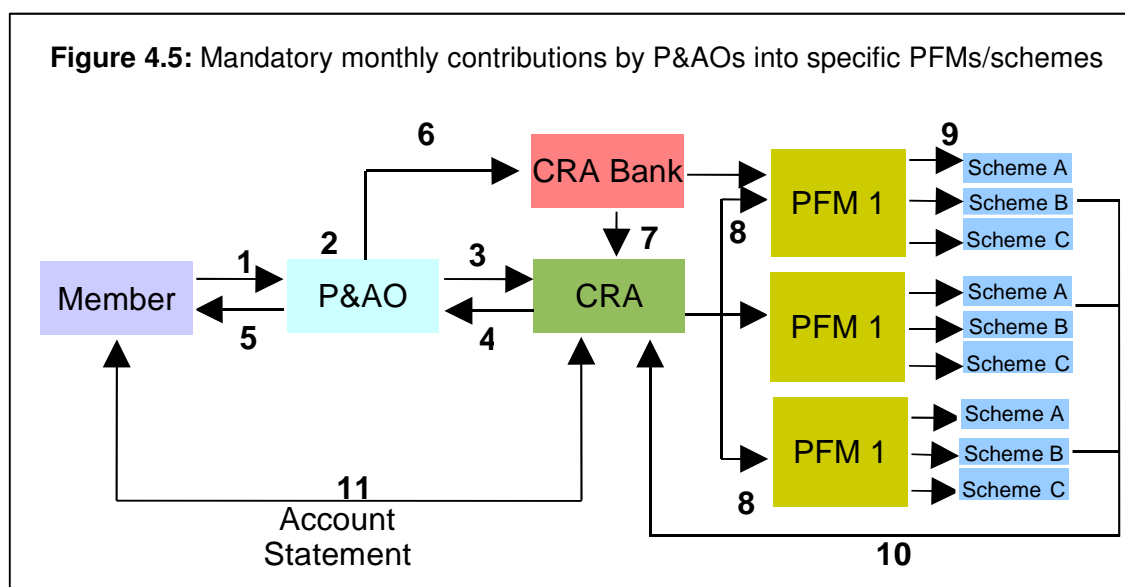
member uses a local cheque to accrete new contributions, it will take up to 3 additional working days for these funds to be credited to the POP and for the POP to transfer them to the CRA. Cash contributions will be transferred to the CRA on the same day. In either case (government employee or voluntary member), the member will be able to verify transactions as well as the NAV and date on which the new units are credited into his PRA through the periodic statement received from the CRA or by simply logging onto the CRA website.



1. The Member fills the PFM and scheme selection form and indicates his choice of PFM and scheme. He hands over the form along with his identity proof and contribution (as cash or cheque)
2. The POP verifies the member's identity, double-checks the form and contribution amount and enters the details on his computer
3. POP logs into the CRA server and transmits its own access code, the member contribution amount and PFM/scheme choice
4. The CRA confirms receipt of the instruction (regarding PFM and scheme) and also confirms the contribution amount due from the POP on behalf of the customer
5. The POP hands over a printout of the transaction confirmed by the CRA (which will include the amount, PFM and scheme selection as well as the date and POP code) to the member. The member will be able to tally this slip with the consolidated account statement or with his account on the CRA website
6. By evening (and at a specified time), the POP collates all financial contributions received during the day and transfers them in a single transaction to the CRA's designated bank.
7. The CRA tallies the funds received by its bank from the POP with the electronic advises received directly by it from POPs in the day. The CRA accepts and allocates the funds only if they exactly match the electronic advise. The CRA will claim and receive short-falls (if any) before allocating the funds from this batch to the PFMs.
8. The CRA collates the sum total of all fresh contributions to each scheme as well as the withdrawals (due to switching) from the same scheme for that day. The CRA then 'nets' the exact amount to be transferred to each scheme of each PFM (including net receivables if there is the netted amount for a scheme is negative). The CRA then collates the gross amount payable or receivable from each PFM. The CRA transfers this single, netted gross amount to each PFM along with an instruction specifying the amounts to be invested under each of the three schemes.

9. Once the PFM receives these funds, it invests them as per the specified investment rules
10. The PFMs confirm the NAV at which the investment under each of the schemes has been affected
11. The CRA reconciles the instructions and the amount contributed by a member with the NAV disclosed by the PFM and updates the PRA of the member by allocating the relevant number of units into it. This transaction as well as the sum total of all units held by a member under each scheme selected by him is included in the consolidated account statement sent by the CRA to the member. This statement may be sent either electronically or physically as per the member's preference.

**Note:** If a branch of a POP does not have the ability to electronically transfer funds to the CRA's bank, it will electronically confirm availability of these funds to its head office. The head office will in turn transfer these (and all other similar instructions received from its other branches for that day) to the CRA's bank along with the codes of the branches and the amounts received from them as a single transaction.



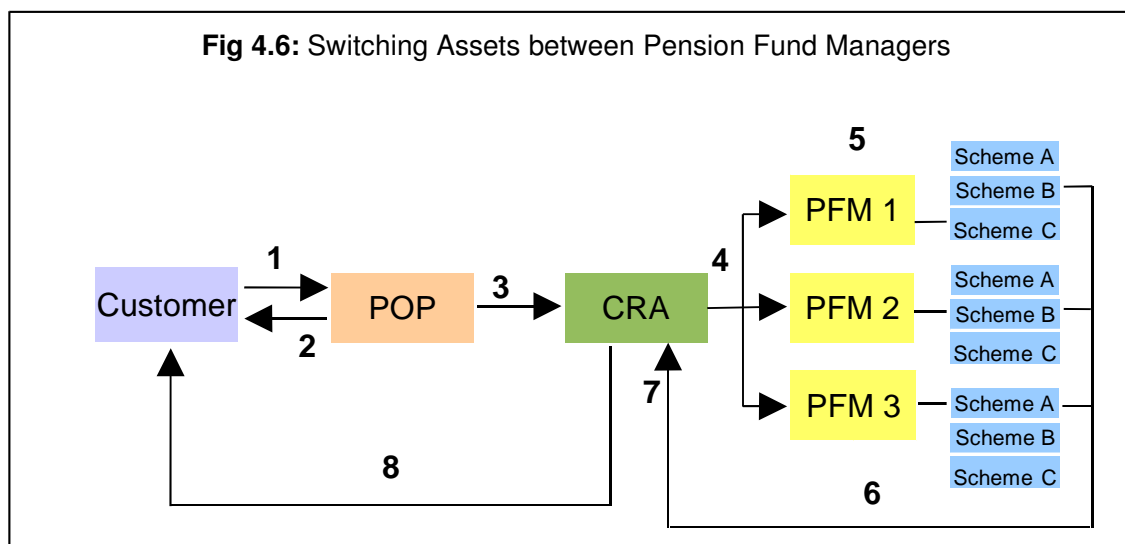
1. The Government Employee (member) fills the PFM and scheme selection form and indicates his choice of PFM and scheme. He hands over the form to the P&AO
2. The P&AO logs into the CRA server and inputs his access code.
3. CRA confirms the access code to the P&AO
4. The P&AO enters the contribution amount and PFM/scheme choice along with the PRA number of each employee
5. The CRA confirms receipt of the instruction (regarding PFM and scheme) and also confirms the contribution amount due from the P&AO on behalf of the member
6. The P&AO hands over a printout of the transaction confirmed by the CRA (which will include the PRA number, employee details, amount of contribution, PFM and scheme selection as well as the date and P&AO code) to the member. The member will be able to tally this slip with the consolidated account statement or with his account on the CRA website
7. The P&AO gives a single instruction to his designated bank to transfer the consolidated sum of all contributions for all new employees covered by him to the CRA's bank.
8. The CRA tallies the funds received from that P&AO's bank with the electronic advise received directly from the same P&AO. The CRA accepts and allocates the funds only if they exactly match the electronic advise. The CRA will claim and receive short-falls (if any) before allocating the funds from this batch to the PFMs.
9. The CRA collates the sum total of all fresh contributions to each scheme as well as the withdrawals (due to switching) from the same scheme for that day. The CRA then 'nets' the exact amount to be transferred to each scheme of each PFM (including net receivables if there is the netted amount for a scheme is negative). The CRA then collates the gross amount payable or receivable from each PFM. The CRA transfers this single, netted gross amount to each PFM along with an instruction specifying the amounts to be invested under each of the three schemes.
10. Once the PFM receives these funds, it invests them as per the specified investment rules

11. The PFMs confirm the NAV at which the investment under each of the schemes has been affected
12. The CRA reconciles the instructions and the amount contributed by a member with the NAV disclosed by the PFM and updates the PRA of the member by allocating the relevant number of units into it. This transaction as well as the sum total of all units held by a member under each scheme selected by him is included in the consolidated account statement sent by the CRA to the member. This statement may be sent either electronically or physically as per the member's preference.

**Note:** If a P&AO does not have the ability to electronically transfer the instructions to the CRA, it will physically convey the PRA number and PFM/scheme preferences of the employees to its head office which will have electronic connectivity with the CRA. The head office will in turn transfer these (and all other similar instructions received from its other manual P&AOs for that day) to the CRA. Simultaneously, this office will instruct its bank to transfer the relevant amount to the CRA in a single transaction.

#### 4.8.4 Switching assets between PFMs

The CRA will provide members (voluntary and mandatory) the option to switch their assets between PFMs and schemes by either using the POP network or directly through its website. This transaction is outlined in Figure 4.6.



1. Customer hands over the form indicating PFM or scheme change to the POP
2. The POP verifies the documents and instructions and provides an acknowledgment slip to the customer
3. The POP logs into the CRA server, provides his access code and transmits the member instructions once his identity is verified by the CRA
4. The CRA collates all such instructions it receives from members and forwards a netted amount with instructions on allocation per scheme to each PFM at a specified time in the day
5. PFM allocates the funds as per the day's instructions
6. PFM confirms the allocation and the NAV information to the CRA
7. CRA updates member PRA with new/updated units
8. CRA sends updated statement to the customer (physical/electronic)

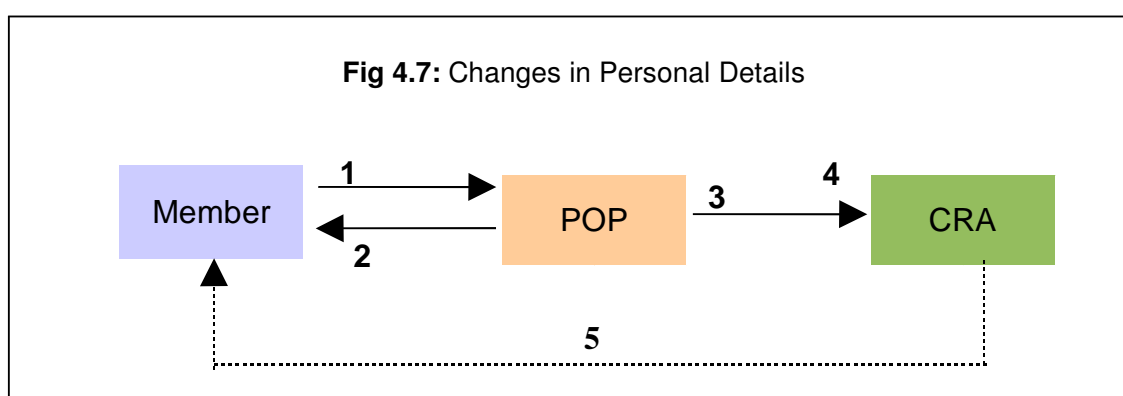
#### 4.8.5 Default option allocation

If the member does not specify a scheme but only selects a PFM, the CRA will credit the

contribution to the 'safe' scheme of the same PFM. However, if a member does not specify a PFM as well, the CRA will credit the contribution to the 'default' option. The details of this 'default' option will be decided by the PFRDA.<sup>9</sup>

#### 4.8.6 Changes in personal information

To change his personal information, a member will route the request to the CRA via the POP or through the CRA website. The transaction is described in Figure 4.7.



1. Customer fills the form indicating the required changes and hands it to the POP
2. POP verifies the customer and the changed information. Provides acknowledgment slip to customer
3. POP connects to CRA database and inputs the access code and changed PRA information.
4. Once the POP and the member data is verified, the CRA accepts the changes
5. CRA mails the updated account info to the customer. If customer has email ID registered with CRA, CRA sends electronic confirmation in any case.

#### 4.8.7 Obtaining information on charges and NAVs

Information on charges and NAV will be available in a standardized format at every POP location, newspapers, as well as through the websites of the PFRDA and CRA. The customer will be able to request for any other system information through the same channels.

#### 4.8.8 Account information and statements

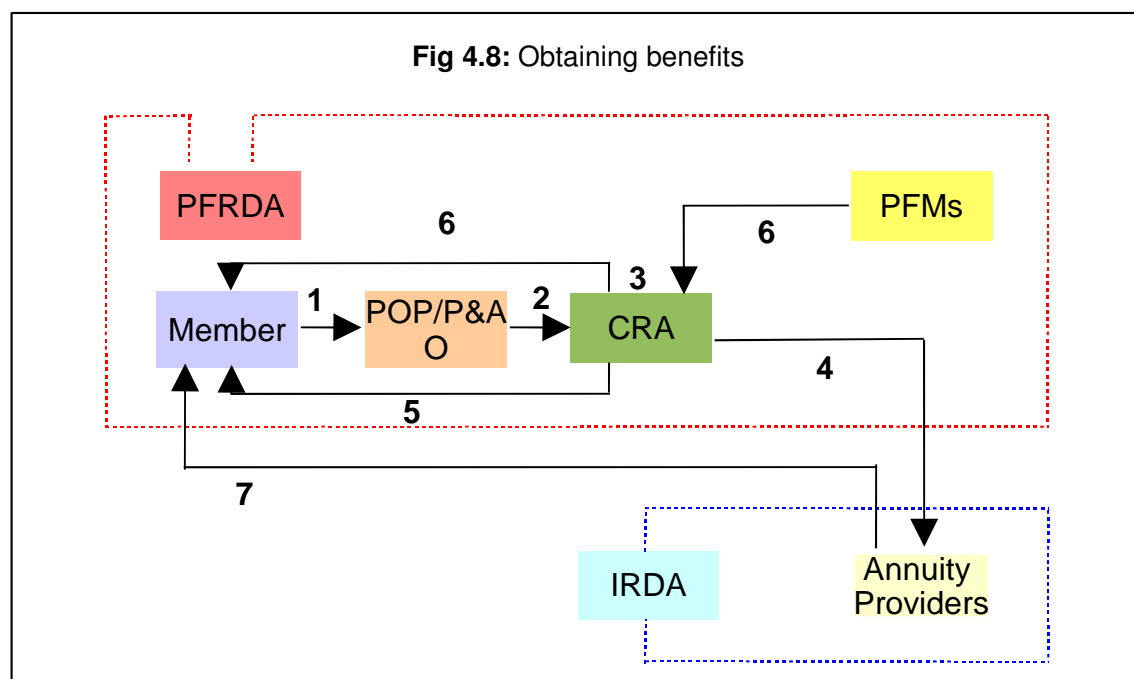
The CRA will provide periodic, consolidated account statement stating the contributions

<sup>9</sup> The precise treatment of the 'Default' option – will one or multiple PFMs manage the default option; which PFM(s) will manage the default option; the investment restrictions on this scheme; whether this scheme will be identical for all categories of members regardless of age, income, risk profile, etc. is being examined in detail in the PFM document titled "Managing Defined Contributions" being produced by IIEF

made, the date at which each contribution was received by the CRA, the POP through which this was transferred, the PFM/scheme selected by the member, the total number of units allotted and the NAV of the scheme as on date. The member will be able to obtain such statements more frequently through the Internet or POPs (perhaps at a fee).

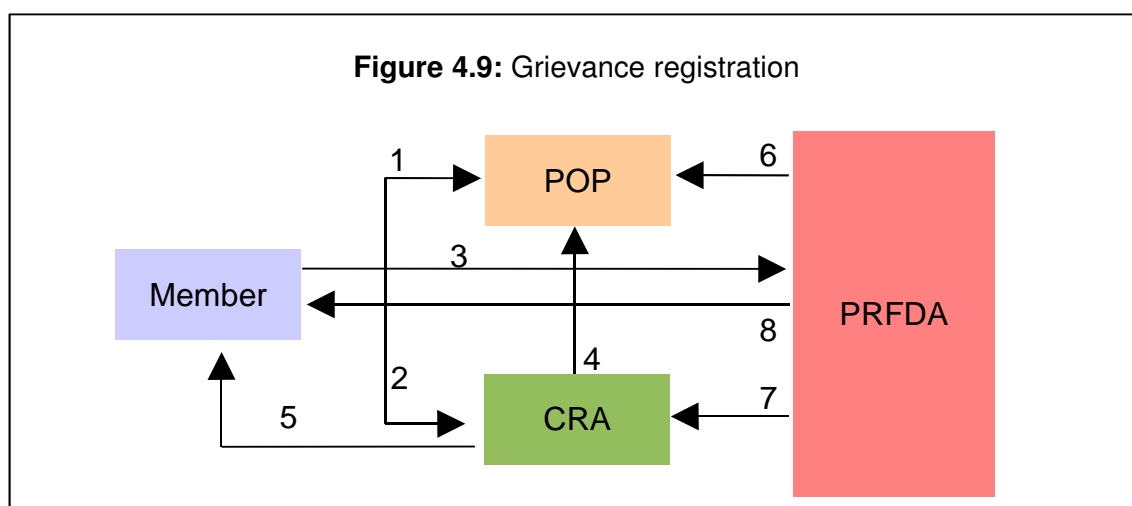
#### 4.8.9 Benefits

When a member retires, he will be permitted to withdraw the savings in his PRA. He will be mandated to annuitise a specified part of his balance to purchase an annuity which will keep him above poverty for the rest of his life. This amount will be decided by the PFRDA every year. The member will be able to withdraw the balance accumulations either as a lumpsum or in a phased manner over time. If he opts for phased withdrawals, his savings will continue to be invested in any scheme or PFM he selects and an amount decided by him will be transferred to his bank at intervals decided by him. The CRA will be responsible for transferring the funds as per the member's instructions to the annuity provider and/or his bank account. The CRA may be mandated by the CBDT to deduct tax (if any) payable on withdrawal of terminal accumulations at the time of exit (as well as periodic withdrawals from Tier-II accounts).



1. Member fills up a withdrawal form at a POP location indicating how he wishes to withdraw his terminal benefits. He will select the annuity provider for the mandatory annuitization amount and specify how he wants to withdraw the balance accumulation – as a lumpsum or in a phased manner. If he wishes to withdraw over time, he will specify his bank account number and the amount of withdrawal per month or any other periodicity.
2. POP verifies the member's identification, and transmits the exit request as well as the name of the selected annuity provider and its own access code to the CRA
3. The CRA verifies the amount of terminal balance in the PRA of the member, the permissible amount for lump sum (or phased) withdrawal and the amount required for the mandatory annuity (The CRA will withdraw the relevant amounts for lumpsum, annuity purchase and phased withdrawals using the usual netting process with PFMs)
4. **Mandatory annuitization:** The CRA will withdraw the requisite amount and transfer it to the selected annuity provider along with the specific type of annuity selected
5. **Lump sum withdrawal:** The CRA transfers the lumpsum withdrawal to the customer's bank account
6. **Phased withdrawal:** CRA leaves the amount marked for phased withdrawal in the PFMs and schemes selected by the member. Each month, the CRA arranges for the amount of phased withdrawal to be reach the customer's bank
7. The annuity provider starts transferring the annuity to the customer's bank account or directly by a local cheque or draft

#### 4.8.10 Grievances



1. If a member has a local complaint against the POP, he can get it solved locally at the the POP office. If he wants, he will also be able to file this complaint by completing a grievance form and getting it acknowledged by the POP,
2. If the member is not satisfied with the response from the POP, he will be able to file a grievance to the CRA who will take the necessary action against the errant POP. A copy of the acknowledgment slip for any earlier complaint will be submitted with this form. For this too he will get an acknowledgment slip from the POP.
3. If the customer is not satisfied with either the POP or the CRA or both, the grievance can be lodged directly with the PFRDA. Copies of earlier acknowledgment slips will be submitted along with this form.
4. CRA takes action if the complaint comes from a customer for a POP (point # 2).
5. CRA responds to customer with action taken against POP.
- 6/7. PFRDA takes action against the POP/CRA as per the grievance (point # 3).
8. PFRDA responds to customer with the action taken against the POP/CRA.

Importantly, customers will have the facility of filing formal complaints with the CRA or PFRDA using the Internet and checking on the status through either the Internet or telephone.

## **4.9 Operational regulation and compliance obligations of CRA**

1. **P&AOs:** The CRA will specify the system specifications for P&AOs and will also provide the software specifications and file formats as well as operations training to each P&AO office. Since the CRA will receive and reconcile the mandatory 20% contributions on behalf of P&AOs every month, it will be very well placed to monitor, identify and report incorrect or delayed contributions by the P&AOs on behalf of the government employees.
2. **POPs:** The CRA will be responsible for the security, efficiency and accuracy of POP transactions. POPs will be able to register as service providers with the CRA on the basis of eligibility criteria approved by the PFRDA, including experience, capital and technology infrastructure. The POPs will sign a service and functional obligations agreement with the CRA. Once a POP is registered, its operations and services will be governed by the Operations Manual prescribed by the CRA and approved by the PFRDA. The PFRDA may prescribe certain limits for POP service charges and fees and POPs will be able to charge any fees below the prescribed ceiling. The POPs may be required to pay a registration fee to the PFRDA or CRA. The staff of POPs will be required to pass a POP Pension System Operations examination mandated by the PFRDA and enforced by the CRA.

Since POPs will not be required to maintain any member records locally, a member will not be required to be 'tied' to any POP on a mandatory level. But members will be free to use the same POP for all transactions (if they wish) on the basis of convenience of location, lower charges or better services. The POPs will be liable to the CRA for errors, malpractices and delays and the CRA may impose appropriate penalties on the POPs. If the services or performance of a POP are found to be unsatisfactory, or if a POP is unable to discharge its service and functional obligations efficiently, the CRA will be able to cancel the POPs registration. Since members will not be 'tied' to a POP, cancellation of a POP's registration will not cause any excessive problems to members. However, in this situation, the CRA may suggest alternative POPs to the members

who's services have been disrupted. Each POP will be required to ensure the following:

- Each POP branch will be expected to ensure electronic connectivity with the CRA.
- POPs will be required to undergo an external systems, operations and controls audit every year by a qualified auditor.
- POPs will be expected to insure themselves and their customers against losses arising from any possible business risk or system failure.

3. **PFMs:** Once a PFM receives a license from the PFRDA, it will be required to sign a service obligations and operations agreement with the CRA. As per the agreement, the CRA will provide each PFM with the system software specifications and file formats which will enable the PFM to be electronically connected to and communicate with the CRA and the PFRDA. If on any day, the total withdrawals (on account of exit or switching) from a PFM are larger than the total contributions, the PFM will be bound to transfer the consolidated sum to the CRA with no delay. PFMs will also be mandated to provide daily reconciliation information on assets and instructions in a standardized format to the CRA and PFRDA. The same software and link will also enable the PFM to report a daily performance which will be based on a standard methodology for computing the NAV of each scheme. The CRA will use this information to credit new units to each member on the basis of new contributions or inter/intra PFM transfers. If the license of a PFM is revoked by the PFRDA or a PFM wishes to discontinue its business, the CRA will be responsible for transferring the assets and funds from this PFM to other PFMs and schemes that are selected by the relevant members.
4. **Annuity Providers:** When a worker retires, the CRA will be responsible for transferring a part of the terminal balance in the member's PRA to the annuity provider selected by the member. The CRA will verify that this transfer has been affected and confirm the same to the member. Since this transaction and the amount paid for annuities may be mandated, the CRA may be required to report such transactions to the PFRDA.
5. **Fees and charges:** Participants in this new system with individual accounts are likely to

face a variety of costs, expenses and fees (fixed Vs. variable charges, contribution Vs. assets based charges, or combinations thereof) with varying impact on benefits. Measuring the impact of administration charges for pension funds is very complex. Financially unsophisticated individuals may be unable to accurately assess the various fees and charges and their impact in the new system. Hence the structure and reporting of charges and costs in the new pension system will be of concern to policy-makers. In view of the target group for the new pension system, it will be important to ensure complete transparency and simplicity in the structure of charges and their reporting to PFRDA and members. The CRA will monitor the limits on fees and charges (if any) that may be prescribed by the PFRDA on POPs, PFMs and ARAs. The CRA may be charged with the responsibility of reporting the fees and charges of various service providers in a standard format to the PFRDA and the members. Regular, standard disclosure of fees and charges will be important for fostering competition among PFMs and POPs and lowering transactions costs.<sup>10</sup> Importantly, the system should be able to calculate and correctly payout the fees / commissions / trails payable to ARAs by PFMs or POPs as per the limits prescribed by PFRDA and the actual fee decided by the POPs or PFMs. These calculations are likely to be complex.

- 6. Members:** The CRA will be responsible for protecting the rights of members – this can be achieved by ensuring timely and accurate transfers, regular and standard reporting of performance and fees, providing periodic consolidated account statements to members, and ensuring speedy action and efficient redressal of member complaints and grievances. Members will be able to file complaints against errant POPs with the CRA through the Internet, email or letters. The CRA will provide a standard, simple and easy format and process for filing complaints. The CRA will furnish a periodic statement of complaints, entities involved and the status on redressal to the PFRDA.

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<sup>10</sup> A detailed discussion of the various fees and charges, their structures and reporting formats as well as their impact on member actions, benefits and profitability of service providers is being provided in the document titled 'Costs, Fees & Charges for DC Personal Retirement Accounts in India' being drafted by IIEF

#### 4.10 Errors, delays and penalties

- a) **Delays in transfers:** CRA will be required to capture, report and act upon delays caused by POPs and P&AOs. These could include delays in transmission of funds or instructions from POPs / P&AOs to CRA. The CRA, in consultation with the PFRDA, will publish system benchmarks for performance standards and transaction time-frames. For instance, it may be specified that all contributions must reach the CRA within a maximum of 3 working days. If a POP delays the transfer of a member's contribution beyond this time-frame, the CRA will be able to identify the source of delay, levy penalties and compensate the member for any losses incurred by them. In this situation, the POP which is responsible for the delay, will be required to compensate the member by paying an interest at the prevailing rate on 91-day T-bill for each additional day taken for effecting the transfer to the member. In the event of a delay caused by P&AO, the government shall have to compensate the member for any losses. The CRA will credit such penalties into the appropriate member account.
- b) **Errors** Errors may occur when a new PRA account is opened funds are transmitted by the POPs to the CRA or from the CRA to the PFMs. These errors can include a mismatch between funds and instructions, or errors in data entry related to account numbers, or errors related to PFM or scheme selection, etc. These errors may subsequently lead to reversal and rectification transactions. Such transactions may have profit or loss implication for the PRA as the NAV may be different when the corrections are carried out. This process needs to be carefully controlled and the member should be compensated appropriately by the concerned POP or the CRA (depending on the source of error). POP should take the member's approval on the system generated report of the member's instructions and on detection of error by the member, rectify the same. PFRDA may prescribe the compensation amount and the mode of recovery from POP and the payment thereof to the member.
- c) **Netting of cash-flows:** While it is important to transfer resultant net cash to/from PFM and CRA, it is necessary that each component of this cash flow viz. fresh purchases,

fresh redemption and switches within/to/fro PFMs are also separately tracked.

Experience shows that errors in netting are difficult to trace.

## **5. CRA Contract Format**

The choice of the agency which is entrusted with the task of central recordkeeping is of paramount importance and interest to policymakers. The full operational and member service framework, as well as the core principles of portability, competition, individual choice, low transactions costs, proactive regulation and compliance enforcement, etc. rest on the ability of the central recordkeeping agency to efficiently and accurately discharge its responsibilities and enforce the service and functional obligations on service providers over multiple decades. Globally, governments have chosen to entrust this task to public companies or government departments which have the necessary experience and capacity to perform this function and/or are already performing similar functions in the areas of tax collection, social security or securities markets.

India already has several agencies which have the necessary experience with low-cost, IT based recordkeeping and administration, and service access to millions of individual account holders across the country as well as the capacity to perform the functions of the CRA. A number of important initiatives and applications for central recordkeeping and administration have been successfully implemented in the securities markets. India already has two well functioning depositories in the securities market (NSDL and CDSL) and agencies like CAMS, UTISEL, etc. provide recordkeeping and administration services to the mutual fund sector. More recently, the Central Board of Direct Taxes has decided to adopt central administration and recordkeeping technology for tax collection and administration and outsource the system design, development, management and service delivery under this Tax Information Network (TIN) to NSDL.

### **5.1 Regulatory assets and ownership issues**

The agency selected to perform the CRA function will be initially required to design and develop an appropriate system architecture which will include the software and service

functionalities of the central administrative and recordkeeping arrangement, as well as the associated hardware including the Disaster Recovery Facility (DRF). In addition, the CRA will need to periodically upgrade and enhance the system software and hardware in keeping with changes in services and functions, changes in response to field practices and new functions, changes in technology, growth in the number of members or service providers, etc. Once the system architecture is in place, the CRA will be required to provide the full set of services to members, appoint and train POPs and other service providers, perform its enforcement and compliance roles, and procure an annual maintenance contract (AMC) from a suitable service provider.

In general, administrative, recordkeeping and communication costs are technologically determined and are a function of (a) the quality of service and, (b) the number of accounts. Hence, the average costs in such a system can be expected to decline till the system capacity constraints are reached and will start rising once new capacity has to be added to accommodate more accounts or new services. The administrative arrangement of this pension system is likely to impose capital costs (of setting up and upgrading the required capacity) and operational expenses (on management and service delivery). In principle, these capital and operational costs can either be fully or partly subsidized by governments, or these can be recovered by the recordkeeping agency through a well regulated charge structure which can include a fee on accounts or transactions or assets or a combination.

It is proposed that the PFRDA will, through a grant of a License, appoint a suitable agency to develop the system architecture, serve as the CRA and offer administrative and recordkeeping services to members. While this License will be valid for a specified period, the PFRDA will be able to prematurely terminate the License at any point in time if the License conditions are not fulfilled. When the CRA license expires, or is terminated, the following issues merit attention in view of the CRA's unique role as a monopoly providing system critical services:

1. **Database Privacy:** Over the years, the CRA will emerge as one of the most critical data

repositories in the country. It will become the central source for private records related to demographic and contact information, investment decisions, returns and account balances, savings behavior, etc. of millions of India's citizens. It is critical that this database becomes the property and the responsibility of the Government of India and that this database does not have any 'commercial value'. The CRA will have no rights to release information at the level of the individual PRA to any third-party. Any violation of this condition shall result in immediate revocation of the CRA license and the imposition of suitable penalties

2. **System architecture**<sup>11</sup>: A consistent quality of services to members will also be of paramount interest to the policymakers. In this regard, it will be necessary for the PFRDA to continually review and measure the performance of the CRA and to ensure that the CRA is indeed discharging its service and functional obligations. If the CRA is found to be lacking in its ability to fulfill its license conditions, the PFRDA should be able to revoke the CRA license and seamlessly transfer the role and responsibilities of the CRA to another entity including a successor licensee.

This database as well as system architecture and software designed and developed by the CRA will be central to the pension system's functioning and any transfer of the administrative arrangement to any new entity (on expiry or termination of the CRA license) should not impose any risks on the system nor changes in the functional specifications and services to members. It is equally important for the PFRDA to be able to expediently enforce any decision on license revocation at any point in time. Poor administration as well as any disruption in the administrative services will greatly undermine the confidence of the public and can pose a grave systemic risk.

In this scenario, the Government should have full *control* on the database and the system architecture which runs the central administrative and recordkeeping facility, and which enables system-wide inter-linkages and POP/P&AO access codes, unique PRA IDs,

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<sup>11</sup>The system architecture will include the system software, the hardware on which this software is run, as well as the Data Recovery Facility (DRF).

reconciliation, information and funds tracking and flow, unitization, statements and reports and clearing, etc., as well as the hardware on which this software runs including the DRF facility. In order to have control over these assets, the Government and PFRDA have the following policy choices:

- 1) The Government can *pay for and own* the system architecture designed and developed by the CRA to meet its service and functional obligations, Ownership of these assets will give complete control on these assets to the Government. In this situation, the Government/PFRDA will be able to seamlessly transfer the database and these assets to any other service provider if and when the CRA License is terminated or expires. Ownership of the assets by the Government will also allow the capital cost of the system to be spread over a longer time horizon and hence make the system available to members at lower charges. In this situation, members who join the system in the early years will not cross-subsidize later entrants.

However, ownership of the system software and hardware exposes the government to significant technology risks and the CRA will have no incentive to install a high fixed cost technology solution. Also, system architecture design and development is not a one-time activity and is likely to be an ongoing process with several ongoing improvements and changes. Importantly, as owner of the assets, the Government will also become responsible for system upgrades.

- 2) In view of the above difficulties with system architecture ownership, and considering of the importance of government control on the assets in the event of license termination or expiry, the PFRDA should, as part of the License conditions of the CRA, declare the database and these assets as *regulatory assets*. This will bring these assets under the continuous supervision and control of the PFRDA. Therefore, it is proposed that the database and the system architecture (software, hardware and the DRF) be declared Regulatory Assets by the PFRDA.

## 5.2 CRA Expenses and Revenues

Since the CRA is expected to function as a monopoly, the structure and value of its costs and expenses will be of special importance to policymakers. The expenses and revenues (from charges and fees) are outlined below:

a) **CRA Expenses:** The capital cost of designing, developing and periodically upgrading the system architecture (including software, hardware and the DRF), and on obtaining an annual maintenance contract for system debugs will be borne by the CRA. In addition to these capital costs, the CRA will incur operating expenses in discharging its functional and service obligations. These operating expenses will include:

- insuring the PFRDA, customers, POPs and PFMs against the risks of system failure
- providing members with a variety of services and updated information including system operations, POP locations, fees and charges of service providers, fund performance, account balances, etc.
- administration and general expenses (including staff salaries, etc.)
- delivering training and system software formats to POPs, P&AOs and PFMs.

b) **CRA Revenues:** The CRA can be expected to recover its capital and operating expenses from the following:

- *Fixed charges:* (Rupees per account per annum): These charges shall compensate the CRA for its capital expenses on system software development and hardware provision, the annual license fee, annual maintenance charges, as well as expenses on periodic system-wide upgrades for new functionalities and additional capacity.
- *Transaction-based charges* (Rupees per transaction): These charges will enable the CRA to recover the variable costs of operations including collection and transfer of contributions, switches between schemes and insurance etc. The cost of delivering operational training to POPs, PFMs, P&AOs, etc shall be recovered as training fees from these service providers.

### **5.3 CRA License Conditions**

- a) The CRA License shall initially be valid for a term of ten (10) years. During this period, no other agency will be granted a CRA license. After this period of 10 years, the CRA license will expire.
- b) Within fifteen days from the date of commencement of the CRA operations, the CRA will deposit the annual License Fee with the PFRDA (the fee will be decided by the PFRDA)
- c) The PFRDA will conduct a periodic system review to satisfy itself that the CRA is adequately meeting its functional and service obligations.
- d) The validity of the CRA license will cease if (a) the CRA contravenes the License conditions and the License is prematurely terminated by the PFRDA, or (b) when the license period expires. The grounds for termination of the CRA license, as well as the treatment of the transfer of regulated assets and system management under the above two conditions is described below.

#### **5.3.1 Grounds for premature termination of the CRA license**

- a) No order of suspension or revocation of license of CRA shall be issued by the PFRDA, except after conducting an enquiry by an officer of the PFRDA, authorized in this regard.
- b) The grounds for suspension / revocation of the CRA license may include inter alia (a) contravention of the License conditions, (b) inability to perform the duties of Licensed service provider, (c) inability to meet the requirements as a Licensed service provider, and (d) commission of a fraud (section 17 of the Indian Contract Act, 1872)
- c) The PFRDA shall give a reasonable opportunity of hearing to the CRA, to enable it to make submissions in support of its reply furnished in response to the notice of commission of enquiry.

### **5.3.2 Transfer of assets in case of suspension / termination of CRA License**

- a) In case of suspension of License, the CRA shall be directed by the PFRDA on specific continuing obligations and services, as well as on the *regulated assets* including the database, system software and hardware, documents or any other relevant material that may be in its custody or control, relating to its activities as CRA
- b) In the case of termination of the CRA license, the CRA shall, with immediate effect be subject to the directions of the PFRDA. In this situation, the PFRDA may direct the CRA to continue discharging its role and responsibilities in the transition phase, and/or appoint an administrator to take over the regulated assets and the management of the CRA functions, and/or ask the Government of India to appoint any agency to take over the regulated assets and the management of the CRA functions, and/or appoint a successor CRA and:
- transfer all or part of the regulated assets and the management of the CRA functions to the new CRA, and/or
  - determine the residual value of the regulated assets based on regulations of the PFRDA, or
  - allow the new CRA to replicate the regulated assets.

### **5.3.3 Process for transfer of assets in case of expiry of CRA License**

- a) The PFRDA shall start the process of re-bidding for the CRA license at least 18 months before the expiry of the incumbent CRA's License term.
- b) The treatment of the *regulated assets* on expiry of the CRA license is outlined below:
- the system software will be transferred at zero cost to the new CRA
  - dedicated system-specific hardware (if any) and the DRF shall be transferred as per the book value of these assets
  - since the database is the property of the government and has zero commercial value, it will be transferred to the new CRA at zero cost.

## **5.4 CRA Performance**

Poor quality of administration, errors in reconciliation and lax enforcement by the CRA on the service provider network will cause multiple accounts, incorrect transfers, delays in asset allocation and therefore lower benefits to members. The CRA will be mandated to design effective reconciliation mechanisms and systems and enforce compliance by service providers to minimize errors, delays and frauds. The PFRDA will establish and enforce a set of practical and clear benchmarks to measure the performance of the CRA and its network of service providers on an ongoing basis. This may form an essential and objective ground for imposition of penalties or for any delicensing proceedings by the PFRDA. The specific benchmarks will be decided by the PFRDA. The CRA shall be mandated to conduct and report specialized external audits on security systems, accounting, operations and control, ISO 9001 and operations of system disaster recovery to the PFRDA on an annual basis.

## **5.5 Regulation of CRA**

There are considerable economies of scale in the recordkeeping and communication activity which shall be managed by the CRA in the new pensions regime. The duplication of assets may hence be costly up to a certain scale size. Thus the market for recordkeeping and communication in the pensions space may be either a monopoly or at best an oligopoly. In either case, the charges and operations of need to be regulated by the PFRDA. This shall be done in a manner that ensures participation by the players and still minimizes monopoly rents.

- a) The CRA shall allow on-line connectivity to PFRDA to enable it to perform any check / collect any information on its system at any time.
- b) The CRA will pay an annual fees of Rs. XX to the PFRDA in a manner in accordance with schedule XX.
- c) The CRA charges (Rupees per account, and Rupees per transaction) shall be linked to

- the number of accounts as quoted by the entity in the financial bid / negotiated by the Evaluation and Selection Committee after selection. The CRA shall provide details of the number of accounts it holds in each financial year. For the purposes of determination of charges for the next financial year, the CRA shall project the number of accounts in the next financial year. PFRDA shall consider an average of the number of accounts as on March 31 of the current financial year and projected number of accounts in the ensuing financial year for which the charges are being decided.
- d) Every CRA shall have adequate mechanisms for the purposes of reviewing, monitoring and evaluating its controls, systems, procedures and safeguards.
  - e) The CRA shall, through an internal audit and submission of the auditor report satisfy the PFRDA about the adequacy of the above once in the six months of a financial year.
  - f) The CRA shall keep the PFRDA informed of the grievances of the pension fund members, POPs and PFMs and their redressal. All grievances must be redressed within 15 days of the receipt of the complaint.
  - g) The CRA may amend the bye-laws after the approval of the proposed amendments by PFRDA.
  - h) No CRA shall assign or delegate to any other person its functions as a CRA, without the prior approval of the PFRDA.
  - i) The CRA shall enter into agreements with the POPs and the PFMs based on the bye-laws approved by the PFRDA in this regard.

### **5.5.1 Ring Fencing of CRA Operations**

In the event that the CRA is already engaged in a similar business of centralized administration and/or recordkeeping, and decides to provide the services as CRA within the same (existing) corporate structure, it shall be required to '*ring fence*' the accounts of the CRA operations from its other business segments. These requirements will not change the legal status of the entity entrusted with the centralized recording keeping and

administrative activities. The objectives of *ring fencing* are to:

- facilitate the effective regulation of monopoly activities by clear definition of service delivery and identification and attribution of costs;
- provide the PFRDA with sufficiently detailed and accurate information to undertake price reviews;
- avoid the anti-competitive effects of cross subsidies between contestable and non contestable activities; and
- ensure that the relationship between the monopoly and the provision of in-house contestable inputs is conducted on an arm's length basis.

**Disaggregated (ring fenced) Statements:** The CRA shall be required to provide information to the PFRDA as per specified regulatory accounting statements. These disaggregated statements (ring fenced statements) shall provide an audit trail to evidence the disaggregation of the base accounts into the various business segments of the entity operating as a CRA. The PFRDA in its accounting regulations shall indicate how disaggregated statements are to be presented. For the purposes of ring fencing, initial assets shall mean assets deemed to be already in service at the appointed date, and at values reflected in the latest financial statements of the CRA.

The CRA shall prepare disaggregated statements for each of the following components of the base accounts:

- Profit and Loss Account;
- Balance Sheet; and
- Statement of Cash Flows.

The disaggregation of base accounts shall be based on the principle that:

- Items which are directly attributable to the CRA are assigned accordingly; and
- Items not completely attributable to any one business segment should be allocated using an appropriate allocator

## 5.5.2 Reports

To closely monitor the activities and charges of the CRA, the Regulator needs to collect performance information from the CRA on a regular basis. The CRA shall make the following submissions to the PFRDA:

- **Annual return**, which may include changes if any in the particulars of the CRA during the financial period, a declaration that the CRA continues to satisfy the requirements of the License / Approval (by the PFRDA) during the financial period or a declaration of any requirements not having been met,
- **Financial statements** including the balance sheet, profit and loss account, auditor report and directors report if the service provider is (or includes) a company
- **Annual statements**, which may include a declaration that the CRA has prudently supervised all the sub-agents (POPs, P&AOs, PFMs) during the financial period, details of failures by the sub agents (if any) during the financial period (This information must be provided whenever such an exigency occurs), details of events of significant nature if any during the financial period (This information must be provided whenever such an exigency occurs), details of non-compliance with the PFRDA Act and Conduct of Business Document or any directive issued by PFRDA in compliance and the governing rules of the scheme if any during the financial period
- **Report on internal controls** which may include a statement of control objectives and procedures and internal control measures for achieving these control objectives

The PFRDA will reserve the right to inspection of the CRA. The CRA shall also make the following disclosures to the members at least once in a financial year:

- **Account statement** which may contain name of member, schemes and PFMs, total contributions made during the financial period, total accrued benefits at the beginning and end of the financial period, particulars of amounts transferred to or from the scheme during the financial period, etc.
- **Information regarding contributions** – amount and date of contributions made, employee and employer contributions during the period

- **Scheme Report** Commentary on the financial development of the scheme, details of changes if any to the governing rules, other information on the scheme
- **Investment Report**, An analysis of investments held by the PFM and particulars of the income derived from such investments, A commentary by the PFM on the analysis, particulars of the investment policy during the period and any change in the statement of investment policy which will materially affect the risk attached to the investments of the scheme, the amount of net income (excluding capital appreciation) derived from the investments, the amount by which the value of the scheme assets have appreciated or depreciated and the value of the scheme assets for the financial period and the 2 preceding periods, investment return during the period, a comparison of such return with appropriate benchmarks such as the inflation rate and the average return of all investment managers surveyed. A member may demand information pertaining to the details of his account. The CRA should provide such information and the charges for the same may be approved by the PFRDA.

## 6. CRA Selection Process

This section outlines the eligibility criteria of an entity which wishes to serve as the CRA, the CRA selection process, contractual terms, implementation tasks and implementation time-frames.

It is proposed that the CRA be selected on the basis of strict and transparent eligibility criteria including existing capacity and experience coupled with a competitive bid on system development fees and pre-committed management fees/charges for the license duration. It is proposed that the selection process be supervised by an Evaluation and Selection Committee set up by the Government for this explicit purpose and should consist of the following steps:

### **Phase-I: Inviting Expressions of Interest (EOI)**

*Step-1:* Open discussion with all interested firms to discuss the role of CRA and provide clarifications on eligibility criteria and preconditions.

*Step-2:* Invitation for Expression of Interest

### **Phase-II: Inviting simultaneous Technical Proposals and Financial Bids**

*Step-3:* Open discussion with shortlisted firms to discuss the bidding and selection procedure.

*Step-4:* Invitation of Technical and Financial Bids

*Step-5:* Announcement of the final CRA appointment

*Step-6:* CRA to submit the final CRA specifications document within one month after contract negotiations.

### **6.1 Constitution of the Evaluation and Selection Committee:**

The full selection process shall be overseen by this Committee. The members of the Committee may include:

1. Representative of PFRDA
2. Joint Secretary (CM & Pensions), DEA, Ministry of Finance
3. Joint Secretary (Ministry of IT) or NIC
4. Two independent technical experts

The Committee will be free to appoint subject experts and specialists to assist the process of evaluation of technical and financial bids.

## **6.2 Phase-I: Expression of Interest**

The Committee will issue an Expression of Interest (EOI) which will list the minimum eligibility and pre-qualification criteria along with a brief outline of the services and systems requirements. The system requirements of the new pension system and the role of CRA shall be discussed in an open forum with all interested entities before the release of the EOI. The EOI will be advertised in the print media.

### **6.2.1 CRA Eligibility criteria**

The following categories of entities would be eligible to apply for a CRA license:

- i. A public financial institution as defined in section 4A of the Companies Act, 1956 (1 of 1956), or
- ii. A bank included for the time being in the Second Schedule to the Reserve Bank of India Act, 1934 (2 of 1934); or
- iii. A recognized stock exchange within the meaning of clause (j) of Section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956);
- iv. A body corporate engaged in providing depository services under the SEBI (Depositories and Participants) Regulations, 1996
- v. R&T Agents registered with the SEBI
- vi. A body corporate engaged in providing financial services where not less than forty-nine percent of the equity capital is held by any of the institutions mentioned in sub-

clause (i), (ii), (iii), (iv) and (v) jointly or severally;

- vii. An institution engaged in providing financial services or pension administration and management services and approved by the Central Government

### **6.2.2 Pre-qualifications and experience**

EOIs of only those entities which satisfy the following pre-qualification and experience criteria will be considered:

- i. Experience with developing a state-of-the-art IT-based central administration and recordkeeping system
- ii. Experience of at least 5 years in central recordkeeping and semi-regulatory functions
- iii. Minimum positive net worth of Rs.50 Crore (Rs.500 million)
- iv. Should be presently handling at least 3 million individual accounts and 5 million transactions per year
- iv. Have the necessary infrastructure to electronically link with the PFRDA, service providers and members and meet the service and functional obligations that may be determined by the PFRDA from time to time
- v. Should not have been indicted in any regulatory / judicial proceedings on account of fraud, malpractice or criminal offense

### **6.2.3 Preconditions**

These entities must also agree to comply with the following if it is selected to serve as the CRA:

- i. To enter into a license agreement with the Interim PFRDA – which will migrate to the new Act
- ii. To comply with the provisions of the legislation (when enacted) and all related guidelines, regulations and directives that are issued by the PFRDA from time to time
- iii. To produce the system architecture as per the milestones and specifications decided by the PFRDA

- iv. To comply with the functional and service obligations set out in its service agreements with service providers
- v. To ring-fence the accounts of its CRA operations from its other business segments (in case of an existing firm which serves as the CRA and is already involved in any other business activity)
- vi. In case of a consortium, the lead bidder for the CRA shall at all times hold at least 51% of the equity capital of the CRA
- vii. No POP or PFM shall at any time hold more than 10% of the equity capital of the CRA
- viii. The CRA shall not be allowed to invest in the stock market
- ix. No Audit Firm shall at any time hold any equity stake in the CRA

Entities which satisfy the above pre-qualification criteria and agree to the above pre-qualification conditions will be required to communicate their interest in serving as the CRA in writing to the Committee. This EOI shall be accompanied with a non-refundable application processing fee and shall be delivered by hand or ordinary post to the Evaluation and Selection Committee by a specified date and in a specified format and manner. EOIs which do not satisfy these qualifications or are received after the prescribed date will not be considered. The Committee may instruct the EOI applicants to furnish any further information that it deems fit or may require the relevant entity to appear in person for representation in the process of evaluation of the EOI application. The entities short-listed after the EOI will be invited to an open forum discussion. The committee will explain the selection process in detail to the potential bidders at this meeting.

### **6.3 Phase-II: Request for Proposals (Technical and Financial)**

Each entity shortlisted after the EOI will be invited by the Committee to simultaneously submit a Technical Proposal and a Financial Bid in separate sealed envelopes. The Committee shall specify the formats for submission of the technical proposal and financial bids. The technical proposals shall carry a weightage of 80% while the financial proposals

will carry a weightage of 20%. The technical proposal will include qualifications, experience with similar activities, understanding of the CRA and pension system objectives, approach and strategy for setting up the CRA, system architecture development time-frames, etc. The financial proposal will include (a) the consolidated cost of developing an appropriate system software which meets the prescribed functionalities, and (b) the pre-committed annual and transactions-based charges that the entity proposes to levy on the members.

### **6.3.1 Evaluation of Technical Proposals**

The Committee will first review only the technical proposals. During this review, the Committee may instruct some of the entities to furnish further information or clarifications. It may also require some of the entities to appear in person before the Committee. The Committee may undertake site-visits to physically verify the system capabilities described in the technical proposals. Based on the quality of the technical proposals, site visits and the presentations, the Committee shall jointly rank each technical proposal on the basis of pre-decided criteria. Each criterion shall be marked (either 0, 4, 6, 8 and 10). The various criteria are further classified under four categories namely, (1) Track Record, (2) Business Processes and Planning (3) Customer Experience and (4) Experience in enforcing compliance. The Committee may rank the proposals based on the following technical criteria:

*(1) Track Record & Experience (50% Weightage)*

1. Past performance in terms of financial stability and external audit results.
2. The senior management of the entity should possess the requisite technical qualifications and experience to manage the CRA
3. The experience and ability of the entity to develop and deliver large IT based applications in a timely manner and to deliver quality customer services at reasonable costs to customers
4. Experience and ability to generate and manage unique account numbers
5. Experience and ability to manage an automated account transfer service which will automate and standardize procedures for transfer of assets in a customer account

from one PFM and/or bank to another.

6. Experience and ability to manage a commission billing system which will provide an automated facility for the debiting and crediting of commissions for all CRA members (POPs, PFMs and members)
7. Experience and ability to manage the netting process which will be an automated book-entry accounting system that centralizes the settlement of various security transactions and maintains an orderly flow of security and money balances. The system should be able to generate reports that provide participants with a complete record of security and money movements and related information. Regardless of volumes, the entity should be able to net the obligations of PFMs on a daily basis, thereby minimizing security movements and associated costs. The entity should be able to automatically debit or credit to members' cash and stock dividends and bond interest.
8. Experience and ability to manage the unitization process
9. Experience and ability to electronically link with a geographically widespread network of locations with adequate redundancies to ensure uptime in excess of 99%.
10. Experience with managing records and data that necessitate privacy, confidentiality and security
11. Experience in managing and operating a disaster recovery facility (DRF) which should be designed to provide reliable and secure services. The agency should have the experience of ensuring at least one live system replica of all live financial and non-financial transactions for all connected service providers. The systems must be able to handle spike loads in excess of 20% over and above the past twelve months average transaction volume at any point of time.
12. Experience with providing operations, compliance and IT system training to service providers across multiple locations

*(2) Business Processes and Planning (20% Weightage)*

13. The business plan of the entity outlining its understanding of the administration and recordkeeping functions, approach and strategy for managing this facility

*(3) Customer Experience (20% Weightage)*

14. Ability to provide a national toll-free call centre and a secure, Internet based customer access to specified services
15. Past Record on customer complaints and their level of satisfaction.

*(4) Experience in enforcing compliance (10% Weightage)*

16. Experience and ability to enforce compliance by service providers – here the entity should also be able to provide the PFRDA with a compliance and control module which will track compliance by POPs and PFMs and exercise regulatory control.

### **6.3.2 Evaluation of Financial Proposals**

After the Committee has reviewed all technical proposals, it will open the financial bids of the three entities which score the highest marks in their technical proposals. The lowest financial bid shall have a score of 100 and the other bids shall be normalized with respect to the lowest bid. The financial bids shall contain:

- a) *Annual account maintenance charge (15% weightage of the financial bid):* These charges will cover the capital costs of the system and shall comprise return on equity, interest on loan, interest on working capital and depreciation. Bidding on this criteria will motivate the bidders to optimize their capital structure and also procure working capital at the lowest possible rates. The capital cost of the system shall include the design of the functional and service specifications, software development and testing, servers and other hardware to run the system software and the disaster recovery facility, documentation including service contracts with service providers, and all other pre-launch expenses incurred in establishing the central recordkeeping and administration facility. The bidders shall also include the cost of annual maintenance charges (AMC) of the system software and hardware in their quote for annual account charge.
- b) *Charges per transaction in Rupees (85% weightage of the financial bid):* These charges shall exclude the capital costs and represent only the *operational* costs per transaction or the management and service charges of the CRA. A transaction for the purpose of this charge shall be uniformly defined as (a) deposition of contribution by a member,

and (b) allocation of fund to one scheme of one PFM. The entities shall also indicate extra charges (if any) in case of allocation of funds to more than one scheme of one PFM and to schemes across PFMs, and will include the management of the Tier-I and Tier-II accounts for mandatory and voluntary members. This will form the 'system management and service' fee of the CRA.

The CRA will be selected on the basis of the weighted average of the technical proposal and financial bid scores and invited for contract negotiations.

## **7. System implementation**

The process of system implementation is both complex and challenging, and will be the single most important phase in India's pension reform. This is especially important for implementing the centralized administrative process which relies heavily on technology and will become the key source for system efficiency, functions and services. The major risks lie in insufficiently articulating the functional and service requirements, inefficient system and process design, inappropriate use of technology, and insufficient capacity and knowledge among service providers. However, the biggest risk lies in prematurely launching a system without adequate testing. The problems experienced in Poland with premature system launch are an important lesson.

While we can rely on the international experience with establishing institutional and regulatory arrangements for private pensions, several features of India's new pension system will impose a number of new and unique challenges for the policymakers. These include the number and profile of potential participants, the geographical spread of the target population, insufficient penetration of technology and telecom infrastructure, a mix of mandatory and voluntary membership, and competition by existing DB schemes.

The challenge and complexity of implementing India's pension reform is also compounded by the need for simultaneous actions on a variety of fronts – establishing the new pensions regulator and adequate supervisory capacity and processes, drafting the legislation and operating guidelines for market participants, establishing the central recordkeeping and administration mechanisms, harnessing existing outreach capacity to provide efficient and widespread service access to members, recruiting professional pension fund managers and finalizing the public information and education formats and strategies. While some of the system features can be implemented in isolation, a number of activities will be interdependent and delays (or mid-way changes) on any one front will impact the full implementation process.

## 7.1 CRA Implementation Process

Once an entity has been selected to develop the CRA system, it will be required to commence the task of system architecture and software design and development within 15 days of being awarded the CRA License. The CRA will first develop a detailed *system specification manual* which describes the CRA system architecture, service obligations and functional specifications for presentation to PFRDA and its approval within one month of obtaining this License. This manual will also outline the specific implementation milestones.

Simultaneously, the PFRDA will constitute an Operations Working Group (OWG) to oversee the process of system development and implementation as per the milestones specified in this manual. This OWG will be guided by the system specifications document, the service and functional obligation contracts that are signed between the PFRDA and the relevant service providers, and the implementation tasks and time-frames that have been agreed to by all parties. The OWG will interface with the various agencies involved in the implementation process and will be able to evaluate and communicate specific mid-course changes, developments or improvements (if any) in the functional or service specifications to the relevant agencies. The OWG should be knowledgeable and empowered to take implementation related decisions – this will ensure that the implementation process is efficient and as per the schedule. The OWG will therefore be an important tool to ensure timely and appropriate implementation of the system<sup>12</sup>.

If during this process of system architecture development, the CRA is unable to implement or execute the terms of its Contract with the PFRDA, or expresses its inability to do so, the CRA License shall be revoked and another agency shall be invited to complete the set-up of the system architecture and serve as the CRA. The decision of the PFRDA to revoke the

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<sup>12</sup>A useful strategy for speedy system implementation may also be to commission existing entities to serve as service providers (CRA, PFMs and POPs) in this pension system. Entities with the existing capabilities and experience will be able to more rapidly adapt to the system requirements

License shall be communicated 30 days prior to such action, stating therein the grounds on which the License is being revoked. The License fee, in such a case shall be forfeited. However, the PFRDA can grant a grace period of 30 days within which the terms of the contract have to be fulfilled. During this grace period, the licensee shall be required to pay a penalty of Rs. 1,000,000 per day of delay.

The broad implementation process can be divided into the following 5 blocks of actions:

1. Selection of CRA,
2. System specification and definition of service providers' functions,
3. System architecture implementation,
4. Testing (of processes including a full system pilot) and debugging; approval of the final system architecture by the PFRDA, and
5. System launch

An outline of the implementation tasks and estimated time-frames for various activities is provided below. The implementation schedule estimate focuses on establishing the central recordkeeping agency (CRA) and the related system software, hardware and inter-linkages. The establishment of the POP network is subsumed by the CRA implementation process. All other actions related to the regulatory infrastructure are excluded from this estimate. The CRA system architecture will be implemented as per the milestones outlined in the CRA system specifications manual approved by the PFRDA in the following *phases*:

#### **7.1.1 Phase-I** (to be completed within 8 months of grant of CRA License)

Under Phase-I, the CRA will be required to design and implement the system architecture for Tier-I accounts using P&AOs and POPs with electronic connectivity capacity. This process of system design and development will include:

- a) design and development of the system architecture including development and/or procurement of the hardware and software
- b) establishment of a unique ID number generation system

- c) development of the interconnection codes with the PFRDA, POPs, P&AOs and PFMs;
- d) design of the reconciliation processes and standard transmission and encryption formats for electronic communication of data;
- e) development (and approval by PFRDA) of the eligibility criteria, selection process and operational bye-laws (in accordance with the CRA Regulations issued by the PFRDA) for POPs and P&AOs (here the CRA will also submit the operational agreements for PFMs for PFRDA's approval);
- f) establishing the institutional inter-linkages and signing connectivity and service agreements with service providers (POPs, P&AOs and PFMs)
- g) distribution of the system operations manuals to these entities and delivery of certification training to the staff of these entities;
- h) developing information tools and transaction forms for members and compliance reports and processes to PFRDA
- i) lab tests of the system software including tests for functionality, loads and agent integration (here, the CRA will also debug the software and evaluate system redundancies);
- j) conduct of pilot (mock) transactions by CRA from multiple POP and P&AO locations to test and verify the smooth functioning of the full system including member transactions and services; and
- k) physical verification by PFRDA of the software, infrastructure facilities and systems developed and established by the CRA

Under Phase-I, the system should be able to efficiently absorb the backlog of government employees and issue them unique Tier-I PRA numbers. In addition, the system should enable launch of the voluntary Tier-I PRA accounts for informal sector workers as well as employees of state governments, PSUs and other large employers.

After Phase-I, the CRA will be able to deliver the following services to members:

- a) Opening of new Tier-I PRA accounts for central government employees and informal sector workers with unique account numbers using P&AOs and electronically connected

(and perhaps initially limited number of) POPs

b) Other operational services for mandatory and voluntary Tier-I accounts including:

- Collecting monthly contributions by government employees to specified PFMs and schemes using the network of P&AOs and designated banks,
- Collecting voluntary contributions by non-government employees to specified PFMs and schemes using a network of POPs and designated banks;
- Central clearing, netting and transferring funds to selected PFMs;
- Unitization and allotment of units to each member's PRA;
- Providing PRA statements to members (directly, through the Internet, or through the P&AO / POP network);
- Disclosure of daily performance information on each PFM through the Internet and the media;
- Changing member information on account of changes in employment (for government employees), location or name etc.;
- Providing units-to-amount / amount-to-units conversion and other calculators / services to members on its Website; and
- Providing secure Internet access rights to the PFRDA through the CRA website for obtaining implementation updates and other MIS reports

#### **7.1.2 Phase II** (to be completed within 4 months of completion of Phase-I)

Under Phase II, the CRA will offer the balance set of services and perform the rest of the functional and service obligations including

- a) Facility for switching between schemes and PFMs
- b) Operation of Tier-II (withdrawable) accounts
- c) Facility of accessing system services from any POP location
- d) Facility for withdrawals from the Tier-II account
- e) Facility for transferring a prescribed percentage of the terminal balance in a member's PRA to an annuity provider of his choice
- f) Providing lists of members to the relevant PFMs (if permitted by the PFRDA)

- g) Display of PFM reports on the CRA website

### **7.1.3 Phase III** (To be completed within 3 months of completion of Phase-II)

When Phase-III is completed, members will be able to access the CRA in various local languages using the Internet and telephones. The CRA will also enable customers to transfer funds using ATMs, net-banking accounts, etc. Simultaneously, the CRA will develop the capability of interlinking with new service providers who will serve as POPs – this will include remote postal and bank branches, NGOs, self-help groups and micro-finance institutions which will provide access to the unorganized sector workforce and serve as an interface between them and the pension system.

## **7.2 Summary of flow of actions for system implementation**

- a) PFRDA sets up the Evaluation and Selection Committee for service providers
- b) The Evaluation and Selection Committee finalizes the EOI for CRA, releases it through an advertisement and also uploads it on its website. The responses to the EOI are required to be submitted within 10 days
- c) The Committee receives and examines the expressions of interest for the CRA license received from several parties and short-lists the eligible firms who will be invited to submit the technical proposals and financial bids for (a) system architecture development, and (b) system services and management
- d) The Committee issues formal letters to the shortlisted firms inviting technical and financial bids in a specified format and by a specified date. The short-listed firms are given three weeks to submit their technical proposals and financial bids
- e) The Committee invites the short-listed firms to a joint meeting to brief them on the request for proposals (RFP), selection criteria and process and provides necessary clarifications and information
- f) The Committee receives the technical proposals and financial bids for CRA from all

interested entities

- g) The Committee evaluates the various technical proposals and produces a shortlist of the most appropriate firms. The proposals of the rejected firms as well as their (unopened) financial bids will be returned to them
- h) The Committee undertakes site visits to examine and verify the infrastructure of the shortlisted firms and invites them for a presentation of their proposals
- i) The committee then opens the financial bids of each shortlisted firm and selects one firm which will serve as the CRA
- j) The Committee signs a contract with the agency which is selected to serve as the CRA and issues the CRA license
- k) The CRA produces the detailed system specification document and presents it to the PFRDA. The PFRDA studies and approves the system specification document
- l) The CRA begins work on system implementation as per the milestones specified for the three phases

### **7.3 Issues in system implementation time-frames**

It is recommended that the CRA is given adequate time to establish and test the system and operational inter-linkages with service providers for each of the three phases. The following implementation activities should be provided with adequate time by the PFRDA:

- a) **System specifications document:** Adequate time in *planning* the implementation is desirable as it will lead to more efficient implementation. This document may also warrant extensive debate and discussion and a very careful examination by the PFRDA. Importantly, this system specifications document will also form an essential backdrop for the service and system specifications for POPs, P&AOs and PFMs and will be an important input in determining their pre-qualifications and in engaging these service providers.

- b) **System implementation:** The CRA should be provided sufficient time to design, develop and procure appropriate software and hardware. The process for system architecture development, testing and debugging is an essential function and should not be compressed as this can lead to serious errors in reconciliation and transfers. Importantly, the CRA will be required to evaluate the existing infrastructure of P&AOs and advise the government on the additional infrastructure that may be required to gear this network towards electronic connectivity with the CRA. This process will also include extensive training of service providers (POPs and P&AOs) who will be located across the country.
- c) **System Testing:** The most crucial phase of the implementation process is the testing and debugging of the system software and processes and should also be provided adequate time. Internal testing as well as multiple mock/pilot tests using the full set of service providers and also the complete set of services and functions (including member services) should be conducted for each phase of system implementation.

## **8. Issues to be addressed**

1. The ability of the banking sector to facilitate electronic funds transfer across banks (as proposed under RTGS) and consequent netting between banks may offer some important benefits and lower transactions costs for the pension system and service providers. The funds transfer processes need further evaluation and analysis.
2. The exact operation and structure of the 'default' option is not covered in depth in this document. It is being examined in more detail in the document related to pension fund managers and investment guidelines.
3. This document proposes an account which is also portable across POPs – where a member is not tied to the services of any one POP and is able to remit instructions or funds from any POP location. The fee structures and incentives for POPs to offer quality service to their non-customers and cross-sell the PRA to their existing customers needs to be evaluated in consultation with potential POPs.
4. A separate study may also be necessary to study the regulatory overlaps and areas of cooperation in the event that the CRA and POP network is regulated by multiple regulators.
5. The administrative processes and related reliance on technology and electronic inter-linkages between POPs and the CRA may limit the outreach of this system to informal sector workers. A separate study may be commissioned to examine the needs of this population as well as secure institutional mechanisms (assuming technology gaps) that can be harnessed to deliver this system to the masses.