Pension Products for the Self-Employed (Bhagidari Sector) in India

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The Bhagidari sector consisting of Partnership/proprietorship firms and professionals constitute a large segment of the Indian economy. They contribute 35 percent to the national income and enjoy more than 75 percent share in the service sectors like trade, transport, construction, hotels and restaurants and other services like doctors, lawyers, architects, accountants, etc.

The activities where they are dominant are the fastest growing sectors in the economy. Their share in savings is more than forty percent. From the tax data one can infer that there were nearly 10 million present during 1994,95 and compared to the corporate and government sector, adequate focus has not been given to these segments.

The Pension products (retirement benefit schemes) available to them are essentially tax schemes and there is a need to focus on providing pension products to this sector whose market potential is very large. Since there is fluctuation in the income flow:; of the Bhagidari sector, the retirement products are to be need based and should have variable contribution facility. Similar to corporate sector, tax breaks should be made available to the Bhagidari sector both for present contributions and also for past benefit funding. Also, there is a need to have innovative products like variable contribution, need based programmed withdrawals, etc. to increase the consumption of pension products. The delivery system can leverage on the banking network and postal network to reach the customers as well as to have market penetration.

Introduction

The economic reforms undertaken by the Government of India in the nineties resulted in significant liberalization in the financial sector pertaining to corporate sector, banking industry and other capital market participants like mutual funds, merchant bankers, stock exchanges, etc. Reforms of the Insurance sector is an important component of the economic reforms due to which the government appointed the Malhotra (1994) Committee to study the insurance sector. The Government has taken steps to bring about changes in this sector by constituting Insurance Regulatory Authority and is also planning to allow private sector (both domestic and foreign) in this business.

One of the aspects covered by the Malhotra Committee, in the context of reforms pertain to pension funds. The Committee suggests that, "It is necessary to encourage pension schemes to serve the needs of this large segment of the population (namely the self-employed including professionals, traders, agriculturists and the vast labor force in the unorganized sector, which represents a massive potential market for pension schemes). The growth of pension funds has the potential to transform the financial markets." (Malhotra R.N. 1994)

Taking a cue the government has initiated some reforms in this area. For instance, The Unit Trust of India, the largest Mutual Fund in the country as well as a private fund (Kothari's) have already been permitted to enter into pension segment and hence some degree of competition is expected in the immediate future. The investment pattern has also been liberalized to a certain extent.

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In this context, it is important to understand the potential of the pension market and the means by which insurers can exploit this potential. In particular, one needs to understand the total market pertaining to the Bhagidari sector consisting of the Partnership/ proprietorship firms and the Self-employed, as well as focus on the type of products and channels for this sector. The Bhagidari sector constitutes the largest segment in terms of national income, savings, employment, etc.

It is also necessary to identify some of the important changes required in the existing regulations pertaining to investment, tax laws, etc. So that the full potential of this market can be explored both from the point of saving for investment in productive avenues as well as from the point of coverage for retirement benefits

Retirement Benefits Schemes: International Scenario

In many developed countries, there are many schemes whereby the employed and self-employed can save for their future income when they cease to be; in active service. There are three types of schemes, which have been labeled as the "three pillar concept" by the World Bank. They are

- Social Security Schemes sponsored by the governments
- Occupational schemes sponsored by the employers for the benefit of their employees and
- Private voluntary schemes to accumulate savings to provide for retirement needs.

Insurance companies play an important role in formulating and administering schemes under the second and third category above.

Social Security Schemes

These are statutory schemes administered by the government on a "pay as you go" basis. It is required for employers and employees to compulsorily contribute to these schemes. Even though the main benefit of the scheme is old age pension available to individuals after a certain age there can also be other benefits like widow benefits, sickness benefit, unemployment benefit, indexation of benefits, etc.

The expected changes in the demographic structure of the population and the resultant financial strain due to the social security scheme are prompting a debate in many developed countries regarding private initiatives needed to sustain such schemes.

Marshall N. Carter and William G. Shipman (1996) analyze the developing crisis in the pension market. It is the aging of the world's population - a truly glacial force that is already straining the national budget throughout the industrialized world. Over the next generation global greying will force major reforms in public pension and retirement systems everywhere to adapt to an unprecedented era of rising longevity. It is suggested that it is possible to craft reforms in public pension system that will safeguard retirement security for the elderly, enable the young and the middle aged to keep more of the fruits of their labor and achieve those first two goals without over burdening national economies but enhancing their long-term prospects.

The most credible way to achieve this, according to the authors, is by allowing workers to invest some of their pension plan contribution and tap the higher returns that private markets, especially equity market, can offer. It seems that the state will provide a very basic minimum amount beyond which people will have to provide for themselves through occupational or personal pension schemes.

Occupational Pension Schemes

Occupational pension schemes are set up by employers with contributions from both employers and employees. In some cases the scheme may not require contributions from the employees. Occupational pension schemes consist of Defined Benefit Schemes and Defined Contribution Schemes.

Defined Benefit Scheme promises to pay a certain level of benefit related to the final salary or the final average salary of the employee. The benefit is partly in the form of a pension payable during the lifetime of the retired employee and partly with the facility of commutation of a portion of the pension, which is tax-free. It is also possible to provide for pension guaranteed for certain number of years (say, five, ten or fifteen years) and afterwards for life or joint life and last survivor pension, etc. Generally, the costs of the schemes are met by contributions from the employers. In developed economies there are many discussions regarding employees also contributing for the scheme.

In the case of ***Defined Contribution Scheme***, the contributions from the employer (or from the employer and employee) is accumulated to provide the pension corpus out of which pension is purchased at the time of retirement of the employee. The other aspects regarding commutation of pension - alternatives like guarantees, etc. - are similar to defined benefit scheme. It is to be observed that in the occupational pension schemes of either type, there is a funding stage during which the contributions are invested and accumulated and there is a benefit payment stage after the employee has retired and hence the annuity payments fall due for payment.

During the stage of funding there is freedom for the employer either to administer the . fund on his own or go to outside fund administrators such as Insurance Companies, Banks, Mutual Funds, Investment Companies, etc. In many countries, Insurance companies are the popular vehicles for funding particularly in the case of small and medium scale enterprises. In all the countries, occupational pension schemes have to necessarily provide annuity benefits, which are related to the lifetime of the retired employee. When the benefits are vested, there is a choice for the employer to pay the pension out of the fund or to purchase pensions from Life Insurance Companies. The ultimate benefit is an annuity payable for life or equivalent pension from the latest vesting age payable either by the fund or through the purchase of an annuity from the Life Insurance Company.

The annuity is a level amount and the guarantee of payment of such an annuity involves mortality risk and investment risk. ***Mortality risk*** is the one relating to the beneficiary living longer than expected. ***Investment risk*** is connected to earning at least the guaranteed rate of return implied in the underlying annuity rate. The employer underwrites the risk of investment performance of the contributions during the funding stage under the defined benefit scheme. In case the employer is to pay the pension from the pension fund, he underwrites both the mortality and investment risk during the period of benefit payment.

Private Pension schemes

As a result of the desire of many governments to gradually reduce their social security commitments and encourage private provision for retirement benefits, many governments have facilitated setting up of personal pension systems by appropriate legislation and tax incentives. Such schemes can be operated by insurance companies as well as banks, mutual funds, investment companies, building, etc.

The main benefit is an annuity payable for life together with option for commutation of a portion of pension for tax-free lump sum as in the case of occupational pension schemes. Many additional features have been brought about in these schemes like choice for participants to defer their pension vesting age and also allowing them to take "Income. withdrawals". The service providers like banks, mutual funds, building societies, insurance companies, etc. administer income withdrawals but there are also regulations by which annuities which are dependent on human life have to be purchased only from life insurance companies.

We have provided in Appendix 1 a quick glance at the global practices. We can conclude that there are two types of trends, which are seen, in the recent past. One is pertaining to the reduced role of Government in the schemes' and other is the gentle nudge for larger contribution from the beneficiaries.

We also find that the self-employed are benefitted by tax breaks In order to save for their retirement benefit plans. This could be in the form of Self, Employed Individuals' Tax Act of 1962 (US) permitting them to set up retirement plans. These are known as Keogh or H.R. 10 plans. The Employee Retirement Income Security Act (ERISA), the Tax Reform Act of 1976, the Economic Recovery Tax Act of 1981 (ERT A) and the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA), etc. have carried forward the reforms for the self-employed retirement benefit schemes. This has been brought out by Levy R. Donald Esq. (1989). The deduction limits have been liberalized over a period and the funding amount has also been enhanced. There has been a close look at the self, employed in the developed markets and emerging markets like India need to pursue some of those reforms.

Indian Scenario

Retirement benefits for the Organized (Corporate and Government) Sector

In India, under Section 2 (11) of the Insurance Act, 1938, Pension contracts are deemed to be part of life insurance business. A comprehensive pension scheme is a long-term savings instrument that provides cover against the risk of death and 'risk of longevity'.

In the case of government, both central and state, as well as quasi-government organizations the pension is provided on "pay as you go" basis. The benefit is related to the last pay drawn by the employee and a portion of it can be commuted which is tax, free. Till recently in India the concept of providing pension as a retirement benefit has not attracted the private employers for the obvious reason that provision of pension is not mandatory unlike provident fund and gratuity. However, income tax benefits have attracted some employers to provide pension benefits to their executives. This also helps them to retain quality executives in their organization.

Now the scenario is changing with the enactment of "The Employees' Pension Scheme, 1995". Which is applicable to the employees of all factories and other establishments to which the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 applies.
This Act covers nearly 275,000 establishments employing about 20 million employees.

Further some public sector organizations like Banks, LIC, GIC, Coal Mines, etc. have entered into agreements for providing pension as a retirement benefit by transferring employers' contribution of provident fund to pension fund. In most of these cases the pension is Index linked, similar to that of Central Government schemes. At this juncture, these schemes are not actuarially viable.

As far as the private sector, employers have a choice between LIC and self, administration through a trust at funding stage. As regards pension payment stage, at present all occupational pension schemes have to go to LIC as per Insurance Act 1938. Thus LIC is the only player as regards pension payment stage even though trusts can manage the funds at the funding stage. It is to be noted that annuitants have several options like annuity for life with five, ten, fifteen years certain. Further, LIC has instituted a novel option of annuity for life with return of corpus to the beneficiary on the death of the annuitant. This is very popular as an individual pension plan.

There are not many attractive schemes for individuals as well as for the self-employed, professionals, partners in a partnership firm, etc. The coverage is also minimal. The OASIS report indicates that out of 314 million workers in India as per 1991 census report less than 11 percent have got old age income security. (Project Oasis 2000). LIC has recently introduced "Jeevan Suraksha" scheme, which to some extent meets the requirements of the segments like individuals, etc. Even in these schemes the Income Tax benefits are not given to the firm.

We have provided in Appendix 2 the different types of retirement benefit schemes operative in India. We find from this Appendix that only the last two categories (which are miniscule in terms of corpus and coverage) are available to Bhagidari sector and these are useful to some extent from tax point of view.

Bhagidari Sector in the Indian Economy

In the case of manufacturing sector in the Indian economy "organized" implies a registered manufacturing unit under the Factories Act and refers to factories employing ten or more people with power or twenty or more without power. One can easily assume that company forms of organizations would have manufacturing units covered under the Factories Act. Hence, all corporate entities having manufacturing units will be coverer! as part of organized sector. Even a partnership firm (unincorporated enterprise) can have a registered factory and it would be classified as belonging to organized sector.

This implies that in the case of manufacturing sector the "Unincorporated" is not the same as the unorganized even though all unorganized firms would belong to the unincorporated sector. This means that there are some unincorporated enterprises in manufacturing that fall under the category of organized sector.

In all other activities (other than manufacturing) it is possible to equate organized with corporate and unorganized with unincorporated sector. We use the term, "Bhagidari Sector" to indicate unincorporated enterprises consisting of partnership, proprietorship firms as well as professional (self-employed) categories.

Share of Bhagidari Sector in National Income

We have provided in Table (1) the share of different sectors like Agriculture, Government, Private organized and unorganized sectors. It may be noted that Agriculture here excludes government agriculture and that of private corporate even though they are marginal. They are included in the respective categories namely Government and organized private sector.

Table 1

Share in National Income of various sectors

	80-81	90-91	94-95	98-99 *
1. Agriculture	38.08	31.46	30.69	27.00
2. Government	17.50	23.90	24.50	24.00
3. Private Organized	12.50	12.30	13.30	14.00
4. Unorganized	31.92	32.34	31.51	35.00
Total	**100.00**	**100.00**	**100.00**	**100.00**

Note: *Computed from the National Accounts Statistics Data*

Source: National Accounts Statistics (NAS) 1997and 2000. *Central Statistical Organization, New Delhi.*

The above mentioned table (Table, 1) provides an insight into the importance of Bhagidari sector in our economy. The share of Government (which include central government plus state Government plus all public undertakings) in the NOP in 1998~99 was around 25 percent and that of Agriculture is around 27 percent. Of the remaining 48 percent the estimated share of unorganized sector is about 35 percent and organized corporate sector is around 14 percent. Let us recall that the unorganized sector is only a large subset of the Bhagidari sector. That is the share of Bhagidari sector is more than the 35 percent estimated for the unorganized sector [Table (1)]. If we look at the developed economies like that of USA we find that significant portion of national income is due to corporate sector. We find from Bureau of Economic Analysis (BEA) that during 1996 and 1997 the share of corporate business in the net domestic product of the US economy was of the order of 66.4 percent and 67.4 percent. (BEA, 1999).

Share of Bhagidari Sector in Manufacturing

We have data regarding the manufacturing sector as pertaining to registered (registered under Factory Act) and unregistered categories. The former is considered as organized and the later as unorganized by the National Accounts Statistics. The share of unorganized sector in manufacturing was 39.1 percent in 1990,91 and 38.8 percent in 1994,95. According to the Annual Survey of Industries (ASI 1993,94) 10.87 percent of the net value added in the factory sector (organized sector) during 1993,94 was due to partnership/ proprietorship firms (Bhagidari sector). Since unorganized manufacturing constitute nearly 39 percent of the value addition of the manufacturing sector, we can say that nearly 50 percent of the manufacturing activities is due to Bhagidari sector.

Share in Service Sectors

In case we consider activities like wholesale and retail trade, hotels and restaurants, road transportation, real estate and business services like medical, legal, etc. we find that more than 80 percent of the national income in these sectors is generated by the Bhagidari sector. We have given the shares in (Table,2).

Table 2

Share of Bhagidari sector in the Service sectors

		1980-81	1990-91	1997-98
1.	Construction	48.0	55.5	53.5
2.	Trade	89.7	92.2	84.2
3.	Hotels and restaurants	87.7	86.7	65.3
4.	Transport [Other than Railways]	65.9	77.7	75.3
5.	Storage	67.5	49.4	53.1
6.	Real estate, ownership of dwellings and business services	99.5	99.8	87.3
7.	Other services	46.2	37.0	32.2

Nore: *Computed from the National Accounts Statistics Data*

Source: National Accounts Statistics I *997and 2000. Central Statistical Organization. New Delhi.*

For instance, in trade we do not have a Wal-Mart or Sears or Mark and Spencer, or a Grey Hound in transportation or a chain of Burger Kings and Pizza Huts in restaurants unlike in the developed economies. In other words, all these service activities are provided by Bhagidari sector. The wholesale trader in food grains or fast moving consumer goods (FMCG) or consumer durable or the retail trader in these activities, [he transporter of goods with one or two trucks, the owners of restaurants in the length and breadth of the country, the construction contractors, the storage owners across the country, doctors, lawyers, architects, and accountants, etc. do not have the retirement benefit plans as in the case of officials in the government or executives or workers in the private corporate sector. It is to be noted that the service sector is one of the fastest growing in the economy in the last decade compared to Agriculture and Manufacturing.

Savings and Bhagidari sector

If we look at the savings data of the economy we find that around 80 percent is due to the household sector and the household sector consists of pure consuming (wage earning)

Table 3

Savings in the Indian Economy

		1990-91	1997-98
1.	ODS as % of ODP	24.27	23.10
2.	Public Sector (as % of ODS)	4.18	7.00
3.	Pvt. Corporate Sector (as % of ODS)	11.49	15.00
4.	Household savings (HHS) (% of ODS)	84.33	78.00
4.1	Saving in Physical Assets (as % of HHS)	54.66	55.00
4.2	Financial Savings (FS) (% of HHS)	45.34	45.00
4.2.1	Currency (% of FS)	12.58	10.60
4.2.2	Net Deposits (% of FS)	22.51	44.30
4.2.3	Shares and Debentures (as % of FS)	16.92	6.00
4.2.4	Net Claims on Oovt. (as % of FS)	14.81	8.50
4.2.5	Life Insurance Funds (as % of FS)	10.74	11.00
4.2.6	Provident and Pension Funds (as % of FS)	22.44	19.60

Nore: *Computed from the National Accounts Statistics Data*

Source: Various Issues of National Accounts Statistics (NAS). Central Statistical Organization. New Delhi.

households as well as the Bhagidari (mixed income households) sector. In other words, Bhagidari sector is included as part of the household sector in the savings data. (NAS 1989). We have given the savings data in Table 3.

A portion of the savings is due to farm households and the share of this is not separately available. We find that the proportion in national income is 44 percent and 56 percent between the unorganized agriculture and other unorganized activities. If we assume that the savings of the farm sector is in the similar fashion compared to the total household sector savings then we can assume that 44 percent of household sector savings could be due to farm households. This may be an overestimate and to that extent will only strengthen our arguments.

This implies that about 56 percent of the household savings would be from the non, agricultural part of the household sector. That is, nearly 45 percent [56 percent of 80 percent] of the total savings is from the non- agricultural households. We have estimated (see Vaidyanathan 1999) the share of Bhagidari sector, in the savings data of the household sector (non agricultural) using indicators like tax data (Table 4) and conclude that around 35,40 percent of the total savings is attributable to the Bhagidari sector in the economy. This provides us a clue regarding the size and value addition and savings of the Bhagidari sector.

Market Potential of the Bhagidari Sector

We have provided in Table 4 the returned income and tax payable for the assessment year 1994,95 for various categories like individual salaried persons, companies (both public

Table 4

Returned Income and Tax Payable for the assessment year 1994-95

Status	No. of Returns	Returned income	Tax Payable
	(000)	(Rs. million)	(Rs. million)
Individual Salaried persons	1637	129,960	17,640
Companies			
Public sector	23	62,130	30,450
Private sector	116	102,690	45,390
Partnership/HUF, etc.	1188	93,110	17,990
Individual non-salary category	3238	294,730	60,450
Total	**6202**	**682,620**	**171,920**

Source: AU India Income Tax Statistics (AIITS) 1994-95. *Directorate of Income Tax, New Delhi.*

and private sectors) and partnership / proprietorship firms including individual non-salaried category. This level of details is available for that year. We find from Table 4 that the total number of returns filed in 1994,95 was 6.2 million of which 139,000 are those of companies.

In all, there were 4.42 million returns filed by non-corporate non, salaried assessees of which 1.188 million returns were for partnership, HUF etc. and they accounted for a returned income of Rs.93,110 million. Another 3.238 million returns were filed by individual non-salaried category (mostly professionals and other self, employed persons) constituting a returned income of Rs.294,730 million.

Hence we find that more than 1.2 million unincorporated (partnership/ proprietorship) firms are tax assessed in India and the partners/proprietors of these units constitute an important market segment. We also find that 3.24 million professionals and self,employed persons are tax assessed and these persons also constitute an important segment since they are not currently covered by the schemes.

Assuming that there are at least three partners in these firms (a conservative approach since up to 20 partners are permitted by the Partnership Act 1932) we have in all 3.6 million in the partnership category and combine~ with 3.24 million in the professional category there are in all 6.84 million tax assessed major customers. Since the tax coverage is inadequate (estimatedly less by at least a quarter of what can be covered) particularly with reference to partnership firms and self-employed professionals we can consider that the actual market is around one and a half times larger than tax assessed. That is, more than 10 million in the Bhagidari sector can be considered as potential market in the next
one or two years. The average returned income for the Bhagidari sector is of the order of
Rs.58, 200 (Rs.582 billion / 10 million) and 25 percent of this is around Rs.15000. This is based on the taxable income and not total income available. The later is much higher and hence a conservative estimate of Rs.20, 000 as contribution per annum can be made. This will give rise to an estimate of possible annual contribution over Rs.200 billion.

If we consider the income returned by these groups from Table 4 we find that it is of
the order of Rs.388 billion. Since the Tax coverage is inadequate among the Bhagidari sector this can be taken to be at least one and half times more namely Rs.582 billion. It is observed that in the Corporate sector in India 25 percent of the salaries paid is allowed as charge on the income account. In case we consider on a similar basis then we find that 25 percent of Rs.582 billion, namely Rs.146 billion is exposed to potential retirement savings for the Bhagidari sector. It is to be noted that the Income of this group is presumed to be like salary in the hands of the Bhagidaris. This is an underestimate since returned income is only taken into account and not the total income which is available to Bhagidaris. Hence the market is between 150 to 200 billion in the year 1994,95 for which

Table 5
Projected Potential of Retirement Benefit Market for the Bhagidari Sector

						(Rs. billion)
	1999-2000	2000-01	2001-02	2002-03	2003-04	2004-05
Annual Contribution (at 10% growth rate)	322	354	390	429	471	519
Annual Contributions** (at 20% growth rate)	597	717	860	1032	1238	1486
Accumulated Funds * (at 10% growth rate)	322	715	1190	1762	2445	3257
Accumulated Funds * (at 20% growth rate)	597	1386	2412	3733	5419	7556

Note: * *The expenses, outgo and the discontinuation of contribution are not taken into account.*

The yield is assumed to be 12 percent, which has been the past trend. Also does not consider past benefit contribution.

detailed figures are available for the different components of the Bhagidari sector. This is assessment year and hence if we take it to be applicable for the financial year 1994,95 then we are erring on the conservative side for our estimations. This is the assumption we have made in projecting the market size in Table 5.

One can assume an average annual growth rate of ten to twenty percent since the coverage can be enlarged in order to tap the potential of the aggregate market and also based on the population growth and economic improvements.

We have provided in Table 5 projections pertaining to the retirement benefit market for the Bhagidari groups (partners and self-employed professionals). This is under the assumption that the growth rate of these segments will be of the order of ten to twenty percent over the coming five-year period. It is to be noted that in the initial periods in a growing market, one experiences high volume and high growth situation. It is to be observed that the Indian market is moving from a Government controlled monopoly market to an open market wherein private players both domestic and international are expected to compete vigorously.

We have assumed an annual contribution of Rs.20, OOO and as already seen the total annual contribution will be Rs.200 billion for the year 1994,95. We have taken it for 94, 95 financial year as well as assessment year (Le. 93,94 Financial Year) under the two assumptions of growth rates. (See table 5)

We find that there exists a large potential for the retirement benefit market in India for the Bhagidari sector .The prospects are encouraging but the constraints are also there which need to be addressed in order to tap this market.

Retirement Benefit Schemes for the Bhagidars

There are some individual schemes, which are available to the self, employed persons. These are Public Provident Fund (PPF) and Jeevan Suraksha Scheme offered by LIC as well as a scheme offered by Unit Trust of India. These are given in Appendix 3. We find that the important aspects of these schemes are tax benefits to the individuals in the year of contribution. This tax benefit is not available to the firms unlike a corporate form of organization wherein the contribution made to the benefit of executives or directors is eligible for deduction against the income of the company.

For instance, in the contribution made by the partner to a pension scheme like Jeevan Suraksha (see Appendix 3) of Life Insurance Corporation of India is not eligible to be treated as the expense of the firm. The message is that these have to fend for themselves in their old age while the Government employees due to their militancy, and corporate employees and even directors of companies due to their clout in the decision making processes have managed for themselves a variety of retirement and social security schemes.

Retirement needs in relation to professional life standard: Bhagidari **Sector**

There are three major trends which are important to observe in the context of retirement plans for the Bhagidari sector.

- Improved Life Expectancy.
- Decline in the Joint Family System.
- Increased aspiration and lifestyle after retirement.

Even though the predictions by Wallace Paul (1999) regarding the Agequake may not be immediately applicable to Indian context we find that the life expectancy is improving and in many parts birth rates are declining. We have provided in Table 6 some of the key data for the same. We find that the proportion of population above 60 years (which is the retirement year for government employees) is 6 percent based on the 1991 census data.

Table 6

Key Census Statistics - India

	2016(P)	1995	1991	1981	1971
Population (million)	1,263	934	846	683	548
Urban population (million)			218	159	109
Birth rate (per 1000)*		28.3	32.5	37.2	41.2
Life expectancy at birth (years)**		60	58.2	50.5	45.6
Infant Mortality rate (per 1000 live births)***		74	80	110	129
Age Group 0,19 years %			47.1		
20-44 years %			35.8		
45,59 years %			11.2		
60 & above %			6.0		

Notes:

* *Estimates further predict a sharp drop in this by year 2016. though no hard data is available*

** Rough *estimates point towards* this touching 75 *years and beyond over* the *next few decades*

*** *Better medical and health facilities may see a further drop with rate touching half of 1971/evels.*

Source: Statistical Outline of India 1998-99. Tata Services Ltd. Mumbai.

This could increase significantly in the coming decades to say 15 percent due to improved living standards and medical facilities and that could constitute significant proportion of 'population. In that case the coverage of the Self-employed categories need to significantly increase and also the market penetration need to be deeper.

The traditional Hindu Undivided Family (HUF) system took care of the needs of the elderly and it was providing a social security net during old age due to the joint family system. But due to modernization and economic development and migration to metros, the joint family system is on the decline and nucleus family has become the norm at Least in the cities. Since brothers used to stay together the requirements of elders were all shared by the family.

For instance, in the past for a widow it is common practice to go and stay in the house of her brother in case she is not having a male progeny. These are becoming less common due to nucleus family system.

Also, due to higher education and opportunities in developed countries like the USA many youngsters have migrated to western countries and their parents are in India and they require retirement benefit plans to suit their purposes even though they may get dollar receipts from their children. This has created a significant need to have retirement benefit plans and products for the Bhagidari sector.

The expectations regarding lifestyle after retirement has also undergone significant change in the last ten years. In other words, individuals aspire to have the same or some times even improved lifestyle after retirement than what they were used to during their working life.

For instance, travel to tourist or pilgrimage centres are undertaken after retirement by couples which they may not have undertaken during their working life due to lack of time. The consumer culture also adds to the requirements of consumer durables (like Fridge, TV etc) which may not have been used during working life due non-availability of many of them.

This implies that the traditional assumptions regarding the nature of income requirements based on life style patterns after retirement, may not hold true in the future. Hence products have to be developed to suit the requirements of the Bhagidari sector in the changing context.

Quantifying the Individual Retirement Benefits

The critical element in the quantification process is the estimation regarding the requirements of the individual after his retirement. Here it needs to be stressed that there is no particular retirement age in the context of Bhagidari sector since they are Self, employed and can decide their time of retirement. They may partly take retirement in terms of reducing their working hours or days and then go for complete retirement. This implies that the products for these groups need to be structured to suit their requirements unlike employees of the organized sectors.

For instance, Fields and Mitchell (1984) report that delaying retirement from age 60 to 61 decreases the present discounted value of the pension payments by 1 percent; between 62 and 63 this value is increased by 5 percent; all subsequent delays until age of 65 are associated with further decreases of 2 percent in the present value. Most private pension plans do not reward delays of the retirement decision beyond social security's 'normal' age of 65 years.

Oliver Fabel (1994), for instance, points out that the benefit schedules associated with early withdrawals lack actuarial fairness. This is attributed to the incentive role of private pensions, given that mandatory retirement rules are precluded.

In case we take that the Self-employed is making a sum of Rs.20, 000 per month and we think that half of this need to be covered in terms of pension benefits and investments yield 12 percent, then the computation for a five-year saving scheme (plain vanilla product) will be as follows:

The Annual requirement after retirement is = Rs.120, *000*

-This needs to be capitalized at say 12 percent and this implies a corpus *ofRs.1, 000,000*

In case we take a 'n' year time horizon, the equal annual amount needed to create this corpus at 12 percent is given by

P x FVIFA (n, 12 percent) = S where FVIFA denotes Future Value Interest Factor Annuity.

where, FVIFA (n,r) = [(1+ r)n - 1] / r

In our example we need to find the sinking fund (P) factor, which gives rise to the sum needed at the beginning of the expected retirement period.

In case we consider a period of 60 months (five years) then

we can find from the discount tables that the value is as follows:

P x FVIFA (60.1 percent) = Rs.l,000,000

P x 81.669 = Rs.l,000,000

This turns out to be Rs.12, 244 for a month or on an annual basis it will be Rs.146, 928

In case we consider annual contributions then it will be higher at the same rate and it will be

P x FVIFA (5, 12 percent) = Rs.l,000,000

P x 6.3528 = 1,000,000 and this will be

P = Rs.157,410

In either case it would be unrealistic to expect more than half of his current income

(Rs.240,000) to be provided as contribution by the Bhagidar.

In case we consider periods of ten years and fifteen years then the annual contributions need be Rs.56,986 (1,000,000 / 17.548) and Rs.26,824 (1,000,000 / 37.279) and these constitute nearly 23 percent and 11 percent of the current income. This may be an acceptable proposition for the Self-employed having longer life span- to go. But those segments that would like to enjoy retirement benefits within say next 5 years may find it impossible to contribute.

In the case of organized sector when pension benefits were initiated, many of the employees were nearer retirement say 5 years, 8 years, etc. In many organizations consequent on mandatory provision for providing gratuity and provident fund, some corpus was built up to help funding for pensions. Even in such cases the available corpus is not sufficient to meet the entire funding. Therefore the Income Tax Act provides for funding of 80 percent of the past service income during the remaining period of service. In a similar fashion benefits should be provided to the Bhagidari sector for past service funding.

Retirement Benefit and other products

It is to be noted at this juncture that identifying market potential is only part of the challenge faced by a pension fund manager. It is essential to develop appropriate products for different segments with competitive pricing and product awareness among potential customers.

There are two issues in looking at the potential of the pension market, which need to be considered. One is pertaining to providing coverage to existing persons who are already covered by provident fund schemes. In such a case it can be given as an additional benefit and to some extent it may cannibalize the existing retirement benefit product.

We find that pension products have to compete with other savings instruments like PPF, Small Savings, Mutual Funds, Bank Deposits, etc. From Table 3 we observe that during 1996,97 the savings in shares and debentures by the households was 7 percent of the financial savings, insurance funds was 11 percent and provident and pension funds 19 percent. It is to be noted that Bhagidari sector is included as part of household sector in our savings data.

This indicates the need to introduce pension products, which have the characteristics of other competing products. For instance, they can provide need based programmed withdrawals for the individual and Bhagidari policies.

In this context one of the major recommendations of the Malhotra Committee (1994) is "Whereas employees in the organized sector may look to their employer or the Employees Provident Fund for a pension, the vast majority who are Self-employed professionals or traders or are employed in the unorganized sector have to look only to insurance companies for providing suitable pension plans. While an employer's contribution to a pension fund gets substantial tax relief the relief available in respect of an individual's contribution to his pension policy is quite meager and does not provide sufficient incentive. In order to popularize the schemes under individual pension plans, contribution to such schemes, up to prescribed limit should be fully exempted from tax. It is essential that such long, term savings should be given a special treatment for tax relief distinct from the benefits allowed to relatively short, term savings."

Hence we stress the point regarding providing adequate tax benefits for Bhagidari pension schemes. The contribution by the Bhagidaris should be eligible as a charge on revenue account up to 25 percent income of the firm as it is allowed in the case of the corporate sector. This will give incentive for him to provide for retirement benefit and also increase consumption of provision of pensions.

The incomes of Bhagidaris are volatile and fluctuating and hence it is advantageous to develop products wherein the contributions can be variable to suit his income patterns. However a minimum annual contribution can be specified to allow for continuity and also meet the requirements of the term assurance premium.

In case of untimely death the contributions may not be sufficient to provide for the dependents a decent living. Therefore it is advisable to develop products in combination with term assurance wherein the insurance amount is sufficient to fund the needs of the dependents.

Channels of Distribution

Consequent to the mandatory provisions the pension can be provided by contributing to the LIC superannuation scheme by formation of a trust or by managing the funds independently as per the provisions of the Income Tax Act. Therefore the marketing channels for group pensions or superannuation is through the marketing officials of the Pension and Group Schemes department. The individual pensions like "JEEVAN SURAKSHA" and some products of the UTI are marketed through the network of agents, along with other insurance products of LIC.

It is possible to think in terms of using the Banking network to sell these retirement benefit products to the self-employed. We find that there are 288 commercial banks with 64,926 branches during 1996. There were 31,913 urban branches and 33,013 rural branches in existence during this period. Other than this there were estimatedly more than 30,000 branches of Non-Banking Finance Companies (NBFC's) spread over the country and out of this at least 10,000 or so are rated and regulated by -the Central Bank. There is also an effective postal system having more than 153,000 Post Offices spread over the country in 1996,97 with nearly 17,000 in the urban areas and more than 136,000 in the rural areas.

Given the breadth and reach of these institutions throughout the country, it is possible for the pension funds to leverage on this network to meet the requirements of the retirement benefit schemes of the Bhagidari sector. It is not only required for the products to be innovative and tailor made for the requirements of the Bhagidari sector but also they should have a fairly extensive reach and market penetration given the geographical size of the market.

This also implies that special studies need to be undertaken by the pension funds regarding the lifestyle and other market characteristics of this sector so that the products can _be developed and customized and delivered at reasonable cost and service effectiveness to the customers.

Conclusion

Role of Bhagidari sector in the Indian economy is relatively large, having more than one, third of national income and more than three-fourth in the service sectors. Nearly 40 percent of the savings in the economy is due to Bhagidari sector.

The estimated number of Bhagidaris are 10 million as of 1994,95 who can be considered as potential consumers for pension products. With an annual contribution of Rs.20,000 we estimate that there exists a market of Rs.200 billion as of 1994,95.

Using the past data and an assumption of 20 percent average annual growth rate we find that by 2005 the annual estimated contribution will be Rs.1500 billion and the corpus will be Rs.7550 billion. This is without taking into account the past service funding. Currently this market has not been fully exploited in our context and this could be due to absence of homogeneity of the sector. Hence in the context of the opening up of the Insurance business, it is expected that specific need based and tailor made products will be available for the Bhagidari sector.

Similar to corporate sector, tax breaks should be made available to the Bhagidari sector both for present contributions and also for past benefit funding. Also there is a need to have innovative products like variable contribution, need based programmed withdrawals, etc. to increase the consumption of pension products. The delivery system can leverage on the banking network and postal network to reach the customers as well as to have market penetration.

Appendix 1

Overview of Retirement Plans (pension and Severance) in selected countries

Country	Benefits Provided
Brazil	There are some private defined benefit plans, but defined contribution plans are growing in popularity. Severance plans resemble a defined contribution retirement plan with an 8 percent annual employer contribution.
Germany	Employers are permitted to established tax-deductible book reserves without establishing a separate trust for pension schemes. Separate trusts and insured schemes are also common.
Japan	Lump sum severance plans are universal, using tax-deductible book reserves as the funding mechanism. Separate pension trusts are allowable only for employers with more than 100 employees. Insured pension schemes are available for smalleremployers. Pension trusts are subject to an annual tax of 3pproximately 1.2 percent on the assets. No vesting is required. Employers with more than 5000 employees may contract out of government-provided pensions.
Norway	Pension schemes are common only in medium and large companies. Nearly all plans consist of insurance contracts rather than separate trusts.
South Korea	Employer-provided defined benefit pension schemes do not exist. Lump sum severance plans with low benefit levels are nearly universal. Individual defined contribution plans with employer contributions are becoming popular. Lump sum severance plans are funded by book reserves and insured contracts.
Thailand	Employer-sponsored pension plans are not mandatory but, where provided, the employees must contribute at least 3 percent of salary. Employers contribute at least as much as the employees and may contribute up to a tax-deductible limit of 15 percent. Invested assets are not in an irrevocable trust, thereby allowing the employer to capture some of the investment income as income to the company. This is equivalent to the book reserve method in other countries.
The United Kingdom	A wide range of defined contribution and defined benefit plans is available. If the benefits provided are substantial, the employer can contract out of the government-provided pension benefits. Lump sum payments at retirement are common, resulting in many arrangements that mimic the severance plans

	found in other countries. The United Kingdom is one of only a few countries that does not require a minimum recognition of accrued liabilities through separate funding or book reserves.
The United States	With less than one-half of the workforce covered, employer, provided retirement plans are not as common as in most other countries where there is nearly universal coverage of employees. A wide variety of defined benefit and defined contribution plans using tax-exempt trusts or insurance contracts is used. Non tax-deductible book reserves, with no separate funding, are common for benefits provided to executives. Mandatory employee contributions are allowable, but are not common. When employee contributions are mandatory or otherwise allowed, their tax status is dependent on the particular type of plan established by the employer.
Zimbabwe	Employees contribute 5.0 to 7.5 percent of salary into employer, sponsored defined benefit plans. Employers typically contribute an additional 10 to 20 percent of employee salaries. Funds must be in a separate trust with one-half of the trustees representing employee interests. Some 555 of all trust fund assets must be invested in government securities.

Source: Adapted from International Group Program (lGP) Country Profiles (1995): *International Benefit Guidelines* (1995). *Quoted in International Risk and Insurance* an *Environmental,Managerial Approach by Skipper Irwin, McGraw,Hill1998.*

Appendix 2 Retirement Benefit Schemes 'in India

Scheme	Salient features and average returns earned	Estimated Corpus (Rs. bn)
The Employees' Provident Fund [EPF] Scheme 1952	Mandatory. Defined contribution plan applicable to all establishments employing over 20 employees. Not applicable to Central Government, LIC, GIC, UTI, IDBI, Public sector banks, armed forces and other Government bodies/agencies (See below). Average return 12 percent (in the nineties)	800
Public sector and armed forces superannuation schemes	Government employees are on "pay as you go" basis. Bank and insurance (public sector) employees have inflation-proofed pensions. Armed force schemes currently earn 12 percent p.a.	200

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Scheme	Salient features and average returns earned	Estimated Corpus (Rs. bn)
The Employees' Pension Scheme 1995	Defined contribution plan mandatory for subscribers of EPF scheme since March 1997. Employer contribution 8.33 percent and Government contribution of 1.16 percent of wages (not exceeding Rs.5000 p.m.)	70
Gratuity	Employer contributory scheme based on actuarial computations. This may or may not be accumulated. Scheme could be privately managed or handed over to LIC Group Gratuity scheme	250
The Employees' Depos it, linked Insurance Scheme	A voluntary employer contribution scheme over and above mandatory contribution schemes. Average return: 8.5 percent p.a.	10
Private sector superannuation schemes	Voluntary benefit provided by employer, to select senior management typically. Maximum tax deductible for contribution of 15 percent of annual wages. Payable as lump sum or annuity.	150
Public Provident Fund	Savings scheme available to all Indians with a typical maturity of 15 years extendable up to 30 years. Employer contribution not necessary . Average return of 12 percent tax, free since 1987. Extra advantage being tax deduction by 20 percent for sum deposited up to Rs.60,000 p.a. (Le. Rs.12000 less tax)	120
Individual Pension Plans	LIC and Private sector mutual fund offered pension schemes: . UTI-RBP . Jeevan Suraksha . Jeevan Akshya . Jeevan Dhara . Kothari Pioneer Pension Plan	2
Total	**Annual accruals around Rs.100 billion**	**Rs.1602**

Appendix 3
Retirement Benefits Schemes for the Self-employed in India

Public Provident Fund (PPF)

The Public Provident Fund scheme (1969) was instituted by the Government of India with a view to enlarge the scope of the retirement benefit to employees of the organized sector as well as to the Self-employed who are outside the existing social security net.

- A PPF account can be opened in any branch of the State Bank of India or any of its subsidiaries.
- The duration of the scheme is 15 years and can be extended thereafter for 5 years. Minimum contribution of Rs.l00 p.a. is needed. Annual subscription up to a limit of Rs.60000 qualifies for tax rebate of 20 percent.
- The PPF is thus an uneven annuity scheme and provides flexibility to investment planning depending on the individuals' tax requirements on a year,to'year basis.
- The rate of interest is 12 percent. It also provides loan and partial withdrawal facility.
- There is no employer contribution in this scheme

Retirement-Benefit Plan of Unit Trust of India (UTI)

Salient features:

- Eligibility: Age group - 18 to 60.
- Lock-in period: Minimum 5 years.
- Benefits: Life time Pension or lump sum savings:
- U/s 88 for taxable income.
- U/s 54EA and 54EB for capital gains of the IT Act 1961.
- Under Wealth Tax Act 1957 for transfer of proceeds to the nominee.
- Under Gift Tax Act 1958 when gifted.
- No limit on contribution amount.
- No limit on number of payments.
- Benefit of lump sum or annuity.
- Transparency of the investment details is an added advantage.

Jeevan Suraksha (pension Plans Offered by LIC of India)

Salient Features

- Eligibility: Age group 30 to 60
- Age limit for maturity: Minimum age 55 years. Maximum age 70 years.
- Policy Period: Minimum 5 years, Maximum 35 years.

- Pension Amount: Minimum pension of Rs.250/- per month.
- Premium Amount: Minimum premium Amount of Rs.1800/- per annum.
- Benefits: Insured pension from vesting date.
- In case of death of the policyholder before vesting date, 50 percent of the pension will be paid to his spouse.

Pension Options:

- Life pension
- Guaranteed for 5/10/15 years and life thereafter
- Joint life
- Bonus additions are given to the benefits

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