NATIONAL PENSION AND PROVIDENT FUND PLAN

TABLE OF CONTENTS

1. BACKGROUND 2

2. TWO FORMAL OLD-AGE INCOME SECURITY 3
2.1 Gratuity Scheme 3
2.2 Government Employees Provident Fund Scheme 3

3. INADEQUACY OF LUMPSUM PAYMENTS 3

4. GOVERNMENT INITIATIVES 4

5. NATIONAL PENSION AND PROVIDENT FUND PLAN 4
5.1 National Pension Plan 4
5.2 Provident Fund Plan 6
5.3 Contributions to the National Pension and Provident Fund Plan 6
5.4 Crediting of contributions under the NPPFP for those GEPF members 7

6. INITIATIVES TAKEN TO REFORM THE CURRENT NATIONAL PENSION PLAN 7

7. PERSPECTIVE 8

Table 1: Summary of Old-Age Benefit Schemes in Bhutan 10

NATIONAL PENSION & PROVIDENT FUND PLAN

1. BACKGROUND

Old age income security is a priority and a concern worldwide. As the world population ages, there is a growing urgency for societies to pay attention for establishing appropriate safety nets and providing support for the elderly citizens. Old age citizens in Africa and Asia, has predominantly been cared for by the extended family arrangements, which is an informal old age protection system. The informal old age family protection systems are much under strain as the informal (traditional extended family or joint family) systems of pooling income and risk diminishes. As such, formal old age protection systems are replacing the traditional and informal systems of old age protection all over the world.

Although informal systems of old age income security continue to function in Bhutan providing support to the retired and elderly (for example, co-residence remain very high i.e. older parents living with their children), but the extent and adequacy of that support systems remains unknown. Little is known about intra-household resource allocations, its implications on the support of the elderly. Empirical evidences showed that family support systems are under increasing strain, thereby diminishing the informal support for the elderly people.

Formal old age provisions were limited to the (1) Gratuity Scheme and (2) Government Employees Provident Fund Scheme (GEPF) which covered primarily the public[1] sector salaried employees including the Armed Forces. Very recently the GEPF Scheme has been restructured to provide a multi-tired retirement schemes with

[1] Civil service, corporations and joint sector companies

a combination of lump sum payment on the date of retirement as well as pension as an annuity for life.

2. TWO FORMAL OLD-AGE INCOME SECURITY

2.1 GRATUITY SCHEME

The Gratuity scheme was introduced in 1962 (concomitant with the Bhutan's First Five Year Plan) and financed out of the general public budget based on final earnings and number of years of service and limited to a fixed ceiling of Nu. 300,000. It is like an employer's financed "Occupational" scheme based on the final earnings.

2.2 GOVERNMENT EMPLOYEES PROVIDENT FUND SCHEME

The GEPF Scheme was established in April 1976 as a compulsory savings scheme for the public sector employees and the Armed Forces. It was financed with 8% to 10% contributions from the members' salary with matching contributions from the employer. On retirement the members were paid in lump sum the accumulated contributions along with returns credited thereon.

3. INADEQUACY OF LUMPSUM PAYMENTS

The GEPF Scheme covers only employees of the public sector including the members of the Armed Forces, which was less than 5% of the total population and 7.2% of the labor force. The main labour force remained out of the purview of the formal retirement scheme.

The lump sum payments from both the Gratuity and the GEPF Schemes for a limited workforce also proved to be insufficient and inadequate instruments for old-age security, especially in Bhutan with a capital market development and an insurance branch in an early stage of development. Empirical evidences showed that the lump sum amount received from the two schemes (Gratuity and the GEPF) were low, which barely covered the expenses of the retirees for over a period of three to four years after retirement. Retirees were then left without any monetary support, which forced them either to look for some sort of menial employment paying very little or depend on the income of the children.

4. GOVERNMENT INITIATIVES

Inadequacies of the lumpsum amounts from the Gratuity and the GEPF Schemes prompted the Royal Government in initiating a formal old-age income security reform. ***The Government restructured the Government Employees Provident Fund Scheme as the National Pension and Provident Fund Plan as on 1st July 2002.*** The reform has been primarily aimed at providing old age insurance (safety net), redistribution of income (from the higher income to the lower income brackets as well as from one generation to another) and a savings vehicle (to allow individuals to redistribute income across their own lifetime to avoid poverty in old age).

Unlike the two formal schemes, the Gratuity and the GEPF Schemes, which covered only the public sectors, the present reform shall extend the coverage ultimately to other sectors especially to the salaried employees in the private sector. The initiatives are in line with much aspired goal and vision of the Royal government's **"Gross National Happiness"**.

5. NATIONAL PENSION AND PROVIDENT FUND PLAN

The National Pension and Provident Fund Plan comprises two separate but linked tiers:

- **The National Pension Plan; and**
- **The Provident Fund Plan.**

5.1 National Pension Plan

The **National Pension Plan,** titled Tier 1 of the NPPFP, is a partially funded pay-as-you-go defined benefit plan under which monthly pension benefits is provided to the members upon retirement. The benefits under the pension plan may be broadly categorized as in Table:

Type of benefits	Condition for payment	Period of payment
Member pension	On retirement	From the date of retirement until member dies
Permanent Disability benefit	On permanent disability of a member	From the date of permanent disability until recovery or attaining minimum civil service retirement age or death whichever is earlier
Surviving spouse benefit	On the death of member	From the date of the death of a member or the spouse attaining 50 years whichever is earlier until remarriage or death whichever is earlier
Surviving children benefit	On the death of a member	From the date of the death of a member until the surviving child attains 18 years limited to maximum of three children
Orphan benefit	On the death of both the parents and when no spousal benefits are payable	From the date of the death of a member until the surviving child attains 18 years limited to maximum of three children
Dependent parent benefit	When no spousal or other benefits are payable	From the date of the death of a member or the dependent parent attains minimum civil service retirement age whichever is earlier until death (only one parent)

A member on retirement attaining the minimum retirement age will be entitled to pension from the date of retirement until death. The pension benefits are based on the following formula:

$$\textbf{Pension} = \frac{\textbf{Total pension points * 60\% * ACSSI}^{2}\textbf{ (pervious year index)}}{\textbf{Full working period}}$$

The pension benefits are directly related to the pension points earned during the active working period and contributions paid. At retirement all the pension points earned from year to year will be added to determine the pension amount payable. In other words, the cumulative pension points earned on retirement is the sum of the pension points credited during the active working period and the contributions.

[2] Average Civil Service Index

Although, a member with higher pension points earned will get higher benefits, the benefits is nevertheless, limited to twice the ACSSI or 4 pension points a year. In other words, a worker may not earn more than four pension points per year and not more than what is required to pay a pension of twice the average civil service salary index. Any contributions in excess of 4 pension points of a member will be transferred to the individual Tier 2 account.

In order to protect those members with low income, a minimum support of 30 percent of ACSSI will be paid as total pension benefits.

Early retirement pension is also allowed to members who make an option to retire five years prior to minimum retirement age with reduced pension benefits.

The pension benefits are indexed to the Average Civil Service Salary Index. The adjustment of pension is lagged by one-year index. Any changes in the civil service salary will affect the pension benefit level in future. This adjustment mechanism has been formulated to maintain the purchasing power of the beneficiaries in future.

5.2 Provident Fund Plan

The **Provident Fund Plan**, titled Tier 2 of the NPPFP, is a defined contribution provident fund plan under which lump sum benefit equivalent to all the contributions credited to a member's Tier 2 account, together with returns thereon will be paid on the date of his/ her retirement or death while in service.

5.3 Contributions to the National Pension and Provident Fund Plan

The present retirement program has been reformed without making any additional contributions from both the members and the employers. The members will continue to contribute 8% to 12% of the monthly basic salary with matching contributions from the employers making total contributions of 16% to 24%.

5.4 CREDITING OF CONTRIBUTIONS UNDER THE NPPFP FOR THOSE GEPF MEMBERS

Out of 16% to 20% contributions (including Employee and Employer matching contribution) equivalent to 10% of members basic salary is being credited to Pension Fund Account while the balance gets credited to the Provident Fund Account. The details of apportionment of contributions are shown in the Table below:

Type of member	Contribution as percent of covered monthly salary	Apportionment to Tier 1 account	Apportionment to Tier 2 account	
		Employer & Employee contribution (%)	Employer contribution (%)	Employee contribution (%)
Simultaneous members of Tier 1 & Tier 2	8% contribution	10	3	3
	10% contribution	10	5	5
Only of Tier 2 members	8% contribution		8	8
	10% contribution		10	10

6. INITIATIVES TAKEN TO REFORM THE CURRENT NATIONAL PENSION PLAN

While the period of standard financial soundness of the pension plan around the world is about 50 to 75 years, the National Pension Plan of Bhutan when valuated under the current scheme was found to be financially sound for over just 30 years. The valuation has shown that if all assumptions in the Bhutan Pension Model remain as projected then the current plan will be in deficit after 2034. The NPPF, therefore, with the help of a consultant Actuary has been initiating possible reforms to the current pension plan in its bid to making the system sustainable atleast for 50-year period.

The possible reforms, which are meant for eliminating the deficits of the current system and achieve a sustainable pension scheme in the 50-year projection horizon, includes: steady increases in the retirement age, a gradual change to the full working period, and indexation of pensions after vesting of pensions. The effect of changes and reforms are summarized as under:

- Increase of retirement age by 3 months per year until 65 years in 2038 instead of increase of retirement ages by 2 months a year as per current regulation
- Increase of Full Working Period by 3 months each year until becoming equal to the pension sustainable age minus 20 i.e., 45 years in 2062, instead of increase of full working period by 2 months a year provided for in the current regulation
- Index pensions after retirement to Consumer Price Index (CPI) or ACSSI whichever is lower instead of ACSSI.
- Increase of contribution to pension (rate) as under:

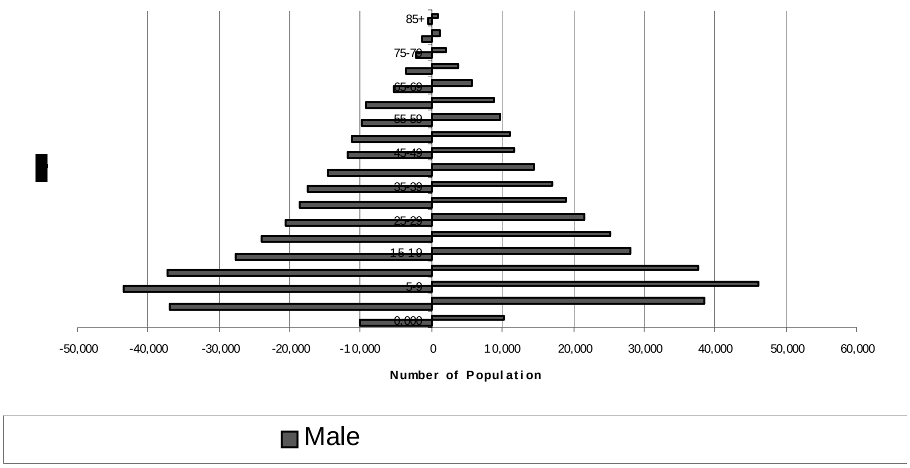
Year	**Increase as a percentage of basic salary**		**Total monthly contribution as a percentage of salary to pensions (Tier I)**
	Employee	**Employer**	
Current year	Nil	Nil	10%
2020	0.5%	0.5%	11%
2030	0.5%	0.5%	12%
2040	0.5%	0.5%	13%
2050	0.5%	0.5%	14%

If the changes or reforms as indicated are adopted the National Pension Plan will be financially in balance for 50 years.

7. PERSPECTIVE

The restructuring of the GEPF scheme to the National Pension and Provident Fund Plan has been initiated taking into consideration among other things favourable economic and young population demographic conditions (see table below) as well as existing types of the old age protection. In wider perspective, the program envisages bringing uniformity in social protection program in the country.

Demography of Bhutan



At present Bhutan’s private sector development is in its nascent, growth phase. Over time development of private sectors is one of the priorities in the development policy agenda of the Royal Government.

The social security reform focused initially to the members of the then Government Employees Provident Fund Scheme covering public sector employees including the Armed Forces. The coverage shall be extended to other sectors such as salaried workforce of the private sector in a phased manner. The reform has been aimed in achieving portability of the social security schemes, especially to encourage the cross mobility of labour force within the labour markets and provide equitable incentives to the private sectors, and the ultimate sustainability of the social protection program.

Table 1: Summary of Old-Age Benefit Schemes in Bhutan

Scheme	Year Started	Objectives	Coverage	Replacement Rate	Administration
Gratuity Scheme	1961	Honour the service of the employee for his employer	Civil Servants, Corporations, Joint Sector Companies and Armed Forces	Last (month) salary * No. of years in service (maximum ceiling of Nu. three hundred thousand)	Ministry of Finance, Individual agencies (for corporate employees)
Government Employees Provident Fund (GEPF)	1976	Compulsory savings scheme	Civil Servants, Corporations, Joint sector companies, Armed Forces and few Private sectors	Based on absolute contributions and rate of returns	Royal Insurance Corporation of Bhutan