

**ASIAN DEVELOPMENT BANK**

**TAR: IND 37061**

**TECHNICAL ASSISTANCE**  
(Financed by the Japan Special Fund)

**TO**

**INDIA**

**FOR**

**STATE-LEVEL PENSION REFORMS**

**December 2004**

## CURRENCY EQUIVALENTS

(as of 26 November 2004)

Currency Unit	—	Indian rupee/s (Re/Rs)
Re1.00	=	\$45.15
\$1.00	=	Rs0.221

## ABBREVIATIONS

ADB	—	Asian Development Bank
DB	—	defined benefit
DC	—	defined contribution
DEA	—	Department of Economic Affairs
EA	—	executing agency
IT	—	information technology
MOF	—	Ministry of Finance
NPS	—	new pension system
PFRDA	—	Pension Fund Regulatory and Development Authority
PROST	—	Pension Reform Options Simulation and Toolkit
RBI	—	Reserve Bank of India
TA	—	technical assistance

## TECHNICAL ASSISTANCE CLASSIFICATION

<b>Targeting Classification</b>	—	General intervention
<b>Sector</b>	—	Finance
<b>Subsector</b>	—	Pensions
<b>Themes</b>	—	Sustainable economic growth, governance, and Private sector development
<b>Subthemes</b>	—	Promoting macroeconomic stability, Financial and economic governance, and policy /institutional reforms

## NOTE

- (i) The fiscal year (FY) of the Government ends on 31 March. FY before a calendar year denotes the year in which the fiscal year ends.
- (ii) In this report, "\$" refers to US dollars.

This report was prepared by V. V. Subramanian, South Asia Department.

## I. INTRODUCTION

1. The Government of India requested the Asian Development Bank (ADB) to provide technical assistance (TA)<sup>1</sup> to help selected state governments in India reform their civil service pensions by reviewing options for addressing the fiscal implications of the growing pension burden of the respective state government, and considering policy and downstream modifications in the existing pension schemes. Accordingly, a TA grant in the amount of \$750,000 was included for the above project in the country strategy and program to India for 2004. The TA is part of ADB's strategic intervention to improve public resource management and develop India's domestic capital market, which is critical to moving the infrastructure agenda forward and financing India's economic growth. A TA Fact-Finding Mission visited India from 12 to 14 May 2004 to discuss the possible scope of assistance and implementation requirements with the Department of Economic Affairs' (DEA) Capital Markets Division, Ministry of Finance (MOF), and other key stakeholders concerned with the reform of India's pension system. This report reflects the findings of the Mission and the understanding reached with the Government regarding the TA objectives, scope, cost, implementation arrangements, and terms of reference.

## II. ISSUES

2. Fiscal stress emanating from the increasing pension liabilities of the central and state government employees in India has emerged as a major area of concern, and is reflected by the following facts:

- (i) The central Government's pension liability has increased from 0.6% of the gross domestic product (GDP) in 1993–1994 to 1.66% in 2002–2003, with pensioners-to-employees' ratio at 0.85.
- (ii) For the state government, the annual average increase in pension expenditure in the period 1995–1996 to 2000–2001 was 27.1%.
- (iii) Of the revenue receipts of the states, 10% was preempted by pension expenditure.

3. The aggregate pension payments of state governments increased significantly from Rs31.31 billion in 1990–1991 to Rs78.13 billion in 1995–1996 and further to Rs281.97 billion in 2001–2002. The ratio of states' pension payments to their revenue expenditure had grown from 4.4% in 1990–1991 to around 9% by 2001–2002. Similarly, the share of state pension payments to their revenue receipts witnessed a sharp rise from 4.7% (Supplementary Appendix 1).

4. As per the Report of the Group to Study the Pension Liabilities of the State Governments, October 2003, the steep increase in states' pension outgo is mainly due to the significant expansion in the number of state government employees during the earlier decades; extension of pension facilities to employees of various non-Government institutions (grant-in-aid institutions, local bodies, etc.); impact of various pay revisions; implementation of the central Government's decision on recommendations of fifth central pay commission by the states (with or without any modifications); periodic dearness allowance increases; and significant improvement in life expectancy.<sup>2</sup>

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<sup>1</sup> The TA first appeared in *ADB Business Opportunities* (Internet edition) on 27 September 2004.

<sup>2</sup> Source: Report of the Group to Study the Pension Liabilities of the State Governments, October 2003. B. K. Bhattacharya, Chief Secretary (Retd.), government of Karnataka, chaired the Group.

5. A major policy initiative in the direction of civil service pension reforms at the center is the Government's decision of 23 August 2003 to replace the existing, unfunded defined benefit (DB) pension scheme with a fully funded defined contribution (DC) scheme for new entrants to central Government service that will exclude the armed forces. The scheme envisages three funds, i.e., safe income, balanced, and growth with safe income as a default option. The new system will also be available on a voluntary basis to all persons including self-employed professionals and others in the organized sectors. The Government is also considering possible options for devising voluntary privately managed pension schemes that could be offered to all eligible participants from the unorganized, or informal, sector of the Indian economy.<sup>3</sup> DEA is currently engaged in establishing the legislative, regulatory, and institutional framework for the new pension system (NPS), and the bill for legislating the Pension Fund Regulatory and Development Authority (PFRDA) is likely to be introduced in the coming winter session of Parliament.

6. In parallel, the growing pension liabilities of various state governments have been clamoring for increased attention, particularly from the policy makers, because of the fiscal deterioration of state finances. The road map for future pension reforms was laid down in the report of the High-Level Committees on Pension Reforms, one constituted by MOF and the other by Reserve Bank of India (RBI). Both committees recommended changing from a DB scheme to a DC scheme. The RBI Committee, which deliberated at length on the pension liabilities of the states, indicated that pension payments would preempt 30% of the states' own revenues and 20% of their total receipts by 2010–2011. It recommended three alternatives for structural change, including the introduction of a new scheme based on DC at the state level.

7. Almost all states are increasingly concerned about the sustainability of their existing pension schemes and their fiscal implications, and are inclined to introduce reforms. In principle, the options in front of the states are to (i) offer NPS to their new employees, and (ii) consider for its existing employees a variety of systematic and parametric reforms that could be either voluntary or mandatory. A number of states are in favor of introducing a contributory pension scheme for newly recruited employees. Several state governments have voluntarily decided to adopt the NPS for their own new employees. These include Tamil Nadu (April 2003), Himachal Pradesh (May 2003), Rajasthan (January 2004), and Andhra Pradesh (September 2004). Several others have announced their intent to move in this direction. These include Assam, Goa, Karnataka, Kerala, Maharashtra, and Punjab. It is clear that the momentum already exists. Many other states are expected to follow suit.

8. Almost all state governments lack proper arrangements to collect and monitor data relating to pensioners. To accurately quantify the financial impact (expenditure and/or savings) from the reforms, the state governments will require good-quality demographic, income, and employment data on their existing employees. Correct estimates would require an age profile of both in-service employees and pensioners, distribution of pensioners over service categories, distribution based on last pay drawn, and regular revision of data to reflect changes on account of death. These problems can be addressed with professional advice from actuaries and information technology experts. It is, therefore, important that state governments put in place appropriate mechanisms to strengthen their existing database on employees and pensioners and periodically update and verify such data. This data will also be necessary to accurately calculate the cost of government inaction on pension reform (in the form of pension liabilities and expenditure) over multiple decades. In addition to data collation and liability assessment, it will be essential to build capacity and knowledge on pension system design, and policy alternatives on reform and implementation issues among senior policy makers in each state.

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<sup>3</sup> ADB. 2003. *Technical Assistance to India for the Unorganized Sector*. Manila (TA 4226-IND, for \$1,000,000).

### **III. THE TECHNICAL ASSISTANCE**

#### **A. Purpose and Output**

9. The TA will assist selected state governments in India in the measurement and reform of their civil service pensions. The core steps in achieving pension reforms for state governments will include (i) estimating liability, (ii) deciding on the reform option to implement, (iii) setting up the requisite systems and procedures relating to the proposed pension system, and (iv) developing capacity and education for implementing the reform proposals. The TA will help the selected states (i) compile information on the full set of employee benefits offered by the government along with related expenditure and income information on the state in a standardized format; (ii) collate accurate demographic, income and other relevant information and data on existing state government employees, pensioners, and dependents, and establishing responsibilities, procedures and processes for regularly capturing and compiling such data in a standard format; (iii) build a liability estimation tool kit for analyzing the fiscal and financial impact of a variety of reform proposals for each selected state; (iv) produce suitable parametric and/or systemic reform proposals and evaluate the merits, implementation processes, and fiscal impact of parametric and/or systemic changes to retirement benefits for various categories of existing employees and pensioners; (v) conduct a sample survey to assess the attitudes of existing government employees and pensioners toward alternative pension benefit structures; (vi) the selected state governments build suitable capacity and processes to harness existing reform initiatives announced under the NPS for new entrants to central Government service; and (vii) evaluate the merits, processes, and financial impact of outsourcing of services and transferring the risks and liabilities (payout of benefits, etc.) of government pension payments so as to reduce administrative costs and risks.

#### **B. Methodology and Key Activities**

10. The TA will therefore be broadly divided into the following three components: (i) data gathering, development of liability assessment tools, and liability assessment; (ii) policy proposals for consideration by each state government; and (iii) coordination between the various ministries and departments in each state, and also between the states and the central Government; and capacity-building efforts for implementing the reform. To have maximum impact, the Government proposes to initially cover about 10–12 states. The Government proposes to allocate those states that are ready between the World Bank and ADB. In addition to its focal states of Andhra Pradesh, Maharashtra, Rajasthan, and Uttar Pradesh, the World Bank has also been allotted the states of Gujarat and Himachal Pradesh. ADB is likely to be allotted the states of Assam, Kerala, Madhya Pradesh (3 of its focal states), Bihar, Goa, and Orissa. The World Bank proposes to use its tool kit called Pension Reform Options Simulation and Toolkit (PROST). PROST is expected to help arrive at correct estimates of pension liabilities over the long run, as forecasting facilitates the formation of alternative solutions. The ADB TA will also examine the feasibility of using alternate models for liability estimation or have a suitable liability estimation tool developed under the TA. However, it will be ensured that a standardized approach is followed for data compilation in all the selected states.

11. For capacity building and project coordination, it is proposed that there be a focal coordination unit at the Executing Agency (EA) at the center, with the necessary project management capacity. In addition, the TA will provide local counterpart arrangements with the relevant state governments to coordinate locally the database and capacity-building activities with the relevant officials of each state government. The EA will closely liaise with the state governments and ADB on a variety of tasks. Details of related activities are in Appendix 1 items

(xii) to (xviii). The reports and research generated in the study will become an input for overall pension reforms and will be the backbone for the final recommendations from this initiative.

12. For each selected state, a broad capacity-building exercise on pension reforms will be undertaken. The exercise will target key officials at each state and will facilitate an understanding of the global and domestic experience with civil service pension reform; the core concepts and principles of pension system design and implementation; clarity on policy options before the relevant governments and government departments; a detailed insight into the existing reform initiatives in India (e.g., the NPS) and the road map through which states can harness these reform initiatives; and specific, immediate actions that the states should undertake.

13. The TA will also assist in setting up a secure web site for the project—all research, data inputs, and related information on the project would be hosted on this web site for access by the TA project team, the EA, selected states, and ADB. The study will become a nucleus for existing expertise in this area and will assist in building sustained capacity by affiliating and collaborating with a number of agencies and individuals across the states, as well as global pension experts and in channeling their knowledge and experience into implementation of the efforts under this project.

15. A 1-week study tour will be prepared for 12–15 officials from the selected state governments and the MOF to visit and discuss with organizations in more developed economies experience with reforming and managing civil service pensions, and the requirements for successfully managing service agreements with private sector service providers.

### **C. Cost and Financing**

16. The total cost of the TA is estimated at \$1,000,000 equivalent of which \$445,000 will be in foreign currency, and \$555,000 equivalent in local currency. ADB will finance \$750,000 equivalent, which includes the entire foreign currency costs and \$305,000 equivalent of local currency costs. The remaining \$250,000 equivalent will be contributed by the Government and will cover office accommodation, counterpart staff remuneration, and other logistical support. The TA will be financed on a grant basis from the Japan Special Fund, funded by the Government of Japan. The detailed cost estimates and financing plan are in Appendix 2.

### **D. Implementation Arrangements**

17. MOF's DEA (Capital Markets Division) will be the EA for the TA and will provide necessary office space, counterpart support, and other services to the consultants. Each co-opted state will be the Implementing Agency for the TA. The international consultants will associate with a local professional consulting firm with experts having the required experience in pension policy and system design, reform, and implementation. In coordination with the international consulting firm, the local firm will also be actively involved in overall local project management including (i) coordinating of the various tasks and deliverables under the TA within each state, between the relevant states, as well as between the states and the central Government; (ii) assisting each state in adopting of the NPS; and (iii) building broad-based capacity and a policy consensus within each state. The TA will also engage a local specialized, professional agency to be subcontracted by the principal consulting firm for the task of data collection and assessment and with a network of data specialists, statisticians, and social sector research experts that will be engaged. Data gathering and processing are expected to be completed within 9–12 months. International consultants (11 person-months total) will comprise a pension policy and system expert (team leader), an actuary, and an information and

technology expert. Domestic consultants (15 person-months total) will comprise a pension policy and system expert, an actuary, an information and technology expert, a financial expert, and a legal/regulatory expert. The international consulting firm will be recruited, using simplified technical proposals under the quality- and cost-based selection method, in accordance with ADB's *Guidelines on the Use of Consultants* and other arrangements satisfactory to ADB. The terms of reference for the consultants are in Appendix 4.

18. The consulting firm will submit to the EA and ADB a work plan for the TA within 2 weeks of the start of its services in the field. The work plan will include the planned activities, methodologies, and output of the TA. The start of services will allow for a proper interface with the local data firm before finalization of the data-gathering exercise and related report. The consulting firm will submit an inception report within 4 weeks of the start of its services in the field. After securing agreement, the local data firm will assist the selected states to gather data (by defining standard data formats), conduct training for the relevant state government staff, efficiently collate and process the data, and make it available to the pension reform team for analysis. At the end of 4 months, the data firm will submit a preliminary report of its findings for the data-gathering exercise to the EA, the international and domestic consulting firms, and ADB. Any adjustments or additional information and data and clarifications that may be required will be communicated at this point to the data firm. On completion of the data collection and processing and related tasks, and 2 weeks before the termination of services of the data firm, a workshop will be held with various stakeholders and representatives from the EA, selected states, the consulting firm, and ADB to present the findings of data gathering for the actuarial experts to conduct specific research and an impact measurement exercise, which will be an input in the final recommendations. The consulting firm in parallel will (i) develop the liability estimation tool kit, (ii) assist the states to evaluate and implement suitable processes and policies for adopting the NPS, and (iii) educate and prepare the state for pension reforms. The processed data once available will be analyzed and researched by the consulting firm as mentioned above. The capacity-building exercise (paras. 12 and 13) will also be simultaneously undertaken.

19. Two interim reports will be submitted: at the end of month 6 and month 12, respectively. The study tour (para. 15) will be undertaken after the submission of the second interim report. The findings of the study tour will form part of the draft final report. A workshop for representatives from the EA, the selected state governments, other stakeholders, PFRDA, and ADB will be held to discuss the outputs of the local data firm and the liability estimation tool to be used for impact measurement. In coordination with the EA, an NPS manual will be developed to serve as a reference for the states on the specific steps to be undertaken by each state once it decides to introduce the NPS. A draft final report will be submitted to form the basis for discussions in a tripartite meeting among the EA, the consulting firm, and ADB, to be held 2 weeks before the finalization of the report. The meeting will consider the results of the actuarial studies and the implementation plan of the pension program. The TA is planned to start by end-March 2005 and be completed by September 2006.

#### **IV. THE PRESIDENT'S DECISION**

20. The President, acting under the authority delegated by the Board, has approved the provision of technical assistance not exceeding the equivalent of \$750,000 on a grant basis to the Government of India for State-Level Pension Reforms, and hereby reports this action to the Board.

## TECHNICAL ASSISTANCE FRAMEWORK

<b>Design Summary</b>	<b>Performance Indicators/Targets</b>	<b>Monitoring Mechanisms</b>	<b>Assumptions and Risks</b>
<p><b>Goal</b></p> <p>Improved fiscal management and the development of the domestic capital market to enhance economic growth leading to poverty reduction</p> <p>Provide social protection and promote old age security in a sustainable manner</p>	<p>Number of pensioners and value of pensions</p> <p>State governments fiscal burden reduced</p> <p>Private pension funds and contractual savings institutions promoted</p>	<p>Consultants' reports</p> <p>Government reports and policy dialogue</p> <p>Asian Development Bank (ADB) review missions</p>	
<p><b>Purpose</b></p> <p>To assist selected state governments in India in the measurement and reform of its civil service pensions</p>	<p>Time-bound reform program for civil service pensions</p>	<p>Consultants' reports</p> <p>Policy dialogue</p> <p>ADB review missions</p>	<p><b>Assumptions:</b></p> <p>Macroeconomic stability</p> <p>State government commitment to pension reforms</p> <p>Cooperation of stakeholders</p>
<p><b>Output</b></p> <p>An agenda for policy and institutional reforms</p> <p>Estimation of liability and capacity development and education in selected states facilitated</p> <p>Increased capacity for poverty reduction through reduced fiscal burden for pension servicing liability</p>	<p>Capacity developed for (i) collating accurate demographic and income data and information, and establishing responsibilities, procedures, and processes for regularly capturing and compiling such data in a standard format in the future; and (ii) compiling information on the full set of employee benefits offered by the government along with related expenditures in a standardized format</p> <p>Liability estimation tool developed and calibrated for modeling of pension reform options and estimation of pension liabilities and transition costs</p> <p>System reforms options developed, including recommendations to minimize fiscal costs</p> <p>Action plan to strengthen the system of pension administration developed</p>	<p>Consultants' reports</p> <p>Stakeholder consultations</p> <p>ADB review missions</p>	<p><b>Assumptions:</b></p> <p>Adequacy and accuracy of data, quality of actuarial support provided by the consultants</p> <p>Success of workshops in disseminating results</p> <p>Interest of stakeholders</p> <p><b>Risk:</b></p> <p>Institutional capacity within selected state governments</p>

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<b>Design Summary</b>	<b>Performance Indicators/Targets</b>	<b>Monitoring Mechanisms</b>	<b>Assumptions and Risks</b>
	<p>Workshop to disseminate technical assistance (TA) results</p> <p>Road map through which each state government can harness existing reform initiatives announced under the New Pension System (NPS) for new entrants to central Government service developed</p>		<p><b>Risk:</b> Failure to reach consensus on recommendations</p>
<p><b>Activities</b> Assist selected state governments in preparing and conducting data gathering and ensuring adequate coverage of the survey to arrive at workable proposals for the design of the state civil service pension reforms.</p> <p>Follow a standardized approach among the selected states for data gathering and compilation so that the data collected on employees, pensioners and dependents is in a usable form.</p> <p>Based on the compiled data, develop suitable liability assessment model and tools.</p> <p>Analyze the financial impact of a variety of reforms as well as of inaction.</p> <p>Actively coordinate with each state government, and also with the Executing Agency, including the Department of Economic Affairs and Expenditure, to build sustainable capacity and a broad-based policy consensus on state government pension reforms.</p>			

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<b>Design Summary</b>	<b>Performance Indicators/Targets</b>	<b>Monitoring Mechanisms</b>	<b>Assumptions and Risks</b>
<p>Recommend suitable strategies for creating awareness of NPS among state government employees.</p> <p>Propose a master plan with a medium-term operational strategy and a proper organizational structure to implement the pension reform plans.</p> <p>Prepare an operation manual on how to conduct on-the-job training. Detail the transition phase (sequence) from the pay-as-you-go system to a largely defined contribution system, and fiscal implications of pension reform (transition from unfunded to partly or fully funded system), and specify possible funding for transition costs.</p> <p>Help develop a road map for implementing the pension reforms.</p> <p>Train the state government officials through seminars and workshops on pension operations.</p> <p>Identify capacity-building requirements within the states to effectively manage proposed pension reforms, recommend suitable training programs for this purpose, and conduct a training workshop for key government staff.</p> <p>Specifically, the ADB TA will assist the EA to perform these activities:</p> <p>(i) Coordinate the process of</p>			

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<b>Design Summary</b>	<b>Performance Indicators/Targets</b>	<b>Monitoring Mechanisms</b>	<b>Assumptions and Risks</b>
<p>standardized data collection and assessment with the relevant central Government departments and the state governments.</p> <p>(ii) Coordinate and conduct periodic project reviews, as well as meetings and technical consultations between the officials of each state government as well as officials of the central Government departments.</p> <p>(iii) Collate and record all data and information produced under this study.</p> <p>(iv) Conduct consultations, conferences, seminars, training programs, and workshops for capacity building.</p> <p>(v) Create capacity, knowledge, and appropriate processes to enable states to efficiently adopt the proposed NPS architecture.</p> <p>(vi) Harmonize efforts on state pension reforms.</p> <p>(vii) Produce, publish, and circulate reports and recommendations and obtain policy inputs and opinions on the same.</p>			
<p><b>Inputs</b></p> <p>11 person-months of international consultants and 15 person-months of domestic consultants. In addition 9–12 months of services by the data gathering firm</p>	<p>Implementation of activities specified as outputs</p>	<p>Consultants' reports</p> <p>Consultation and dialogue with the executing and implementing agencies and consultants</p>	<p><b>Assumption:</b> Commitment and cooperation from state governments, the EA, stakeholders</p>

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<b>Design Summary</b>	<b>Performance Indicators/Targets</b>	<b>Monitoring Mechanisms</b>	<b>Assumptions and Risks</b>
<p>Data gathering</p> <p>International consulting firm</p> <p>Support from the Department of Economic Affairs and Department of Expenditure, Ministry of Finance (MOF), the state governments, and Pension Fund Regulatory and Development Authority (PFRDA)</p> <p>Workshops outcomes</p>	<p>Preliminary report submitted at the end of 4 months</p> <p>Draft final report of the survey results submitted 2 weeks before the completion of the survey assignment</p> <p>Presentation of inception report by international consulting firm within 4 weeks of the start of services</p> <p>Interim report submitted at the end of first 6 and 12 months</p> <p>Workshop held at the end of 12 months to discuss the findings of the data gathering firm, and before termination of the services of the international consulting firm, to discuss the recommended reforms</p> <p>Draft final report submitted for the tripartite meeting to be held 2 weeks before finalization of the report</p> <p>Final report submitted by September 2006</p>	<p>Progress reports</p>	

**COST ESTIMATES AND FINANCING PLAN**  
(\$'000)

Item	Foreign Exchange	Local Currency	Total Cost
<b>A. Asian Development Bank Financing<sup>a</sup></b>			
1. Consultants			
a. Remuneration			
i. International Consultants	225.0	0.0	225.0
ii. Domestic Consultants	0.0	90.0	90.0
b. Per Diem			
i. International Consultants	60.0	0.0	60.0
ii. Domestic Consultants	0.0	55.0	55.0
c. International and Local Travel	25.0	10.0	35.0
2. Data Gathering <sup>b</sup>	0.0	110.0	110.0
3. Study Tour	75.0	0.0	75.0
4. Workshops	0.0	10.0	10.0
5. Miscellaneous Administration and Support Costs	5.0	5.0	10.0
6. Contract Negotiations	5.0	0.0	5.0
7. Contingencies	50.0	25.0	75.0
<b>Subtotal (A)</b>	<b>445.0</b>	<b>305.0</b>	<b>750.0</b>
<b>B. Government Financing</b>			
1. Office Accommodation and Utilities	0.0	130.0	130.0
2. Remuneration of Counterpart Staff	0.0	40.0	40.0
3. Communication	0.0	35.0	35.0
4. Contingencies	0.0	45.0	45.0
<b>Subtotal (B)</b>	<b>0.0</b>	<b>250.0</b>	<b>250.0</b>
<b>Total</b>	<b>445.0</b>	<b>555.0</b>	<b>1,000.0</b>

<sup>a</sup> Financed by the Japan Special Fund, funded by the Government of Japan.

<sup>b</sup> Involves gathering demographic data on the existing employees and pensioners in a standardized form for all the pension-paying offices in all the six states. As none of the states have an existing system for gathering such data, this activity will involve not only gathering such data in coordination with different pension payment offices at each state but also developing the capacity within each state to maintain such data on a continuous basis.

Source: Asian Development Bank estimates.

## SUMMARY INITIAL POVERTY AND SOCIAL ANALYSIS

### A. Linkages to the Country Poverty Analysis

<b>Sector identified as a national priority in country poverty analysis? Yes</b>	<b>Sector identified as a national priority in country poverty partnership agreement? No</b>
<p><b>Contribution of the sector/subsector to reduce poverty in India:</b></p> <p>The technical assistance (TA) will assist selected state governments in India in the measurement and reform of their civil service pensions; help consider the feasibility of introducing necessary modifications in the existing pension schemes, and, in the process, suggest appropriate mechanisms to address the fiscal implications of the growing pension burden for the respective state governments. The TA will provide a reliable and cost-effective method of old age support. The pension reforms will reduce the fiscal burden of the states and will facilitate economic growth and efficiency in resource allocation. Important byproducts are increased flow of long-term institutional savings and the boost to the overall development of the financial market. As pension funds are longterm in nature, their bulk could be invested in infrastructure projects. The focus on infrastructure projects recognizes the contributions they make to sustainable economic growth, and in turn, the contribution that economic growth can make to poverty reduction. In India's case, a considerable number of potential contributors to the proposed pension arrangements are located in the formal sector. This fact would increase the rate of savings, which could lead to a higher rate of capital accumulation and economic growth, crucial for a developing country like India.</p>	

### B. Poverty Analysis

<p>The shift to a defined contribution pension scheme will (i) help prevent poverty among the elderly, (ii) improve overall labor market mobility, (iii) facilitate economic growth, (iv) deepen capital markets, and (v) lead to an increase in the national savings rate. It can create new opportunities for self-discipline in savings and can help increase investment in human capital and physical assets. It will improve the financial sustainability of the old age system and thus provide better protection for the old in the long run. These gains could generate higher economic growth rates, raising living standards for those not participating directly in the pension system.</p>
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### C. Participation Process

**Targeting Classification:** General Intervention

<p><b>Is there a stakeholder analysis?</b> <input checked="" type="checkbox"/> Yes <input type="checkbox"/> No</p> <p><b>Is there a participation strategy?</b> <input checked="" type="checkbox"/> Yes <input type="checkbox"/> No</p> <p>The TA will recommend suitable strategies for creating awareness of the new pension strategy among state government employees. The strategy will likely improve the returns on pension funds.</p>
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#### a. Gender Development

<p><b>Strategy to maximize impacts on women:</b></p> <p>The TA will assist in the reforms of the state government pensions covering all employees, including women. A number of aspects in pension reforms are extremely gender sensitive. An equal retirement age will enable men and women to build up the same pension entitlements. A</p>
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survivor's pension could reduce the vulnerability of the dependent spouse considerably. The introduction of credit periods for raising children and/or taking care of the elderly, responsibilities that are mainly taken up by women, could allow them to build up more complete pension entitlements. These possible pension reforms will effectively reduce the vulnerability of future pensioners and would, as such, be considered among the policy proposals. Consideration of these reform options requires gender-disaggregated figures to estimate possible future costs. The TA will consider policy reform for promoting gender equality and the collection of gender disaggregated figures.

Has an output been prepared?  Yes  No

**b. Social Safeguards and other Social Risks**

	<b>Significant/ Not significant/ None</b>	<b>Strategy to Address Issues</b>	<b>Plan Required</b>
Resettlement	<input type="checkbox"/> Significant <input type="checkbox"/> Not significant <input checked="" type="checkbox"/> None	No issues under the proposed pension scheme	<input type="checkbox"/> Full <input type="checkbox"/> Short <input checked="" type="checkbox"/> None
Indigenous Peoples	<input type="checkbox"/> Significant <input type="checkbox"/> Not significant <input checked="" type="checkbox"/> None	No issues under the proposed pension scheme	<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
Labor	<input type="checkbox"/> Significant <input type="checkbox"/> Not significant <input checked="" type="checkbox"/> None	Positive labor impact is expected.	<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
Affordability	<input type="checkbox"/> Significant <input type="checkbox"/> Not significant <input checked="" type="checkbox"/> None	Attitude and willingness to save will be covered in the proposed TA.	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No
Other Risks/ Vulnerabilities	<input type="checkbox"/> Significant <input type="checkbox"/> Not significant <input checked="" type="checkbox"/> None	No other adverse issues are anticipated.	<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No

## **OUTLINE TERMS OF REFERENCE FOR CONSULTANTS**

1. The technical assistance (TA) will assist selected state governments in India in the measurement and reform of their civil service pensions and other retirement benefit arrangements for their employees. The TA will include (i) estimation of liability, and (ii) capacity development and education for implementing the pension reform. The TA will be broadly divided into the following three components: (i) data gathering and development of liability estimation tools; (ii) policy proposals for consideration by each state government; and (iii) coordination between the various ministries and departments in each state, and between the states and the central Government, and capacity-building efforts for implementing the reform. The process of estimating liability will include (i) collecting data and building databases, (ii) building tools for estimating liability, and (iii) actuarial valuation based on mortality and other projections. The consulting team comprising a combination of an international and a domestic firm will include three international consultants (11 person-months total) and five domestic consultants (15 person-months total). The TA will also engage a local specialized, professional agency for collecting and processing data on employees and pensioners in each state. The international/domestic consultants will associate with the local firm to assist in data gathering, estimated to be completed in 9–12 months. The TA is expected to begin in March 2005 and be completed in September 2006.

### **A. International Consultants**

#### **1. Pension Policy and System Expert-Team Leader (5 person-months)**

2. The international consultant will be a pension policy and system expert and team leader (TL). As TL, the consultant will be responsible for the overall management of the TA and the timely delivery of outputs. The expert must have an extensive global experience with public/pensions policy issues, particularly, with the design, establishment, and management of civil service pension reforms, moving from a defined benefit (DB) pension scheme to a defined contribution (DC) pension scheme, from “pay-as-you-go” to funded pensions systems. Experience in both developed and developing economies in these respects will be highly desirable. The consultant will have the following responsibilities:

- (i) Oversee and supervise the preparation and conduct of the data-gathering exercise by the local firm and ensure adequate coverage of the survey to arrive at workable proposals for the design of the state civil service pension reforms.
- (ii) Oversee the collection of gender-disaggregated figures for policy reform proposals promoting gender equality.
- (iii) In coordination with the actuary, guide the data-gathering firm in designing and implementing the data-gathering exercise and other surveys required to establish a database for the pension computer model and for estimating future pension liabilities under different scenarios.
- (iv) Ensure that a standardized approach for data gathering and compilation is followed by the selected states and that the data collected on employees, pensioners, and dependents is in a usable form.
- (v) Help the actuary develop a suitable liability assessment model and tool.
- (vi) Work closely with the international and domestic actuary in analyzing the financial impact of a variety of reforms as well as of inactions.
- (vii) Work closely with each state government and also with the Executing Agency, including the Department of Economic Affairs and Department of Expenditure, to

- build sustainable capacity and a broad-based policy consensus on state government pension reforms.
- (viii) Recommend suitable strategies for creating awareness of the new pension strategy among the state government employees.
  - (ix) Propose a master plan with a medium-term operational strategy and a proper organizational structure to implement the pension reform plans.
  - (x) Prepare an operation manual on how to conduct on-the-job training. Detail the transition phase (sequence) from the pay-as-you-go system to a largely DC system and the fiscal implications of pension reform (transition from unfunded to partly or fully funded system); specify possible funding for transition costs.
  - (xi) Help develop a road map for implementing of the pension reforms.
  - (xii) Train the state government officials on pension operations through seminars and workshops.
  - (xiii) Identify capacity-building requirements within the states to effectively manage proposed pension reforms, recommend suitable training programs for this purpose, and conduct a training workshop for key government staff.
  - (xiv) Organize a suitable study tour for key officials of the selected state governments and the Ministry of Finance (MOF) to provide exposure to best practice models in the reform and management of civil service pension schemes.

**2. Professional Actuarial Model Development Specialist (3 person-months)**

3. The expert must have experience in building liability estimation models and pension liability forecasting for DB pension systems. The consultant will have the following responsibilities:

- (i) Review and assess the validity of the information used for the existing pension cash flow model related to the pension fund, and economic and demographic data. Identify data needs for the liability estimation models and assist the data gathering firm in extracting relevant data through sampling or other appropriate methods.
- (ii) Carry out necessary updating of the database if existing data is not sufficient. Create a dynamic actuarial model for liability estimation to simulate and project the outcomes of various scenarios, based on actuarial parameters such as demographics (population data, mortality rates, long-term disability rates, and fertility rates), economic assumptions (income distribution, inflation, real wage growth, interest rates, and administration), and pension plan benefits (retirement benefits, disability benefits, surviving children benefits, spouse benefits, and children benefits). Ensure that the outcomes from the model include projected figures of pension contribution, pension payment, and pension liabilities.
- (iii) Ensure that the outcomes from the model are projected figures of pension contribution, pension payment, and pension liabilities. The model should also produce management information system reports including past and future liabilities, fund reserves, fund ratios (assets/liabilities), current account balance, and implicit and explicit pension debts. The outputs should be convertible to be illustrated in graphs and other formats.
- (iv) Conduct on-the-job training to staff of selected state governments in building up the necessary database, pension cash flow modeling, and measurements for keeping the outcomes from the model continuously updated.

- (v) In coordination with the TL and the relevant Government officials, develop and model the fiscal implications of alternative transition paths to fuller funding of the state pension system.

**3. Information and Technology Expert (3 person-months)**

4. The consultant should have satisfactory experience in building information technology (IT)-based analytical tools/models, databases, and IT-based processes and payroll systems. The consultant will have the following responsibilities:

- (i) Evaluate the system of pension administration in each selected state, including its organizational structure, financial management system, and supporting electronic database with a view to determining its capacity to meet its objectives.
- (ii) Evaluate the changes in payroll processes and administrative procedures required for capturing information both for adoption of the new pension system as well as parametric changes in the existing pension schemes and for collecting and transferring pension contributions.
- (iii) Assist in ensuring that the payroll processes are made compatible with the Central Record Agency (being established for the DC pension system).
- (iv) Help identify the required software for implementing (ii) and (iii).
- (v) Assist in installing databases and the software required for operating their accounts and reporting system.
- (vi) Identify the IT-related organizational capacity required for carrying out the proposed changes in the pension system.
- (vii) Assist the TL and the actuary in carrying out all their IT-related tasks.
- (viii) Help develop a secure web site for the project—all research, data inputs, and related information on the project would be hosted there. The study will become a nucleus for existing expertise in this area by affiliating and collaborating with a number of agencies and individuals and channeling their knowledge and experience into implementation of the efforts under this project.

**B. Domestic Consultants**

**1. Pension Policy and Strategy Expert (5 person-months)**

5. The domestic consultant must have broad experience with public/pensions policy issues and should have a good knowledge of existing pension arrangements in Indian state governments. The consultant will assist the TL in all his tasks under the TA and for timely delivery of TA outputs. The consultant will have the following responsibilities:

- (i) Provide the international consultant with strategic information on existing state-level pension arrangements.
- (ii) Assist the TL in evaluating the results of the data survey.
- (iii) Assist the international consultant with preparing an implementation plan for the new pension system as well with making parametric changes under the existing pension scheme(s).
- (iv) Assist the TL in carrying out activities detailed in para. 2 above.
- (v) Arrange meetings and help conduct discussions with relevant persons and organizations.
- (vi) Assist the TL in organizing stakeholder meetings to disseminate the findings of the survey and agree on strategies.

## **2. Legal Expert (2 person-months)**

6. The legal consultant must be familiar with legal issues related to postretirement schemes, particularly pension and provident funds. The consultant will assist the TL in all the TL's tasks under the TA. The consultant will also assist the TL for timely delivery of TA outputs. The consultant will have the following responsibilities:

- (i) Collect and evaluate all legislations, including government and ministerial decrees affecting the regulation and operation of the state pension system.
- (ii) Assist the TL in designing pension schemes that conform with the requirements of states laws, rules, and regulations.
- (iii) Identify and recommend any changes in state laws, rules, and regulations that will be required for implementing the new pension arrangements in each selected state.
- (iv) Assist the states to build appropriate governance mechanisms based on the new pension arrangements in each selected state.
- (v) Assist the states in putting in place the required reporting and compliance systems for supervising the new pension arrangements.
- (vi) Arrange meetings and help conduct discussions with relevant persons and organizations.

## **3. Information and Technology Expert (3 person-months)**

7. The expert should have extensive experience in building IT-based analytical tools/models, databases, and IT-based processes and payroll systems. The expert will assist the international IT expert in carrying out all the latter's tasks under the TA.

## **4. Professional Actuarial Model Development Specialist (3 person-months)**

8. The domestic actuarial expert must have experience in liability estimation models and pension liability forecasting for DB pension systems. The consultant will have the following responsibilities:

- (i) In coordination with the international actuarial expert, provide technical and actuarial inputs to the international/domestic IT experts in developing the policy tool kit for liability estimation.
- (ii) Provide relevant local data (mortality, population, long-term disability rates, fertility rates, income distribution, inflation, wage growth, interest rates, retirement benefits, disability benefits, surviving children benefits, spouse benefits, etc.) to the international actuarial expert.
- (iii) Assist the local data firm in developing the necessary formats for data collection and verify the data quality.

## **5. Financial Sector Expert (2 person-months)**

9. The expert must be familiar with financial and fiscal issues related to postretirement schemes, particularly pension and provident funds. The expert will work closely with the policy team in evaluating the fiscal/financial impact of any reform proposals and assist the states in designing models to finance any transitional costs of reforms.

### **C. Domestic Firm for Data Gathering**

10. The local firm must have the required network for the survey, together with data specialists, statisticians, and social sector research experts, who are qualified, both academically and in terms of experience, in collecting and analyzing of quantitative and qualitative labor market and income distribution data. The task is expected to be completed in 12 months. The specific tasks of the local firm are as follows:

- (i) On the basis of contemporary methodologies, develop a standardized format for data gathering among the states selected for pension planning and management purposes.
- (ii) Ensure that the data-gathering exercise is focused on collection and compilation of good quality demographic, income and employment data on the states' existing employees.
- (iii) Assist the selected states to implement the data-gathering exercise and other surveys required to establish a database for the pension computer model and for estimating the future pension liabilities under different scenarios.
- (iv) Train the relevant officials in each state government to create a full database of their employees and pensioners in a standardized format. While making this database for the first time, it would be desirable to simultaneously set up ongoing mechanisms through which the databases would be maintained, to facilitate and ease the process of producing annual, updated liability assessments.
- (v) Help establish responsibilities, procedures, and processes for regularly capturing and compiling such data in a standard format in the future.
- (vi) Present the results of the analysis to a workshop of key stakeholders from the state government, the EA, and the Pension Fund Regulatory and Development Authority.