INSURANCE INDUSTRY IN INDIA AND RELATED REFORMS

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INSURANCE

Introduction

Insurance is a contract whereby the insurer undertakes to compensate the insured for any loss suffered by the later in consideration of premium paid for certain period. There are different insurance companies such as LIC, GIC, United India, New India assurance etc., offering wide range of insurance options. They provide comprehensive coverage with affordable premium. An insured can choose the policy according to his needs and ability to pay periodical premium to cover the risk of insurance for the stipulated period. The periodical insurance premiums are calculated according to the total insurance amount specified or estimated value of the property/things insured.Thus, Insurance provides financial protection against a loss arising out of happening of an uncertain event. Hence, insurance is used as an effective tool for risk management.

Definition

Insurance is a contract between two parties, whereby one party agrees to undertake the risk of another, in exchange for consideration known as premium and promises to pay a fixed sum of money to the other party on happening of an uncertain event (death) or after the expiry of a certain period/maturity period in case of life insurance or to indemnify the loss to the other party on happening of an uncertain event in case of general insurance. The party bearing the risk is known as the 'insurer' or 'assurer' and the party whose risk is covered is known as the 'insured' or 'assured'.
Types of Insurance

Various types of insurances are as mentioned hereunder:

Life insurance: Descendant's family receives insured amount in the case of death of the insured.

In other case the insured himself gets the insured amount Automobile/Motor insurance:
Usually automobile insurances cover damages to the automobile and legal financial expenditure of the automobile driver/cleaner.

Workmen Compensation Insurance: It covers the employee for the loss of life or total/partial permanent disablement (loss of limb) or for occupational disease arising out of his employment during and in the course of his employment.

Health insurance: Health insurance covers the expenditure associated with treatment and medical expenditure including medicine.

Credit insurance: Borrowers often fail to repay the debts, loans and mortgages, due to certain unavoidable circumstances. Credit insurance can be of great help to the lenders during such crisis.

Property insurance: Property protection insurance provides protection from risks associated to theft, fire, floods etc.

This type of insurance can be further classified into specialized forms as follows: -

- Fire insurance
- Earthquake insurance
- Flood insurance
- Home insurance
- Boiler insurance

At present insurance market is much vibrant than before and this has an impact on the rates of insurance

premium.
Types of Insurance Companies
Insurance companies can be categorized into two main divisions which are classified asfollows:

General Insurance Companies: They provide all types of insurance apart from life insurance i.e., fire insurance, marine insurance, vehicle insurance etc.,
Life Insurance Companies: The companies, dealing with life insurance, pension products and annuities are life insurance companies.

Types of Insurance Policies

Insurance provides compensation to a person for an anticipated loss to his life, business or an asset. Insurance is broadly classified into two parts covering different types of risks:

Life Insurance (Long-term)
General Insurance (Non-life Insurance)
Life Insurance
"A contract in which the insurer undertakes to a pay a certain sum of money to the insured, either on the expiry of a specified period, or on the death of the insured, in consideration of payment of 'premium' for a certain period of time, is known as 'life insurance".

It is otherwise called as 'Life Assurance'. Generally, the tenure of Life insurance policy is long-term in nature; it may either be for a certain period or whole life period of the insured. Insurance against risk to one's life is covered under ordinary life assurance. Ordinary life assurance can be further classified into several types:

Types of Ordinary Life Assurance:

Whole Life Assurance
In whole life assurance, insurance company collects premium from the insured for whole life or till the time of his retirement and pays claim to the family of the insured only after his death.

Endowment Assurance

In case of endowment assurance, the term of policy is defined for a specified period say about 15, 20, 25 or 30 years. The insurance company pays the claim to the family of the assured in the event of his death, within the policy's period or in an event of the assured surviving the policy's period. In the event of the insured surviving beyond the coverage/specified period, the maturity value/sum assured along with bonus will be paid to the insured himself.

Assurances for Children

Child's Deferred Assurance

Under this policy, the insurance company pays the claim to the insured on the maturity date of the policy, which is calculated to coincide either with the date of child's eighteenth or twenty first birthday or attaining majority. The policy holder may either claim the payment on the date of maturity period or continue the insurance coverage. If the parent dies before the option date, the policy remains continued until the option date without paying premium for the remaining period. Suppose, the child dies before the option date, the parent gets back the premium plus bonus.

School fee policy

School fee policy can be availed by affecting an endowment policy on the life of the parent with the sum

assured, payable in installments over the schooling period of their children.

Term Assurance

Term assurance is life insurance which provides coverage at a fixed rate of payments for a limited period of time in respect of the term offered by the assured. In case, the insured dies during the term, the death benefit will be paid to the beneficiary. If the insured survives after that period expires, either he has to pay additional premium for obtaining further coverage or he has to forgo coverage. It is the least expensive way to purchase a substantial death benefit on a coverage amount over a specific period of time.

Annuities

Annuity is a contract under which the insurer (insurance company) promises to pay the insured a series of payments until the insured's death. The insured make the premium payment in the mode of either lump sum or installments to the insurer. Generally, life annuity is chosen by a person having surplus wealth and wants to use this money after his retirement.

The annuities can be further classified into two types, which are as follows: -

Immediate Annuity: It means that the insured pays a lump sum amount (purchase price) to the insurer and in turn the insurer promises to pay him a specified sum on a monthly/quarterly/half- yearly/yearly basis.

Deferred Annuity: A deferred annuity can be purchased either by way of installments or by paying a single premium. The insured receives the annuity after the deferment period.

Money Back Policy

A money back policy is issued for a particular period, and the sum assured is paid through periodical payments to the insured, spread over this time period. In case of death of the insured within the term of the policy, full sum assured along with bonus accruing on it, is payable by the insurance company to the nominee of the deceased. Generally, Money back policy is preferred by the person, who requires periodical receipts.

General Insurance

General insurance is also known as non-life insurance. It is normally meant for a short-term period of twelve months or less. In recent years, insurance companies are entering the long-term insurance agreements also and the period would not exceed five years. General insurance can be classified into the following categories:

Fire Insurance

Fire insurance provides protection against damage to property caused by accidents due to fire, lightening or explosion. Fire insurance also includes damage caused due to other perils like storm, tempest or flood, burst of pipes, earthquake, riot, civil commotion, malicious damage, explosion, impact (e.g. - aircraft).

Marine Insurance

Hull, cargo and freight are the three basic risk covering area for Marine insurance. Those risks areas are exposed to are collectively known as "Perils of the Sea". These perils include theft, fire, collision etc.

Marine Cargo: Marine cargo policy provides protection to the goods loaded in a ship against all perils

between the departure and arrival to warehouse. Therefore, marine cargo covers carriage of goods by sea as well as transportation of goods by land.

Marine Hull: Marine hull policy provides protection against damage to ship caused due to the perils of the sea. In the event of any loss sustained due to collisions at sea, Marine hull policy covers only 3/4th liability of the hull owner (ship-owner) and the remaining 1/4th of the liability is looked after by associations formed by ship owners for the purpose.

Miscellaneous

Miscellaneous insurance covers all types of general insurance, except the fire and marine insurances. Some of the examples of general insurance are motor insurance, theft insurance, health insurance, personal accident insurance, money insurance, engineering insurance etc.

INSURANCE INDUSTRY IN INDIA

- India has a deep-rooted history in the field of Insurance. In fact, the principles of insurance finds place, even in Manu (Manusmrithi), Yagnavalkya (Dharmasastra) and Kautilya (Arthasastra). Those writings talk in terms of pooling of resources that could be re-distributed in times of calamities such as fire, floods, epidemics and famine. This was probably a pioneer to modern day insurance. Ancient Indian history has preserved the earliest traces of insurance in the form of marine trade loans and carriers' contracts.
- In 1818, the Oriental Life Insurance Company was established in Kolkata. It failed in the year 1834 due to the business of the Madras Equitable life insurance which was started in Madras from the year 1829. The Triton Insurance Company Ltd was formed in 1850 and it was the first general insurance sector in India. The British Insurance Act was enacted in 1870. The Bombay Mutual (1871), Oriental (1874) and Empire of India (1897) insurance companies were started. In 1907, Indian Mercantile Insurance Limited was started, which was the first company to handle all forms of Indian insurance.

- A new era began in the Indian insurance sector, by passing of the Life Insurance Act, 1912. The Indian Insurance Companies Act was passed in 1928. This Act empowered the Government of India to gather necessary information about the life insurance and non-life insurance organizations operating in the Indian financial markets. This Act was amended in 1938 with comprehensive provisions for effective control over the activities of insurers to protecting the interest of public. The Principal Agencies system was abolished in the Amendment Act of 1950. On 19th January, 1956 an ordinance was passed for nationalizing the Life Insurance Sector and the Life Insurance Corporation came into existence.

- In 1972, with the passing of the General Insurance Business (Nationalization) Act, general insurance business was nationalized with effect from 1st January, 1973. 107 insurers were amalgamated and grouped into four companies, namely National Insurance Company Ltd., the New India Assurance Company Ltd., the Oriental Insurance Company Ltd and the United India Insurance Company Ltd. The General Insurance Corporation of India was incorporated as a company in 1971 and it commenced business on January 1st 1973.

REFORMS IN INDIAN INSURANCE SECTOR

- In 1993, the Government set up a committee under the chairmanship of RN Malhotra, former Governor of RBI, to propose recommendations for reforms in the insurance sector. The objective was to complement the reforms initiated in the financial sector. Following the recommendations of the Malhotra Committee Report, in the year 1999, the Insurance Regulatory and Development Authority (IRDA) was constituted as an autonomous body to regulate and develop the insurance industry.

- The IRDA was incorporated as a statutory body in April, 2000. The key objectives of the IRDA

include promotion of competition so as to enhance customer satisfaction through increased consumer choice and lower premium, ensuring the financial security of the insurance market, to safeguard the interests of insurance policy holders and to initiate different policy measures to help sustain growth in the Indian insurance sector.

- IRDA has notified 27 Regulations on various issues such as Registration of Insurers, Regulation on insurance agents, Solvency Margin, Re-insurance, Obligation of Insurers to Rural and Social sector, Investment and Accounting Procedure, Protection of policy holders' interest etc. IRDA brought out guidelines on Initial Public Offers (IPOs).

- At present, the number of Insurance companies operating in India is 24 General insurance companies and 23 Life insurance companies. The growth rate of insurance sector is enormously increasing day-by-day. The contribution of Insurance services sector in the country's GDP is 7%. Insurance sector is strengthening the risk taking ability of the country and promoting for economic development by providing long- term funds for infrastructure development.

CREDIT CARDS

Credit Cards Origin

Credit is a method of selling goods or services without the buyer having cash in hand. The concept of the credit card is "buy now, pay later" and it is a way of offering credit to a consumer. Credit card carries an identifying number that speeds shopping transactions. According to Encyclopedia Britannica, "the use of credit cards originated in the United States during the 1920s, when individual firms, such as oil companies and hotel chains, began issuing them to customers." In olden days, Credit cards were issued by merchants to their customers on credit sales. These cards were accepted only by the issuer himself not by any other person and the seller would not accept the others' card. Around 1938, companies started to accept each other's cards. Today, credit cards allow making purchases with countless third parties.

The Shape of Credit Cards

Long ago, credit cards were made from metal coins, metal plates, celluloid, metal, fiber, and paper. Now-a-days, credit cards are mostly made of plastic.

First Bank Credit Card

The Flatbush National Bank of Brooklyn, New York was the first bank started issuing credit cards in 1946. The card was invented by John Biggins in the program namely "Charge-It" conducted between bank customers and local merchants. Merchants deposited sales slips into the bank and the bank billed the customer who used the card.

Diners Club Credit Card

In 1950, the Diners Club issued their credit card in the United States. Diners' Club founder Frank McNamara invented the Diners Clubcredit card and introduced to his customers intended to pay restaurant bills. The card holder of diners club could eat without money at any restaurant which would collect money from Diners' Club. Diners' Club would settle the restaurants' bill first and later they collect the bill amount along with some charges from the customer (card holder). So, the Diners Club card was called as charge card. In 1958, the first credit card was issued by American Express. Later bank of America also issued America bank credit card which is popularly known as Visa card.

The Popularity of Credit Cards

During 1960s, more companies offered credit cards, advertising them as a time-saving device rather than

a form of credit. American Express and Master Card became popular overnight.

Standard Credit Cards

Standard credit cards are otherwise called as "plain-vanilla" credit cards which offer no additions or rewards. This is a common kind of credit cards which allows the card holder to have a revolving balance up to a certain credit limit. Card holders can use the card according to his needs and they have to settle their account before the due date. If he fails to pay before the due date interest is charged on outstanding balances at the end of each month.

Premium Credit Cards

Many incentives and benefits are offered by premium credit cards
e.g. Gold and Platinum cards which offer cash back, reward points, travel upgrades, and other rewards to cardholders. The card holder ofpremium cards are charged higher fees and the card is issued to the person who has prescribed higher income and credit score requirements.

Charge Cards

Charge card is a type of credit card that requires the cardholders to pay their balance in full at the end of each billing cycle instead of making payments on the balance over several months. Charge cards do not have spending limit and finance (interest rate) charge. Late payments are subject to a fee, charge restrictions, or card cancellation depending on the card agreement.

Limited Purpose Cards

Limited purpose credit cards can only be used at specific locations. Limited purpose cards are used like credit cards with a minimum payment and finance charge. Store credit cards and gas credit cards, petro card are examples of limited purpose credit cards.

Secured Credit Cards

Insteadofassessingcreditworthiness,somemoneyistobedeposited to get a secured credit card. The credit limit on a secured credit card is limited up to the amount deposited. The credit limit may be extended in some cases. Cardholder must make monthly payments on their secured credit card balance.

Prepaid Cards

Prepaid cards are similar to debit cards. The cardholder can use the card after payment of some money in advance. The spending limit is limited up to the amount paid in advance by the cardholder. If the cardholder wants more credit limit, he has to load more money into the card. Prepaid cards do not have finance charges or minimum payments since the balance is withdrawn from the deposit.

Business Credit Cards

A card which is designed specifically for business use is called as business credit card. It is an easy method for business people to maintain business and personal cash transactions separately. There are 12 major types of credit cards provided by banks and financial institutions in India. These cards provide a wide variety of financial benefits to holders.

MAJOR INDIA CREDIT CARD TYPES

Following are various types of credit cards available in India:

- Premium Credit Cards
- Cash Back Credit Cards
- Gold Credit Cards
- Airline Credit Cards
- Silver Credit Cards
- Business Credit Cards
- Balance Transfer Credit Cards
- Co-branded Credit Cards
- Low Interest Credit Cards
- Lifetime Free Credit Cards
- Rewards

There are some additional credit cards that are available in India as well. Rewards credit cards available in India can be subdivided into six categories – Points, Hotels and Travels, Retail, Auto and Fuel.

Premium Credit Cards

There are 33 various premium credit cards available in India:

- ABN AMRO Make My Trip Go Credit Card
- ABN AMRO Platinum Credit Card
- ABN AMRO Titanium One Credit Card
- American Express Kingfisher First Credit Card
- American Express Platinum Credit Card
- Axis Bank Visa Platinum Credit Card
- Bajaj Allianz Super Value Titanium Credit Card
- Citibank Platinum Credit Card
- Deutsche Bank Landmark Platinum Credit Card
- Deutsche Bank Miles & More Platinum Credit Card
- Deutsche Bank Miles & More Signature Credit Card
- Deutsche Bank Platinum Credit Card
- HDFC Bank Platinum Plus Credit Card
- HDFC Bank Platinum Plus Credit Card
- HDFC Bank Titanium Credit Card
- HDFC Bank Visa Signature Credit Card
- HSBC Platinum Credit Card
- ICICI Bank Ascent American Express Credit Card
- ICICI Bank Platinum Credit Card
- ICICI Bank Platinum Identity Credit Card
- ICICI Bank Platinum Premiere Credit Card
- ICICI Bank Thomas Cook Titanium Credit Card
- ICICI Bank Titanium Credit Card
- ICICI Signature Credit Card
- Jet Airways Citibank Platinum Credit Card
- Kotak Mahindra League Platinum Credit Card
- Kotak Mahindra Royal Signature Credit Card
- SBI (State Bank of India) Platinum Credit Card
- Standard Chartered Emirates Platinum Credit Card
- Standard Chartered Emirates Titanium Credit Card

- Standard Chartered Platinum CreditCard
- Standard Chartered Super Value Titanium Credit Card
- Yare Barclaycard Platinum CreditCard

Features of Credit Card Interest Rate

Interest rate is the prime feature of any credit card. Interest rate is directly influencing the payment for borrowing money on the credit card. In general, the interest rate is expressed as the annual percentage rate (APR).

Grace Period

The card issuers may provide a grace period to pay off the balance. The grace period is the amount of time given to the cardholder for the payment of his credit card balance in full to avoid interest charges. Credit card grace periods range is subject to the conditions of the card issuers.

Fees

Annual fee is normally charged by the card issuer. Over-limit fee is charged on the amount exceeding the credit limit of the card holder. Cash advance fee is charged when the card holder makes a cash advance on his credit card. Balance transfer fees are added when a cardholder transfers a balance to his creditcard.

Credit Limits

Credit limit is the maximum spending amount of the cardholder by using his card. The cardholder may exceed his credit limit if he has opted 'over-the-limit' option. He is charged with the fee for over-the-limit when a transaction goes over the credit limit.

Debit Cards vs Credit Cards

Debit card	Credit card
The spending power depends on the drawing capacity which in the case of Debit Card is your own assets with the bank.	It allows a borrowing power on the bank, for which you have to pay some charge or fees.
Debit card is as good as money in the accounts with the bank	Credit card has the additional advantage of your overdrawing if necessary, payments are made by the bank to the extent of the purchases and if they exceed the limit, Interest has to be paid to the excess amount spend.
There is no risk of overspending, and it does not involve interest payment	Borrowing is possible and interest to be paid on the overdrawn amount.

Both Credit Cards and Debit cards complement each other and are precursors to the electronic card which consolidates all the cash account in various branches of a bank, connected through the Bank Internet and allows managing the payments most economically in tune with the receipts and promotes efficient cash management.

Travelers' Cheques Vs Credit Cards

	Travelers' Cheque	Credit Cards
What is it?	A Travelers Cheque is bearer cheque in foreign currency for a predeter- mined value.	A Credit card enables one to make an immediate "cashless purchase" and pay later.
Issued by?	Authorized dealers in foreign currency	Banks
Eligibility	In order to procure tra- velers cheque we have to furnish your passport and a confirmed ticket	In order to procure a credit card, we are assess- ed by the bank in terms of the income and credit worthiness.
Revolving Credit Facility	A Travelers cheque when procured, involves an upfront payment or an immediate debit the bank account.	Credit cards allow carrying forward the outstanding due on a month to month basis while paying only the minimum balance. This is called revolving credit facility. Banks charge interest on the outstanding for the period of time it is due.
Pre determined spending limit	The travelers cheque is already drawn for particular amount, it cannot be exceeded	Credit cards have a predetermined spending limit based on the bank's assessment of the credit worthiness. We can spend within this limit and carry forward the outstanding if we cannot pay it at the month end.

CREDIT RATING

Meaning

Credit rating is an opinion of rating agency about a debt instrument. The opinion is expressed through symbols which indicate the degree of risk associated with repayment of principal and payment of interest on debt instrument. Credit rating agency gets fee for their services from corporate entities which approach for rating of their instruments. Credit rating is not mandatory to all corporate sectors except for certain instruments. The financial position of the corporations is reviewed frequently and the ratings are revised by the credit rating agency.

Origin

In 1841, the first mercantile credit agency was set up in New York to rate the ability of merchants to pay their financial obligations. Later on, it was taken over by Robert Dun. This agency published its first rating guide in 1859. The second agency was established by John Bradstreet in 1849 which was later merged with first agency to form Dun & Bradstreet in 1933. It became the owner of Moody's Investor's Service in 1962. Since 1970's, a number of credit rating agencies have been set up all over the world including countries like Malaysia, Thailand, Korea, Australia, Pakistan, Philippines etc. In India, CRISIL (Credit Rating and Information Services of India Ltd.) was setup in 1987 as the first rating agency.

RATING INDICATIONS

Rating symbols assigned to a security issue is an indicator of the following:

- The nature and terms of the particular security being issued;
- The ability and the creditworthiness of the issuer of a security to make payments in time;
- The probability that the issuer will make a default in payments.

FACTORS INFLUENCING ASSIGNED RATINGS

The ratings are assigned by the credit rating agency based on the following factors:

- The issuer's ability to meet the obligations of debt.
- The volume and composition of outstanding debt.
- The earning capacity of the company and its stability of 'future cash flows'.

- The interest coverage ratio i.e. it is the relationship between fixed interest and profit of the company (EBIT) whose ability to meet its fixed interest obligations.
- Current Ratio which is calculated to assess the liquidity position of the issuing firm.
- The value of assets pledged as collateral security
- Market demand for the products, competitors' market share, and distribution channels etc.
- Operational efficiency is judged by capacity utilization, prospects of expansion, modernization and diversification, availability of raw material etc.
- Track record of promoters, directors and expertise of staff.

BENEFITS OF CREDIT RATING

The beneficiaries of Credit rating are investors, companies and intermediaries benefited in the following ways:-

Benefits to Investors Safety

Investors get an idea about the degree of financial strength of the issuer company through credit rating.

Risk and Returns

Credit rating indicates the degree of risk and possibility of returns on debt instruments. The indication (symbol) helps the investor to take decision for making investment on such instruments.

Investment Decisions

Credit rating symbol expresses the creditworthiness of the instruments as a layman can easily understand about the risk & return status of such instruments. Hence, he can take his own decision instead of seeking any advice from the stock brokers.

Investment Choice

Commonly, there are two different types of investors i.e., risk taker and risk averter. The level of risk taking is different for different investors. Hence, the investor can choose the securities for his investment based on his risk bearing capacity.

Easy Perception

All debt instruments are rated mandatorily. No analytical knowledge is required to make investment on debt

instruments. Therefore, investors can make investment easily and quickly.

No Need of Issuing Company Details

Credit rating agencies conduct detailed investigation about the issuing companies' details like nature of business, financial position, liquidity and profitability position before evaluating the instruments issued by them. Therefore, investors need not bother about the company.

Monitoring System

The constant monitory system is followed by credit rating agencies after grading the instruments.

THE REGULATORY FRAMEWORK FOR CREDIT RATING AGENCIES SEBI REGULATIONS

The Securities and Exchange Board of India (Credit Rating Agencies) Regulations, 1999 empower SEBI to regulate CRAs operating in India. In fact, SEBI was one of the first few regulators, globally, to put in place an effective and comprehensive regulation for CRAs.

SEBI regulation for CRAs has been designed to ensure the following:

Credible players enter this business (through stringent entry norms and eligibility criteria)
CRAs operate in a manner that enables them to issue objective and fair opinions (through well-defined general obligations for CRAs)
There is widespread investor access to ratings (through a clearly articulated rating dissemination process).
The applicant should be registered as a company under the Companies Act, 1956 and possess a minimum network of` 5 crore.

The following are some of the General Obligations specified in the CRA regulations.

CRAs are amongst the very few market intermediaries for which such detailed operating guidelines have beenprescribed under the regulations.

- Code of Conduct stipulated by SEBI
- Agreement with the client
- Monitoring of ratings
- Procedure for review ofrating
- Internal procedures to be framed by the CRA
- Disclosure of Rating Definitions and Rationale by the CRA
- Submission of information to the Board
- Compliance with circulars etc., issued by the Board
- Appointment of Compliance Officer
- Maintenance of Books of Accounts records, etc.
- Confidentiality

Rating process

These regulations cover issues with respect to confidentiality of information and disclosure with respect to the rationale of the rating being assigned. Several other provisions exist, like the regulator's right to inspect a CRA. An important feature of the regulation is that CRAs are prohibited from rating their promoters and associates.

SEBI Code of Conduct

SEBI's code of conduct for CRAs addresses some of the basic issues relating to conflicts of interest. The Code of Conduct is designed to ensure transparent and independent functioning of CRAs.

Some of the salient provisions of the Code of Conduct are:

- A CRA shall make all efforts to protect the interests of investors.
- A CRA shall at all times exercise due diligence, ensure proper care and exercise independent professional judgment in order to achieve and maintain objectivity and independence in the rating process.
- A CRA shall have in place a rating process that reflects consistent and international rating standards.
- A CRA shall keep track of all important changes relating to the client companies and shall develop efficient and responsive systems to yield timely and accurate ratings.
- A CRA shall disclose its rating methodology to clients, users and the public.

REGULATING AUTHORITY

In India, the regulating authority of Credit Rating Agencies and financial instruments are SEBI, RBI and IRDA. The list of various financial instruments, and the relevant regulators, are given below:

Products / Instruments requiring mandatory rating before issuance

Sl. No	Instrument	Regulator
1	Public / Rights/ Listed issue of bonds	SEBI
2	IPO Grading	SEBI
3	Capital protection oriented funds	SEBI
4	Collective Investment Schemes of plantation companies	SEBI
5	Commercial Paper	RBI
6	Bank loans	RBI (Basel II capital computation for banks)
7	Security Receipts	RBI (For NAVdeclaration)
8	Securitised instruments (Pass Through Certificates)	RBI ((Basel II capital computation for banks)
9	Fixed Deposits by NBFCs& HFCs	RBI
10	LPG/SKO Rating	Ministry of Petroleum and Natural Gas
11	Maritime Grading	Directorate General of Shipping (for some courses)

REGULATORY FRAMEWORK

S. No	Product	Regulator
1	Banks'investments in unrated non-SLR portfolio	RBI
2	Investments by Insurancecompanies	IRDA
3	Provident Fund investments	Government of India

International Regulations

The International Organization of Securities Commission (IOSCO) has formulated a Code of Conduct Fundamentals for the working of CRAs. The IOSCO Code of Conduct broadly covers the following areas:

Quality and integrity of the rating process – This includes the measures to ensure quality of the rating process and monitoring and updating by the CRAs.
CRA's independence and avoidance of conflicts of interest – The procedures and policies to ensure the same.
CRA's responsibilities to the investing public and issuers – These address issues such as transparency and timeliness of ratings disclosure and the treatment of confidential information.
Disclosure of the code of conduct and communication with market participants – This requires CRAs to disclose to the public in accordance with the IOSCO Principles regarding the activities of Credit Rating Agencies

Credit Rating Agencies in India

The Indian credit rating agency has evolved over a period of time. Indian credit rating agencies include mainly CRISIL, ICRA, CARE, FITCH and Brickworks. CRISIL is the largest credit rating agency in India, with a market share of greater than 60%. CRAs registered with SEBI

Name of the CRAs	Year of commencement of Operations
CRISIL	1988
ICRA	1991
CARE	1993
Fitch India	1996
Brickworks	2008

Credit Rating Information Services of India (CRISIL Ltd.)

CRISIL is the first rating agency in India. It was set-up in 1987 jointly by the erstwhile ICICI Ltd. and UTI. The other shareholders are Asian Development Bank (ADB), LIC, State Bank of India, HDFC etc. The head office of the company is located at Mumbai and it has established offices outside India also. The CRISIL Ltd. is the world's fourth largest rating agency. 'CRISIL' has rated over 4700 debt instruments issued by 2200 companies.

The activities of CRISIL Ltd. are as under

To provide credit rating service in respect of Ratings of corporate debt issuances, Ratings of banks, non-banking finance companies, Ratings of borrowing programmes of governments and government bodies, Ratings of structured finance instruments and Ratings of micro-finance institutions
To provide analytical tools for management of risk such as market risk, credit and operational risk and valuation services
To undertake research on economy, industry and company performance and publish suchreports
To provide corporate as well as market advisory services to corporate and non-corporate clients.
Investment Information and Credit Rating Agency of India Ltd. (ICRA)

ICRA was established in the year 1991 by the collaboration of financial institutions, investment companies, and banks. The company has formed the ICRA group together with its subsidiaries. The company offers products like short-term debt schemes, Issue-specific long-term rating and offers fund based as well as non-fund based facilities to its clients.

The objectives of the ICRA Ltd. are as follows:

- To rate rupee denominated debt instruments issued inter alia, by manufacturing companies, commercial banks, non-banking finance companies, financial institutions, public sector undertakings and local bodies, etc.

- To take-up assignments for credit assessment of companies/ undertakings intending to use the same for obtaining specific line of assistance from commercial banks, financial institutions, non-bank financial services companies.

- It provides services of general assessment. At the request of banks or any other potential users, it prepares, as per their requirements, general assessment reports. It does not assign any specific symbols in respect of such general assessments. It provides a report on various aspects of the functioning of companies such as operations, quality of management etc.

- To undertake research-based study reports to address the unique needs and requirements of an individual client. The assignments include due diligence studies, equity assessment/valuation, industry analysis, and market studyetc.

- To offer advisory services to banks, finance companies, manufacturing companies, government, regulatory authorities and local bodies in the following areas of strategic consulting, risk management and inputs for policy formulation

Credit Analysis and Research Limited (CARE)

CARE was incorporated in 1993. It was promoted by Industrial Development Bank of India (IDBI), Canara Bank, Unit Trust of India (UTI) and other financial and lending institutions. CARE has completed over 7,564 rating assignments since its inception in 1993.

The functions of CAREL are as under

To undertake credit rating of all types of debt instruments, both short term and long term.
To make available information on any company, industry or sector required by a business enterprise.
To undertake equity research study of listed or to be listed companies on the major stock exchanges
FITCH Ratings

Fitch Ratings is a global rating agency committed to provide the world's credit markets with independent

and prospective credit opinions, research, and data. The headquarters of Fitch Ratings is in New York and London and it is a part of the Fitch Group.

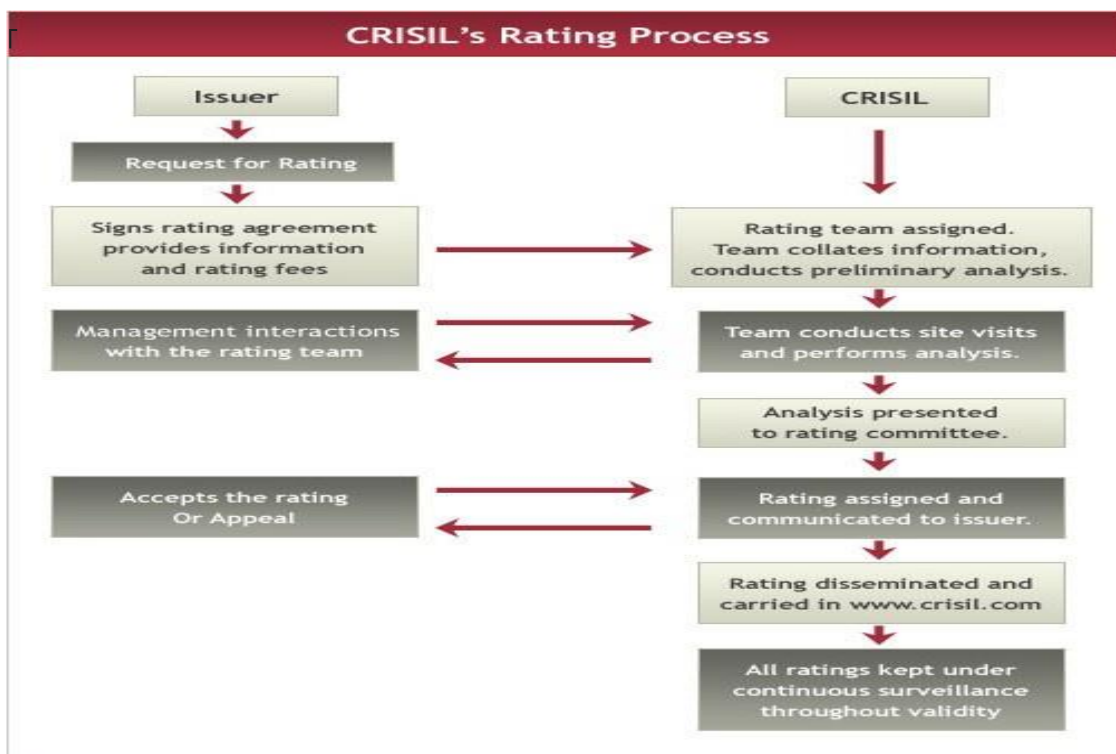
BRICK WORK Ratings

Brickwork Ratings is a private credit rating agency. It was registered under SEBI in the year 2008. It was founded by bankers, credit rating professionals, former regulators as well as professors, was committed to promoting Financial Literacy.

Credit Rating Process

The rating process is designed to ensure that all ratings are based on the highest standards of independence and analytical rates. From the initial meeting with the management to the assignment of the rating, the rating process normally takes three to four weeks. However, the rating agency has sometimes arrived at rating decisions in shorter time frames, to meet urgent requirements. The process of rating starts with a rating request from the issuer, and the signing of a rating agreement. Credit rating agency employs a multi-layered, decision-making process in assigning a rating.
The following picture depicts the CRISIL's Credit rating process:

The process/ procedure followed by all the major credit rating agencies in the country are almost similar



and usually comprises of the following steps.

Receipt of the Request

The issuing company approaches the credit rating agency to rate their instruments which are issued to the public. It is the starting point in the process of rating. The rating agency and Issuer Company enter into an agreement.

The general terms and conditions of the agreement are as follows:

- To Keep confidential information about the issuing company
- Acceptance of the rating is in the hands of issuing company
- Providing all information is essential on the part of issuing company

Assignment to Analytical Team

Credit rating agency entrusts the job to its expertise team for investigating the issuing company after entering into the agreement with them. Normally, the team consists of two members and it may vary depending upon jobs.

Obtaining Information

The issuing company must provide all the requisite information to the analytical team. The analytical team analyses the information relating to its financial statements, cash flow projections and other relevant information.

Team Visits and Interacts with Management

The analytical team must visit the issuing company for better understanding of the client's operations and interact with the company's executives.

Presentation of Findings

The analytical team presents the report on the issuing company to the internal committee of the credit rating agency.

Rating Committee Meeting

The rating committee conducts meeting with the analytical team to discuss about the assessment of all factors concerned to the issuer. After a deep discussion, the rating committee evaluates the issuing company and rates their instruments. The decision of the rating committee is final. The issuing company cannot be involved directly in the process of rating.

Communication of Decision

The issuing company gets the information from CRA about the rating grade assigned by them. The supported documents or explanations would be furnished to the issuing company. The issuing company may accept or reject the ratings. The rejected ratings are not disclosed by the Credit rating agency.

Broadcasting to the Public

The credit rating agency can broadcast the rating information through printed reports to the public after the acceptance of the issuer.

Continuous Surveillance

The Credit Rating Agency is continuously monitoring the issuing company till the validity period of the ratings.

RATING PROCESS AND METHODOLOGY

The rating methodology is a detailed analysis of all the factors affecting the creditworthiness of an issuer company. The important factors are business, financial and industry characteristics, operational efficiency, management quality, competitive position of the issue, commitment to new projects etc.

The credit rating agency analyses the following factors for evaluating the instruments such as:

- Business Risk Analysis
- Financial Analysis

- Management Risk Analysis
- Project Risk Analysis
- External support
- These are explained as under:

Business Risk Analysis

Business risk analysis involves the analysis of the industry risk, market position and operating efficiency of the company which has various factors that depicts in the following chart:

Industry risk

The rating agency evaluates the industry risk by considering the following factors:

- Strength of the industryprospect,
- Nature and basis ofcompetition,
- Demand and supplyposition,
- Structure of industry,
- Pattern of business cycleetc.

Market Position

The credit rating agency determines the market position of the issuing company with reference to the following parameters:

- Revenue Generation Addressed
- Market Size and Segments
- Market Share and Trends
- Entry Barriers and Capacity
- Product Range and Customer Diversity
- Competitive Advantages
- Brands, Product Quality
- Strength of Distribution network and geographical Reach
- Long Term contracts for Product off take / marketing arrangement
- Ability to pass on Input Cost Increase

Operating Efficiency

Operating Efficiency can be measured by using the following aspects:

- Cost Structure
- Technology used
- Capacity Utilization
- Regular up keep / modernization of facilities
- Input Structure
- Access to resource, cost of key inputs
- Level of Integration
- Assured, Quality supply of Critical Utilises
- Labour Relations – Union

Financial Analysis

Financial risk analysis aims at determining the financial strength of the issuer company. The credit rating agency can use some accounting tools & techniques to analyze the financial risk which are depicted in the following picture.

Accounting Quality

Qualification of Auditors Inventory Valuation Policies. Income recognition method Off Balance Sheet Items

Past and Future Financial Record

Past performance
Capital Structure (Debt –Equity)
Debt Protection measure (Interest Coverage & Cash DSCR) & Liquidity
Profitability Trends in Operating / Net Margins (indicating asset side Performance) – provide a tool to measure cash generation.
Trends in Company's Funding mix Philosophy – Phasing of Capex Programmes.
Future Performance Based on Industry Trends, Company's own operations and future plans.

Cash Flow Adequacy and Financial Flexibility

Assess the adequacy and stability of cash Flow in relation to debt, working capital needs and capital expenditure requirement.
Comparison of sources and uses of funds
Ability to raise alternative financing eg. Equity, Quasi Equity, Loans from Promoters
Financial support from group / promoters and its past track record
Availability of un encumbered liquid assets

Management Risk Analysis

Rating of a debt instrument requires evaluation of the management strengths and weaknesses because company's performance is highly influenced by the management goals, plans, strategies etc., which can be analyzed through the followingaspects:

RATING SYMBOLS

Definition

Rating symbols are used in terms of alphabets. Instruments for Rating CRAs in India rate a large number of financial products:

- Bonds/ debentures- [the main product]
- Commercial paper
- Structured finance products and loans
- Fixed deposits and bank certificate of deposits
- Mutual fund debt schemes Initial Public Offers (IPOs)

CRISIL has revised the symbols and definitions of its long-term and short-term credit ratings on debt instruments, structured finance instruments, and debt mutual fund schemes. This is following a June 15, 2011, Securities and Exchange Board of India (SEBI) circular, “Standardisation of Rating Symbols and Definitions,” which mandates the use of common rating symbols and rating definitions by all credit rating agencies (CRAs). As per the circular, all CRAs are required to revise their rating symbols and definitions as recommended by SEBI. Accordingly, CRISIL has effected changes in rating symbols and definitions with effect from July 11, 2011. The rating symbols and definitions of the following class of instruments have been revised:

- Long-term debt instruments;
- Short-term debt instruments;
- Long-term structured finance instruments;
- Short-term structured finance instruments;
- Long-term mutual fund schemes; and
- Short-term mutual fund schemes.

CRISIL Long Term Debt Instruments Symbols and Definitions (Period >= 365 Days)

Long Term Rating Symbols	Rating Definitions under Basel II	Risk Weight age under Basel II
CRISIL AAA	Highest Safety	20 %
CRISIL AA	High Safety	30%
CRISIL A	Adequate Safety	50 %
CRISIL BBB	Moderate Safety	100%
CRISIL BB	Moderate Risk	150%
CRISIL B	High Risk	150%
CRISIL C	Very High Risk	150%
CRISIL D	Default	

Long-Term Debt Instruments	
Revised Rating symbol	**Revised rating definition as stipulated by SEBI in its Circular No. CIR/MIRSD/4/2011 dated June 15, 2011**
CRISIL AAA (Highest Safety)	Instruments with this rating are considered to have the highest degree of safety regarding timely servicing of financial obligations. Such instruments carry lowest credit risk.
CRISIL AA (High Safety)	Instruments with this rating are considered to have high degree of safety regarding timely servicing of financial obligations. Such instruments carry very low credit risk.
CRISIL A (Adequate Safety)	Instruments with this rating are considered to have adequate degree of safety regarding timely servicing of financial obligations. Such instruments carry low credit risk.
CRISIL BBB (Moderate Safety)	Instruments with this rating are considered to have moderate degree of safety regarding timely servicing of financial obligations. Such instruments carry moderate credit risk.
CRISIL BB (Moderate Risk)	Instruments with this rating are considered to have moderate risk of default regarding timely servicing of financial obligations.
CRISIL B (High Risk)	Instruments with this rating are considered to have high risk of default regarding timely servicing of financial obligations.
CRISIL C Very High Risk	Instruments with this rating are considered to have very high risk of default regarding timely servicing of financial obligations.
CRISIL D (Default)	Instruments with this rating are in default or are expected to be in default soon.

CRISIL Short Term Debt instruments Symbols (Period < 365 Days)

Rating Short Term Rating Symbol	Rating Definitions under Basel II
CRISIL A1	Very Strong Degree of Safety
CRISIL A2	Strong degree of safety
CRISIL A3	Moderate Degree ofSafety
CRISIL A4	Minimum Degree of safety
CRISIL D	Default

Short-Term Debt Instruments	
Revised Rating symbol	Revised rating definition as stipulated by SEBI in its Circular No. CIR/MIRSD/4/2011 dated June 15, 2011
CRISIL A1	Instruments with this rating are considered to have very strong degree of safety regarding timely payment of financial obligations. Such instruments carry lowest credit risk.
CRISIL A2	Instruments with this rating are considered to have strong degree of safety regarding timely payment of financial obligations. Such instruments carry low credit risk.
CRISIL A3	Instruments with this rating are considered to have moderate degree of safety regarding timely payment of financial obligations. Such instruments carry higher credit risk as compared to instruments rated in the two higher categories.
CRISIL A4	Instruments with this rating are considered to have minimal degree of safety regarding timely payment of financial obligations. Such instruments carry very high credit risk and are susceptible to default.
CRISIL D	Instruments with this rating are in default or expected to be in default on maturity.

Long-Term Debt Mutual Fund Schemes	
Revised Rating symbol	Revised rating definition as stipulated by SEBI in its Circular No. CIR/MIRSD/4/2011 dated June 15, 2011
CRISIL AAAmfs	Schemes with this rating are considered to have the highest degree of safety regarding timely receipt of payments from the investments that they have made.
CRISIL AAmfs	Schemes with this rating are considered to have the high degree of safety regarding timely receipt of payments from the investments that they have made.
CRISIL Amfs	Schemes with this rating are considered to have the adequate degree of safety regarding timely receipt of payments from the investments that they have made.
CRISIL BBBmfs	Schemes with this rating are considered to have the moderate degree of safety regarding timely receipt of payments from the investments that they have made.
CRISIL BBmfs	Schemes with this rating are considered to have moderate risk of default regarding timely receipt of payments from the investments that they have made.

CRISIL Bmfs	Schemes with this rating are considered to have high risk of default regarding timely receipt of payments from the investments that theyhave made.
CRISIL Cmfs	Schemes with this rating are considered to have very high risk of default regarding timely receipt of payments from the investments that they have made.

Short-Term Debt Mutual Fund Schemes

Revised Rating symbol	Revised rating definition as stipulated by SEBI in its Circular No. CIR/MIRSD/4/2011 dated June 15, 2011
CRISIL A1mfs	Schemes with this rating are considered to have very strong degree of safety regarding timely receipt of payments from the investments that they have made.
CRISIL A2mfs	Schemes with this rating are considered to have strong degree of safety regarding timely receipt of payments from the investments that they have made.
CRISIL A3mfs	Schemes with this rating are considered to have moderate degree of safety regarding timely receipt of payments from the investments that they have made.
CRISIL A4mfs	Schemes with this rating are considered to have minimal degree of safety regarding timely receipt of payments from the investments that they have made.

ICRA (Investment Information and Credit Rating Agency of India Limited)

ICRA's Long-Term Rating Scale

Long-Term Rating Scale: All Bonds, NCDs, and other debt instruments (excluding Public Deposits) with original maturity exceeding one year.

Symbols	Indicator	Profile
LAAA	Highest Safety	The rated instrument carries the lowest credit risk
LAA	High Safety	The rated instrument carries low credit risk.
LA	Adequate Safety	The rated instrument carries average credit risk.
LBBB	Moderate Safety	The rated instrument carries higher than average credit risk.
LBB	Moderate Risk	The rated instrument carries high credit risk.
LB	High Risk	The rated instrument carries very high credit risk.
LC	Very High Risk	The rated instrument has limited prospects of recovery
LD	Default	The rated instrument has very low prospects of recovery.

ICRA's Medium-Term Rating Scale (only for Public Deposits) ICRA's Medium-Term Rating Scale

Symbols	Indicator	Profile
MAAA	Highest Safety	The rated deposits programme carries the lowest credit risk
MAA	High Safety	The rated deposits programme carries low credit risk

MA	Adequate Safety	The rated deposits programme carries average credit risk.
MB	Inadequate Safety	The rated deposits programme carries high credit risk
MC	Risk Prone	The rated deposits programme carries very high credit risk.
MD	Default	The rated instrument has very low prospects of recovery.

ICRA's Short-Term Rating Scale

(All instruments with original maturity within one year)

Icra's Short-Term Rating Scale

Symbols	Indicator	Profile
A1	Highest Safety	Instruments rated in this category carry the lowest credit risk in the short term. Within this category, certain instruments are assigned the rating of A1+ to reflect their relatively stronger credit quality.
A2	High Safety	Instruments rated in this category carry higher credit risk than instruments rated A1.
Symbols	Indicator	Profile
A3	Adequate afety	Instruments rated in this category carry higher credit risk than instruments rated A2 and A1.
A4	Risk Prone	Instruments rated in this category carry high credit risk.
A5	Default	Instruments rated in this category have very low prospect of recovery.

International Credit Rating Agencies

Credit ratings are in use in the financial markets of most developed economies and several emerging market economies as well.

The principal characteristics of the major internationally known rating agencies are as follows:

Name of the agency	Home country	Ownership	Principle
Moody's Investors Service	U.S.A	Dun and Bradstreet	Full Service
FitchInvestors Service	U.S.A	Independent	Full Service
Standard and Poor's Corporation	U.S.A	Mcgraw Hill	Full Service
Canadian Bond Rating Service	Canada	Independent	Full Service (Canada)
Thomson Bank Rating	U.S.A	Thomson Company	Financial Institutions

Japan Bond Rating Institute	Japan	Japan Electronic Journal	Full Service (Japan)
Duff and Phelps Credit Rating	U.S.A	Duff and Phelps Corporation	Full Service

Name of the agency	Home country	Ownership	Principle
Japanese Credit Rating Agency	Japan	Financial Institution	Full Service (Japan)
IBCA Ltd.	U K	Independent	Financial Institutions

Rating by Two Pioneer Agencies

Moody's Investor Services and Standard and Poor (S&P) of the USA

Moody's Investor Service Rating (MIS)
Aaa- Best Quality
Aa - High quality
- Higher Medium Grade Baa
- Possesses safety
-Generally lack characteristics of desirable investment
Caa --Poor standing may be indefault
Ca -Speculative to a high degree often in default

Standard & Poor's Rating (S&P)
AAA - Highest grade
AA - Higher grade
- Upper medium grade BBB - Medium grade
BB - Lower medium
- Speculative elements CCC-CC - Outright speculation
DDD-D - Default with rating indicating relative salvage value.

The Rating Challenge

- Borrowers, be it an individual or a corporate entity are rated for their creditworthiness. And why not, the banks themselves are now entering the capital market to raise funds. It has become all the more important in the context of the new code of greater transparency and prudential norms. While ratings act as a guide to the average investor, it also enhances the credibility of the rated organizations.

- Presently, credit rating is mandatory in India for debt instruments with conversion/redemption exceeding 18 months for fixed deposit programmers' of all non- banking finance companies. It is optional for PSU bonds and privately placed non-convertible debentures.

- Are the Indian rating agencies able to meet evaluation standards and eliminate influence of vested interests? For this, it is imperative that they are independent. In the Indian case, the existing three rating agencies, viz CRISIL, ICRA, and CARE are promoted by financial institutions. They may well serve as in-house rating agents to assess credit risk of their customers. But what would be the yardsticks and whether they would remain impartial when their promoters themselves would be the clients? We may think of other independent rating agencies in the field but there is every likelihood that industrial groups may start their own rating agencies, on the patterns of their own financial agencies. In such an eventuality, there is every danger of such agencies becoming an in-

house sort of entity thereby compromising on objectivity in rating standards.

- Multiple agencies may increase competition in rating but it may also land up in indifferent rating standards and there is also the risk of succumbing to pressures for attracting business. There have been criticisms of Indian credit rating agencies. First, that they assign ratings which are not comparable against international standards, Secondly the rating symbols they assign are internally inconsistent, and thirdly agencies are not kept at arm's length from their sponsors.

PENSION PLAN

Retired persons require reasonable money continuously to lead a comfortable life till their death. A Retirement Plan provides financial assurance for the payment of certain sum of money periodically to the retired persons. In India, the government servants are receiving pension after retirement. There is no such pension to the private employees. Instead, there are various retirement plans available to private employees. Hence, the private employees can take private Retirement Plans to secure their future in terms of finance. The trend of opting for Retirement Plans is becoming increasingly popular inIndia.

Definition

According to the Supreme Court of India (1982), "Pension is a term applied to periodic money payments to a person, who retires at a certain age, considered age of disability; payments usually continue for the rest of the natural life of the recipient."

Is Retirement Plan Essential?

There are several reasons for the popularity of Retirement Plans in India, these are as follows: -

Socio - Cultural Change

The trend of joint family system is slowly deteriorating and the nuclear family system is being followed especially in urban areas in India due to various reasons like employment, income, independency and reluctance etc. Due to socio-cultural changes, the retired persons are increasingly under pressure to arrange their own income after retirement. Now-a-days, the retired/old age persons also like to be more financially independent.
Increase in Cost of Living

At present, the cost of living is very high due to various economic reasons like inflation, food scarcity, population etc. The medical service is very expensive and causes heavy financial burden to the old age persons as the coverage of medical insurance is limited besides, the process of medical insurance claim being cumbersome. Therefore, the old age persons are increasingly looking at creating a sufficient and reasonable post-retirement income for the bare survival after retirement.

Longer span of life

The life span of human being has increased due to advanced medical facilities. Hence, a strong financial support is required to the retired persons due to the longevity.

Types of Retirement Plans

There are various retirement plans and schemes in India, both in the private and public sectors such as:-

Life Annuity Plan

Life annuity plan guarantees a person a specific amount of income until he survives. After the person's

death, the originally invested amount is refunded to his nominee or legal heirs, in the absence of any nominee.

Guaranteed Period Annuity

In this plan, the person is guaranteed a specific income for a minimum number of years. If the person dies before that period, the nominees will continue to receive that income till the period is completed. If the person outlives that period, he or she can continue to receive the income till his death.

Annuity Certain

Under this retirement plan, a fixed amount of income is paid for a fixed number of years. The payments will stop at the end of the fixed period, even if the retiree lives beyond this fixed period.

Deferred Annuity

Under this plan, the person first saves from his income to create a corpus fund for a number of years. Thereafter, that fund is used for investing in a specific retirement plan that gives him an assured income till his life time.

Defined Benefit Pension Plan

Under this plan, the pension amount is known and assured, but it is not dependent on any external factor. The investor must contribute some amount periodically either by himself or through his employer or both. This amount is invested which earns some returns. But the investor can get assured sum irrespective of the kind of returns generated by the investment. Their pension amounts were linked to their grade and last drawn salary.

Pros of Defined Benefit Plan

Investor can get peace of mind because they know they will get assured and defined pension amount. Investors need not worry about monitoring the investments periodically.

Cons of Defined Benefit Pension Plans

- There is no disadvantage to the employees whereas this plan is disadvantageous to the employee because they have to ensure that the funds contributed for the pension are invested in such a way that they generate adequate returns to cover future pension of the employee. If the returns are not enough to pay the pension, the employer has to provide the deficiency either from other sources or contributions of serving employees. (e.g.,Government)

Defined Contribution Pension Plan

- The amount of contribution towards pension is fixed but the benefit amount is undetermined. This type of plan is called defined contribution pension scheme or plan. Here pension depends on the returns made on the investments. There are multiple options of investments such as equity (high risk and high returns), debt (low risk and moderate returns) or govt. securities (no risk and low returns). The Fund would grow into a large amount at the time of retirement through the investment (of both contribution and returns) over the years. Investors are permitted to withdraw only a part of pension fund as lump-sum. Remaining portion of fund would be invested in annuity and that would provide fixed amount every month.

Advantages of Defined Contribution Pension Plans

The main advantage to the employees is that the pension fund investment is market-linked. They can make excellent returns on the investments through proper selection of portfolio of investments.

The advantage for the employer is that it doesn't have to worry about the management of the pension funds and the returns generated by them.

Disadvantages of Defined Contribution Pension Plans

The disadvantage to the employees is that there is a chance of getting lower amount of pension due to improper selection of investment. Continuous monitoring is a burden to the employees.

New Pension System (Nps) for Non-Government Employees

The Structure of the scheme and entities involved are as follows:

- The New Pension System is administered by the Pension Fund Regulatory Development Authority (PFRDA).
- A Central Recordkeeping Agency (CRA) maintains all the records (like account balances) related to the NPS.
- National Security Depository Limited (NSDL) has been selected as the nationwide CRA for the New Pension System.

There are six Pension Fund Managers (PFMs). The PFM are responsible for investing funds and generating returns from them.

There are also entities called Points of Presence (PoPs). The PoPs are responsible for the sales and marketing of the NPS. (These are similar to the distributors of mutual funds).

List of Pension Fund Managers (PFMs)

ICICI Prudential Life Insurance Company Limited
IDFC Asset Management Asset Management Company Limited
Kotak Mahindra Asset Management Company Limited
Reliance Capital Asset Management Company Limited
SBI Pension Funds Limited
UTI Retirement Solutions Limited

FEATURES AND OPTIONS OF THE SCHEME

Permanent Retirement Account Number (PRAN)

Each investor in the New Pension Scheme (NPS) would be allotted a Permanent Retirement Account Number (PRAN). This would be a unique identification number that would be used to identify an investor irrespective of his PFM.

Investment Options Available to an Investor

Investors would get multiple options for investing their funds in the NPS. These options span the entire risk spectrum from risky to risk- free. There are three investment options

Growth option: A growth option would be an equity-based option, wherein the investments would be primarily done in equities. This option has the potential to give the highest returns but it carries a higher risk. The investment would be passive. There wouldn't be any active buying and selling of stocks based on the fund manager's analysis. Instead, funds would be invested only in the 50 stocks comprising the NSE's NIFTY stock index. This option is most suitable for young people who are just starting their careers. This would also be suitable for middle-aged people who do not have many dependents.

Moderate option:
The funds would be invested in corporate debt and other fixed income instruments. This option has the potential to give moderate returns but it carries a moderate risk. This option is most suitable for risk-averse young people and for mid-career people. This would also be suitable for some of the more adventurous (risk taking) people nearing retirement.
Cautious option:
Here, investors' money would be invested in government securities. These securities are risk free and hence this option would give risk free returns. The returns are expected to be the lowest among all three options. This option is most suitable for employees approaching their retirement and risk-averse mid-career employees. Investors would get an option to allocate their funds between these three options in any proportion they prefer. Thus, they can create a balance between the risky and risk-free options based on their own risk profile. If they do not want to allocate their funds, there is an auto choice feature. Here, investments would be allocated among the three options depending on their age. Thus, when they are young, more investment would be made in the equity-based fund, and when they are old, more and more funds would be invested in the low risk government securities-based fund.

Switching Options: Investors could periodically reallocate their funds among the three options once in a year. Also, they could switch the fund managers (PFMs) periodically. That is, they would be able to move the management of their funds from one PFM to another. This process is expected to be simple, as all the records are centrally kept by the CRA and the Permanent Retirement Account Number (PRAN) would be investors' identification number across all Pension Fund Managers (PFM). Costs and Fees involved in the scheme the management fee for NPS is less than 0.01% per annum. The annual record keeping fee for NPS would be just ` 280. Transaction fee is 6 for each transaction.

Defined Contribution system: The periodical payment is fixed, but the pension amount is not fixed. It totally depends on the returns on investment. This scheme is a defined contribution scheme, without the benefit not being defined. Maturity withdrawals: Investor can get money only at the age of 60 years. Early withdrawals are not allowed except for marriage of sons/daughters and purchase of house. Investor can get only 60% of the corpus as lump sum and remaining 40% should be invested in an annuity (accumulated corpus), which is used to provide a fixed monthly amount.

Coexist with other schemes (EPF / EPS): New Pension System (NPS) would not replace any existing scheme like the Employee Provident Fund scheme or the Employee Pension Scheme.
Income tax exemption: The amount of contribution to NPS is exempted from income tax under section 80C and also the interest or profit earned on the investment in NPS would not be taxed in the year in which it is earned; but, the amount would be taxed at the time of withdrawal.