Tax alert: Finance Ministry launches NPS Vatsalya Scheme

24 September 2024

Finance Minister Smt. Nirmala Sitharaman launched the National Pension System Vatsalya (NPS Vatsalya) scheme on 18 September 2024. NPS Vatsalya, 'a pension scheme for minors' was announced by the Finance Minister on 23 July 2024, in her Union Budget 2024-25 speech.

In a nutshell

For the first time, the Finance Ministry has introduced NPS Vatsalya, a pension scheme for minors. Previously, NPS could only be subscribed by individuals above 18 years of age.

NPS Vatsalya was announced by the Finance Minister in her Budget speech in July 2024. The scheme has since been launched.

Eligibility:
Minors (i.e individuals under 18 years of age) can open a pension account managed by a guardian.

Contribution:
The scheme offers flexible contributions, with a minimum contribution of INR 1,000 p.a., and no upper limit.

Investment choice:
Guardians can select one from the various Pension Funds and a mix of asset classes (e.g. Government security, corporate debt, equity) as per their risk appetite.

Partial withdrawal (till age of 18 years):
Partial withdrawal of up to 25% of contribution after completing a lock-in-period of 3 years is permissible, for education, treatment of specified illness and disability, for a maximum upto 3 times.

Death of the minor:
In case of death of a minor, corpus to be returned to the guardian.

Upon attaining age of 18 years:

- **Option to shift to NPS Tier 1 (All citizen)**: Upon transitioning, features, benefits, and exit norms of NPS-Tier I will apply
- **Option to Exit:**
  - If corpus exceeds INR 250,000, at least 80% to be utilised for annuity, and the remaining amount can be withdrawn.
  - If corpus is less than INR 250,000, entire balance can be withdrawn.

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Highlights of the scheme

- All minor citizens (age below 18 years) are eligible for the scheme.
- Account can be opened in the name of minor and operated by parent or guardian. Minor will be the beneficiary.
- Permanent Retirement Account Number (PRAN) to be issued in the name of minor.
- Scheme can be opened through various points of presence regulated by Pension Fund Regulatory Authority of India (PFRDA) such as major banks, India Post, Pension Funds and Online platform (e-NPS).
- Minimum annual contribution to be made amounting to INR 1,000 p.a. There is no limit on the maximum contribution.
- **Documents required**:
  - Proof of date of birth of the minor;
  - KYC of the guardian to be completed by submitting identity and address proof. Additional requirements (NRE/ NRO bank account) of the minor in case guardian is an NRI.
- Option to select any one Pension Fund registered with PFRDA.
- Option to select an investment choice, as per risk appetite:
  - Default Choice: Moderate Life Cycle Fund (LC)-50 (50% equity)
  - Auto Choice: Aggressive LC-75 (75% equity), Moderate LC-50 (50% equity) or Conservative LC-25 (25% equity).
  - Active Choice: Guardian can actively decide allocation of funds across Equity (up to 75%), Corporate Debt (up to 100%), Government Securities (up to 100%) and Alternate Asset (up to 5%).
- In case of withdrawal before 18 years of age: Partial withdrawal up to 25% of contribution on declaration basis, is allowed after lock-in-period of 3 years for education, specified illness and disability for maximum three times.
- Exit upon attainment of 18 years:
  - If accumulated corpus is equal to or greater than INR 250,000: At least 80% of balance to be utilized for purchase of annuity and remaining balance in lump sum.
  - If accumulated corpus is less than INR 250,000: Option to withdraw entire balance as lump sum
- **In case of death of minor:** Entire accumulated Corpus is returned to the guardian
- **In case of death of the guardian:** Another guardian is to be registered through fresh KYC. In case of death of both parents, the legally appointed guardian can continue the account with or without making contributions to the account, and upon attainment of 18 years of age, the subscriber has an option to continue or exit from the scheme.
- Upon attainment of 18 years of age, there is an option to seamlessly shift to NPS Tier – I (All citizen) account. Fresh KYC of the minor required within 3 months from date of attainting 18 years of age. Upon transitioning, the features, benefits and exit norms of NPS-Tier I for All Citizen Model shall apply.

Comments

NPS Vatsalya scheme encourages a culture of early saving and investment among young subscribers, promoting financial discipline from a young age. The scheme has restrictions on withdrawal and primarily focuses on the need to save for retirement, from a young age. Accordingly, future cash flow requirements for various short term/ long term goals (e.g. higher education, specified illness, disability etc.) may also be kept in mind while investing in this scheme. Further, one needs to wait for the official clarification/ gazette notification on the tax benefits under NPS Vatsalya scheme.