

## **Taxability of Provident Fund Contributions**

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### **Is the accumulated balance exempt?**

Section 10(11) provides for tax exemption in respect of any payments received from statutory provident fund or public provident fund set up by the Central Government. The contributions to these funds by the assessee enables claim of rebate under section 88 and the interest earned in respect of such contribution are also exempt from tax.

Under section 10(12) accumulated balance received by the employee from the recognized provident fund is exempt from tax in following situations.

- The employee must have rendered five years of continuous service with the employer before resignation or retirement.
- The employee's service coming to an end by reason of his ill health or discontinuance of business by the employer or because of the causes beyond the control of the employer.
- Where the employee obtains another employment then the accumulated balance of the previous employer will be taken for deciding the tenure of continuous service.

However, employer's contribution of more than 12% of salary is chargeable to tax in the assessment of the employee. Similarly, interest credited in excess of the prescribed rate, in the RPF account will be chargeable to tax.

In respect of unrecognised provident fund, contribution of the employee will not be chargeable to tax when it is obtained upon discontinuance of service.

However, interest credited towards employees contribution to URPF is chargeable to tax as income from other sources. Employer's contribution to the unrecognised provident fund is not chargeable to tax in the year of contribution and the principal sum with interest attributable to such contribution, however, will be chargeable to tax as salary in the year of receipt of the sum from unrecognised provident fund.

### **Position w.r.t tax deduction availability if the employer's contribution to the PF is made after the due date**

In computing business income of those following the mercantile system of accounting, usually, tax deduction is allowable in the year in which the liability is incurred, unless otherwise specifically provided in the Income-Tax Act, 1961. Section 43B of the Act specifically provides that deduction for certain liabilities would be allowable in computing the income of the year in which the sum is actually paid. The 'due date' for PF payments as defined in Section 36(1)(va) is the date by which the assessee is required to credit an employee's contribution on his account in the relevant fund under any Act, rule *et al.* According to the PF scheme, the employer is required to pay contribution to the fund within 15 days of the close of every month.

Further, a grace period of five days is allowed by a CPFC circular. It has been held that PF payments made within the grace period are allowable as deduction [Hunsur Plywood Works vs DCIT (54 ITD) 394 (Bang)].

Whether the period of 15 days is to be calculated from the end of the month for which the salary is paid or from the end of the month in which the salary is paid.?

In the case of Madras Radiators and Pressing vs DCIT (159 ITD 515), the Madras Tribunal has held that in the absence of definition of 'month', the assessee can choose the beneficial view that the period of 15 days should be computed from the end of the month in which salary is paid. This view would effectively give the period of one month and 20 days for payment of PF dues relating to a particular month. This view has been upheld in the case of Fluid Air (India) vs DCIT (63 ITD 182).

***What happens if employer's contribution to PF is paid after expiry of the grace period but within the relevant previous year? On this issue, contrary views are available. According to one view. Under Section 43B, the deduction is allowable in the year in which the sum is paid and hence, where such payments have been made during the relevant previous year, the deduction ought to be allowed under Section 43B, notwithstanding the fact that payment is made after the due date.***

***This view has been confirmed by the Mumbai and Madras tribunals.***

The tribunals also stated that the legislative intent is not to deny deduction totally in the year of accrual of liability and also in the year of actual payment when the payment is beyond the due date. This view is followed recently in the case of DCIT vs. Assam Tribune (116 Taxman (Mag) 230).

However, according to the Kerala High Court, in the case of CIT vs. South India Corporation (242 ITR 114), PF payments made after the due date are not allowable as deduction even though they have been paid within the previous year.

While, the Kerala High Court judgment would be binding on the assessee within its jurisdiction, the assessee in other jurisdiction may claim protection under Mumbai and Madras tribunal decisions.

Whether the above principle is applicable to employee's contribution deducted and paid by employer also? Under the IT Act, employee's contribution received is added to income of the employer under Section 2(24) and then deduction is allowed under Section 26(I) (va) if payment is made within the due date. Section 43B applies to the 'sum payable by assessee as an employer' which includes employee's contribution also. Since Sec 43B has a 'non obstante' clause, it has overriding effect over Section 36(I)(va). Therefore the assessee could claim that even employee's contribution paid beyond the due date but within the previous year would be deductible.

**For tax exemption, a) The employee must have rendered five years of continuous service with the employer before resignation or retirement. b) The employee's service coming to an end by reason of his ill health or discontinuance of business by the employer or because of the causes beyond the control of the employer. c) Where the employee obtains another employment then the accumulated balance of the previous employer will be taken for deciding the tenure of continuous service**