Different scenarios arising due to reduced PF contribution for May, June, July 2020

The world is facing financial crisis arising out of Covid-19. India has taken many steps to meet the challenge. The Prime Minister announced his vision and thereafter, the Finance Minister announced reliefs under various schemes to lessen the impact.

One such measure was intended to allow more money in the hands of the employees. A notification was issued by the Ministry of Labour and Employment on May 18, 2020 wherein, the Labour Ministry said, "In exercise of powers conferred by first proviso to section 6 of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 (19 of 1952), the central government, after making aforesaid inquiry, hereby makes the following amendments in the said notification number S.O. 320 (E) dated the 9th April, 1997."The statutory rate of provident fund contribution has been reduced from 12% to 10% of monthly pay for May, June and July 2020. The ministry again came out with some clarifications on the same on May 19, stating for whom the reduced rate is applicable and for which establishments it is not applicable.

The notification further added, "Whereas, due to COVID-19 pandemic, lockdown is in force across the country and the central government after making necessary inquiry is satisfied that to provide liquidity in the hands of employers and employees, there arises a need to amend the notification of the government of India in the Ministry of Labour, dated 9th April, 1997."

It also explained how employers and employees will get impacted under different scenarios of reduced PF contribution and how they will get some relief in times of the current crisis. Analysing the situation, we look at the following scenarios:

Scenario 1:

Both employer and employee contribute at statutory rate of 10% of monthly pay

This is as per the announcement in the relief package provided by way of reduction in statutory rate of provident fund contribution. The reduction in employee's share of contribution from 12% to 10% of monthly pay will increase the monthly take-home salary in the hands of employee as there will be lower amount of deduction towards employee's share of contribution.

If one sees from the angle of the CTC model, reduction in employer's share of contribution from 12% to 10% of monthly pay will further increase the monthly take-home salary in the hands of employee-where the employer pays the differential to the employee as additional payment. However, such additional payment will be taxable in the hands of the employee,"

e.g. If monthly provident fund wage is Rs 10,000, the employer and the employee contribute Rs 1,000 each as employer's and employee's share of provident fund contribution respectively. In the CTC model, the employee has additional take home salary of Rs 400 less applicable income tax on Rs 200 paid by the employer as additional payment in lieu of the reduced employer's contribution.

Scenario 2:

One can look into another angle if different rates for employer's and employee's contribution are possible where employer's contribution is part of the CTC of the employee?

Under Section 6 of the Provident Fund Act, if an employee so desires, the employee may avail an option to contribute in excess of 10% of monthly pay subject to the condition that the employer shall not be under any obligation to pay any contribution over and above the contribution payable under the Provident Fund Act.

Where employer's contribution is part of the CTC of the employee, an option may be given to the employee to expressly opt for the rate at which the contribution should be made by the employer and the rate at which the contribution should be deducted from his / her salary.

An employee may opt for any of the following options:

1. Both employer and employee contribute @ 12% of monthly pay

2. Employer contributes @ 10% of monthly pay and employee contributes @ 12% of monthly pay

3. Employer contributes @ 12% of monthly pay and employee contributes @ 10% of monthly pay

In **situation (a)**: there is no additional take-home salary or income tax implications in the hands of employee.

e.g. If monthly provident fund wage is Rs 10,000, the employer and the employee continue to contribute Rs 1,200 each as employer's and employee's share of provident fund contribution respectively. There will be no additional take-home salary or income tax implications in the hands of employee.

In **situation (b)**: reduction in employer's share of contribution from 12% to 10% of monthly pay will increase the monthly take-home salary in the hands of employee- where the employer pays the differential to the employee as additional payment. Such additional payment will be taxable in the hands of employee.

e.g. If monthly provident fund wage is Rs 10,000, the employer contributes Rs 1,000 as employer's share of provident fund contribution. Further, the employee contributes Rs 1,200 as employee's share of provident fund contribution. In the CTC model, the employee has additional take home salary of Rs 200 less applicable income tax on such additional payment paid by the employer in lieu of the reduced employer's contribution.

In **situation (c)**: reduction in employee's share of contribution from 12% to 10% of monthly pay will increase the monthly take-home salary in the hands of employee. However, clarity from the provident fund department may be required on the feasibility of this situation.

e.g. If monthly provident fund wage is Rs 10,000, the employer contributes Rs 1,200 as employer's share of provident fund contribution. Further, the employee contributes Rs 1,000 as employee's share of provident fund contribution. Such reduction in employee's share of contribution from 12% to 10% of monthly pay will increase the monthly take-home salary in the hands of employee.

Scenario 3:

Whether different rates for employee's contribution is possible where employer's contribution is not part of the CTC of the employee

Where employer's contribution is not part of the CTC of the employee, an option may be given to the employee to expressly opt for the rate at which the contribution should be deducted from his / her salary.

An employee may opt for any of the following options:

a. Employee contributes @ 12% of monthly pay

b. Employee contributes @ 10% of monthly pay

In both situations, there will be loss of provident fund benefit to the employee on account of reduced employer's share of contribution.

In **situation (a):** there is no additional take-home salary in the hands of employee.

Example: If monthly provident fund wage is Rs 10,000, the employer contributes Rs 1,000 as employer's share of provident fund contribution. Further, the employee contributes Rs 1,200 as employee's share of provident fund contribution. This will result in loss of provident fund benefit to the employee to the extent of reduced employer's share of contribution.

In **situation (b):** reduction in employee's share of contribution from 12% to 10% of monthly pay will increase the monthly take-home salary in the hands of employee.

Example: If monthly provident fund wage is Rs 10,000, both the employer and the employee contribute Rs 1,000 as employer's and employee's share of provident fund contribution respectively. Such reduction in employee's share of contribution from 12% to 10% of monthly pay will increase the monthly take-home salary in the hands of employee. However, this will also result in loss of provident fund benefit to the employee to the extent of reduced employer's share of contribution.

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