



Analysis of NPS with income tax

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Abstract

National Pension System (NPS) is a contributory pension system whereby contributions from subscribers along with matching contributions from respective governments as an employer, are collected and accumulated in an individual pension account of the employee. NPS uses a system of Government/ Autonomous Bodies' Nodal offices, a Central Recordkeeping Agency (CRA) and designated Pension Funds (PFs), as specified by the respective regulations to achieve synergy and maximum efficiency in operations. NPS is mandatory to all employees joining services of Central Government (except Armed Forces) and Central Autonomous Bodies on or after 1st January 2004. Almost all State Governments have adopted NPS architecture and have implemented NPS mandatorily through Gazette Notifications for the State Government/ Autonomous body employees joining on or after their respective cut-off dates. As a subscriber, you have to submit NPS registration form to your employer on the date of joining itself, it will help in timely generation of PRAN and initiation of uploads in your NPS account. As a subscriber under NPS you are provided with an individual pension account identified by Permanent Retirement Account Number (PRAN) which is unique & portable across locations and employments.

Keywords: national pension system (NPS), income tax

Introduction: Types of Account

Under NPS, two types of accounts are available to you i.e., Tier I & Tier II Tier I account – where you and the Government contribute funds into your individual account. As a subscriber you contribute 10% of your Basic Pay and DA into your Tier-I account on a mandatory basis every month, which is invested along with the matching contribution from the employer. The regular NPS contributions and the accumulated amounts are reflected in your PRAN while you are in service and shall be used at retirement for procurement of your pension. Tier II account – a voluntary savings account from which you are free to withdraw the savings at your own choice any time. An active Tier I account is a pre requisite for opening of a Tier II. It should have Minimum contribution Rs 250 & have minimum balance of Rs 2000/- as on 31st March. Furthermore, since Tier II is a voluntary savings account, the government does not contribute any amount into your Tier II account and no tax benefits are available for the contributions.

Benefits of NPS

Dual benefit of Low Cost & Power of Compounding the pension wealth accumulates over a period of time till retirement; grows with a compounding effect and the account maintenance charges are also low. On Employee's own contribution is eligible for tax deduction under sec 80 CCD (1) of Income Tax Act up to 10% of salary (Basic + DA). This is within the overall ceiling of Rs. 1.50 Lacs under Sec. 80 CCE of the Income Tax Act. On Employer's contribution: Up to 10% of Basic & DA (no monetary ceiling) under 80CCD (2). This rebate is over and above 80 CCE limit of Rs 1.50 lacs. From F.Y. 2015-16, subscriber is being allowed tax deduction in addition to the deduction allowed under Sec.

80CCD(1) for contribution in his NPS account subject to maximum of Rs. 50,000/- under Sec. 80CCD 1(B). At present, At the time of exit, the amount utilized for purchase of annuity is tax exempted. From 1 st April, 2016, 40% of the total accumulated corpus under NPS has been made tax free. It is Regulated by the Pension Fund Regulatory & Development Authority (PFRDA) and introduced by the Government of India & respective states so there is not any chance of fraud. It is easy to access pension account & disclosure of information by PFMs in their annual reports. Across all geographical locations and employments across India, PRAN is portable across all the sectors by submitting Inter Sector Shifting form it means same PRAN may be used with new employer or may be used in the individual capacity, if not employed.

NPS with Income Tax

Deduction for Contribution to Pension Account Employee's contribution – Section 80CCD (1) Allowed to an individual who makes deposits to his/her pension account. Maximum deduction allowed is 10% of salary (in case the taxpayer is an employee) or 10% of gross total income (in case the taxpayer being self-employed) or Rs 1, 50,000, whichever is less. Under Section 80CCD of Income Tax where an assessee, being an individual employed by the central Government or any other employer, or any other assessee, being an individual has in the previous year paid or deposited any amount in his account under a pension scheme notified by central Government, he shall, in accordance with, and subject to, the provisions of this section, be allowed a deduction in the computation of his total income, of the whole of the amount so paid or deposited as does not exceed,- a)In the case of employee, 10% of his salary in the previous year; and b)In the any other case, 10% of his

gross total income in the previous year. No deduction is available in respect of employee's contribution which is in excess of 10% of salary of the employee. In case other than employee (Self Employed individuals) which is in excess of 10% of Gross Total Income the excess shall not be taken into consideration for the purpose of section 80CCD. The amount received by the assessee or his nominee from NPS trust shall be taxable in the hands of recipient. For the purpose of this section the assessee shall be deemed not to have received any amount in the previous year if such amount is used for purchasing any annuity plan in the same previous year. The benefit of NPS has been extended to self employed individuals. NPS is optional and NPS trust has been set up to manage the assets and funds of NPS. The deduction under section 80CCD is based on formula of EET (Exempt, Exempt, Taxable) i.e. contribution made to NPS are excluded from Total Income. Accrual of income is Exempt and receipts from NPS shall be taxable in the hands of recipient. Income received from NPS Trust is exempt from tax (Section 10(44)). NPS Trust will receive all the income without deduction of tax at source (Section 197A). Dividend paid to NPS trust is not liable to dividend distribution tax (Section 115-O(1A)). Amount received from NPS is taxable but if the amount is withdrawn to be used for purchasing an annuity plan in the same previous year, it will not be taxable. Sum allowed as deduction under section 80CCD will not be allowed under section 80C. For the purpose of section 80CCD Salary includes DA if the terms of employment so provides, but excludes all other allowances and perquisites. From FY 2017-18 – In the case of a self-employed individual, maximum deduction allowed is 20% of gross salary instead of 10% (earlier subject to a maximum of Rs 1,50,000). However, the combined maximum limit for section 80C, 80CCC and sec 80CCD (1) deduction is Rs 1,50,000, which can be availed. Deduction for self-contribution to NPS – section 80CCD (1B) A new section 80CCD (1B) has been introduced for an additional deduction of up to Rs 50,000 for the amount deposited by a taxpayer to their NPS account. Contributions to Atal Pension Yojana are also eligible. Employer's contribution to NPS – Section 80CCD (2) Additional deduction is allowed for employer's contribution to employee's pension account of up to 10% of the salary of the employee. There is no monetary ceiling on this deduction.

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