Deloitte Tax LLP
Global Employer Services

GES NewsFlash

India – Indian Provident Fund – Significantly Increased Costs for Employers with Assignees Working in India

In this issue:

January 4, 2011

Summary

The Indian government amended the Provident Fund Scheme (PFS) to extend its applicability to 'International Workers' (IWs) with effect from 1 November 2008. As a consequence, most overseas employees assigned to India became liable to pay PF contributions at the rate of 12% with a matching contribution by the employer. The accumulated funds plus interest charges paid by the Indian government would be repayable when the IW completed their assignment in India.

The Indian government has now introduced further amendments to the PFS and has modified the Employee Pension Scheme (EPS) rules. These changes have a significant effect on when the PF funds can be withdrawn and the amount of benefits payable from the accumulated funds. The changes take effect from 11 September 2010 and the details of the new provisions are outlined in this Bulletin.

Key amendments to the Provident Fund

The main amendment to the PFS is that withdrawals are now only permitted in the following circumstances:

- on employee retirement from service upon reaching **58 years** of age; or
- on employee retirement from service on medical grounds as certified by a specified medical practitioner; or
- upon satisfying the conditions specified in the Social Security Agreement (SSA) under which the IW is covered, if applicable

In most cases, withdrawals from the fund can only be paid into the IW's Indian Bank account.

Key amendments to the Employee Pension Scheme (EPS)

Under the existing provisions of the Scheme, a part of the employer contribution, 8.33% of the individual's monthly pay (limited to income of INR 6,500 per month i.e. INR 541) is remitted to the Pension Fund, and the Indian Government makes additional contributions of 1.16% (limited to of INR 6,500 per month i.e. INR 75). Under the new regulations, there will not be any contribution by the Indian Government to the EPS accounts of IWs. Also, the monthly employer contribution may no longer be restricted to 8.33% of 6,500. Rather, it would be computed on the monthly pay. The accumulation to pension fund will be substantially higher going forward resulting in significant funds being locked up.

In addition, IWs from countries with which India does not have a Social Security Agreement (e.g. UK, US, Australia) who previously had been entitled to withdraw pensions on the same basis as domestic Indian employees will no longer be entitled to access these funds.

Further cost and reporting implications

Employers who have put in place loan arrangements to reduce the impact of the PF contribution requirement on their assignees working in India may find their arrangements rendered ineffective due to the delayed withdrawal date. In addition, failure to amend the terms of any loan arrangement may also lead to additional and ongoing income tax liabilities and annual reporting requirements.

Deloitte's View

We understand the amendments to the PF legislation are aimed at encouraging India's trade partners to sign social security agreements, so as to reduce the amount of foreign social security payable by Indian employees assigned overseas. India has signed eleven social security agreements, but only two are in force at present (with Belgium and Germany).

The PF and EPS amendments will significantly increase the cost of Indian assignments and employers will have to factor this additional cost into their assignment budgeting processes. Without action, PF contributions will, in most circumstances, have to be regarded as a "lost cost" for employers assigning employees to India.

It is therefore vital that employers with IWs already in India, and those which intend to send IWs to India in the near future, take appropriate action to minimise the impact of the changes and take steps to become compliant if they are not already so.

Cost Mitigation

Given the impact of the latest amendments, from an assignment cost perspective it is increasingly important to consider ways of minimising, or eliminating completely the requirement to pay to PF contributions.

Deloitte can advise you on planning opportunities to achieve this through:

- Configuring assignee remuneration packages for new assignments to arrive at optimum compensation subject to PF contributions.
- Structuring assignment arrangements and policies for secondment of workers to India.

People to Contact

If you have any questions concerning the issues in this GES NewsFlash, please contact one of the tax professionals as follows:

Rajesh Srinivasan
Tel: +91 (44) 6688 5007

John Weekes
Tel: 0207 007 1466

George Milmine
Tel: 0207 007 6783

This NewsFlash information is also included in our bi-weekly GES newsletter, *Global InSight*, which you will receive directly if you are on the central distribution list.

If you are not on the central distribution list and received this communication by some other means, you can follow these few simple steps to be added to the central distribution list.

- Go to the Deloitte Subscriptions Page on Deloitte.com
- Make sure that under Step 1 you select “Tax” and “Global Employer Services”
- Under Step 2, select “Global Insight”
- Under Step 3, fill out your contact information and click “Save my profile”

Be sure to visit us at our Web site: www.deloitte.com/tax

Back to Top

1633 Broadway
New York, NY 10019 – 6754
United States