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**No BPS/ SG/pension/I.Tax/018/1** **Dated: 23.11.2018**

**To**
**The Arun jaitley ji**
**Honourable Cabinet Minister for Finance**
**Government of India**

**Subject : Pension of ex-Govt employees to be net of Income Tax**

Sir,

With passage of time, the purchase value of pension due to steep rise in the cost of food items,caregivers and medical facilities etc gets substantially reduced.Due to inflation coupled with low interest rates value of their deposits in Banks/Post offices etc too go on reducing year by year adversely affecting the net-worth of Pensioners.Thus compelling them to compromise their standard of dignified living.

As was worked out & recommended by TECS (Tata Economic Consultancy Services) consultant to Vth CPC (Para 127.9 Vol III 5th CPC report) Pension need to be 67% of the last drawn to enable a pensioner to live with the same standard to which he was living while in service (Supreme Court pronouncement in DS Nakara vs UOI) but only 50% of last drawn is being paid. Old age relief given to Sr citizen in Income tax is too little to compensate.

You are therefore, requested to reconsider & accept the recommendation of Vth CPC vide their 167.11(copy attached) in this regard and spare the pension/family pension along with DR & FMA from the levy of income-tax.

Further to compensate fall in purchase value of their savings in deposits with banks & post offices rate of interests for senior citizens on their deposits should be 2% above the normal rate of interests as against the existing 0.25% to 0.50%.

Hoping for your sympathetic consideration

Thanking you in anticipation
With Regards
Sincerely yours,

DA/Vth CPC report on Income tax on Salaries & Pensions

Maheshwari

S.C.Maheshwari
Secy Genl Bharat Pensioners Samaj

Vth CPC report

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# Income Tax on Salaries and Pensions

## INTRODUCTION

*Existing Law of Income Tax*

167.1 The law of Income Tax being followed at present in India is enshrined in the Income Tax Act, 1961. As per Section 4 of this Act, all individuals having taxable income exceeding Rs.40,000 are liable to pay income tax. Taxable income comprises all incomes received by, or accruing or arising to, a tax payer during the previous year and includes income chargeable to income tax under the head `salaries' as per Section 15 of the Income Tax Act, 1961. Salaries payable to its employees by the Central Government are chargeable to income tax under this Section. The total income tax collection from Central Government employees accounts for three per cent of the total tax revenue.

*Taxability of Allowance*

167.2 Income tax is not only deducted on the basic salary but also on various allowances, including those which have been given to counter inflation. These provisions are equally applicable to employees of public sector undertakings and the private sector. In their case, however, there are two major differences. Firstly, the allowances are very liberal and already include an adequate cushion for payment of income tax thereon. Secondly, many companies pay the tax on their employees' salaries and allowances, or give them the equivalent amount in cash outside their legitimate account books. On the other hand, the allowances of Government employees compare poorly with those available in the other sectors and even these are subjected to income tax.

## STUDY REPORT

*Observations made by FRF*

167.3 In our sponsored study on `feasibility of exempting the salaries of Government employees from income tax', the Fiscal Research Foundation (FRF) has favoured complete exemption of salaries paid by the Government to its employees from income tax. It has been pointed out that such provisions already exist in neighbouring countries like **Sri Lanka**. In case the entire salary is not exempted from income tax, the FRF has strongly favoured exclusion of various allowances which are in the nature of a compensation payment to employees for erosion in the real value of their salaries resulting from price rise. Complete exemption of pensions received by Government employees from income tax has also been suggested.

*Exemption not a good option*

167.4 We have considered these recommendations. Although there is considerable merit in the suggestions offered by FRF, it may be difficult for the Central Government to exempt only its own employees from income tax in respect of their salaries, allowances and pensions. Although it is legally possible to treat Central Government employees as a special category for purposes of income tax, it may not be equitable to do so without according the same treatment to other employees. **We would, therefore, not favour exemption of Central Government employees from tax as a good option.**

*Salaries net of tax*

167.5 However, it is a fact that it has not been possible for us to fully meet the aspirations of Central Government employees in respect of both salaries and allowances. As has been shown so vividly by the IIPA study on the emoluments received by senior employees, a salary level of Rs.36,000 is what we should have given to a Secretary if it was a taxable salary. Against this, we have recommended a salary of Rs.26,000 only. **It is, therefore, only reasonable that such a moderate salary should be net of tax**.

*Hastening slowly*

167.6 This is an area where we would like to tread with circumspection. Much though we would have liked to make the full emoluments of Government employees net of income tax, **we have decided to start with allowances and pensions only, as a first step.**

*Allowances net of tax*

167.7 The logic of giving allowances net of tax is irrefutable. Government decides a particular basic salary. Other allowances are added only to ensure that the real value of the basic salary is not eroded due to cost of living, or to provide partial reimbursement of expenses incurred on certain items of expenditure like house rent, children's education, entertainment and the like. **If such allowances are taxed, then either the basic salary gets eroded in its real value from year to year or the partial reimbursement of expenditure incurred on certain items becomes less and less with the passage of time**. In both the cases, the objective of giving allowances is partially nullified. As noted earlier, the private sector has both open and covert methods of solving this problem, but Government has so far left its employees totally vulnerable to this malaise.

*Present position in MEA*

167.8 There is just one exception. We have noticed that the Ministry of External Affairs pays 'net of tax' salaries to its employees on foreign postings. Provision for paying net of tax salary already exists under Section 195A of the Income Tax Act. Under this Section, the employees do not have to pay income tax on the salaries received by them and it is the liability of the employer to calculate the tax leviable on such salaries and pay the same to the income tax department.

*Extension of 'net of tax' concept to all employees*

167.9 **The solution to the problem of Central Government employees in general, therefore, lies in the application of this legal provision.** If the precedent of the Ministry of External Affairs is implemented in the rest of the Government, Government employees would not have to pay any income tax on the emoluments received by them from the Government and it would be the liability of the concerned departments to calculate the tax leviable and, through book adjustment, credit the Tax Revenue Head. But, as stated earlier, we would like to tread this road with caution and make a beginning with allowances and pensions in the first place.

## OUR RECOMMENDATIONS

*Allowances*

167.10 **Accordingly, we recommend that all the allowances of Central Government employees, including those of various union territories, may henceforth be paid net of taxes.** These allowances will include Dearness Allowance too. There is just one snag here. One of our recommendations suggests that Dearness Allowance should be merged into pay for all purposes, whenever the cost of living index rises by 50%. Thus every 3-4 years, the D.A. component, which would be net of tax till then, would be converted into basic pay and therefore remain net of tax no longer. This will cause great hardship to Government employees. It will be logical to continue the tax relief on this D.A. component even after its merger with basic pay. **In the case of Dearness Allowance, therefore, we may extend the tax concession to such part of D.A. as may be converted into Dearness Pay from time to time.**

*Pensions*

167.11 The above concessions, however, will not bring much of a relief to pensioners, as in their case, apart from Dearness Relief, no other allowances are available. We note that in recent times the Government has shown genuine concern for senior citizens and various tax reliefs are already available to them beyond the age of 65 years under section 88B of the I.T. Act. **We are of the opinion that retired Government employees in their old age deserve sympathy and accordingly recommend that pensions including dearness relief of all retired Central Government employees may be paid net of taxes.**

*Procedure for payment of tax*

167.12 As regards the procedure for payment of income tax on allowances and pensions, we would like to make it as uncomplicated as possible. **The simplest solution is for the Department of Personnel to make a lumpsum payment on account of tax on allowances on behalf of all Government employees to the Department of Revenue, and for the Department of Pensions to do the same with regard to pensions.** Such lumpsum payments will ensure that there is no loss of revenue as far as income tax collections are concerned, and no unnecessary paperwork is generated for Government offices across the country