PalArch's Journal of Archaeology of Egypt / Egyptology

IMPACT OF COVID-19 ON EMPLOYMENT: A TAXATION CONUNDRUM

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Bineet Kedia and Tanushree Gupta , Impact Of Covid-19 On Employment: A Taxation Conundrum , Palarch's Journal Of Archaeology Of Egypt/Egyptology 18(7). ISSN 1567-214x.

Keywords: Covid-19, Lockdown, Pay cuts, Tax implication, Tax planning.

ABSTRACT:

As we all know that this covid-19 has affected not only India but almost every part of the world. Every country imposed lockdown to safeguard the life of their citizen. In India, the lockdown was first imposed on 24th of March, 2020 by our Prime Minister Narendra Modi. At present, India is unlocking the lockdown through phase wise looking into the threat of pandemic Covid-19 virus. As we know, during this lockdown businesses were shut, which results in detrimental impact on business operation of many entities in India and globally. For instance, company like Maruti Suzuki has not been able to sale single car in India in the month of April 2020. To overcome this crisis many companies have implemented stringent ways, which includes job reduction, salary cut and deferment of salary. So in this paper, we shall be discussing all such measures and tax implication thereof in the hands of employees.

INTRODUCTION:

Covid-19 pandemic has severely affected the economic activity and unprecedented skill. Due to this long lockdown of the Indian market, many employees have lost their jobs and it is unfortunate that many companies are firing their employees. According to a Layoff

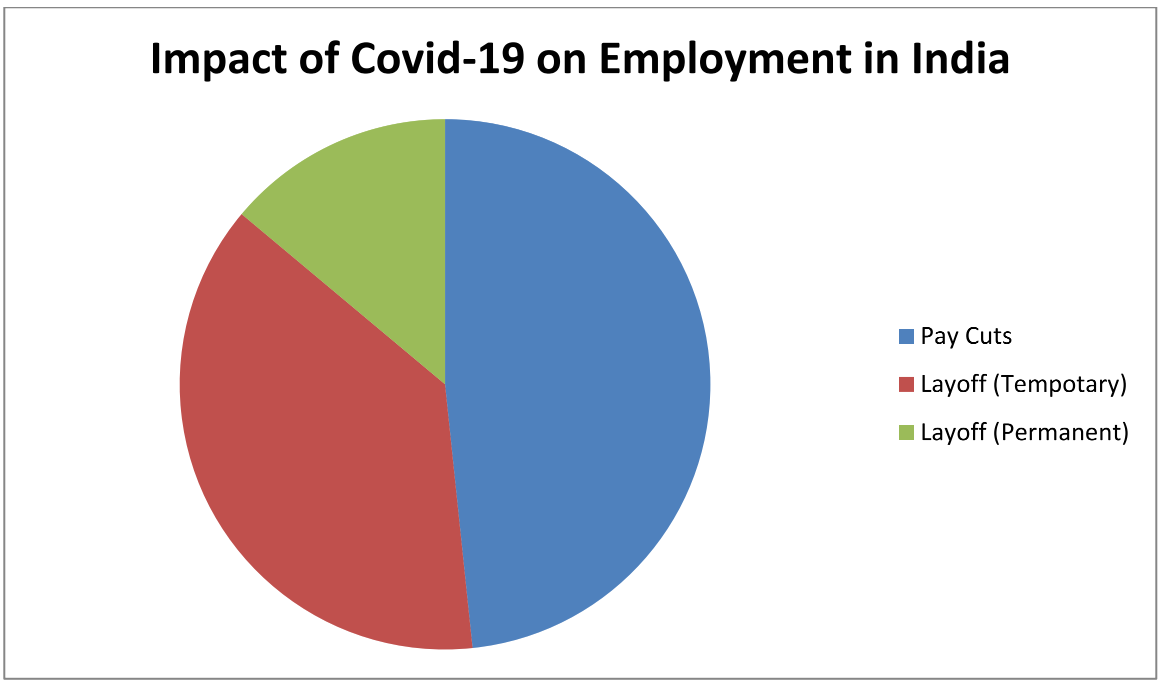
Survey 2020, sixty eight percent of surveyed employers have already started pay cuts/layoff or are planning to do so.[1]

The survey conducted from 1st May 2020 to 10th May 2020 covered 1,124 companies across 11 industry sectors in 25 major cities. The result of the survey says that about seventy three percent employers have for pay cuts, fifty seven percent are doing temporary layoff and twenty one percent have already done permanent lay off. However, it is good to know that about thirty two percent of the organizations are ready to face the difficulties even in this Covid-19 crisis and have not made any play of pay cuts or layoff.[2]

Interestingly, 32 per cent employers did not have any job cut/layoff plans. "All industries are suffering in the current pandemic situation and the pain is now translating into layoff in every industry at every level. Companies are even cutting salaries of those employees whom they are planning to retain.[3]

According to Rajesh Kumar[4]

"This crisis is very much temporary and once companies come out of this, new job creation and hiring will surely start."



[1] The survey was conducted by MyHiringClub.com and Sarkari-Naukri.info
[2] Read more at: https://economictimes.indiatimes.com/jobs/covid-19-effect-organised-private-sector-planning-layoffs-salary cut/articleshow/75736642.cms?utm_source=contentofinterest&utm_medium=text&utm_campaign=cppst
[3]Ibid
[4]CEO, MyHiringClub.com & Sarkari-Naukri.info.

It is also seen that many employers are exploring the situations by non-cash compensation like ease off and long term incentive plans to handle the situation of immediate cash back. As off, the finance minister Ms. Nirmala Sitaraman has already reduced the rate of TDS and TCS by twenty five percent of specified payments but the TDS rate of salary has not been reduced. TDS on salaries are paid on average rate so that an employee should not be liable to pay tax at the time of filing his/her annual income tax return. Thus, it can be concluded that TDS rate on salary has not been reduced to prevent the salaries people from facing tax burden at the year end and also not liable to pay advance tax on regular intervals. In order to understand the impact of Covid-19 on employees and how can they minimize its affect on take home pay, this paper will broadly focus on following five points:

1. Tax implications on pay cuts
2. Tax implications in case of deferment of salary
3. Tax treatment of allowances due to lockdown
4. Issues involved in withdrawal from saving schemes
5. Changes in the rule for contribution to provident fund

Before we jump to discuss the abovementioned issues, let's first understand the taxability of salary and applicability of TDS thereof. The Income Tax Act provides that the salary is taxable on due or received basis, which ever happens earlier.[5] Taxable salary includes allowances, perquisites, retirement benefits, profit in lieu of salary etc.[6] Certain deductions are also allowed from salary income.[7] TDS is deduction under section 192 of the Income Tax Act at the time of payment of salary. So every person responsible for paying any income chargeable under the head salary is required to deducted taxes there from.[8] Thus the estimated tax liability of the employee recovered from his monthly salary income over the financial year and this tax is deducted at the time of payment of salary.

TAX IMPLICATIONS ON PAY CUTS:

Before discussing the tax implication in the hand of employees when there is a salary cut issue due to ongoing crisis, we want to clarify that the implication which we are discussing shall apply whenever there is a pay cut,[9] but no where it means that these

[5]As per section 15 of the Act, following income shall be chargeable to income-tax under the head "Salaries"—

a) any salary due from an employer or a former employer to an assessee in the previous year, whether paid or not;
b) any salary paid or allowed to him in the previous year by or on behalf of an employer or a former employer though not due or before it became due to him;
c) any arrears of salary paid or allowed to him in the previous year by or on behalf of an employer or a former employer, if not charged to income-tax for any earlier previous year.

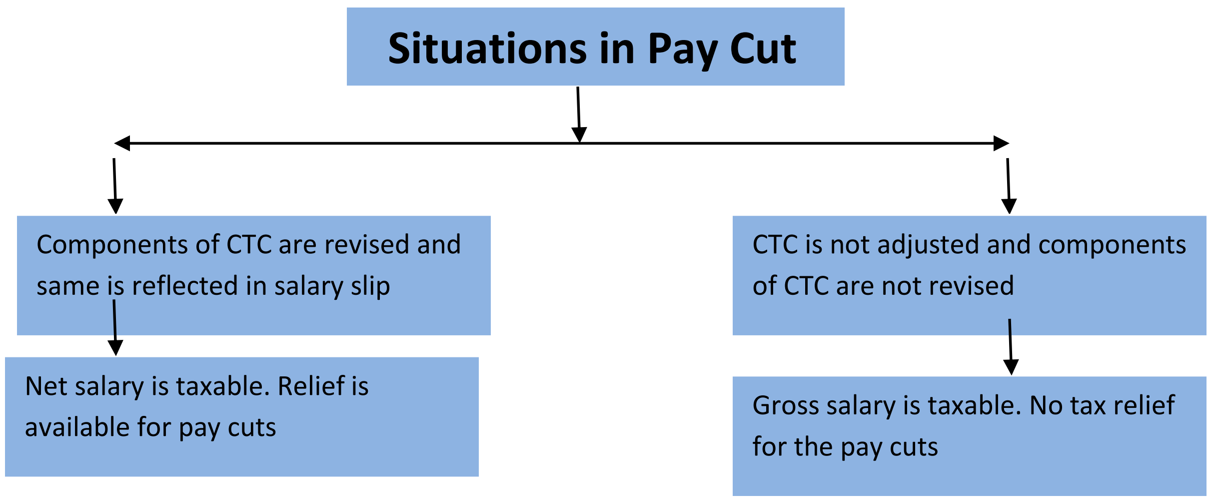
[6] Section 17 of the Income Tax Act

[7] Section 16 of the Income Tax Act

[8]Section 192 (1) says: "Any person responsible for paying any income chargeable under the head "Salaries" shall, at the time of payment, deduct income-tax on the amount payable at the average rate of income-tax computed on the basis of the rates in force for the financial year in which the payment is made, on the estimated income of the assessee under this head for that financial year".

[9] Pay cut is a situation where the amount deducted by the employer is not payable at all, i.e., employee has lost the right to receive this amount.

provisions are applicable only if the pay cut is because of Covid-19. Pay cut can happen in two possible situations:



The first one is, when the employer revises the 'cost to company' (herein after mentioned as CTC) and same is reflected in the salary slip of the employee and the other situation is that the CTC might not be reflected in the employee's salary slip, since the CTC has not been revised. If the CTC of an employee undergo any revision, i.e., cut or hike, than such revision should be reflected in the employee's salary slip as well. Thus, it means that the component of the salary, such as basic pay, house rent allowance (HRA), special allowances should be revised correspondingly. Considering the fact that income from salary is taxable on due basis, it will be taxable in the hands of employee, whether received or not. Hence, if CTC is not adjusted and components of salary are not revised accordingly, than the income tax officer will consider employee's salary slip for the purpose of considering his income under the head salary and tax thereof. Further, it is known to everyone that employer is required to deduct TDS from salary at the time of payment only. Therefore, in case employer has cut employee's salary and has not revised his CTC than he might be liable to pay tax on entire salary; even if the same is not received by him.[10]

The finance Act, 2020 has introduced an alternative tax regime for the individual tax payers from the financial year 2020-21 onwards. There are multiple factors which an employee needs to consider while deciding which tax regime to opt for. Income tax department issued a circular on 13th April 2020 wherein it has been provided that tax payers intending to opt for new regime may convey his intention to employer and the employer after receipt of such information from employee shall compute total income and deduct TDS as per provision of section 115BAC. And in the absence of any such intimation, employer shall calculate TDS without considering the provision of section 115BAC, i.e., as per normal provision of the Income Tax Act. Reason for discussing section 115BAC is that, there might be possibility an employee who has conveyed his intention to employer to opt for old

[10]Preeti Motiani , 'Got a pay cut? You may still be taxed on your original CTC ', ET Online; for more detail see, https://economictimes.indiatimes.com/wealth/tax/got-a-pay-cut-you-may-still-be-taxed-on-your-original-ctc/articleshow/75844000.cms?from=mdr

tax regime would like to switch to new tax regime considering his revised annual income due to pay cuts and the amount he can spare for making tax saving investments. New tax regime provides for low tax rates with seven tax slab and assessee (i.e., employee) is not required to make investment in order to save tax. It will leave more money at its disposal. But the challenge here is that the intimation made to employer cannot be changed by the employee during the year. Hence, the employer will continue to deduct TDS as per the intimation submitted to him. However, the employee may opt for different option at the time of his income tax filling. And if there is any excess or short fall in the deduction of tax because of changing option, that can be paid or claimed as refund respectively at the time of filing income tax return (ITR).

TAX IMPLICATIONS IN CASE OF DEFERMENT OF SALARY:

The term 'deferment of salary' means shift in the payment of some portion of salary. This implies that the component of salary in with read by employer and shall be paid on a later date. Many companies are not doing pay cuts but delaying certain part of salary because of liquidity issues. In case, if employee's salary has just been deferred and will be paid to him after a period to time, it will be included in his taxable salary for the period, irrespective of the fact that it is not yet received. Deferment will not anyway affect the ultimate taxability as the salary is still due and will be received later on.

The issue which will arise here is that TDS will not be deducted by employer as the same is deductible at the time of payment of salary. Now, if employee's salary is deferred, the employer is liable to deduct TDS at the time of payment, but it will remain taxable in the hands of employee on due basis. Now since his salary (i.e., due amount) is taxable in the hand of employee even if the deferred amount is not paid and the employer has not deducted the TDS thereon, technically it is responsibility of the employee to pay advance tax on that extra amount. Therefore, if not TDS is deducted and employee fails to pay the advance tax, he may be liable to pay interest and penalty.[11]

TAX TREATMENT OF ALLOWANCES DUE TO LOCKDOWN:

The term 'allowance' means additional components of salary which are given regularly to the employees for the purpose of meeting specific expenditure; such as, Dearness Allowance, House Rent Allowance, Transport Allowance, Servant Allowance etc. Allowances are generally fixed, irrespective of actual expenditure and are taxable. However, some exemptions are allowed under the Income Tax Act.[12] Certain allowances are exempted from tax to the extent spent by the employees, such as conveyance allowance. If the allowances are not spent, they are taxable.

The current situation is such that the employees are forced to work from home and it is not possible for them to spend these allowances for the designated purposes. Given this situation, the allowances will attract tax. Thus, depending upon the specific provision

[11] Section 234 B and section 234C of the Income Tax Act

[12] Taxability of the allowances are three different type. First, fully taxable such as Dearness Allowance; Second, fully exempted, such as allowances paid to judges of Supreme Court and high courts and third, partly taxable and partly exempted, such as House Rent Allowance. For more detail see, section 17 and section 10 of the Income Tax Act.

providing taxability and considering the exemptions let down, the allowances will be taxable in the hand of employees.[13]

WITHDRAWAL FROM SAVING SCHEME:

We have seen that many people these days are making withdrawal from saving schemes to meet their day to day expenses. This is on account of cash flew issues faced by them due to losses. Some people are making withdrawal because of the rumors that their money is not safe in the bank and post office due to this corona situation in the country.

These withdrawals may be necessary, but the assessee must remindful of tax implication as it may lead to additional tax cost. The Indian government has allowed partial withdrawal in the light of Covid-19 out break from EPF account. So now EPF subscriber can withdraw seventy five percent of their savings up to the maximum of three months basic pay and dearness allowance. And for this purpose, no certificate or documents are required to be submitted by the employee and his employer. The amounts withdrawn by the employee due to the outbreak of Covid-19 are non-refundable. Therefore, he is not required to refund the withdrawn amount back into his EPF amount.[14] But the government has not relaxed the conditions of withdrawal from other saving schemes. So, pre-mature withdrawal of other schemes may attract some penal charges and have tax implication as well. And there are different set of rules of withdrawal from different schemes. So before making the withdrawal, an employee should know the tax implication on it.[15]

CHANGES IN THE RULE FOR CONTRIBUTION TO PROVIDENT FUND:

The government has also relaxed in rules of making EPF contribution. Recently, EPFO waived off the penal damages for delay in deposit during the lockdown period.[16] The other major change is reduced employer's contribution to employee's EPF account from twelve percent to ten percent. On 26th March, 2020 the Indian government announced Pradhan Mantri Garib Kalyan Yojna (PMGKY) package for helping the poor to fight from corona virus pandemic. Central government has said that it will contribute twenty four percent of the employee's salary (i.e. twelve percent share of both employer and employee) as EPF in their EPF accont.[17] It is applicable to employees working in firm having up to hundred workers of which ninety percent are having salary not more than Rs. 15,000 per month. Earlier it was announced for three months, i.e., March, April and May; but at the

[13] Navneet Dubey, '10 salary components that can help employees reduce tax burden', ET Online; for more detail see, https://economictimes.indiatimes.com/wealth/tax/10-salary-components-that-can-help-employees-reduce-tax-burden/articleshow/70259461.cms?from=mdr

[14] 'Are you withdrawing from Public Provident Fund, NPS, FD, PF, NSC? Must check these tax implications'; for more detail see https://www.financialexpress.com/money/cash-crunch-covid-withdrawing-from-savings-check-tax-impact/1955518/

[15] See, http://www.taxmann.com/small-saving-schemes.aspx

[16] https://www.epfindia.gov.in/site_en/covid19.php

[17] *Ibid*

time of announcing AatmNirbhar Bharat package the finance minister Ms. Nirmala Sitaraman extended it for another three months, i.e., June, July and August.[18]

The reduction in EPF contribution was announced by finance minister Ms. Nirmala Sitaraman as a part of AatmNirbhar Bharat package to provide some release to employer and also increase the take home pay of the employees. The statutory rate of EPF contribution of both employer and employee has been reduced to ten percent of basic pay and dearness allowance from existing rate of twelve percent.[19] This shall increase the take home pay of employees and relief people financial burden to certain extent. But at the same time the employees need to recalculate their tax saving, so that they need not pay extra taxes because of increased in-hand salary. This benefit of reduced rate of contribution from twelve percent to ten percent is applicable for three months of May, June and July. The reduced rate is not applicable to the establishment like Central and State Public sector enterprise and establishment controlled by the central government or state government. Further, the reduced rate is also not applicable to the establishment eligible for Pradhan Mantri Garib Kalyan Yojna (PMGKY) package. Since, the entire contribution for those establishments (i.e., twenty four percent of salary) is being contributed by the central government. However, one should need to keep in mind that the reduced rate of contribution is minimum rate of contribution during period of package. The employer, employee or both can contribute at higher rate also.[20]

CONCLUSION:

Every employee will have to make sure that he does not face such situation bearing that he has not received salary and paying taxes thereof; as this is going to be double hit on him. To avoid such circumstances, certain points must be strictly taken care of. If the salary has been cut, employee must insist on the written communication from his employer and ensure that cut gets reflected in all the components of the salary as well. It is advisable that he gets clarification from his employer as to whether the deduction from salary is a pay cut or deferment of payment, because treatments in both the cases are different. Employee should also ensure that the revise salary is completely evidence through a revision in the appointment letter and pay slip. Taxable salary is very much dependent on how the pay cut is administrated and the documentation around it. Ultimately at year end employee's tax liability will be decided by TDS deducted, which is reflected in Form-16 issued by the employer. So make sure that employer correctly reports your salary for the year end deduction.[21]

Deferment of payment of salary does not attract any provision in the contractual terms agreed between the employer and employee. The employee only needs to take care on the basis of calculation so that he does not end up becoming a defaulter due to non-payment of advance taxes.[22] However, there is no guarantee that the deferred salary will be paid to

[18]'Key Highlights of the Finance Minister's whole economic package'; for more detail see, https://bfsi.economictimes.indiatimes.com/news/policy/key-highlights-of-the-finance-ministers-whole-economic-package/75797903

[19] For more detail see, the Employees' Provident Funds and Miscellaneous Provisions Act, 1952

[20]*Supra note 18*

[21]*Supra note 10*

[22]*Supra note 11*

the employee ever or not. And if this case happens, it affects the employees from all corners.[23]

Taxing the allowances which cannot be used due to lockdown is neither morally not legally wrong. But, it may disturb the tax planning of an employee. Employee is not required to do much, but need to be extra careful and making the tax planning in proper consultation with financial expert in order to avoid the extra tax liability.[24]

There are different set of rules for withdrawal for different schemes. So, before making withdrawal employee should consider the tax implication on it.[25]

Reducing the rate of employer's and employee's contribution to EPF account can be seen as both benefit and loss from the side of employee. It will be beneficial for the employees who need more money in his hand to deal with the lockdown situation, but loss for the employees whose earlier take-home salary was enough for dealing the lockdown situation. Though it is being said that this reduction in rate of EPF contribution is optional and they can contribute at higher rate also, but many organizations taking the undue benefits of the power have compulsorily reduced the rate of contribution in EPF account.[26]

[23] Employees of 'Jet Airways' were liable to pay tax on salary which was due even though not received. Interesting fact is that the employees are not assured whether they will ever receive due salary or not, as the airline is already closed.

[24] *Supra note 13*

[25] *Supra note 15*

[26] *Supra note 20*