

Expatriates Confront Social Security Changes in India

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Many Indian companies are sending their employees abroad, to work. At the same time, foreign nationals employed by multinational companies outside India are also sent on assignment to India. The period of their international assignment may vary from a few months to a few years. These cross-border transfers have given rise to a multitude of issues of both a tax and regulatory nature. Among the most complicated and important issues is social security.

Indian employees sent to other countries are generally required to contribute towards the social security system as per the laws of the respective host country. In the absence of any totalization agreement between India and the host country, those Indian employees sent to other countries are required to make mandatory contributions towards the host country social security system. Further, generally speaking, according to the social security system of the

host country, the assignees in that country are entitled to social security coverage typically only when there is a contribution for a minimum prescribed period (e.g., 10 years in the case of the U.S.A.).

With many assignees working in other countries generally not on long-term assignments, they could be losing out on the potential benefits to be provided at a later date under the social security system of the host country.

In addition, when no totalization agreement exists, or employers and employees are caught unaware and fail to be compliant, the cost of overseas assignments can mount for companies.

Background

The Employees' Provident Fund Organization ("EPFO"), is a statutory body of the government of India under the Ministry of Labour and Employment ("MoLE"). It administers a compulsory contributory provident fund, pension, and insurance schemes for the Indian workforce.

The Employees' Provident Funds and Miscellaneous Provisions Act, 1952 ("the Act") was enacted by Parliament and came into force with effect from 14 March 1952. Presently, the following three schemes are in operation:

- Employees' Provident Funds Scheme, 1952 ("EPFS")
- Employees' Pension Scheme, 1995 ("EPS")
- Employees' Deposit-Linked Insurance Scheme, 1976 ("EDLS").

Until October 2008, foreign nationals sent to India were required to contribute towards the Indian social security system only if their salary did not exceed INR 6,500 per month. As foreign nationals working in India generally are paid salaries in excess of INR 6,500 per month, they typically fell outside the ambit of the Provident Fund ("PF") regulations in India.

In order to level the playing field, the government of India in its notification dated 1 October 2008, widened the scope of the EPFS and the EPS to include a specific category of workers known as "International Workers" (or "IWs"). The salary limit above

which these IWs/employees and their employers were not required to contribute to a provident fund was removed for such IWs, thereby, bringing them within the ambit of the PF regulations.

IWs are defined to include foreign nationals working for an establishment in India to which the PF legislation applies and Indian employees sent (deputed) to a country with which India has entered into a social security agreement ("SSA" also known as a totalization agreement). Therefore, with effect from 1 November 2008, IWs (other than excluded employees) and their employers are required to make Indian social security contributions at 12 percent of monthly pay. However, under the rules, IWs were allowed to withdraw the accumulated balance available in their PF accounts immediately upon completion of their assignments in India.

Recent Changes in the Employees' Provident Fund and Pension Scheme

The MoLE issued a Notification in September 2010, which has imposed further restrictions on the withdrawal of PF balances vis-à-vis the IWs, in addition to other changes to pension contribution rules.

Various reports in the press suggest that the recent changes in the EPFS and the EPS are prompted by the issues several countries have had tied to signing totalization agreements with India despite the changes that were made to the PF regulations in 2008.

Below, we describe in brief, recent changes to the EPFS and EPS in the case of IWs.

Amendments to EPFS

Withdrawal – Position before Amendments

A member of the PF (including IWs) could withdraw the full amount of the credit in the fund on retirement from service after attaining the age of 55. The PF amount could also be withdrawn before the age of 55 years under the following circumstances, amongst others:

- at the time of termination of service;
- upon migration from India for permanent settlement abroad or for taking employment abroad.

Withdrawal – Position after Amendments

Situations under which IWs can withdraw sums from the PF:

- On retirement from service after attaining 58 years of age.
- In case of permanent and total incapacity to work or suffering from tuberculosis, leprosy, or cancer, even if contracted after leaving service.
- In respect of the member covered under an SSA, on such grounds as specified in such SSA.

Therefore, in respect of members from non-SSA countries, withdrawal is possible only on retirement from service after attaining 58 years of age, or in case of permanent and total incapacity to work or suffering from tuberculosis, leprosy, or cancer, even if contracted after leaving service.

Payment – Position before Amendments

The amount due shall be payable to the credit of the employee's bank account in India.

Payment – Position after Amendments

In respect of the IWs covered under an SSA, the payment shall be made in the manner as specified in such SSA. In all other cases, the amount due shall be payable to the credit of the IW's bank account in India.

Exchange Rate to Be Used to Convert Salary Paid in Foreign Currency into INR – Position before Amendments

No method specified.

Exchange Rate to Be Used to Convert Salary Paid in Foreign Currency into INR – Position after Amendments

A telegraphic transfer buying rate offered by the State Bank of India as on the last working day of the month in which the salary is due is to be used.

Amendments to EPS

Government Contribution – Position before Amendments

The government of India contributed 1.16 percent of monthly pay subject to a maximum of INR 75 per month (1.16 percent of INR 6,500) to the Pension Fund.

Government Contribution – Position after Amendments

The government of India will no longer make any contributions to the IWs Pension Fund.

Employer Contribution – Position before Amendments (from November 2008 until August 2010)

With respect to contributions under the EPS, out of the employer's contribution of 12 percent, 8.33



percent (subject to maximum cap of INR 6,500 p.a) was required to be contributed towards the pension scheme.

Employer Contribution – Position after Amendments (with effect from September 2010)

The upper limit of INR 6,500 has been removed. Hence a full 8.33 percent of the employee's total monthly salary gets contributed to the pension scheme.

Withdrawal – Position before Amendments (from November 2008 until August 2010)

IWs coming from a country with which India does not have a SSA, will be allowed to withdraw the benefit only where the principle of reciprocity applies.

Withdrawal – Position after Amendments (with effect from September 2010)

In the case of IWs seconded from a country with which India does not have an SSA, there is insufficient clarity as to whether they will be entitled to any pension benefits. Further clarification in this regard is awaited from the EPFO.

Impact on IWs

- IWs coming from non-SSA countries will only be eligible to withdraw their PF balances on retirement from service after attaining 58 years of age, or in case of permanent and total incapacity to work or suffering from tuberculosis, leprosy, or cancer, even if contracted after leaving service. This would block large amounts of contributions made by IWs and their employers and could cause potential financial hardships to IWs who were making contributions to the PFs in the hope that they could withdraw the PF balance in their accounts upon completion of their assignments in India.
- IWs will need to keep their bank accounts in India open, long after their departure from India until the refunds are received in such accounts.
- In the case of IWs coming from countries with which India has an SSA, withdrawals of PF sums (if any) will be governed by the respective provisions of the applicable SSAs.

- Employees who qualify as IWs would have to make much higher pension contributions (and correspondingly lower PF contributions) and this may have to be treated as a “sunk” cost as there is no clarity with regard to the withdrawal of pension benefits.
- Further, with effect from 1 April 2011, where the PF account becomes “inoperative” (i.e., for a period of 36 months from the date it becomes payable and no application for withdrawal or transfer has been made) interest currently payable at 8.5 percent p.a. (applicable for Financial Year 2009-10) may not be paid on the balance remaining in such accounts. Clarifications are further awaited with regard to whether the accounts of IWs will also cease to earn interest when their accounts become inoperative after they leave India and return to their home countries, as these workers are allowed to withdraw only upon reaching 58 years of age (subject to certain exceptions as mentioned above).

Open Issues

There are several issues remaining at this stage subsequent to the above-noted amendments.

- An Indian employee going out of India on an assignment to a country with which India has entered into an SSA is also considered an IW. It is not clear as to whether (1) he or she will continue to qualify as an IW even after he or she returns to India after completing the overseas assignment and (2) he or she will be governed by these changes.
- The question remains as to whether the withdrawal applications filed in the cases of employees who have completed their Indian assignments before this amendment will be accepted by the PF authorities.
- In addition, there is some ambiguity concerning the feasibility of keeping bank accounts open in India until the employee reaches the age of 58 years, even after leaving India and the Indian employment visa expires.

Summary

In summary, the changes to India’s pension system, especially as they concern foreign national employees in India, will not only impact new IWs, but will also impact IWs who are already on assignment. IWs already in India who have made significant social security contributions will have to await the attainment of 58 years of age before they can withdraw their contributions.

Trade and industry associations are making representations to the relevant ministries in order to seek some relaxation of the recent amendments.

Further clarifications from the PF authorities in relation to these amendments by way of a “frequently asked questions” (FAQs) – or other method – are awaited. Hopefully, such clarifications will help resolve many of the outstanding issues tied to these amendments.

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