

Tax treatment of Pension

Pension is a retirement benefit. Since this is payable to an employee or to his dependents by virtue of past employment, this is taxed as salary in the hands of the employee. However, family pension received by the dependents of the employee will be taxed under the head income from other sources as there is no employer employee relationship between the payer and payee.

The provisions under Income Tax is enumerated below:-

S.No	Particulars	Tax treatment
1	Pension is received from UNO by the employee or his family members	It is not chargeable to tax
2	Family pension received by the family members of armed forces (after the death of the employee)	It is exempt under section 10 (19) in some cases.
3	Family pension received by the family members of other cases (after the death of the employee)	It is taxable in the hands of recipients under section 56 under the head 'income from other sources'. Standard deduction is available under section 57 which is 1/3 of such pension or Rs. 15000, whichever is lower.
4	Pension received by an employee (during his lifetime) in any other cases.	Tax treatment depends on whether Pension is Commuted or Uncommuted pension:- 1. Uncommuted Pension :- This is a periodical payment of pension. This is always chargeable to tax. 2. Commuted Pension:- This is a lumpsum payment in lieu of periodical payments. a]. For Govt Employees - fully exempt from tax b]. For other employees:- i] If Gratuity is received - One-third of the pension, which he is normally entitled to receive, is exempt. ii]. If Gratuity is not received - One-half of the pension which he is normally entitled to receive is exempt.

Example: 1

Mr. X retires from Govt service as on May 31, 2012. He gets pension of Rs. 15,000 per month up to December 31, 2012. With effect from January 1, 2013, he gets One third of his pension commuted for Rs. 10,00,000 . He is not in receipt of Gratuity.

Solution:-

Uncommuted pension [periodical payments] is always chargeable to tax. Commuted pension is exempt from tax in the case of Government Employees. Therefore, commuted pension of Rs. 10,00,000/- is exempt. The amount of taxable uncommuted pension is calculated as under:

Uncommuted pension June 1 to Dec 31, 2012 = Rs.1,05,000/-
[ie Rs. 15000 x 7].

Uncommuted pension Jan 2013 to March 2013 = Rs. 30,000/-
[Rs. 15,000 x 2/3 x 3].

Total amount of uncommuted pension chargeable to tax = **1,35,000 /-**

Example: 2

Mr. X retires from ABC Ltd as on June 30, 2012. He gets pension of Rs. 20,000 per month up to Jan 31, 2013. With effect from Feb 1, 2013, he gets 60% of pension commuted for Rs. 10,00,000/-. He also received Gratuity of Rs. 50,000/- up on his retirement.

Solution:-A]. Uncommuted Pension :-

July 2012 to Jan 2013 @ Rs. 20,000/ Month = 1,40,000/-

Feb 2013 to March 2013 @ Rs. 20,000/ Month x 40% = 16,000/-
[since 60% is commuted, only remaining 40% will be received monthly].

Total amount of uncommuted pension for the year 12-13 = 1,56,000/-

[1,40,000 + 16,000]

B]. Commuted Pension :-

Amount of commuted Pension = Rs.10,00,000/- [being 60%]

Therefore full value of commuted pension = 10,00,000 / .6 = 16,66,667/-

As Mr. X receives gratuity, 1/3 of full value of commuted pension is exempt from tax ie;

16,66,667 X 1/3 = 5,55,556 is exempt from tax, hence the taxable amount of commuted pension = commuted pension received minus pension exempted

Ie; 10,00,000- 5,55,556 = 4,44,444 is taxable

C]. Total amount of taxable pension for the p/y 2012-13 = 1,56,000 + 4,44,444
= 6,00,444 /-

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