



# Will VPF remain attractive option after new tax rules?

**SMRITI CHAUDHARY**

Voluntary Provident Fund (VPF) is seen as an attractive investment as it offers the same rate of interest as Employees' Provident Fund (EPF). However, as part of the Union Budget 2021, the government has now decided to tax employee contributions to provident fund above ₹2.5 lakh per annum.

EPF is a retirement fund for organized sector employees. Every month, at least 12 percent of the employee's basic salary are compulsorily deducted as provident fund, while the employer contributes an additional 12 percent.

VPF is also a retirement account on a par with EPF, however, employers do not contribute to it.

While contributions made to VPF do not enjoy any tax cut under Section 80C as EPF contributions (up to ₹1.5 lakh per annum), they earn the same interest as EPF.

Until now, interest accrued was tax-free and so were withdrawals.

From April 1, if the employee's contribution to PF - statutory or voluntary - is exceeding Rs 2.5 lakh a year, then the interest earned on this excess contribution will become taxable at the prevailing income tax rates.

Will the move affect the attractiveness of VPF?

"VPF tended to be significantly more attractive than other fixed income options because the return from it was completely tax free and the PF interest rates are at 8.5 percent, which makes it a very attractive proposition," said Vishal Dhawan, Founder of Plan Ahead, a SEBI-licenced Registered Investment Advisory firm.

He added that the new tax rules have made it "relatively less attractive".

"Person who is in a 30 percent tax bracket will see their return fall slightly below 6 percent after tax, which is still relatively attractive than other fixed income options except Public Provident Fund (PPF). PPF is the only other viable option to contribute for someone who is working as it gives a higher post-tax return. However, it has a restriction of Rs 1.5 lakh per year."

He advised that the best approach is to consider how far away is an individual from retirement. In cases where retirement isn't imminent, options like equity and mutual funds can be considered.

"Since they have a long time horizon before they'll require the money, they can get over the volatility that comes with equity in the short run," he said.

"The decision now will have to be made on a case to case basis of each investor rather than a standard solution used by anyone."

Talking about the rationale behind the government's new tax rules, Dhawan said this was also done as part of the standardization across retirement products so as to make them relatively similar from a taxation perspective and to avoid making one product superior to the other product just because of taxation.

"There is an element of subsidy in the PF as the interest rates are much higher in comparison to other alternative solutions. If the intention was to keep an exempt-exempt-exempt (EEE) tax structure meaning a tax deduction benefit at investment, accrual and withdrawal. It was framed keeping a certain amount of restrictions in mind. If you look at most other retirement products, they are all subject to an exempt-exempt-tax (EET) structure," Dhawan noted.