

Provident fund tax: a backward step

by Quazi Tafsirul Islam

THE Income Tax Act of 2023 in Bangladesh has stirred unease, mainly in the private sector, by mandating a 27.5 per cent tax on employee welfare funds like provident and gratuity funds. While this might seem like a simple way for the government to increase revenue, the actual implications extend much further. The change not only affects the financial planning of retirees but also impacts long-term employment incentives.

This hefty tax has sparked debates around fairness and equity, especially when it comes to imposing taxes on retirement benefits. The law takes a discriminatory approach, exempting government-managed provident funds while imposing the tax on similar private-sector funds. This differential treatment creates an imbalance in the system, challenging the principles of tax fairness and raising ethical questions around social justice.

The new tax provision also has potential ramifications for social behaviour, particularly affecting the culture of savings and long-term financial planning. In a country with limited social security measures, provident funds serve as a crucial safety net. Taxing these funds could discourage saving, thereby reducing financial security for future retirees and possibly leading to higher employee turnover in companies.

In Bangladesh, a country with limited social security provisions, provident funds are not merely a financial instrument but a lifeline for retirees, especially those from the private sector. Provident funds are a core long-term motivation for employees. A heavy tax on these funds could demotivate workers, negatively impact recruitment strategies, and increase employee turnover rates.

The new tax law's discriminatory angle is what makes it particularly contentious. While it spares government-managed provident funds from taxation, it imposes a 27.5 per cent tax on similar funds in the private sector. This creates a clear divide, adding an additional financial burden on private-sector employees while public-sector employees remain unaffected.

The law's selective approach to taxation strikes at the heart of tax equity, a cornerstone of any fair taxation system. Tax equity dictates that similar entities should be taxed similarly, but the law's current structure contradicts this principle. By treating private and public sector provident funds differently, it undermines the core tenets of a just tax system.

This differential treatment raises serious ethical questions. Why should two sets of employees contributing to similar welfare funds be subjected to different tax rules? It not only creates financial inequality but also questions the government's com-

mitment to equitable treatment for all citizens, regardless of their employment sector.

The government's recent introduction of a universal pension scheme seemed like a step in the right direction. It encouraged everyone, regardless of their employment sector, to contribute towards a retirement fund. While the pension scheme is commendable, the new 27.5 per cent tax on provident funds is a contradictory move. It's like giving with one hand and taking away with the other.

One of the most immediate effects of this tax will be its discouraging impact on savings. Any increased tax on savings income discourages people from saving. Unlike many developed nations, we do not have universal medical, education, and other coverage in Bangladesh, and often family savings are a last resort for the citizens. In a country where savings often serve as the only financial cushion, this tax might deter people from utilising provident funds as a saving mechanism, reducing overall savings rates and potentially creating a future financial crisis. This is particularly alarming when we will become an aging population in two decades.

The tax amendment also introduces a layer of complexity that begs for clarification. For instance, should the employer's contribution be considered tax-approved business expenses? Should income accruing to the employee's provident fund account

be taxable? These questions have created an air of uncertainty and ambiguity, making it challenging for companies and employees to navigate the new tax landscape.

Taxation is not a collection by force but should ensure equity and justice. The new tax law, as it stands, seems to contradict this principle. It raises more questions than it answers and poses significant challenges to the socio-economic fabric of Bangladesh. It's not just about generating revenue; it's about doing so in a manner that is fair, justifiable, and in line with the country's broader social and economic goals.

In light of these issues, it is crucial for policymakers to reconsider this provision. The government should aim for a taxation system that not only fills its coffers but also upholds the principles of equity and social justice. After all, a tax system should serve the people it governs, not create additional burdens and divisions among them.

Would this tax law, then, survive the scrutiny of public opinion and experts alike? Only time will tell. But one thing is clear: as it stands, this tax is a step backward for Bangladesh. And steps backward, especially ones that affect the social and financial security of its citizens, are luxuries that Bangladesh cannot afford.

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