Don't worry about TDS on RDs

There is some bad news for investors who thought their recurring deposits (RDs) will not be subjected to tax deduc tion at source (TDS). The Budget has made RDs liable to TDS if the income in a financial year exceeds `10,000. Till now, only income from fixed deposits was subjected to TDS.

There is also a significant change in the rules relating to interest income from FDs. Till now, the TDS kicked in only if the income from FDs made in a particular bank branch exceeded the threshold of `10,000 in a financial year.It was common for investors to open FDs at multiple branches of their bank to avoid TDS. The Budget has proposed that TDS be levied if the combined interest income from FDs in all branches of a bank exceeds `10,000 a year.

The new rules come into effect from 1 June but banks are already witnessing a rush of investors prematurely closing their RDs and FDs. "The new rules on TDS will help nail tax evasion and improve tax collections," declares Sudhir Kaushik, Co-founder and CFO, Taxspanner.

However, taxation experts say the new rules should not be a concern for honest taxpayers. They already pay tax on their RDs and FDs. Instead of paying the tax themselves, it will get deducted as TDS. If they fall in the higher tax bracket, they will pay the balance tax.

The third major change in TDS rules is that co-operative bank deposits are no longer exempt. The Budget has proposed that TDS will also be applicable to deposits with co-operative banks.This was more or less expected. Last year, the Karnataka Income Tax Tribunal had ruled that if the interest exceeded `10,000 in a year, it must be subjected to TDS.

Following this, several cooperative banks had received notices from the Income Tax Department asking them to deduct tax for the year 2013-14. Now the Budget has put a stamp of certainty on the rule. "This will bring a lot of revenue to the government through TDS and increase the tax base because depositors would need to adjust or claim refund at the time of filing their income tax returns," says Kaushik.

Only an interim tax

Investors should note that TDS is only an interim tax. It is 10% of the income.If the investor has not provided his PAN, it is higher at 20%. But the interest earned on RDs and FDs is fully taxable. If the income is below `10,000 and TDS has not been deducted, you have to add the interest to your total taxable income and accordingly pay tax.

The actual tax will depend on the income of the individual. Even if TDS has been deducted, it does not mean that your tax liability is taken care of.If you are in the 20-30% tax bracket, you are required to pay more tax on the income. If the investor has an income of over `10 lakh in a year,

the interest from the RD or FD will be taxed at 30%.The balance 20% will have to be paid as self-assessment tax. If he earns less than `2.5 lakh a year, the TDS will be refunded after he files his tax return.

Can you avoid TDS

If you are not liable to pay tax because your total income is below the basic exemption limit, you can avoid TDS by submitting a declaration to the bank."Those who do not fall under the tax bracket and are below the age of 60 can submit Form 15G to the bank to claim TDS exemption. Those not under the tax bracket and above the age of 60 can submit Form 15H," says Suresh Sadagopan, a Mumbaibased certified financial planner.Forms 15G and 15H have to be submitted at every branch of the bank where you have a deposit.

Before you rush to submit the Form 15G or 15H, make sure you are eligible. An individual must satisfy two conditions to avoid the TDS. First, the estimated taxable income for the financial year should be less than the basic exemption limit. This is `2.5 lakh for individuals below 60 years, `3 lakh for senior citizens, and `5 lakh for very senior citizens-above 80 years.

The second condition, which is applicable only to Form 15G, is that the total interest income from all sources should not exceed the basic exemption limit.Senior citizens have been exempted from this condition because most retirees get the biggest chunk of their income from interest.

These forms also require the individual to mention details of other incomes, including dividends from shares and mutual funds. Dividend income is taxfree but the Income Tax Department still wants to know how much you earned from them.

You must carefully assess your income before submitting Form 15G to escape TDS. If you are not eligible to receive the exemption, but you submit the form, it can have serious repercussions. "Giving incorrect information to avoid TDS amounts to tax evasion. A penalty of up to `1 lakh can be slapped in such cases," warns Kaushik.

Investors are rushing to close their RDs before the taxman gets a whiff of their wealth. "Premature closure of my RD will fetch me a lower interest rate. But at least there won't be a tax deduction," said an investor at a public sector bank in Delhi.

Banks may see more premature closures of deposits. It is not difficult to see why investors are panicky. Since the TDS is credited to the permanent account number of the investor, not mentioning the income in the tax return can lead to problems. The computer-aided scrutiny system of the tax department could pick up the mismatch in the tax credit and income declared by the assessee, which can lead to a detailed scrutiny by the tax authorities. If tax has been deducted at source but returns have not been filed, the tax department may want to know why.

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