

## Get more out of tax-free bonds

Tax-free bonds are a good opportunity to earn a fixed income without increasing your tax liability. The 15-year option of the REC bonds is offering a coupon rate of 8.71%. This is equivalent to a pre-tax return of 12.6% for someone in the 30% tax bracket. Even in the 20% tax bracket, the pretax return is no less attractive at nearly 11%.

While this should be reason enough to invest in these bonds, there is an opportunity to derive additional tax benefits if your spouse is in a lower tax bracket or does not have taxable income. If you gift money to your spouse to invest, the clubbing provisions under Section 60 come into effect. The income from the investment is treated as your income, not hers.

You can still squeeze a tax arbitrage by investing in her name because the clubbing happens only at the first level of income. The income from the investment will be treated as yours, but if the interest income is subsequently reinvested and earns an income, it will be treated as your wife's, not yours. "The income from the reinvested income does not attract the clubbing provision," says Sudhir Kaushik, chartered accountant and co-founder of tax filing portal Taxspanner.com.

Here's how you can make this rule work for you. Gift money to your spouse and then get her to invest in these tax-free bonds. The interest will be added to your income, but since it is tax free, there won't be an additional liability for you. Your wife can then reinvest that money elsewhere. This time the income will not be clubbed.

This strategy works only if your spouse is in a lower income bracket or does not have taxable income. Also, it is not possible to extend the same strategy to investments made in the name of minor children. The income of a minor child is clubbed with that of the parent who earns more. Even the reinvested amount is subject to the clubbing provisions under Section 60. There is only a small annual exemption of Rs 1,500 per child for such income.

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