



February 15th 2021 BIMONTHLY VOLUME II

Taxability of Interest on Excess PF Contribution

The Union Budget 2021 has proposed taxing the income on provident fund contributions of over Rs. 2.5 lakh a year. As per clause 5 of Finance Bill 2021, the interest on any contribution above Rs 2.5 lakh by an employee to a recognized provident fund will be taxable from 01 April 2021.

Existing Statutory Provisions:

Section 10(11) and 10(12) of the Income Tax Act provides an exemption for the statutory provident fund and recognized provident fund respectively. Interest credited every year in the Employee provident fund account (EPF) is exempt from tax. The deposits in EPF fall under the Exempt tax category. Thus, an employee is not liable to pay tax at all three levels – investment, earning, and withdrawal.

Proposed Amendment:

For the first time, the government has proposed to tax the employees' provident fund (EPF), albeit only the interest income on contributions exceeding Rs 2.5 lakh in a year. In the recent Budget proposals, the government has proposed that tax exemption will not be available on interest income for the year on all contributions to provident funds exceeding Rs 2.5 lakh. While this may cause concern to all salaried individuals contributing to EPF, it will in fact impact only those who contribute more than Rs 2.5 lakh in a year and it will not affect their existing corpus or the aggregate annual interest on that. This change applicable to contribution made on or after the 1st day of April 2021 and computed in such manner as may be prescribed".

Reason for the Amendment:

This amendment has been proposed as the Government noticed that some employees have been contributing a huge amount to these funds. The interest rate on EPF is generally higher than other small savings schemes and fixed deposits that offer guaranteed returns. The higher interest rate on EPF prompts employees to put higher corpus in EPF, which in turn makes it difficult for the government to pay interest on the same.

Salient Features of the Proposed Amendment:-

- This interest taxability shall be applicable only for the contribution made on or after April 1, 2021.
- The employee's principal contribution, employer's contribution, entire interest earned on employers' contribution, and interest earned by the employee till 31st March 2021 are not taxable.
- The interest income earned on excess contribution will be taxable only in those cases where the employees' annual PF contribution exceeds Rs. 2,50,000/-.
- The contribution to PPF is already restricted to Rs. 1.5 lakhs p.a. currently, so this amendment will not have any impact on PPF contribution."

Manner to tax the Interest:

There would be no double taxation and it will work exactly in the same manner as the way interest income on bank fixed deposits is taxed today. Such interest component shall be subject to TDS under Section 194A by the EPFO. However, prescribed rules are awaited in this regard.

The interest income accruing in respect of the employee's contribution over Rs. 2, 50,000 shall be taxable under the head 'Income from other sources' as it is not accruing from a source emanating from an employer-employee relationship.

This interest income will become part of the total taxable income of the taxpayer. There are no special rates for the taxability of this interest. Hence, such income shall be taxed at the prevailing income tax rates.

Illustration:

Mr. A's total contribution (including voluntary provident fund) to Employee Provident Fund (EPF) is Rs 3, 50,000 in the FY 2021-22. Assuming the rate of interest on EPF is 8.5% per annum; his tax liability will be calculated in the following manner: -

FINANCIAL YEAR	EMPLOYEE'S CONTRIBUTION IN EPF IN A YEAR (Rs.)	CONTRIBUTION LIABLE FOR TAX ON INTEREST (B- 2,50,000)	INTEREST ON THE EXCESS CONTRIBUTION (C*8.5%)	TDS @ 10% UNDER SECTION 194 A (10% ON D)
(a)	(b)	(c)	(d)	(e)
2021 - 22	3,50,000	1,00,000	8,500	850

In the illustration above, Rs. 8500/- will be added to the employee's taxable income and tax will be payable by him according to his tax slab. Rs. 850/- will be reflected in his form 26AS as TDS deducted.

COMPLIANCE CALENDER FEBRUARY 2021



GST	
GSTR 3B JAN 2021(Turnover in the previous financial year more than Five Crores)	20-02-2021
GSTR 3B JAN 2021 (Others)	22-02-2021
GSTR 1(Turnover more than Rs. 1.5 Crores)	11-02-2021
Income Tax	
Deposit of TDS	07-02-2021
ESI	
Payment for the month of JAN 2021	15-02-2021
PF	
Payment for the month of JAN 2021	15-02-2021
Return Filing for the month of JAN 2021	25-02-2021