

## DILEMMA OF TDS ON INTEREST OF DEPOSITS IN COOPERATIVE BANKS



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### ABSTRACT

TDS on interest income from deposits of small and nonscheduled cooperative banks has been made applicable with effect from 1st June, 2015. Earlier, exemption from TDS was given to member (shareholder) depositors of cooperative societies. Most of the people give preferably deposit their money in cooperative banks because of friendlier staff, additional interest rate than nationalized banks and exemption from TDS. However, the Finance Bill-2015 removed all exemptions in regards to TDS and also expanding definition of time deposits, recurring deposits (RDs) have been included in the domain of time deposits.

These provisions have created worries by the side of cooperative banks as well as depositors' side. This is one of the most significant steps to create more competition and keep aside the cooperatives from enjoying special exemption in order to make cooperative banks feeble. On this backdrop, to make aware the depositors and alongside to study the effects of TDS on the business of cooperative banks, the present study has been carried out and tried to focus on the current issue.

**KEYWORDS :** *TDS on Interest , Deposits in Cooperative Banks , recurring deposits (RDs) .*

### INTRODUCTION :

Section 194-A of Income Tax deals with the provisions regarding TDS on interest income of deposits in banks. There is a hot discussion regarding TDS on interest of deposits in the cooperative banks. The budget 2015-16 has put RDs (Recurring Deposits) at par with FDs (Fixed Deposits) for TDS (Tax Deducted at Source) purpose. Banks will deduct TDS on Recurring Deposits (RDs) too from 1st June, 2015. If a depositor receives more than Rs.10000 as interest from RDs, bank will deduct Tax and directly pay to the Govt. of India on behalf of the depositor.

Previously the provision of TDS on interest was applicable only to the nationalized banks but, now it has become applicable to Cooperative banks too. Many middle and high income group tax payers to avoid TDS and for saving income tax were making deposits in cooperative banks under different names but, this will not be possible now. All money will be depicted due to this provision. Tax evader will now have to give justification for the source of income of such deposits. Rural depositors

and tax payers may be more affected due to this provision. Tax exemption on Savings Bank account interest earned up to Rs. 10000 has been exempted from income tax. However, interest income from other kind of deposits i.e. term deposits/fixed deposits; recurring deposits are not now exempted from income tax. As the policy of 'one size fits to all' all banks including cooperative banks are treated equal in regards to TDS from 1st June, 2015.

#### Recurring Deposits With-in the Ambit of Time Deposits:

Formerly, the definition of "time deposits" provided in section 194-A of the Income Tax Act, 1961 excludes recurring deposits and only income from fixed deposits was subjected to TDS. Therefore, payment of interest on recurring deposits by banking company or co-operative bank was not subject to TDS. However, in the Budget-2015-16, Hon'ble Arun Jaitley, the FM has proposed to amend the definition of 'Time Deposits' so as to include 'Recurring Deposits' within the ambit of TDS for deduction of tax U/S 194-A of the Act. Hence, interest earned on recurring deposits exceeding Rs 10,000 will be subject to tax deduction at source at the relevant rates.

#### Removal of TDS Exemption to Members (Shareholders) of Cooperative Banks:

Under the existing provision of Income Tax Act- Sub-section (3) of Section 194-A provides exemption from deduction of tax in respect of following interest payments by co-operative society:

- (i) Interest payment by a co-operative society to a member thereof or any other co-operative society. [Section 194A(3)(v) of the Act]
- (ii) Interest payments on deposits by a primary agricultural credit society or primary credit society or co-operative land mortgage bank or co-operative land development bank. [Section 194A(3)(vii)(a) of the Act]
- (iii) Interest payment on deposits other than time deposit by a co-operative society engaged in the business of banking other than those mentioned in section 194A(3)(vii)(a) of the Act. [Section 194A(3)(vii)(b) of the Act].

Captivating benefit of the provision in Income Tax section 194A(3)(v), cooperative banks generally, making depositors to their members (shareholders) grabbed deposits of higher and middle income groups. On the contrary depositors easily became members of cooperative banks and saved their income from tax deduction. This has led to dispute as to whether the co-operative banks, for which the specific provisions of tax deduction exist in the form of section 194A (1), section 194A(3)(i)(b) and section 194A(3)(vii)(b) of the Act, can take the benefit of general exemption provided to all co-operative societies from deduction of tax on payment of interest to members. The matter of discrepancy between depositors and depositor-members of cooperative banks regards to TDS carried to judicial forums viz. Aurangabad Bench of Mumbai High Court gave a decision on 21st April, 2014 in the case of The Marathwada Urban Banks Association v/s Government of India (writ petition no.4935/2003) that the exemption provided from deduction of tax from payment of interest to members by a co-operative society under section 194A(3)(v) of the Act shall not apply to the payment of interest on time deposits by the co-operative banks to its members. As a result, the amendment in Section 194-A of the Income Tax Act has been made and exemption from TDS which was given to members of cooperative societies has been removed from 1st June, 2015.

#### TDS Doesn't End our Tax Liability

TDS and tax liability are quite different. Tax burden is depended upon the size of income of a

person in which slab/limit of taxable income that arrives. This is to be remembered that TDS doesn't end our tax liability. Interest on RDs and FDs is fully taxable as at the stipulated rate. So even if TDS has been cut, we might have to pay more tax, depending on income tax slab which is indicated in the following table.

Table No. 1 Income Slab, TDS on Interest Income of RDs and FDs.

Income Slab	TDS Rate Levied by Banks	Tax Beyond TDS
Below Rs. 2.5 lakh	10 percent	0 percent
Rs.2.5 lakh to Rs. 5 lakh	10 percent	Nil
Rs.5.00 lakh to Rs. 10.00 lakh	10 percent	10.30 percent
Above Rs.10 lakh	10 percent	20.60 percent

If taxable income is below Rs 2.5 lakh and banks deduct TDS (we can submit Form 15 G/15H to avoid TDS), we can claim back TDS as refund in our Income Tax Returns (ITR). In the following situations we cannot claim for refund as against we have to pay more tax.

1. If our income is between Rs. 2.5 lakh to Rs. 5 lakh, we need not pay any extra income tax. Because, the income tax rate of 10 percent matches with Bank's TDS rate which is also at 10 percent.
2. If our income is in the range of Rs 5 lakh to Rs 10 Lakh, we need to pay 10.30 percent beyond the TDS rate.
3. If our income is over Rs 10 lakh, the differential tax rate is 20.60 percent which we must pay.

**More Benefit to Lower Income Group and Less Benefit to Higher Income Group:**

In a higher interest rate scenario, the going is good for investors in lower tax bracket. The investments from fixed deposits yield them returns that are worth talking about. But as your income go into the higher slabs, the taxation starts affecting the net earnings.

Consider an interest rate of 9 percent p.a. on a 10-year fixed deposit of Rs.2 lakh. It's surely an attractive interest rate to invest. However, the real picture is quite different from what is presumed when taxation is considered:

Table No. 2 Net Return on Bank Deposits after TDS (Rs.)

Income Tax Slab	Amount Invested	Interest (9 % p.a.)	TDS Amount	Net Interest Earned	Post Tax Return
10 percent	200000	18000	1854	16146	8.07 percent
20 percent	200000	18000	3708	14292	7.14 percent
30 percent	200000	18000	5562	12438	6.21 percent

As we can see from the above illustration, for individuals in higher tax slab of 30 percent, the post-tax returns are 6.21 percent, which do not even match the current inflation rate. As against this, an individual in the lowest tax slab will be able to fetch 8 percent return on the same investment post taxation. Surely, the benefit accruing to the lower tax category has a lot to cheer.

### Significant Changes to Be Acknowledged

1. Previously the provision of TDS on interest was applicable only to the nationalized banks but, now it has become applicable to Cooperative Banks too.
2. There was an exemption of TDS to member-depositors of cooperative banks not to depositors; this discrepancy came to end and now all depositors will be treated equal.
3. The banks which have adopted Core Banking Solutions (CBS) should determine tax liability of a depositor not at per branch level, but at per bank level (clubbing interest income on all FDs in all branches).
4. Recurring Deposits are included in the scope of fixed deposits and TDS is made applicable to recurring deposits also.
5. Under section 194A(3)(ix) of the Act, tax is not required to be deducted from the interest credited or paid on the compensation amount awarded by the Motor Accident Claim Tribunal if the amount of such interest credited or paid during a financial year does not exceed Rs.50,000/-.
6. The Government will collect more taxes and tax evasion will be avoided. It may be one tool to garner revenue.
7. The interest earned up to Rs 10,000 on savings bank accounts in a financial year is exempted from tax. The excess income is added to the total income and be taxed at marginal rate applicable to the investor.
8. TDS is also deducted on interest accrued (but not yet paid) at the end of the financial year viz.31st March.
9. Taxpayer should submit a copy of PAN Card to Bank. If depositor does not have PAN or does not submit PAN then TDS will be deducted at 20 percent.

### To Whom TDS On Interest Income Is Not Applicable

1. In the financial year-2015-16, if the annual income of a depositor will be less than 2.5 lakh and who will submit 15-G/15-H form. The form 15G and 15H are submitted to banks by depositors who DO NOT want that TDS be deducted from their interest earned on fixed deposits. A person who is below 60 years can file the Form 15 G. However, only a person of 60 years or more is eligible to file Form 15 H.
2. Time Deposits (FD and RD) in those banks which have not adopted Core Banking Solutions (CBS). In the other words people who deposit money in banks which have not adopted core banking solutions (CBS) may perhaps escape from TDS at least for the economic year 2015-16.
3. If depositors do not want TDS to be deducted, they can split their deposits in two or more banks so that the total interest earned at one bank is less than Rs. 10000 (However, this does not mean that income earned from such deposits is exempted from income tax).

### Why People Prefer Co-Operative Banks to Keep Deposits?

Lower income group, small traders, middle income group, senior citizens/ retired people park their money in co-operative banks. Basically, there are four main reasons behind the selection of cooperative banks for depositing the money.

1. The bank is closer to their home/residential place.
2. The staff is friendlier compared to the staff in nationalized banks.
2. The bank offers higher rate of interest compared to nationalized banks.
3. The interest on bank deposits is not subject to TDS provisions. The Finance Bill 2015 has plugged this loophole and made the interest earned on deposits at co-operative banks subject to TDS, like any other nationalized banks.

### Impact of TDS on Cooperative Banks

The provision in the union budget 2015-16 regarding TDS has made worrisome to cooperative banks. The depositors who predominantly keep their money in cooperative banks to avoid TDS, they will withdraw money from cooperative banks and same will deposit in nationalized banks. Tough competition will take place to impound deposits. Those cooperative banks which have yet not adopted core banking solutions (CBS) they can grab the deposits from other cooperative banks and some extent from nationalized and private sector banks also. Because of TDS provision, special uniqueness of cooperative banks in favour of depositors came to end with diminishing deposits. End of exemption from TDS to members and inclusion of RDs is the ambit of time deposits; together will hamper the business of cooperative banks. So that District level, State level associations and National level federation of cooperative banks are in the stance to meet Union Finance Minister to increase the limit of interest income for TDS and also continuation of exemption for members. Anyway, TDS has increased stress on cooperatives banks.

### CONCLUSION:

In the post LPG era, small and nonscheduled cooperative banks in India in general and Maharashtra in particular, are going through very hard-hitting days. Cooperatives have created special place amongst the rural as well as urban lower and middle income group. Deliberately sidelining all unique characteristics of cooperatives, RBI and Central Government both are continuously trying to reduce special identity of cooperative banks and treating them as equal to nationalized and private sector banks. In case of TDS on interest income from deposits of small and nonscheduled cooperative banks has been made applicable with effect from 1st June, 2015. Earlier, exemption from TDS was given to member (shareholder) depositors of cooperative societies. Because of friendlier staff, additional interest rate and especially exemption from TDS; most of the people prefer cooperative banks for depositing their money. However, the Finance Bill-2015 removed all exemptions in regards to TDS and also expanding definition of time deposits, recurring deposits (RDs) have been included in the domain of time deposits. This TDS provision created worries by the side of cooperative banks as well as depositors' side.

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