Planning Your Income Tax- A Guide for Salaried Persons

Prepared by

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Introduction

The start of this new Financial Year 2020-21 has been marred by the disruptions caused amidst Covid-19 pandemic. The lockdown brought the life almost to a standstill. However, with restrictions easing up, economic activities are resuming again. As we hope for things to become normal, we are sharing a small guide for salaried persons to plan their Income Tax.

In the Finance Act, 2020, the Government of India has introduced a new tax regime, giving tax payers an option to pay taxes at a lower rate. This option comes with the condition of giving up various deductions and exemptions available under the Income Tax Act. In this draft, we analyse this new Income Tax Regime and whether one should opt for it or not. We also give you brief information about various tax saving options available for the taxpayers.

New Tax Regime

Reduced Tax Rates

Finance Act, 2020 introduced 'New Tax Regime' by inserting Section 115BAC. As per the new Section, individuals and HUFs have the **option** of paying taxes at a lower rate from Financial Year 2020-21 (Assessment Year 2021-22), if they do not avail deductions and exemptions available under the Income Tax Act.

The intent of this New Tax Regime has been:

- To reduce the burden of tax for taxpayers
- To increase liquidity in the hands of taxpayers by delinking tax savings with investments
- To simply the Income Tax laws and its compliance

Income Tax Slab Rates under the New Tax Regime are as under:

Tax Slab	Existing	New Tax Regime
Up to Rs. 2.5 lakhs	Nil (No change)	
Rs.2.5 lakhs – 5 lakhs	5% (No change)	
Rs. 5 lakhs – 7.5 lakhs	20%	10%
Rs. 7.5 lakhs – 10 lakhs	20%	15%
Rs. 10 lakhs – 12.5 lakhs	30%	20%
Rs. 12.5 lakhs – 15 lakhs	30%	25%
Above Rs. 15 lakhs	30% (No change)	

New Tax Regime
Deductions/ Exemptions Not Allowed

For availing reduced tax rates under New Tax Regime, taxpayer need to surrender the following exemptions and deductions:

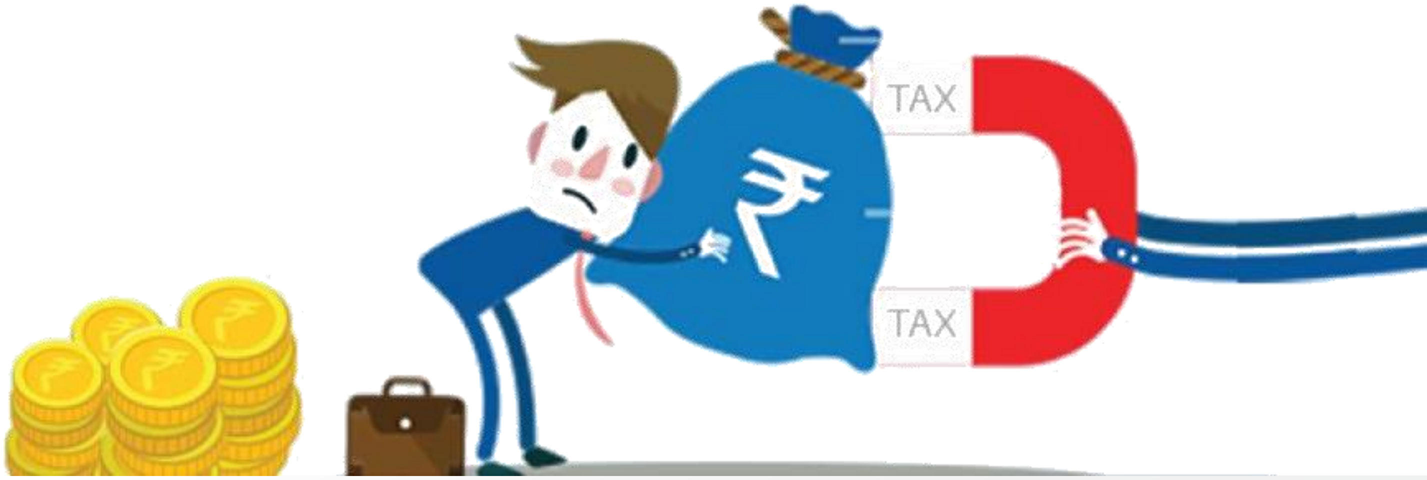
- House Rent Allowances
- Leave Travel Allowances
- Children Education Allowances
- Transport Allowances
- Uniform Allowances
- Entertainment Allowances of Rs. 5,000
- Standard Deduction of Rs. 50,000
- Professional Tax
- Exemption of Rs. 1,500 in case of clubbing of minor income
- Interest on Housing Loan under Section 24
- Deductions under Chapter VI-A including:
  - 80C/ 80CCC- Tax Saving Investments such as Mutual Funds, Fixed Deposits, PPF, Life Insurance, etc. (upto Rs. 1.5 lakhs)
  - 80CCD- Pension Contribution (expect employer contribution)
  - 80EE- Interest on House Loan
  - 80D- Medical Insurance Premium
  - 80TTA- Interest on Savings Account upto Rs. 10,000
  - 80G- Donations

Exemptions/ deductions allowed in New Tax Regime includes:

- Employer contribution in Pension Funds
- Transport Allowance for specially abled employee
- Travelling and Daily Allowances for tour or transfer (to the extent actually incurred)

New vs Old Tax Regime

Option for Taxpayers



It is entirely upon the taxpayers if they want to pay their taxes as per the New Tax Regime or on basis of the old structure. It is important to carefully analyse both the structures, before opting for one. It is also recommended to take this decision in the beginning of the Financial Year, so that the taxpayer can plan their investments accordingly.

Salaried employees are also required to convey the tax structure opted to their employers. This enables employers to deduct tax on employees salaries accordingly. Conveying incorrect tax regime can result in excess TDS which can only be claimed next year as refund from Income Tax Department.

Factors required to be carefully analysed while opting for a tax structure includes:

- Tax Bracket in which taxpayer falls.
- Exemptions and deductions available
- Liquidity desired by the taxpayer
- Alternate investment options other than tax saving schemes

New vs Old Tax Regime
Comparative Analysis

A taxpayer can save more than Rs. 60,000 by opting for New Tax Regime. However, in certain circumstances, New Tax Regime can result in higher tax liability. A comparative analysis of tax amount payable under Old and New Regime at various levels of Income and deductions opted for is provided below:

Income	Tax Payable under Old Regime			Tax Payable under New Regime
	NIL Deduction	Rs. 1,00,000 Deduction	Rs. 2,00,000 Deduction	
5,00,000	NIL	NIL	NIL	NIL
5,50,000	NIL	NIL	NIL	17,500
6,50,000	32,500	NIL	NIL	27,500
7,50,000	52,500	32,500	NIL	37,500
10,00,000	1,02,500	82,500	62,500	75,000
12,50,000	1,72,500	1,42,500	1,12,500	1,25,000
15,00,000	2,47,500	2,17,500	1,87,500	1,87,500
17,50,000	3,22,500	2,92,500	2,62,500	2,62,500
20,00,000	3,97,500	3,67,500	3,37,500	3,37,500
25,00,000	5,47,500	5,17,500	4,87,500	4,87,500

Note:
1. Health and Education Cess @ 4% not included above
2. Under Old Tax Regime, Standard Deduction of Rs. 50,000 has been considered.

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New vs Old Tax Regime

Which One Should I opt for?

Based on the data in comparative sheet, a salaried taxpayer can determine the tax regime, by answering few basic questions as below:

Whether Total Salary and Other Income ≤ Rs. 5,50,000	
If Yes, opt for Old Regime	If No, move to next step

Whether, tax free allowances and deductions such as HRA, mandatory PF contribution, medical insurance & interest on House Loan ≥ Rs. 2,00,000		
If Yes, opt for Old Regime	If No & Income ≥ Rs. 15,00,000, opt for New Regime	If No & Income < Rs. 15,00,000, move to next step

Whether taxpayer has liquidity to make long term investments?	
If Yes, then taxpayer can invest in tax saving instruments and opt for Old Regime	If No, then option need to be determined on case to case basis

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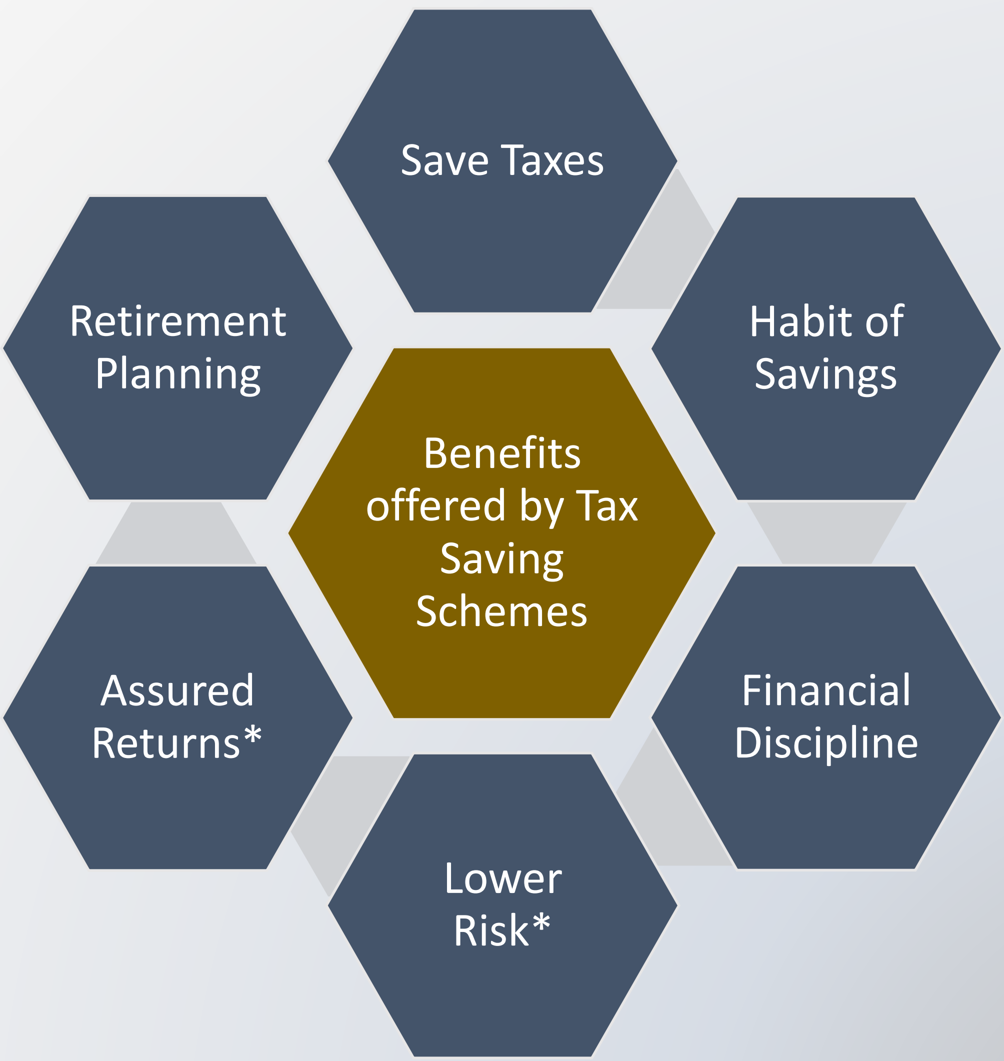
Tax Saving Instruments
Are They Still Relevant?

While, the new tax regime has reduced the dependency on tax saving schemes; such schemes might still be helpful for taxpayers to save taxes as well as in developing the habit of savings. Under Section 80C of the Income Tax Act, deductions upto Rs. 1,50,000 can be claimed from total income by investing in tax saving schemes. These schemes comes with lock in period which ensures financial discipline. Irrespective of tax benefits, these schemes are also preferred for the returns offered by them at comparatively lower risks.



*Depends upon the tax saving instrument opted

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Tax Saving Instruments
Options Available

Depending upon the risk appetite and liquidity preferred, taxpayer can choose their preferred scheme:

1. Public Provident Fund (PPF)
One of the most preferred scheme, PPF comes with a lock-in period of 15 years. The rate of return are determined by Central Government and updated quarterly. For Apr-Jun 2020 quarter, interest rate is 7.1%. PPF interest is tax free. Mandated by government, PPF is preferred for investors with low risk appetite.

2. 5 Years Bank Fixed Deposit
It is similar to the fixed deposits, with a lock in period of 5 years. Current interest rate on 5 years FD provided by State Bank of India is 5.4% (6.2% of senior citizens). Interest earned is subject to Income Tax. This option is preferred by taxpayers with low risk appetite and shorter lock in period.

3. National Pension Scheme (NPS)
Aimed to encourage savings for retirement, NPS returns are linked with market and has a lock in period till the age of retirement. NPS withdrawals are also partly taxable. Apart from limit of Rs. 1.5 lakhs, additional Rs. 50,000 deduction can be claimed under NPS. Further, contribution of 10% of salary by employer are also available as deduction over and above these limits. NPS is preferred by taxpayers considering to save further taxes.

4. Equity Linked Saving Schemes (ELSS)
ELSS are Mutual Fund Schemes with a lock in period of 3 years, where investments are made in equity share market. Since, investments are made in equities, the associated risk is high. However, in the long run, it is expected to give higher returns than other saving schemes. Returns on ELSS are taxable @ 10% if they exceed Rs. 1 lakh in a year.

5. Unit Linked Insurance Plan (ULIP)
ULIP is a combination of insurance and investment plan. The policyholder pays premium on monthly/ annually. A small portion of premium is deducted for life insurance and the remaining is invested just like a Mutual Fund. There are no assured returns and hence associated risk is high. The lock in period is 5 years.

6. Life Insurance Premium
The purpose of Life Insurance Scheme is not investment, but as an instrument to provide financial stability to your family in your absence. To encourage life insurance, tax savings have been linked with them. It is always recommended to insure one's life for financial safety.

7. National Saving Certificates
This is fixed income tax saving scheme, which can be opened from any post office. The interest rates are fixed and there is lock in period of 5 years. It is preferable for low risk appetite investors. The interest earned is taxable.

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8. Sukanya Samriddhi Yojna
Launched under 'Beti Bachao, Beti Padhao', account under this scheme can be opened for girl child below 10 years of age. Interest rates are generally higher than FD and has a lock in period of 21 years. However, withdrawls can be made for girl's higher education and marriage.

9. Provident Funds
Where the employer is covered under Provident Fund law, 12% of salary is required to be deposited each by employee and employer. Contribution by employer is allowed as deduction over and above Rs. 1.5 lakhs limit. Employees contribution is also allowed as deduction and is covered under overall limit of Rs. 1.5 lakhs. These are mandatory contributions and withdrawals can be made only on retirement. Partial withdrawals are allowed in special circumstances. Employees can also voluntary contribute additional amount in Provident Fund by informing their employer in this regard.

Tax Saving Instruments

Other Available Deductions & Exemptions

Apart from above mentioned tax saving instruments, a taxpayer can save taxes on following transactions as well:

- Medical Insurance Premium for self, spouse and children- Rs. 25,000 / Rs. 30,000 (for senior citizen)
- Medical Insurance Premium for dependent parents- Rs. 25,000 / Rs. 30,000 (for senior citizen)
- Under the above limits, up to Rs. 5,000 can be claimed for preventive health check-up.

- Principal payment of Housing Loan*
- Interest on Housing Loan can be claimed as deduction u/s 24 upto Rs. 2,00,000
- Additional Rs. 50,000 deduction available on Housing Loan Interest for eligible first time house owners under Section 80EE

- Children Education Allowance- Rs. 1,200 per child for maximum 2 children
- Hostel Education Allowance- Rs. 3,600 per child for maximum 2 children
- Tuition fees of any two children paid to any educational institute in India*
- Interest on education loan of self or children

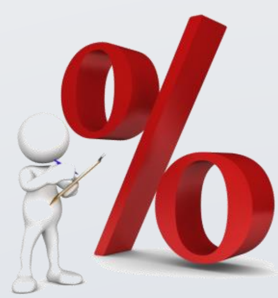
- under overall limit of Rs. 1,50,000 of Section 80C

Tax Saving Instruments

Other Available Deductions & Exemptions

- House Rent Allowances (HRA), lower of-
  - Actual HRA Received
  - 40%/ 50% (for metros) of Basic Salary + DA
  - Actual Rent Paid Less 10% of Basic Salary + DA
- Where no HRA Received, lower of-
  - 25% of total income
  - Rs. 5000 per month
  - Rent Paid less 10% of total Income

- Interest earned on saving bank deposits upto Rs. 10,000.
- For senior citizens- Limit is Rs. 50,000 and is available on FDs as well.



- Standard Deduction of Rs. 50,000 available to all employees
- Leave Travel Allowances- For two trips within India in a period of 4 years.

- under overall limit of Rs. 1,50,000 of Section 80C

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Tax Saving Instruments

Benefits at a Glance

Tax Free Allowances-
HRA, Children Education, Leave Travel

Overall Limit of Rs. 1.5 lakhs

- Employee Contribution in Provident Fund
- Voluntary Investment in Tax Saving Instruments
- Life Insurance Premiums
- Repayment of Principal Amount on Housing Loan
- Tuition Fees of Children

Employer Contribution in PF (12%) & NPS (10%)-
(Limit of Rs. 7.5 lakhs)

Contribution in NPS (upto Rs. 50,000)

Medical Insurance Premium & Preventive Health Check-up

Interest on Housing Loan upto Rs. 2,00,000
+ Rs. 50,000 (for first time house owners)

Interest on Saving Bank (Rs. 10,000)
Interest on Saving Bank & FD (Rs. 50,000 for Senior Citizen)

Standard Deduction of Rs. 50,000 for all employees

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To Conclude

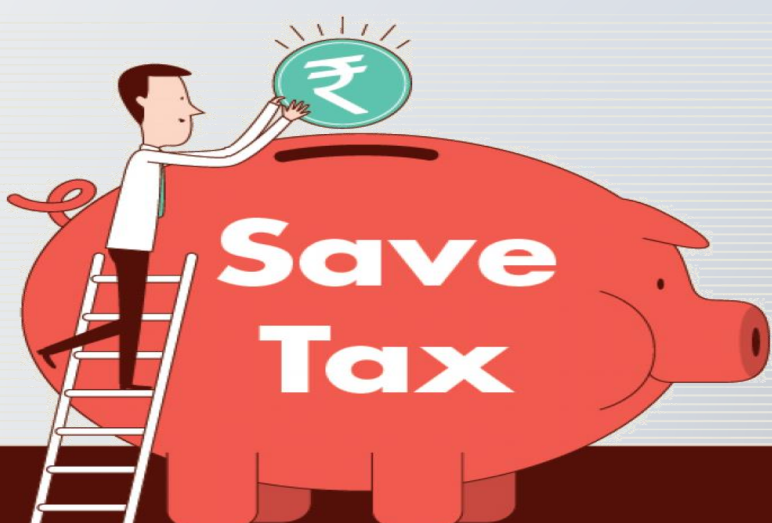
- With an ever increasing surveillance and use of technology, tax evasion is no longer an option.

- However, taxpayers can take benefit of New Tax Regime or Tax Saving Instruments to save their tax liability.

- Considering the disruptions caused by Covid-19 pandemic, some taxpayers may face liquidity concerns this year. They can opt for New Tax Regime and save taxes without any investments.

- Other taxpayers are recommended to keep investing in tax saving schemes and continue in old tax regime.

- The option opted should be conveyed to employer at earliest to avoid excess TDS.



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How We can Contribute

- As Shiv & Associates, we can assist you in determining your tax liability under both new and old tax regime.
- We can help you to plan your taxes to minimise your tax liability and ensure 100% compliance.
- We can guide you to evaluate and invest in tax saving option, best suited to your needs.
- We can also help you regarding tax compliances, pending refunds and demand notices.

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THANK YOU

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