



## Interest accumulated in a recognised Provident Fund account post retirement/end of employment is considered taxable

### Background

Post-employment, whether on account of termination, resignation or retirement, several employees continue to maintain their PF accounts and earn interest on the same. In this context, the Bangalore Bench of the Income Tax Appellate Tribunal (the Tribunal) has recently held in the case of Dilip Ranjrekar<sup>1</sup> (the taxpayer) that interest accumulated in the Provident Fund (PF) account post cessation of employment is taxable in the hands of the taxpayer.

### Facts of the case

- The taxpayer had ceased to be an employee of Wipro Ltd. in tax year (TY) 2001-02 after 26 years of service, and the amount of contributions accumulated in his PF account (including interest) as on date of retirement was INR3.7 million. Nine years later, the taxpayer withdrew the total accumulations from his account, which amounted to INR8.2 million. This withdrawal also included interest accrued post his retirement, amounting to INR4.4 million;
- During the TY 2010-11, the taxpayer filed his India income tax return (ITR) without declaring the accumulated balance withdrawn from his PF account;
- The ITR was subject to scrutiny assessment and an order was passed<sup>2</sup>, whereby the Assessing Officer (AO) *inter-alia* added the entire balance withdrawn to the total income.

- Aggrieved by the order of the AO, the taxpayer had filed an appeal with the Commissioner of Income-tax (Appeals) (CIT(A)), who deleted the entire addition made by the AO;
- Aggrieved by the order of the CIT(A), the Revenue had filed an appeal with the Tribunal.

### Tax department's contentions

- The Revenue's contentions were on the following grounds:
  - Accumulated PF balance: The Revenue argued that the exemption<sup>3</sup> provided to the taxpayer on the withdrawal of accumulated PF balance amounting to INR3.7 million is not allowable for the following reasons:
    - Exemption<sup>4</sup> is available only to an 'employee' and in the instant case the taxpayer had ceased to be an employee in 2002 itself;
    - Relying on a judicial precedent<sup>5</sup>, any claim of exemption not made in the ITR is not allowable even when such claim is made during assessment proceedings.
  - Interest accrued in the PF account post retirement: The interest accrued on the accumulated PF balance post retirement amounting to INR4.4 million should not be eligible for exemption under Section 10(12)

<sup>1</sup> ACIT v. Shri Dilip Ranjrekar (ITA No 858 of 2016) (Bang)

<sup>2</sup> Section 143(3) of the Income-tax Act, 1961 (the Act)

<sup>3</sup> Section 10(12) of the Act

<sup>4</sup> Section 10(12) of the Act read with Rule 8 of Part A of Fourth Schedule

<sup>5</sup> Goetze (India) Ltd v. CIT [2006] 284 ITR 323 (SC)

of the Act for the following reasons:

- The accumulated balance<sup>6</sup> (including interest) only till the date of cessation of employment will be exempt, and any further income generated (post-employment) would not be exempt.
- Further, the taxpayer had also not offered the interest income accrued on the PF account (post cessation of employment) to tax in the relevant TYs, when the interest so accrued.

### Tribunal's decision

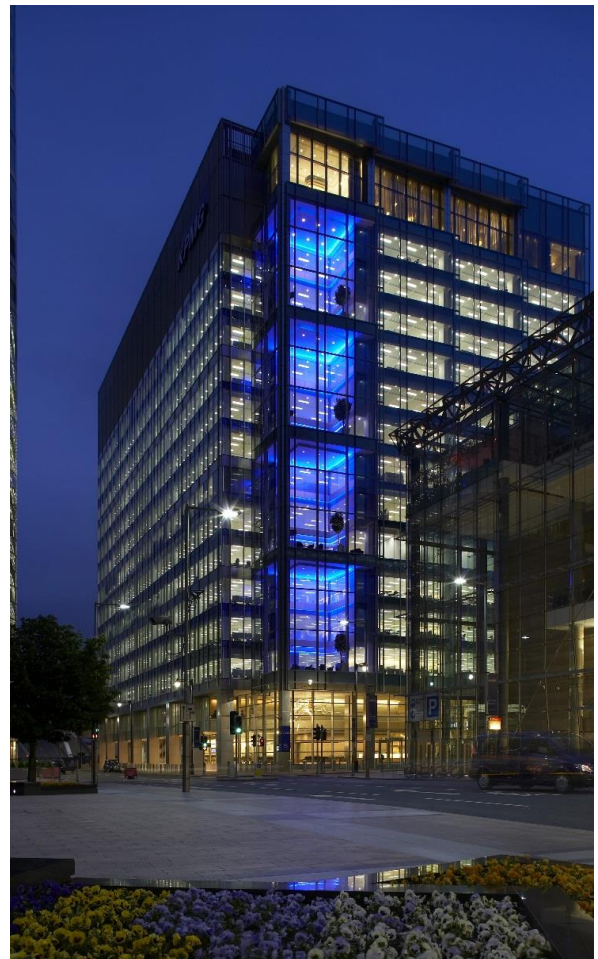
- The Tribunal took cognisance of the taxpayer's contentions and held as under, in relation to the accumulated PF balance as on date of retirement:
  - The withdrawal of accumulated PF balance amounting to INR3.7 million (viz. contributions and interest upto retirement) is eligible for exemption<sup>7</sup>.
  - The said exemption is further reinforced as no taxes were deducted at source<sup>8</sup> on the withdrawn amount by the Trustees of the PF.
  - Based on a judicial precedent<sup>9</sup>, a mere non-mentioning of exempt income in the ITR cannot be construed as a new claim. The Tribunal had further observed that such claim of exempt income was already put forth by the taxpayer during the course of assessment proceedings.
- In relation to interest accrued in the PF account post retirement, the Tribunal observed as under:
  - Though there is a provision<sup>10</sup> for the Trustees of the PF to allow the balance accumulated in the fund to be retained even after cessation of employment, the exemption<sup>11</sup> is limited to the accumulated PF balance due and payable to the taxpayer only upto the date of cessation of employment. Any further interest accrued (post cessation of employment) cannot be construed as earned in the capacity of an employee;
  - Given the above, in the instant case, the accumulated interest post retirement amounting to INR4.4 million is not eligible for exemption<sup>12</sup>;

- Further, the said interest income should be offered to tax in the respective TYs in which such income actually accrued, as the taxpayer followed a mercantile system of accounting.

### Our comments

This decision is pertinent to individuals who have retired or resigned from their employment and have continued to retain their PF accounts, without being employed elsewhere. Based on the decision, it would appear that such individuals need to track the interest accrued in the PF account post cessation of employment, in order to consider the same for taxation in the year of accrual, where the individual follows a mercantile system of accounting.

Considering this is a fact specific case and a ruling of the Tribunal, adoption of the same in other jurisdictions/ set of facts could be evaluated on a case-to-case basis.



<sup>6</sup> Clause (f) of Rule 2 of Fourth Schedule supported by Circular No 134, dated 17 June 1974

<sup>7</sup> Section 10(12) of the Act read with Rule 8 of Part A of Fourth Schedule

<sup>8</sup> Rule 10 of Fourth Schedule

<sup>9</sup> NTPC Ltd v. CIT [1998] 229 ITR 383 (SC)

<sup>10</sup> Sub-rule 3 of Rule 5 to Fourth Schedule

<sup>11</sup> Section 10(12) of the Act

<sup>12</sup> Section 10(12) of the Act

[www.kpmg.com/in](http://www.kpmg.com/in)

#### Ahmedabad

Commerce House V, 9th Floor,  
902 & 903, Near Vodafone House,  
Corporate Road,  
Pralhad Nagar,  
Ahmedabad – 380 051  
Tel: +91 79 4040 2200  
Fax: +91 79 4040 2244

#### Bengaluru

Maruthi Info-Tech Centre  
11-12/1, Inner Ring Road  
Koramangala,  
Bengaluru – 560 071  
Tel: +91 80 3980 6000  
Fax: +91 80 3980 6999

#### Chandigarh

SCO 22-23 (1st Floor)  
Sector 8C, Madhya Marg  
Chandigarh – 160 009  
Tel: +91 172 393 5777/781  
Fax: +91 172 393 5780

#### Chennai

KRM Tower, Ground Floor,  
No 1, Harrington Road  
Chetpet, Chennai – 600 031  
Tel: +91 44 3914 5000  
Fax: +91 44 3914 5999

#### Gurugram

Building No.10, 8th Floor  
DLF Cyber City, Phase II  
Gurugram, Haryana – 122 002  
Tel: +91 124 307 4000  
Fax: +91 124 254 9101

#### Hyderabad

Salarpuria Knowledge City,  
ORWELL, 6th Floor, Unit 3, Phase  
III, Sy No. 83/1, Plot No 2,  
Serilingampally Mandal, Raidurg  
Ranga Reddy District,  
Hyderabad, Telangana – 500081  
Tel: +91 40 6111 6000  
Fax: +91 40 6111 6799

#### Jaipur

Regus Radiant Centres Pvt Ltd.,  
Level 6, Jaipur Centre Mall,  
B2 By pass Tonk Road  
Jaipur, Rajasthan, 302018.  
Tel: +91 141 - 7103224

#### Kochi

Syama Business Center  
3rd Floor, NH By Pass Road,  
Vytilla, Kochi – 682019  
Tel: +91 484 302 7000  
Fax: +91 484 302 7001

#### Kolkata

Unit No. 603 – 604,  
6th Floor, Tower – 1,  
Godrej Waterside,  
Sector – V, Salt Lake,  
Kolkata – 700 091  
Tel: +91 33 4403 4000  
Fax: +91 33 4403 4199

#### Mumbai

Lodha Excelus, Apollo Mills  
N. M. Joshi Marg  
Mahalaxmi, Mumbai – 400 011  
Tel: +91 22 3989 6000  
Fax: +91 22 3983 6000

#### Noida

Unit No. 501, 5th Floor,  
Advant Navis Business Park  
Tower-B, Plot# 7, Sector 142,  
Expressway Noida, Gautam Budh Nagar,  
Noida – 201305  
Tel: +91 0120 386 8000  
Fax: +91 0120 386 8999

#### Pune

9th floor, Business Plaza,  
Westin Hotel Campus, 36/3-B,  
Koregaon Park Annex, Mundhwa Road,  
Ghorpadi, Pune – 411001  
Tel: +91 20 6747 7000  
Fax: +91 20 6747 7100

#### Vadodara

iPlex India Private Limited,  
1st floor office space, No. 1004,  
Vadodara Hyper, Dr. V S Marg  
Alkapuri, Vadodara – 390 007  
Tel: +91 0265 235 1085/232 2607/232 2672

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